



Stockholm School of Economics in Riga
“Informal Entrepreneurship Index”
for Latvia

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Why?

- **Positive and Negative sides of entrepreneurship.**
- **What is the amount of the “underground economy”/ “shadow economy”, “informal economy”, etc.**
 - ATKearney 2009: 39,4% (largest in the EU)
 - 10 - 45%: various sources (including CSB of Latvia)
- **What is measured and how?**
 - Existing surveys: representativeness/ methodology?
 - Experts: “how do they know”/ subjective?
- **Need for accurate data for policy making purposes!**
 - Finance Ministry plan for battling the shadow economy (www.baltic-course.com, January, 2010)
 - Ministry of Welfare proposes steps to decrease illegal employment (www.apollo.lv, April 6, 2010)

Aims of the SSE Riga Informal Entrepreneurship Index for Latvia

- **Measure the level of informal entrepreneurship activity in Latvia.**
 - Annual survey
- **Explore the main reasons and influential factors behind such activity.**
- **Opinion of entrepreneurs: what is needed to decrease informal entrepreneurship activity in Latvia?**

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aims to provide *entrepreneurship policymakers* with data for making justified policy decisions as well as to foster a deeper understanding of entrepreneurship processes in *Latvian society*.

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in cooperation with:

- **European Council for Small Business and Entrepreneurship (www.ecsb.org)**
- **Lursoft (www.lursoft.lv)**

What is measured and how? The survey.

- **Conceptual framework for the survey: W. Baumol (1990); A. Sauka (2008).**
- **Approaching entrepreneurs: 591 telephone interviews with owners-managers of SMEs in Latvia.**
- **March, 2010: data for 2009.**
- **Data provided by Lursoft.**
- **Sensitive nature of questions: ‘indirect approach’, entrepreneurs as experts.**

Level of Informal Entrepreneurship Activity in Latvia (2009)

- **Degree of underreporting business income (net sales profits).**
- **Degree of underreporting number of employees.**
- **Proportion of 'official' vs. 'unofficial' salaries: Envelope wages.**
- **% of revenues paid to 'get things done': corruption.**
- **% of contract value offered to secure business contracts with the government.**

Influential Factors

- **Industry and region.**
- **Satisfaction of entrepreneurs with the tax system in Latvia.**
- **Satisfaction with the performance of the State Revenue Service.**
- **Satisfaction with government's support.**

Influential Factors (cont'ed)

- **Tolerance towards underreporting.**
- **Tolerance towards bribing.**
- **Size of the company and experience of owner-manager: various measures.**
- **Strategy: innovativeness, risk taking, proactiveness of the company.**
- **Performance: profits, turnover, employment.**

Suggestions from entrepreneurs: how the Latvian government can help

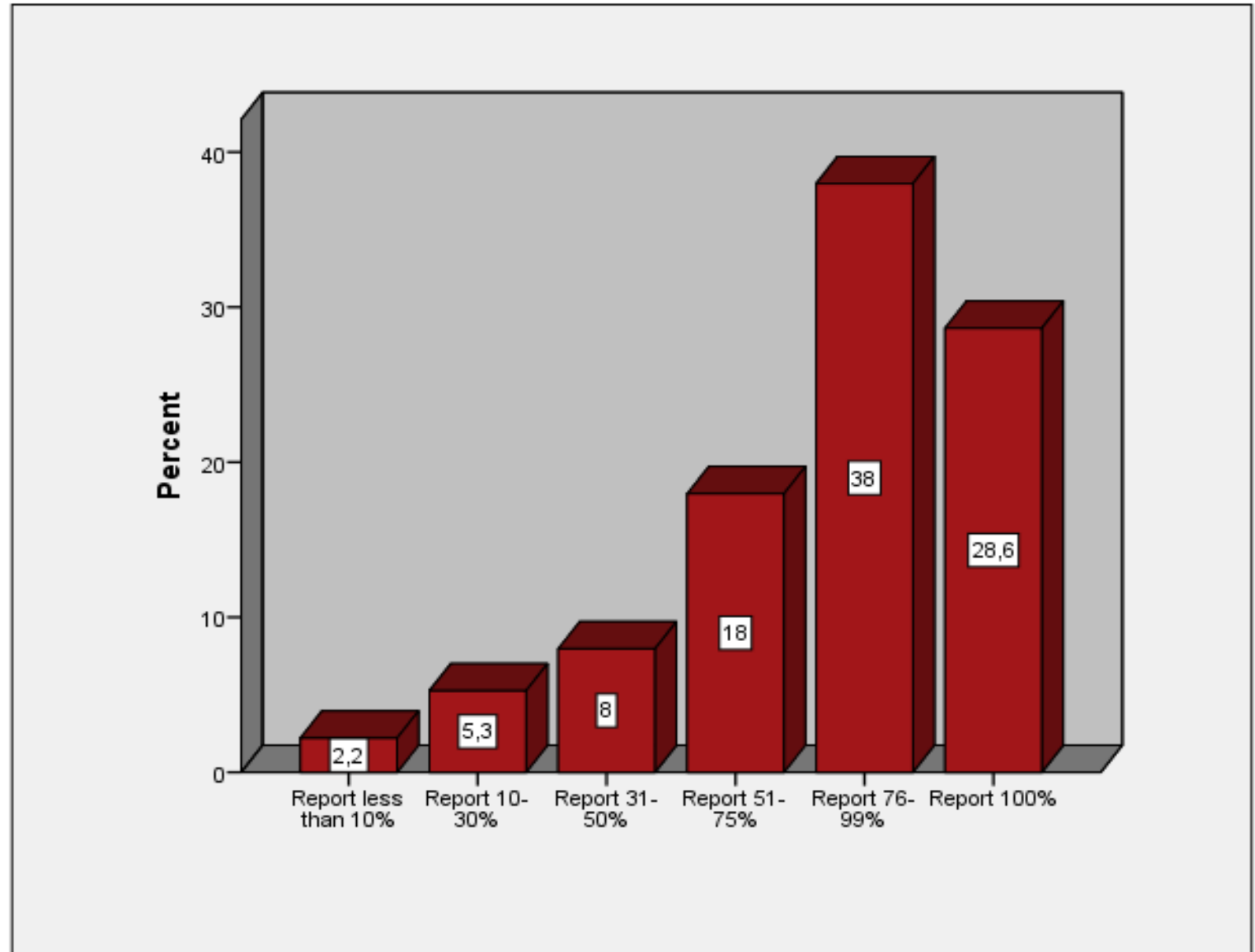
- **Please name the 3 most important factors that have to be fulfilled by the Latvian government to ensure that entrepreneurs in Latvia pay all taxes.**

Possible Negative and Positive Consequences of Informal Entrepreneurship Activity

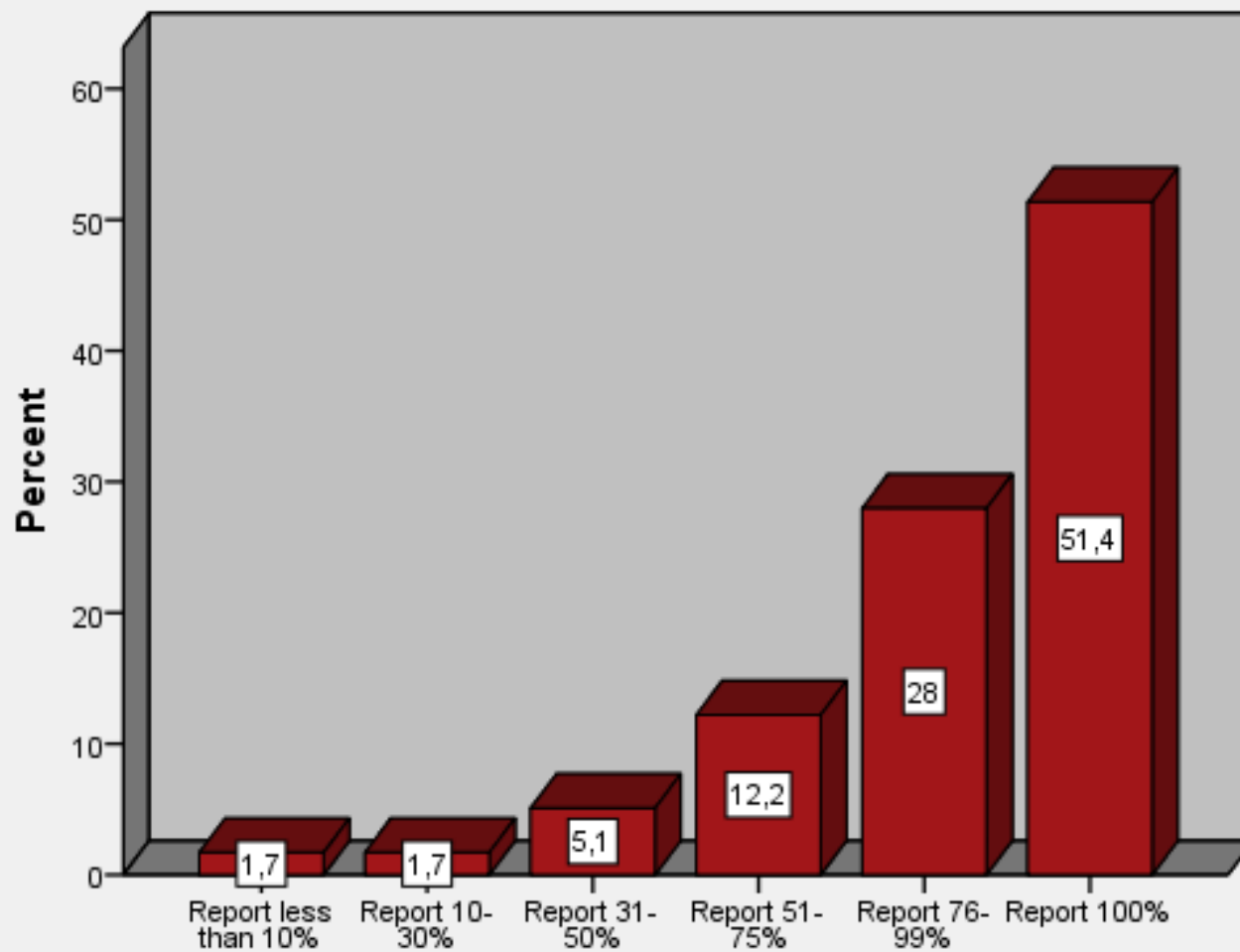
RESULTS:

**The level of informal entrepreneurship activity
in Latvia**

Degree of underreporting business income, n=590



Degree of underreporting employment, n=590



Index: Degree of Underreporting

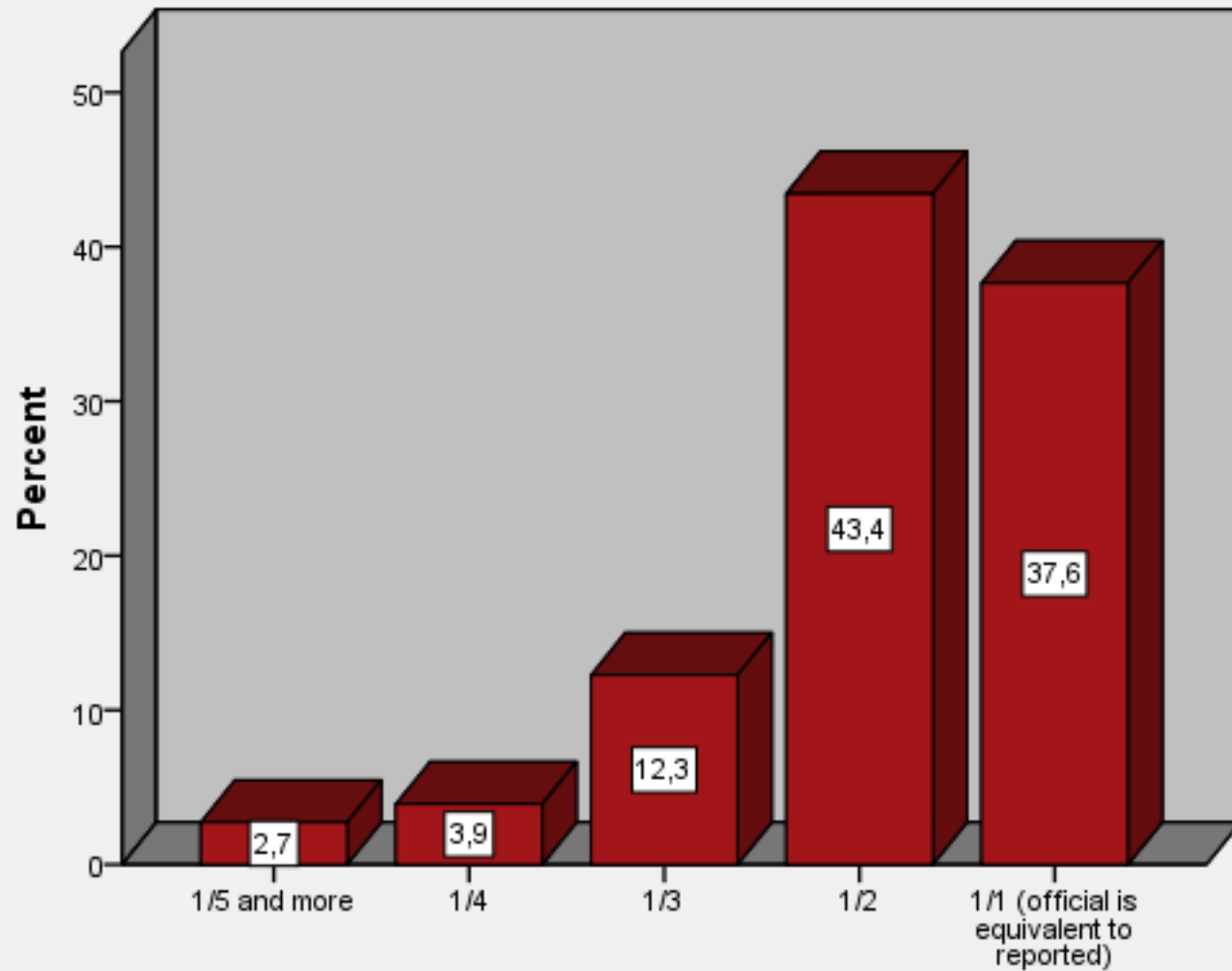
18.26%

0%

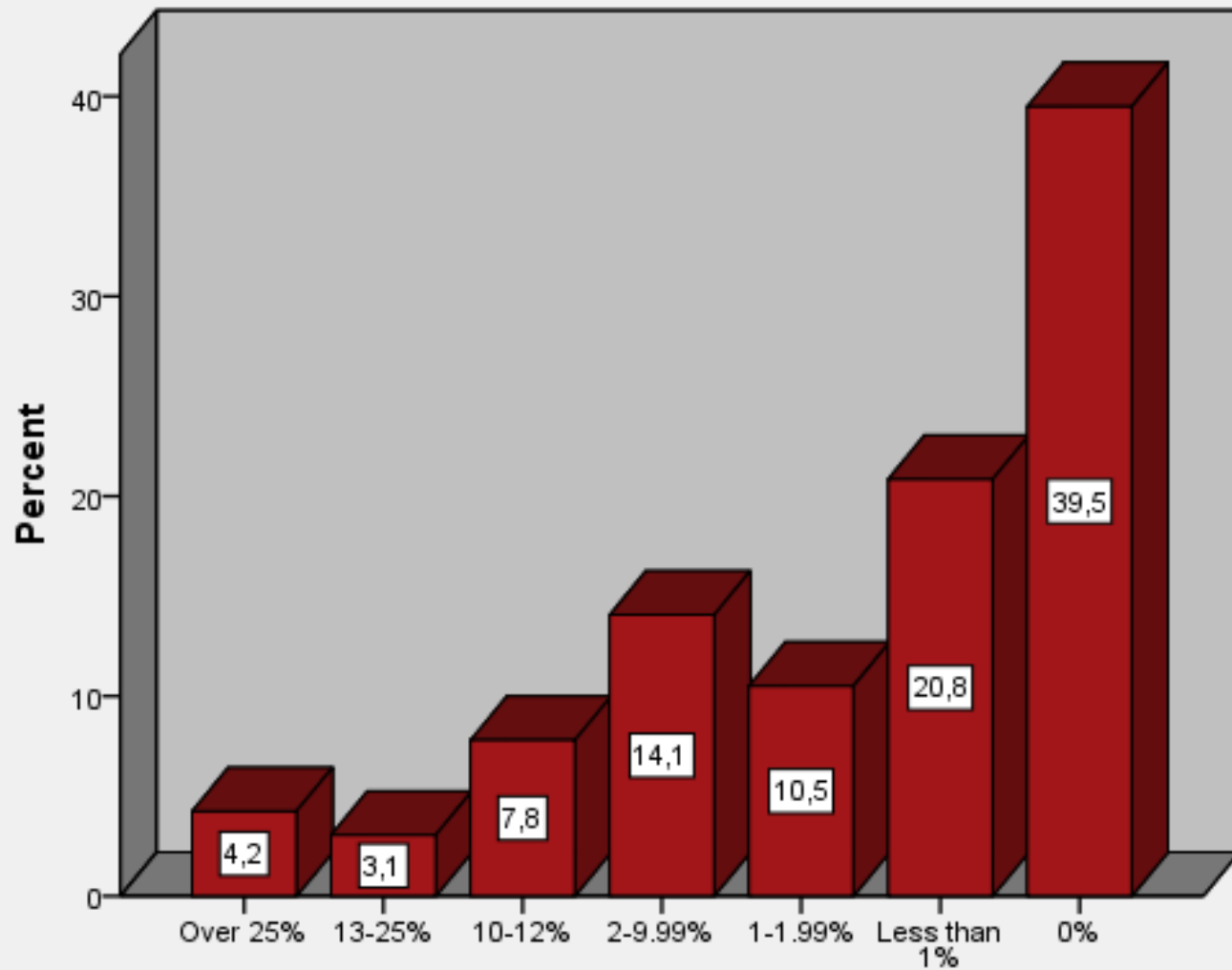
100%

- The index consists of 2 questions: measuring underreporting of business income and number of employees.
- Each of these 2 questions is converted to a scale of 1-100%, with 0% representing no underreporting. Then both percentages are averaged.

Official vs. unofficial salary, n=587



Revenues paid to 'get things done', n=590



SSE Riga “Informal Entrepreneurship Index” for Latvia (2009)

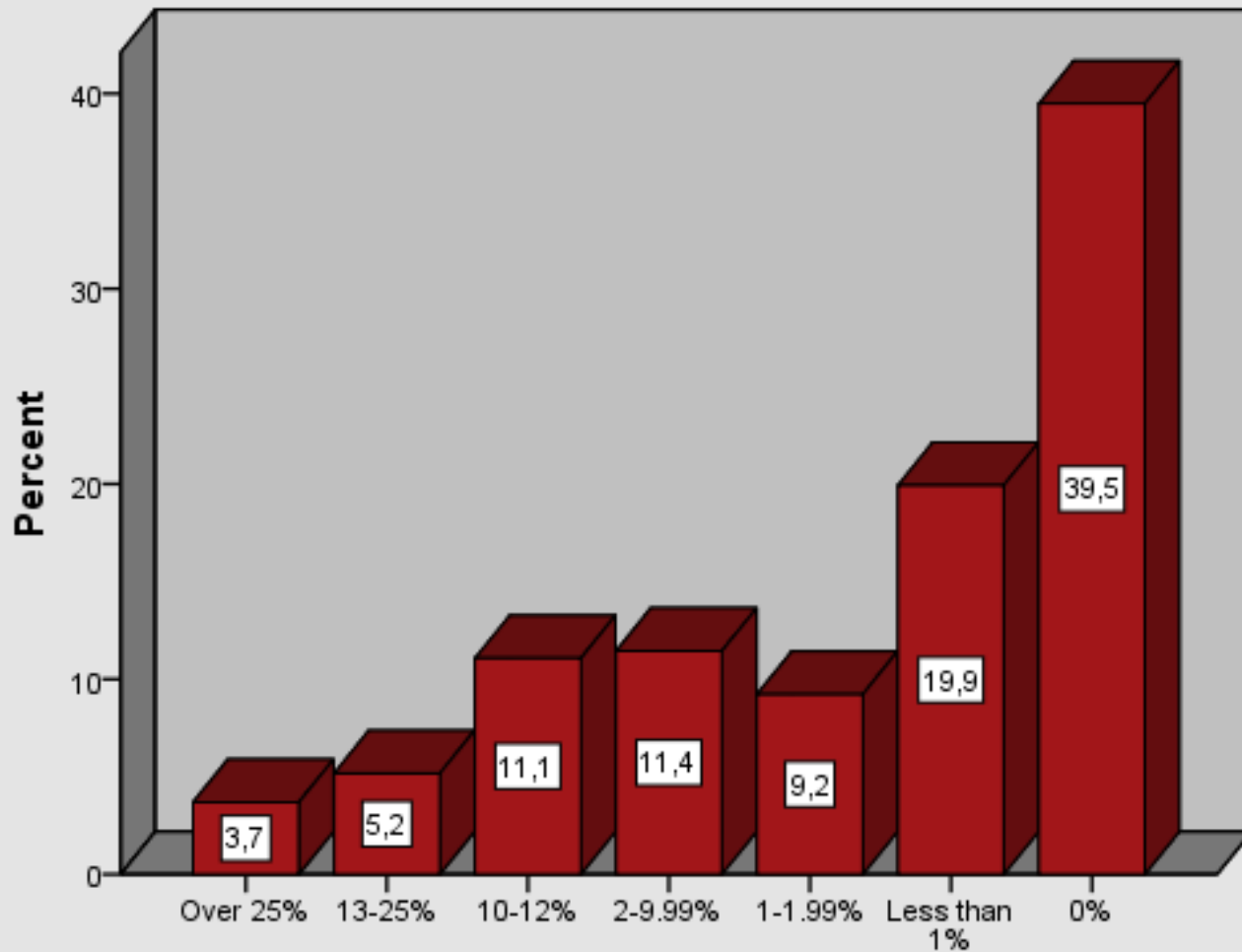
19.01

0

100

- **Represents ‘indirect %’ of informal entrepreneurship activity in Latvia: different scales.**
- The index consists of 4 questions: measuring underreporting of business income, number of employees, envelope salaries and bribing.
- Each of these 4 questions is equally weighted in terms of their contribution to the index. The index is then normalized to a scale of 1 – 100.

Contract value business-government, n=271



RESULTS:

Factors influencing the degree of informal entrepreneurship activity in Latvia

Index: Degree of Underreporting (2009) in Regions of Latvia

Riga: 16.86%

Latgale: 18.76%

Zemgale: 19.65%

Kurzeme: 22.03%

Vidzeme: 23.06%

18.26%

0%

100%

- The index consists of 2 questions: measuring underreporting of business income and number of employees.
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SSE Riga “Informal Entrepreneurship Index” for Latvia (2009): Regions

Riga: 18.04

Latgale: 16.35

Zemgale: 19.84

Kurzeme: 21.89

Vidzeme: 22.68

19.01

0

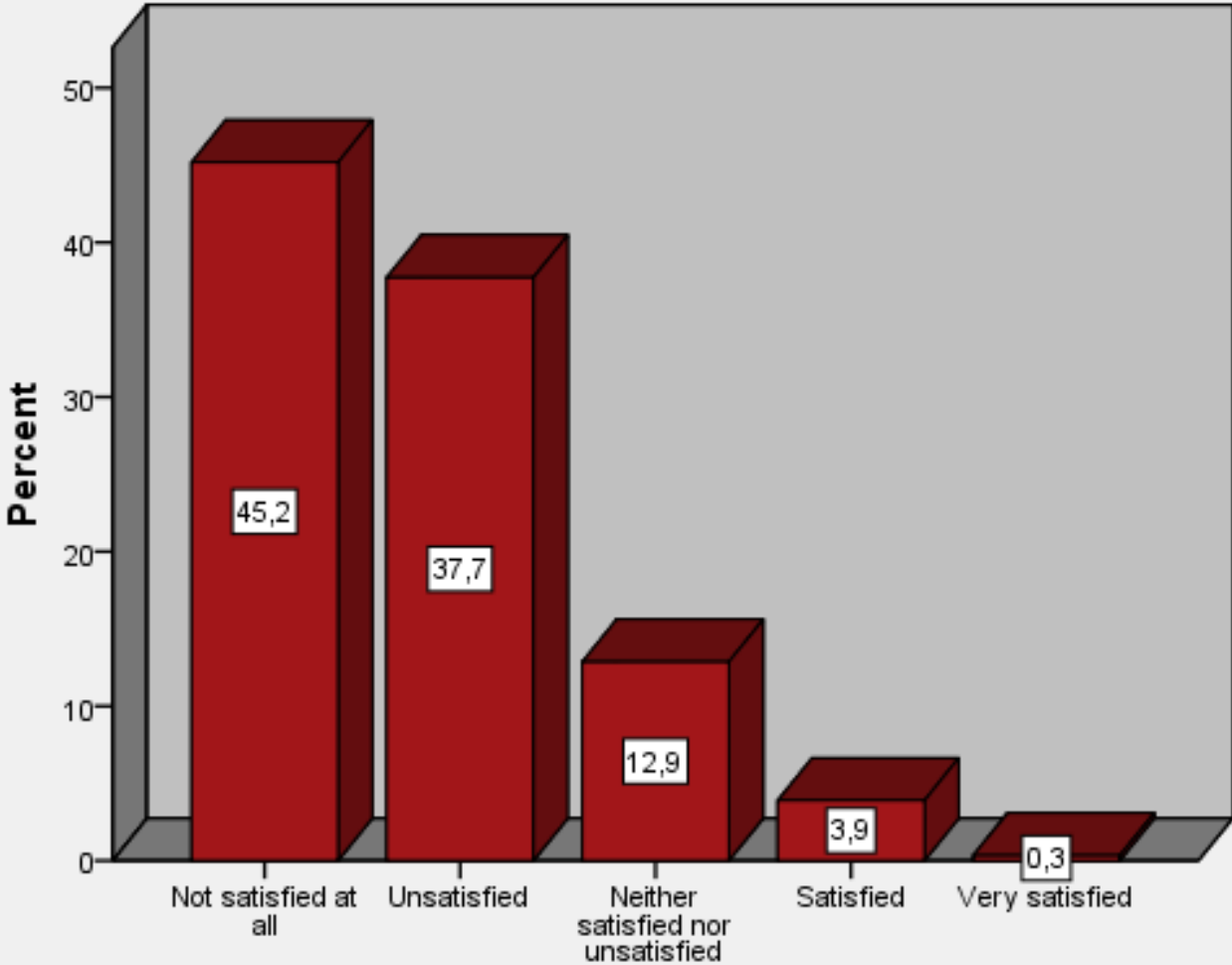
100

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- The index consists of 4 questions: measuring underreporting of business income, number of employees, envelope salaries and bribing.
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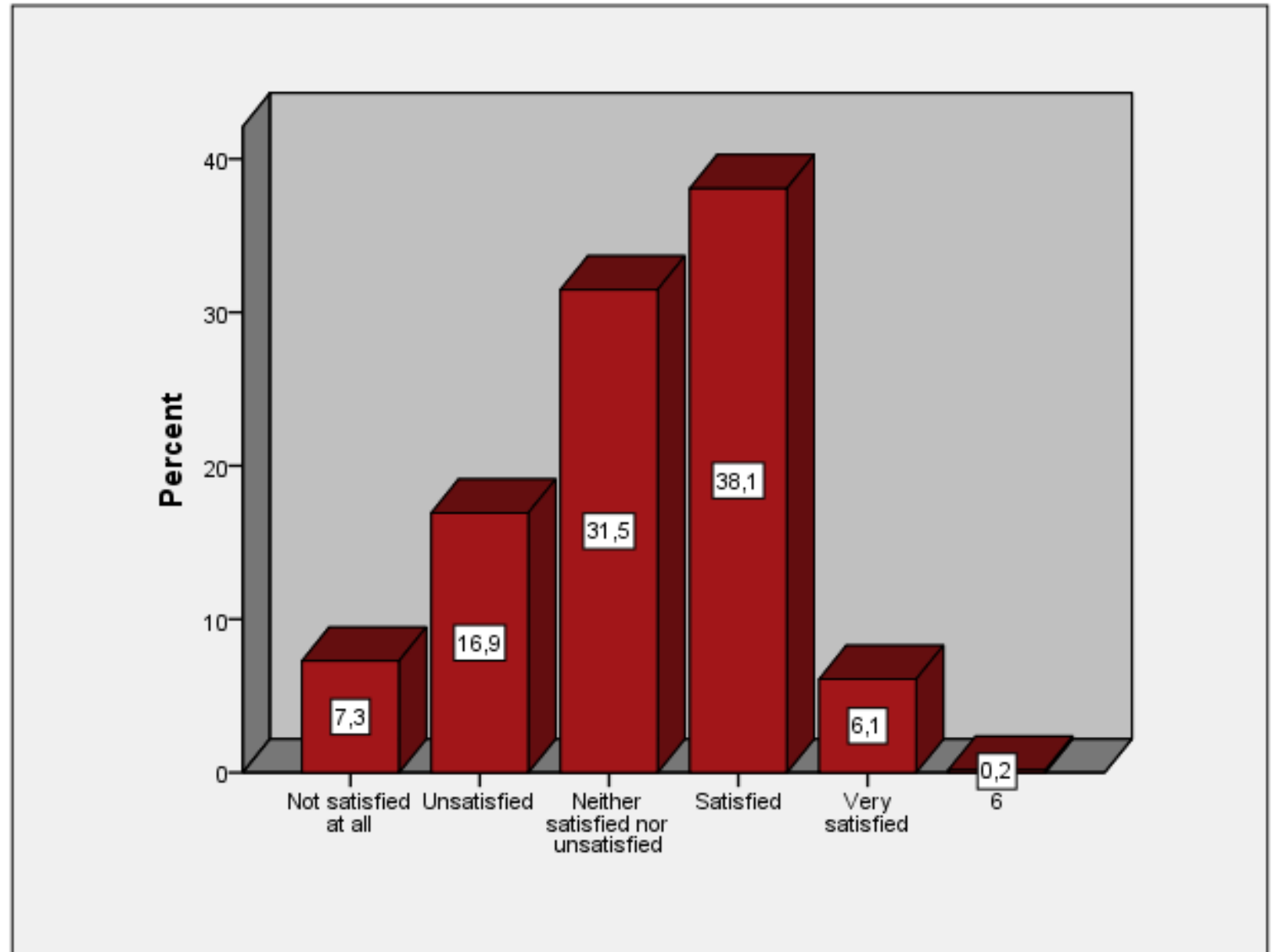
Industry as an influential factor

- **Overall, companies in the construction sector are more involved in informal entrepreneurship as compared to companies in the service sector.**

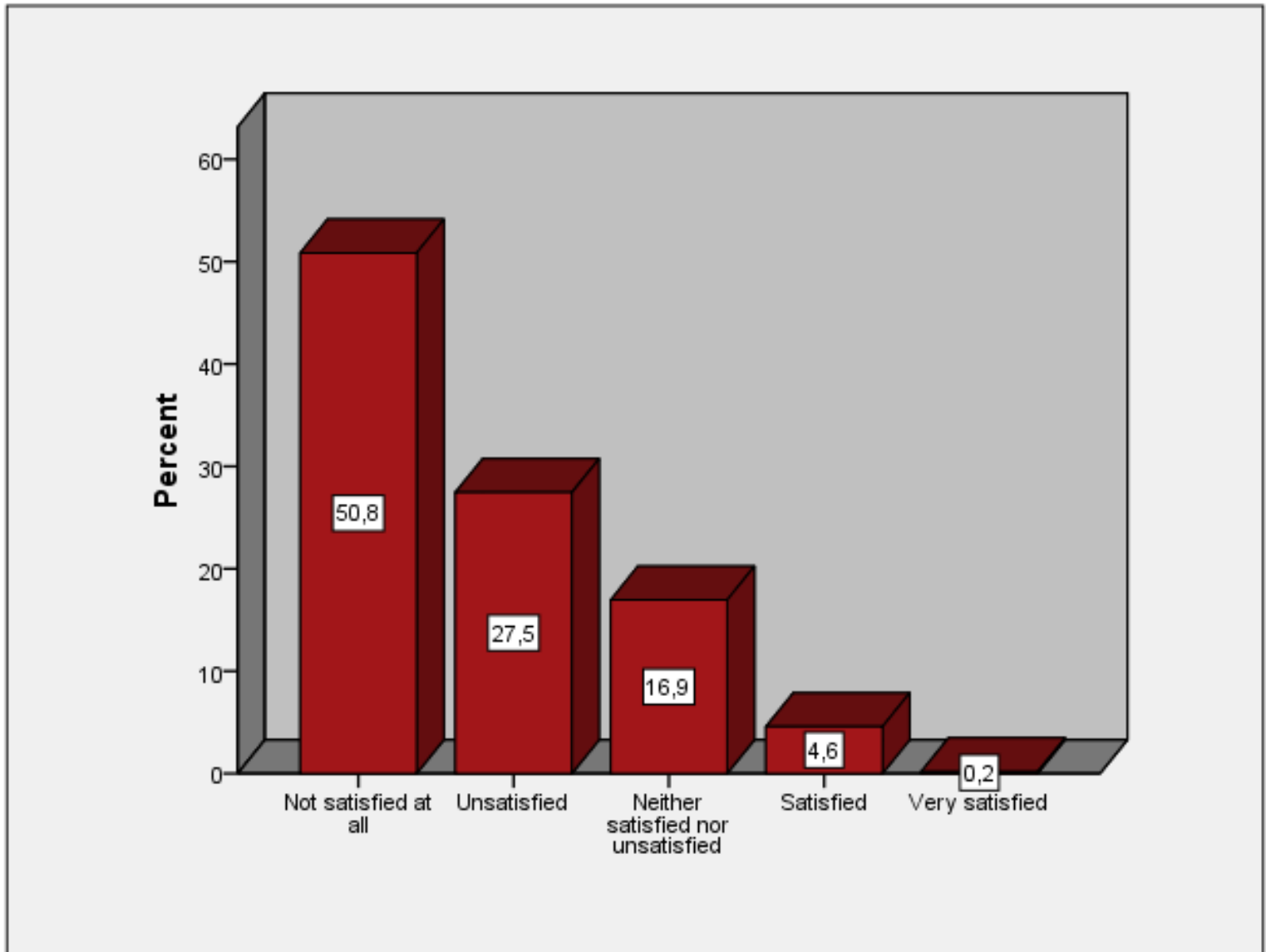
Satisfaction of entrepreneurs with the Latvian tax system, n= 591



Satisfaction of entrepreneurs with the performance of SRS, n=591

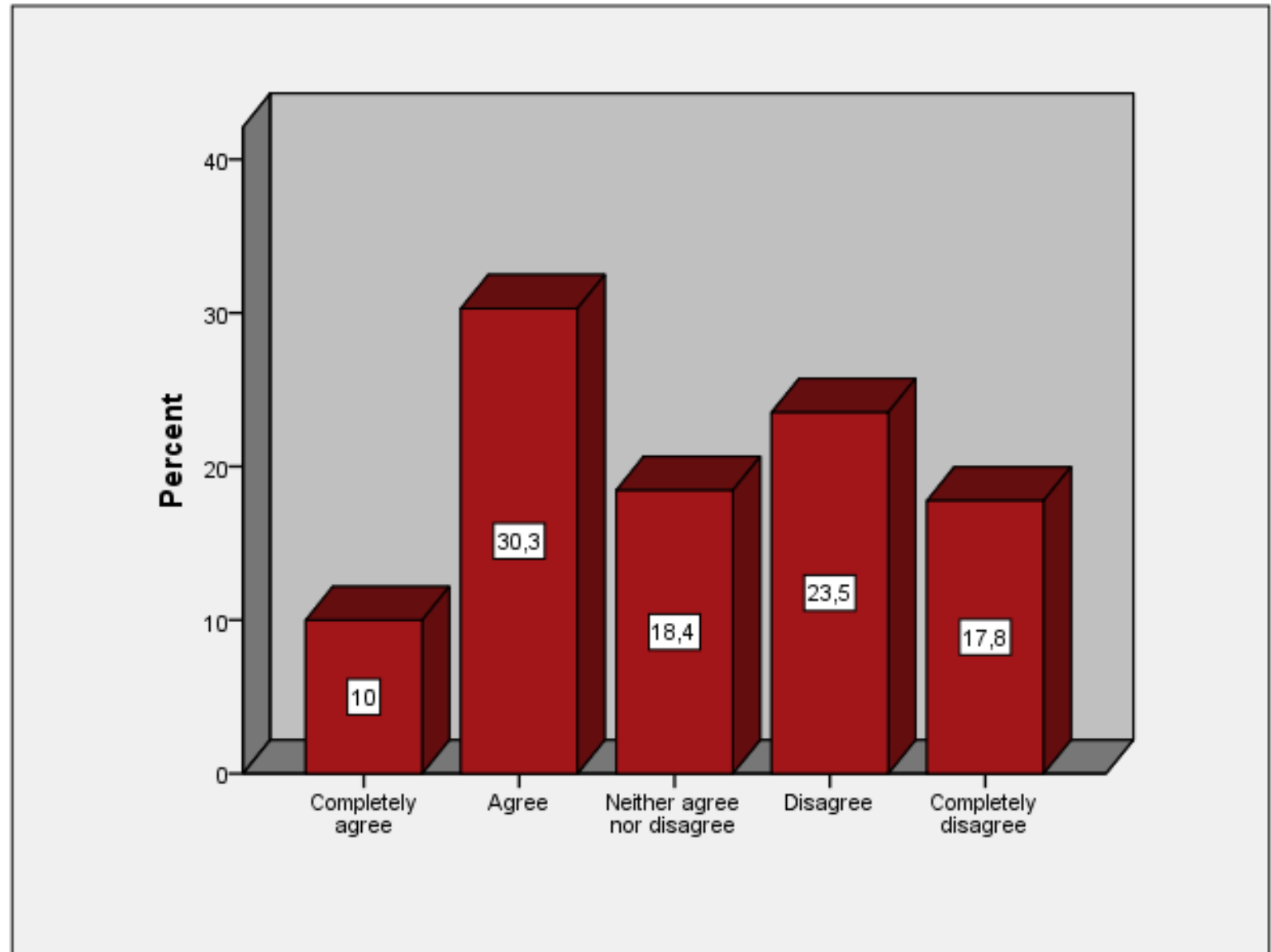


Satisfaction of entrepreneurs with government support for entrepreneurship in Latvia, n=590

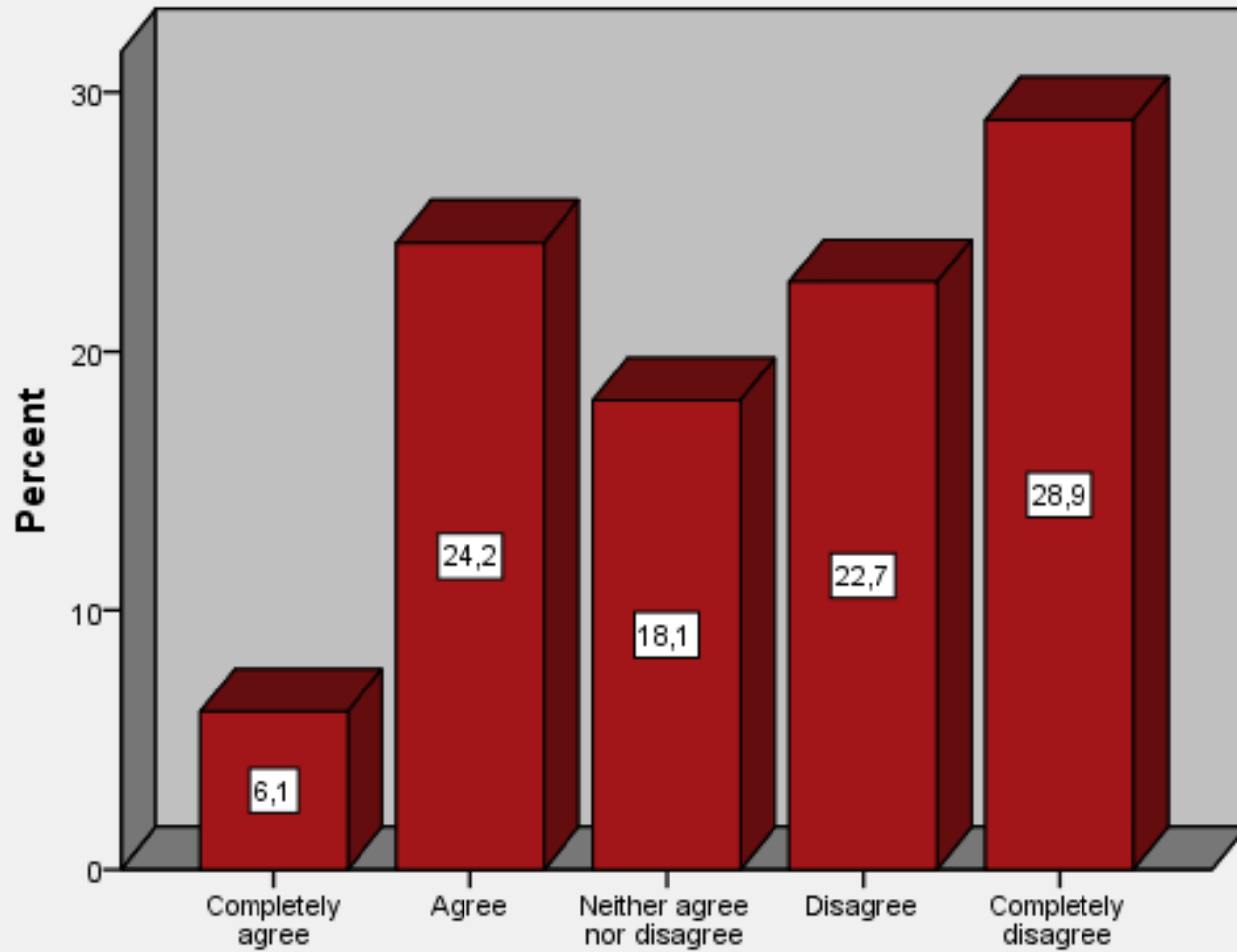


- **However, the survey suggests that there is *no statistically significant relationship* between satisfaction of entrepreneurs with the tax system, SRS, government support and the level of informal entrepreneurship in Latvia.**
- **In other words, satisfaction of entrepreneurs with the tax system, SRS or government support for entrepreneurship does not influence the degree of involvement in informal entrepreneurship activity in Latvia.**

Underreporting is tolerated behavior in Latvia, n=591



Bribing is tolerated behavior in Latvia, n=591



- **According to the survey, those who think that underreporting is tolerated more are less involved in informal entrepreneurship activity (**).**
- **The survey suggest that there is no statistically significant relationship between tolerance towards bribing and involvement in informal entrepreneurship activity.**

Size of the company and experience of the owner manager as influential factors

- **The only significant finding: companies *that employ more employees tend to underreport employment less* (*)**
- **No statistically significant results as regards previous business experience and education of the owner-manager, turnover and age of the company.**

Firm level strategy as an influential factor

- **Entrepreneurial orientation**

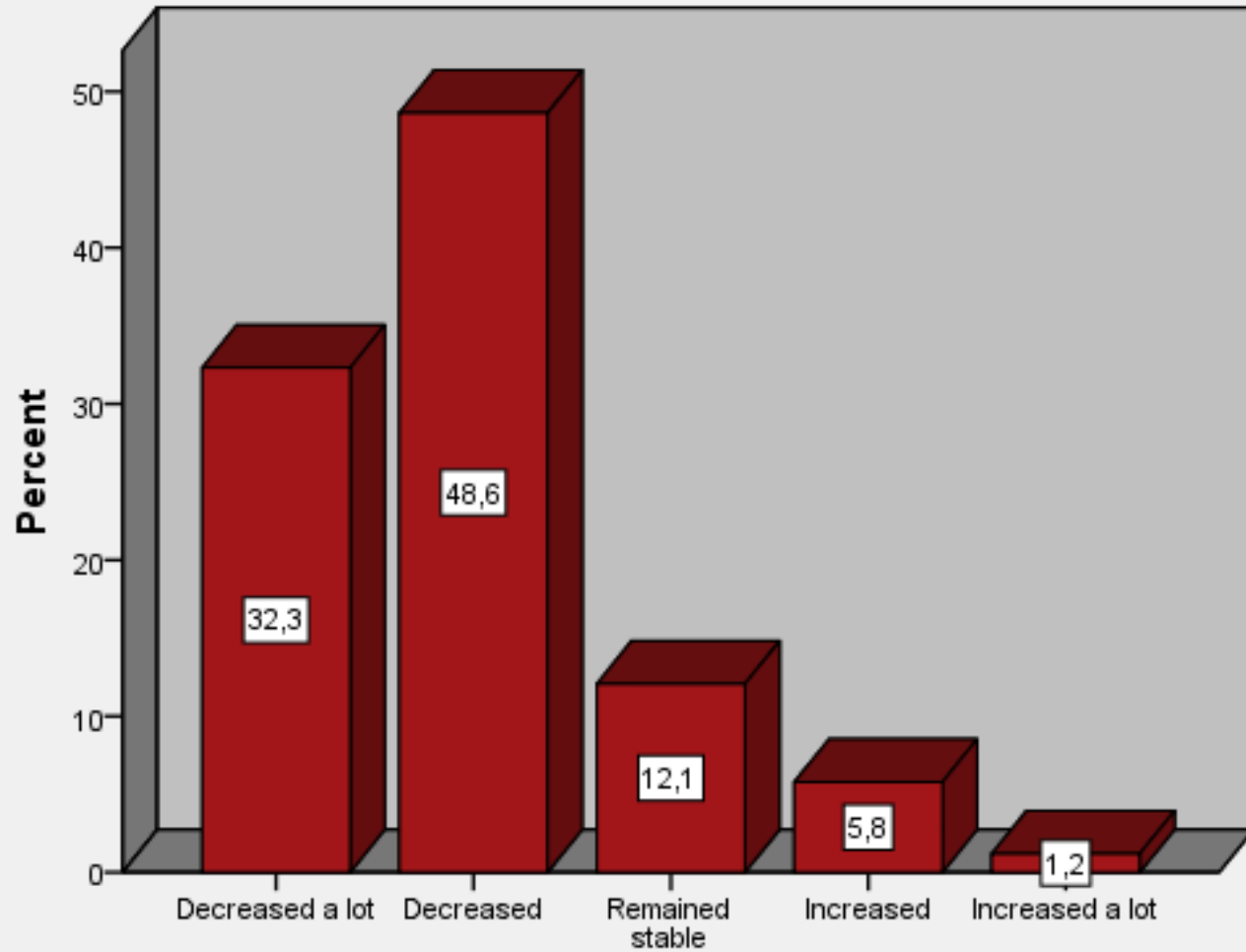
- **Innovativeness:** refers to a firm's efforts to find new opportunities and novel solutions. Support for inventions and new ideas even when the benefits are unclear.
- **Risk taking:** refers to a firm's willingness to seize a venture opportunity before a successful outcome is ensured and act boldly without knowing consequences. Willingness to take business, financial and personal risks.
- **Proactiveness:** refers to the ability to create a competitive advantage by shaping the industry and forcing competitors to follow; monitor trends, identify future needs, take the first mover advantage.

- ***Innovative companies* are more involved in informal entrepreneurship activity (*)**
- ***Risk takers* are more involved in informal entrepreneurship activity (**)**

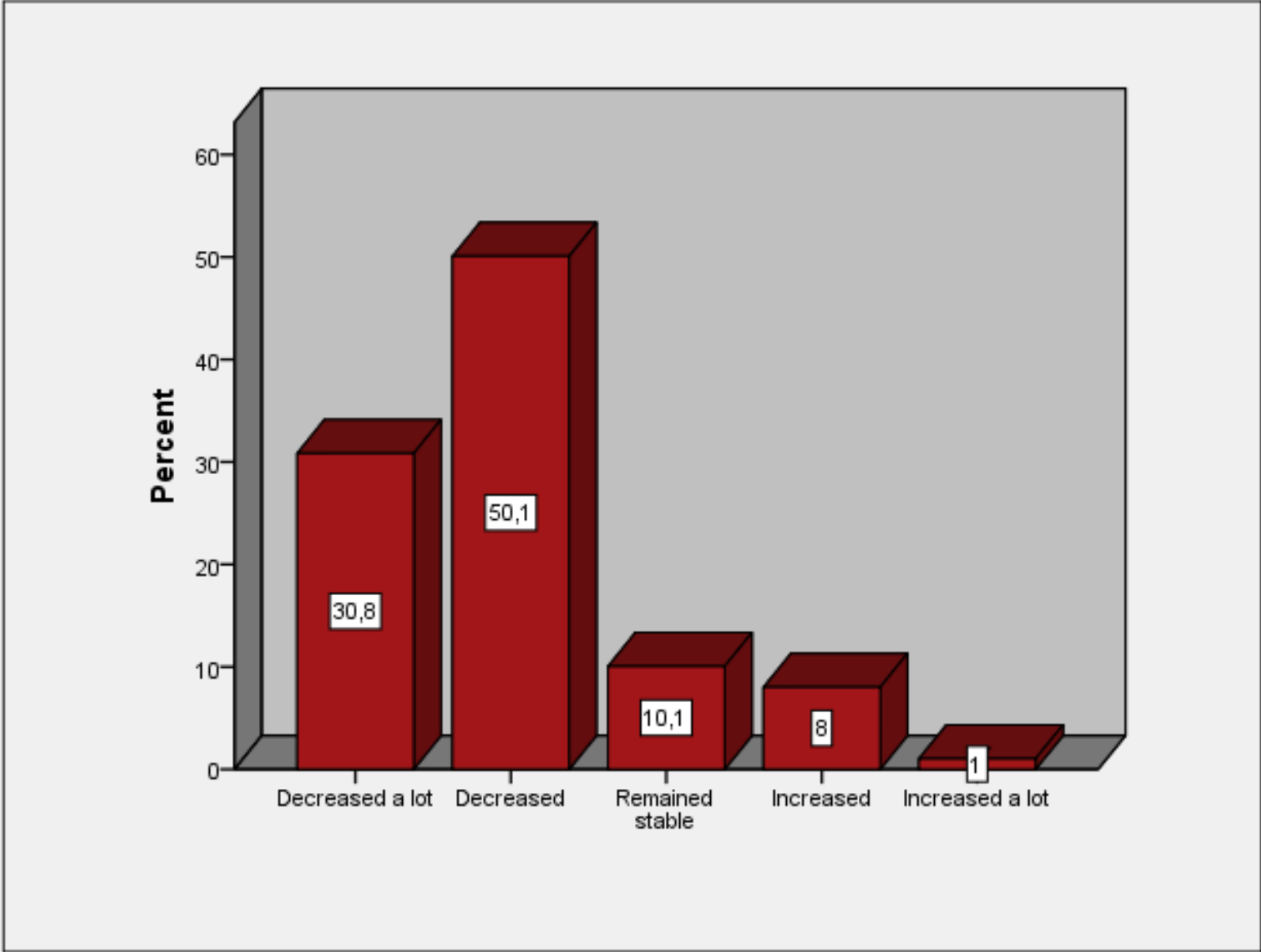
Performance of the company as an influential factor

- **Firm performance is measured as an 'increase' or 'decrease' in:**
 - **Profits**
 - **Turnover**
 - **Number of employees****as compared to the situation 12 months ago.**

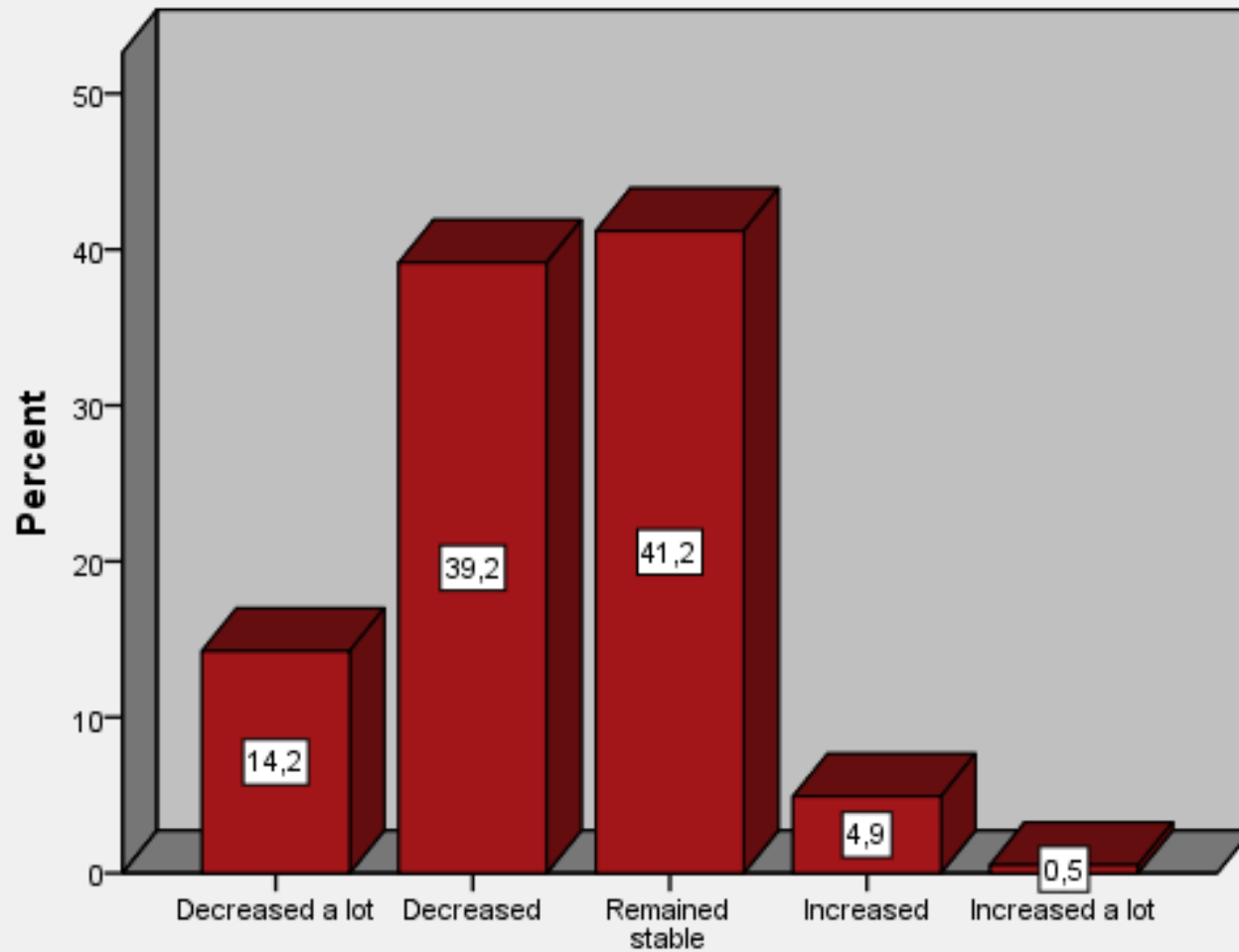
Net sales profits, n=588



Sales turnover, n=587

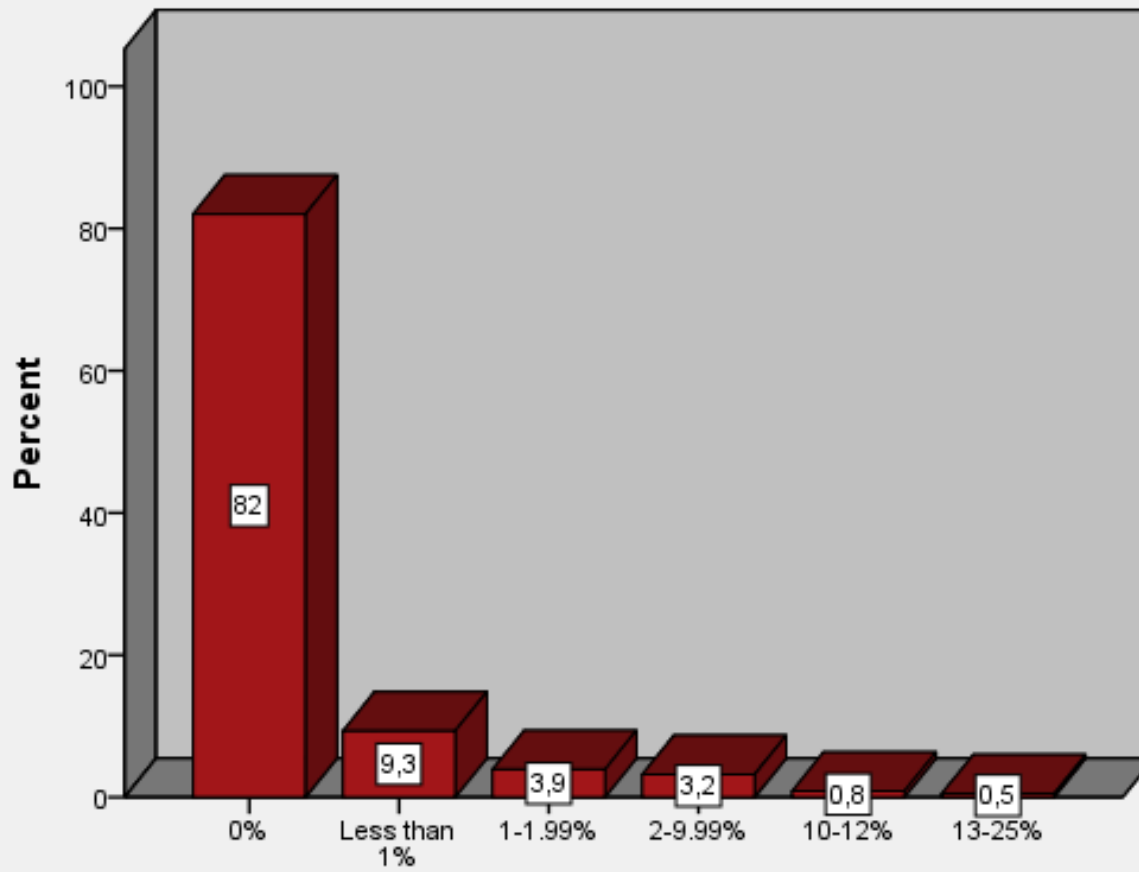


Employment, n=590

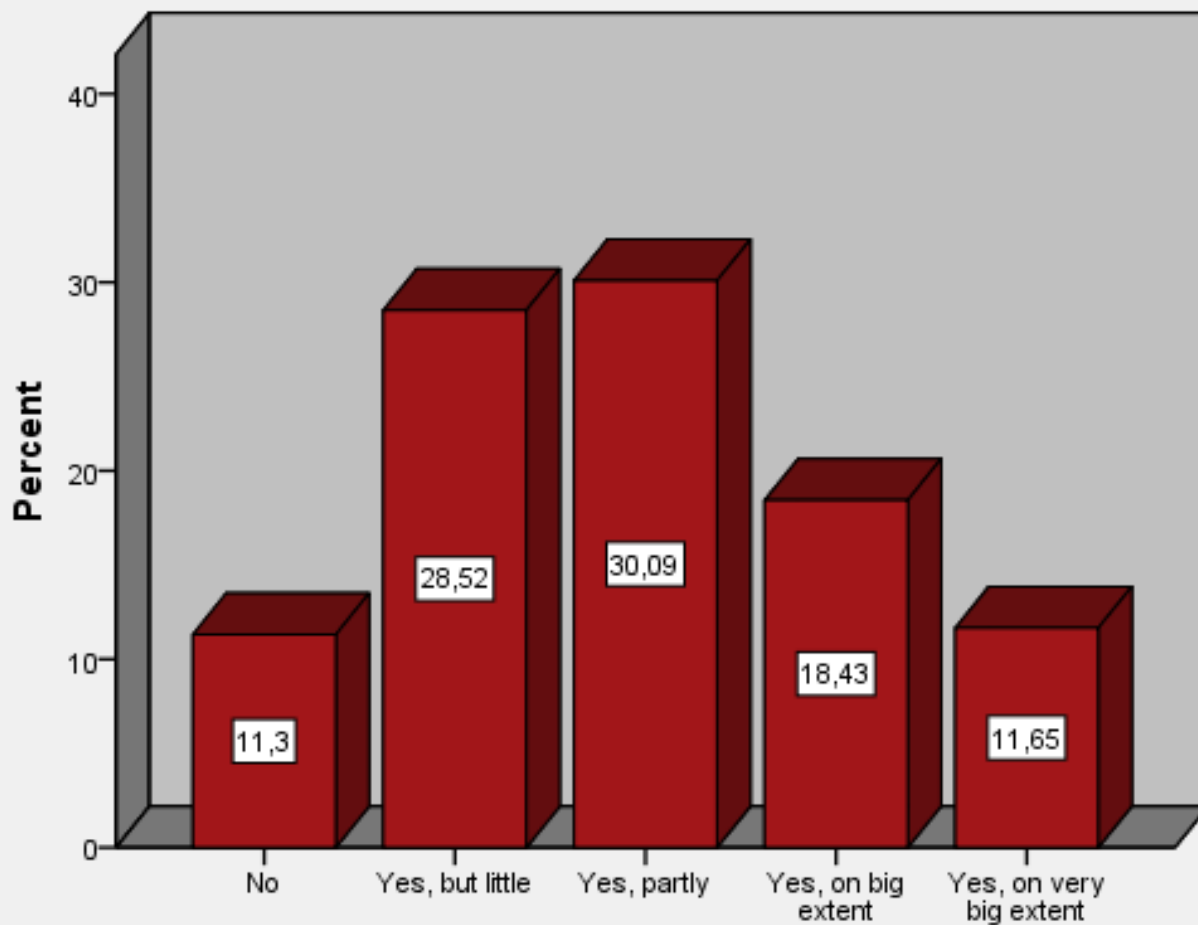


- **Companies with a higher increase in turnover are *more involved in informal entrepreneurship activity* (*)**
- **No statistically significant results for profits and employment.**

Contribution to society: sponsorship/philanthropy as an influential factor, n=590



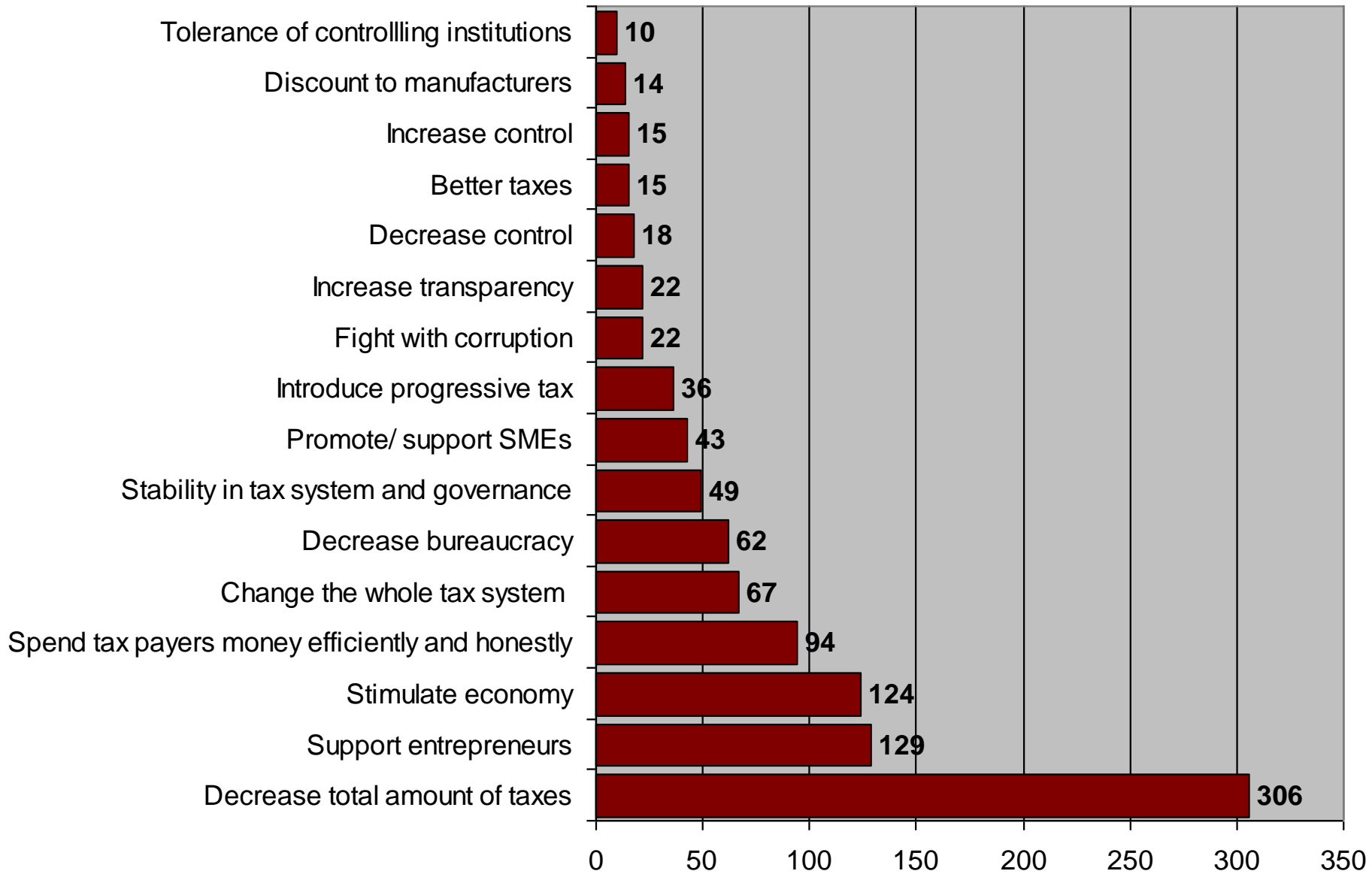
Do you consider that a business such as yours contributes to the growth of the Latvian economy, n=575



- **Companies involved in sponsorship/philanthropy are *more involved in informal entrepreneurship activity (***)***
- ***Nature of sponsorship/philanthropy in Latvia?***

RESULTS:

Suggestions from entrepreneurs on how the Latvian government can help to decrease the level of informal entrepreneurship activity





**Positive and Negative
Consequences of Informal
Entrepreneurship**

Framework by P. Davidsson (2004)

		Venture level outcome	
		+	-
Societal level outcome	+	Quadrant I Hero or success enterprises	Quadrant II Catalyst enterprises
	-	Quadrant III Robber or re-distributive enterprises	Quadrant IV Failed enterprises

Main conclusions by Davidsson (2004):

- ‘Catalyst’ and ‘re-distributive’ enterprises are not marginal phenomena, and **may have a significant impact on the economy.**
- “... if one enjoyed the luxury of dealing with an economy characterized by a perfect and just institutional framework, it would be easy to argue that this type of entrepreneur (p.s. re-distributive) equals illegal ventures. Regrettably, we have to live with the fact that in real economies ‘legal, yet re-distributive’ and ‘illegal, yet societal beneficial’ are both possible.”
(Davidsson, 2004:14)

For conclusions:

**Message to the policy makers by
W. Baumol (1993: 47)**

“...we do not have to wait patiently for slow cultural change in order to find measures to redirect the flow of entrepreneurial activity toward more productive goals. It may be possible to change economic rules in ways that help to offset undesired institutional influences or supplement other influences to work in beneficial directions.”

Contributors:

- **Data collection:** **Matīss Brunavs, Alisa Sokolska, Ilze Zumente, Maija Marinčenko, Kārlis Putriņš, Kristīne Ingelande, Margarita Jevsignejeva, Staņislavs Filatovs, Aleksandra Jakušenko, Laura Danberga**
- **Data analysis:** **Dr. Tālis Putniņš, SSE Riga**
- **Logo:** **Fionn Dobbin, SSE Riga**
- **Company data from Lursoft**

The image shows a close-up, low-angle view of a highly ornate classical building facade at night. The architecture is illuminated by warm, golden lights, highlighting the intricate details of the stone carvings. On the left, a large, expressive face is carved into the wall. In the center, a tall, slender column is topped with a complex, multi-tiered capital. To the right, another large face is carved, looking towards the viewer. Below these, there are more detailed carvings, including what appears to be a winged figure or a bird-like creature. The sky in the background is a deep, dark blue, suggesting twilight or night. The overall composition is dramatic and emphasizes the grandeur and artistry of the architecture.

Thank you!