

IS ENTREPRENEURSHIP A CHANNEL OF SOCIAL MOBILITY IN LATIN AMERICA?*

FRANCESCA CASTELLANI**
EDUARDO LORA***

This paper summarizes the findings in this special issue of the Latin American Journal of Economics on entrepreneurship's role in upward social mobility in Latin America, especially for the middle class, often considered the cradle of entrepreneurship. The income-persistent coefficients estimated with pseudo-panel data for Colombia, Ecuador, and Uruguay indicate that entrepreneurship is a channel of intergenerational mobility, while asset persistence estimates for Mexico show that entrepreneurship increases mobility across generations. Although persistence coefficients don't indicate the direction of such mobility, estimates of income differentials between entrepreneurs and non-entrepreneurs for Ecuador and Mexico support the hypothesis that upward mobility dominates.

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1. INTRODUCTION

Lack of social mobility is arguably one of the key reasons for the extreme levels of inequality observed in many countries in Latin America, consistent with both theory and empirical observation in several countries and regions (Erickson and Goldthorpe, 1992; Jantti *et al.*, 2006; Solon, 1992). Since low intergenerational mobility transmits high inequality from one generation to the next (UNDP, 2010), identifying the main barriers to social mobility and the vehicles that could potentially break this intergenerational vicious circle is a commendable objective for public policy-minded researchers (Torche, 2010).

Entrepreneurship may be seen as a vehicle for upward social mobility, especially for the middle class, which is often considered the cradle of entrepreneurship. Countries with a large middle class are believed

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** Inter-American Development Bank. Email: francescac@iadb.org.

*** Center for International Development, Kennedy School of Government, Harvard University. Email: eduardo.a.lora@gmail.com

to support a vigorous business class because middle-class values and attitudes are conducive to investing and innovating (Acemoglu and Zilibotti, 1997; Doepke and Zilibotti, 2005). However, the entrepreneurial spirit of the middle classes is the subject of debate and in apparent contradiction to the fact that the share of entrepreneurs is larger among the upper classes (Banerjee and Duflo, 2008; OECD, 2011).¹

Similarly, although public policies in both developed and emerging economies often encourage entrepreneurship as a means to create employment and promote growth, the effectiveness of such policies is far from warranted. This is especially the case in developing countries, where entrepreneurship is the only recourse for many workers with no other opportunities to earn a living and where most firms are small and characterized by low productivity (Levy, 2008; Pages, 2010).

These observations and findings prompt the main questions addressed by the papers in this volume: Do Latin American entrepreneurs experience more mobility within and across generations than non-entrepreneurs? Is this mobility absolute or relative, and upward? Do entrepreneurs from different social backgrounds face different prospects for mobility? What family and personal background factors seem to be more conducive to entrepreneurship? Should public policy promote entrepreneurial activity in order to increase social mobility and further the possibilities of improvement of the lower classes?

The papers included in this special issue were prepared under the auspices of the Korean Social Development Fund in a project led by the Inter-American Development Bank (IDB). A volume published jointly by the IDB and the World Bank (Castellani and Lora, 2014) presents other studies prepared under the same project that address other aspects of the relationship between entrepreneurship and social mobility, with a focus on the potential and limits of policies to promote entrepreneurship as a vehicle for social mobility.

1. Banerjee and Duflo (2008: 26), analyzing data on patterns of consumption and investment by the middle class, conclude that: “Nothing seems more middle class than the fact of having a steady well-paying job. While there are many petty entrepreneurs among the middle class, most of them do not seem to be capitalists in waiting. They run businesses, but for the most part only because they are still relatively poor and every little bit helps. If they could only find the right salaried job, they might be quite content to shut their business down. If the middle class matters for growth, it is probably not because of its entrepreneurial spirit.” The OECD (2011) finds the highest concentration of entrepreneurs among the wealthiest segment of the population rather than the middle sector and no systematic differences in attitudes toward entrepreneurship across social groups.

2. LITERATURE REVIEW

There have only been a few studies in developed countries and almost none in developing countries that assess the extent to which entrepreneurship promotes (greater) social mobility. In this work, entrepreneurship is often seen as an engine of economic and social change for lower-income earners, including disadvantaged groups such as minorities, women, and migrants (Glazer and Moynihan, 1970; Fairlie 2004, 2005; Holtz-Eaking, 2000) or low-skilled workers (Lofstrom, 2009).

In the case of the United States, the empirical evidence has found mixed roles of entrepreneurship in intragenerational economic mobility and significant differences by socioeconomic group. It should be kept in mind that these studies use self-employment as a proxy for entrepreneurship, a method whose value is debatable (see discussion below). Hamilton (2000) finds that self-employed men, on average, have lower initial earnings and earnings growth than their salaried counterparts. Holtz-Eakin *et al.* (2000) show that self-employment leads to an increase in the earnings distribution for low-income individuals but a decrease for high-income ones. Fairlie (2004, 2005) finds that self-employed, less-educated young men and women experience faster earnings growth on average than their counterparts in salaried or paid employment, and that young self-employed black and Hispanic men have greater earnings over time than their salaried counterparts after a few initial years of lower earnings.

Exploring the role of entrepreneurship in social mobility, Quadrini (1999) characterizes the different accumulation behavior of agents across the wealth distribution, using data from the U.S. Panel Study of Income Dynamics and the Survey of Consumer Finances. He finds that the existence of borrowing constraints has the effect of concentrating the occurrence of entrepreneurship in the upper-income groups. He concludes that, while entrepreneurship enhances upward social mobility across all classes, the presence of borrowing constraints and the higher cost of external financing make undertaking entrepreneurial activity less likely for those households located in the lower portion of the wealth distribution. Because undertaking entrepreneurial activity increases a household's probability of moving to a higher wealth class, those households with lower levels of wealth—due to financial constraints and/or to the higher cost of external finance—have fewer opportunities to move up the wealth ladder.

Entrepreneurship, narrowly defined as the creation of new firms, is considered a key factor in socioeconomic mobility. Robson and Davidsson (2004), in a theoretical study, argue that creation of new firms, innovation, and competition are the three major channels through which entrepreneurship can contribute to economic development by changing wealth distribution patterns. Similarly, Spencer, Saemundsson, and Kirchhorr (2005) suggest that entrepreneurs may contribute to the democratization of wealth through the process of creative destruction. Amoros and Cristi (2010), in turn, show that new firms have a positive effect on human development, reducing poverty. Finally, Saini (2001) shows that entrepreneurship has a direct impact on poverty reduction.

Several studies have empirically explored the factors that apparently contribute to entrepreneurship. According to Hurst and Lusardi (2004), the propensity to become a business owner is a nonlinear function of wealth. The relationship between wealth and entry into entrepreneurship is essentially flat along most of the wealth scale. It is only at the top of the wealth distribution—after the 95th percentile—that a positive relationship can be found. Segmenting businesses into industries with high and low starting capital requirements, they find no evidence that wealth matters more for businesses requiring higher initial capital. When using inheritances as an instrument for wealth, they find that both past and future inheritances (rather than simply liquidity) predict current business entry.

Ardagna and Lusardi (2008) explore the role of individual characteristics as potential explanations of international differences in entrepreneurship in a cross-country setting using micro data. They distinguish between entrepreneurs driven by an interest to pursue a business opportunity (“opportunity entrepreneurs”) and what they call “remedial” or “necessity entrepreneurs,” whose businesses are merely a means of basic sustenance—as portrayed by Banerjee and Duflo (2008) in reference to middle-class entrepreneurs. They find that opportunity entrepreneurs are slightly younger and more likely to be male, to have higher education levels, and to have higher incomes. These results hold across country groups divided by income and geographic areas.

In a study of Argentina, Anchorena and Ronconi (2014) find that the probability of becoming an entrepreneur is substantially higher for individuals raised in families headed by entrepreneurs: more specifically, the probability is 15.8 percentage points higher if the parents were owners of a firm, while it is only between 1.5 and 6.3 percentage points higher if the parents were wealthy.

Recent evidence from several Latin American countries reveals that while only a very small proportion of the population can be regarded as entrepreneurs, entrepreneurship is a vehicle for increased social mobility. As shown in the case of Bolivia, the degree of social mobility hinges on the type of entrepreneur (Hernani-Limarino, Eid, and Villarroel, 2012). Employers, defined as those who hire labor, tend to experience higher mobility than self-employed workers (organized in cooperatives or working on their own) and waged workers (formal and informal). Employers are significantly more likely to move upward in terms of both labor income and overall income distribution and much more likely to enter the upper class relative to other types of self-employed workers or waged workers.

Using data from a survey on entrepreneurship in emerging economies, Kantis, Koenig, and Angelelli (2004) find that dynamic entrepreneurs in Latin America come from a narrower range of social classes primarily from the highly educated and middle classes than in the case of East Asia. Nearly half—48%—of the dynamic ventures in East Asia are founded by people from the lower and middle classes, while in Latin America only about one-quarter of entrepreneurs (28.6%) come from the lower and middle classes. This suggests that the contribution of entrepreneurship to social mobility and to wealth creation is lower in Latin America than in East Asia.

3. ENTREPRENEURSHIP IN LATIN AMERICA: DESCRIPTIVE STATISTICS

Measurements of entrepreneurship can be elusive. Across the papers in this special issue, entrepreneurs are defined as those individuals whose occupational category is “employers”: namely, those individuals who work independently and employ at least one additional person.² This definition excludes self-employed individuals working on their own, most of whom are necessity entrepreneurs (also called remedial entrepreneurs) rather than opportunity entrepreneurs. This differs from the way entrepreneurship is usually defined in studies that focus on founders of start-ups and young ventures, which includes individuals working on their own as entrepreneurs.

2. This definition also coincides with the OECD-Eurostat Manual on Business Demographics (OECD, 2007).

By our definition of entrepreneurship, between 3.5 and 9.9% of the Latin American working population are entrepreneurs, depending on the country (Table 1). The share of self-employment is substantially larger: between 20.6 and 45.8% of the working populations of countries in the region. The shares of entrepreneurs bear no resemblance to levels of economic or social development of the countries: Peru, followed by El Salvador and Mexico, has the largest share of entrepreneurs, and Colombia has the lowest, while Argentina and Uruguay, the most developed countries within the sample, have intermediate levels of entrepreneurship. In general terms, the composition of the population by occupational category is relatively stable over time.

Latin American entrepreneurs tend to be middle-aged males with secondary and often tertiary education. Middle-class entrepreneurship dominates the sample in part since this is the largest group in society. However, as a percentage of each social class, entrepreneurship tends to be more common among the upper class, followed by the middle and lower class (tables 2 and 3).

Concerning social origin, in general terms the middle class represents an important and increasing portion of entrepreneurs, especially in Argentina and Brazil, where it has comprised more than 60% of the entrepreneurial population in recent years. In Ecuador, El Salvador, and Peru, lower-class entrepreneurship is a more dominant phenomenon than in Argentina and Brazil. In the region as a whole, the proportion of middle-class entrepreneurs has tended to increase in recent years. However, the share of the middle class has also increased in other occupational categories as a consequence of the general expansion of the middle class in the region (ECLAC, 2010). In some countries, the middle class has increased more among employers and/or employees than among entrepreneurs. Nonetheless, the share of the middle class for entrepreneurs is higher than for employees and self-employees in all of the countries studied except in Peru, where both proportions are quite similar.

Entrepreneurs tend to be older than the rest of the population; they are predominantly male and better educated than non-entrepreneurs. Entrepreneurs have higher labor income than employed workers. Males predominate in all occupational categories, but this predominance is even greater among entrepreneurs. On average, women make up slightly more than 10% of the total entrepreneurial population. Participation by women is lowest in Argentina and Peru, while it is more important in Brazil, Ecuador, and El Salvador.

Table 1. Occupational category*(% of working population)*

Country	Entrepreneur	Self-employed	Employee	Source
Argentina	6.3	20.6	73.1	Kantis, Federico and Trajtenberg (2014)
Bolivia	5.3	38.5	56.2	Hernani-Limarino, Eid, and Villarroel (2012)
Brazil	6.3	22.1	70.8	Kantis, Federico, and Trajtenberg (2014)
Colombia	3.5	44.4	52.2	Mejía and Meléndez (2014)
Ecuador	7.1	45.8	47.1	Kantis, Federico, and Trajtenberg (2014)
El Salvador	9.6	33.9	59.2	Kantis, Federico, and Trajtenberg (2014)
Mexico	8.3	31.7	60.0	Vélez-Grajales and Vélez-Grajales (2014)
Peru	9.9	44.4	45.7	Kantis, Federico, and Trajtenberg (2014)
Uruguay	5.3	–	–	Bukstein and Gandelman (2014)

Source: Authors' compilation.

Table 2. Entrepreneurs and social origin*(% of social class)*

Country	Lower class	Middle class	Upper class	Source
Colombia	1.8	5.3	21.4	Mejía and Meléndez (2014)
Mexico	5.7	7.6	16.9	Vélez-Grajales and Vélez-Grajales (2014)
Uruguay	1.5	5.8	15.3	Bukstein and Gandelman (2014)

Source: Authors' compilation.

Table 3. Entrepreneurs: distribution by social origin*(% of all entrepreneurs)*

	Argentina	Brazil	Colombia	Ecuador	El Salvador	Peru
Lower class	23.3	19.8	34.4	42.3	51.6	62.0
Middle class	63.9	61.3	46.3	50.6	44.2	33.2
Upper class	12.8	18.9	19.3	7.0	4.2	4.8

Source: Authors' compilation based on Kantis, Federico, and Trajtenberg (2014) and Mejía and Meléndez (2014).
 Note: Social classes are defined according to the thresholds recently proposed by Ferreira *et al.* (2013). Lower class: daily per-capita income under US\$ 10 (PPP); middle class: US\$ 10 to US\$ 50 (PPP); upper class: more than US\$ 50 (PPP).

Lower-class and middle-class entrepreneurs are concentrated in businesses of 10 or fewer employees. Entrepreneurs and employed workers also differ by the sectors of activity in which they participate. While a majority of entrepreneurs in all social classes work in wholesale and retail trade activities, employees tend to work more in services.

4. FINDINGS ON MOBILITY

Following previous literature on the subject, mobility is defined by the authors of the papers in this issue as the lack of persistence of individuals' income with respect to their own past income (*intragenerational* mobility) or that of their parents (*intergenerational* mobility). If incomes are compared in absolute values (after adjusting for inflation), the results are measures of *absolute* mobility. If incomes are measured with respect to the *median* income of the country (or relevant group), the results are measures of *relative* mobility.

Whether mobility (either absolute or relative) is upward is a question that is ideally tackled with so-called panel data: longitudinal surveys that follow individuals or families over time. None of the studies in this issue uses panel data in the strict sense. Those on Colombia by Mejía and Meléndez, Ecuador by Ordeñana and Villa, and Uruguay by Bukstein and Gandelman rely on pseudo-panels constructed by the authors, which follow cohorts of individuals that share some characteristics (typically age, gender, and education), rather than specific individuals. Depending on the number and size of the cohorts, and the time during which they are followed, pseudo-panels may provide reliable estimations of absolute or relative intragenerational mobility, and may shed some light on whether the share of entrepreneurs in the cohorts is associated with higher or lower mobility (upward or downward mobility), depending on the estimation technique.

The study on Mexico by Vélez-Grajales and Vélez-Grajales, which focuses on intergenerational mobility, uses a special survey which—although it is a cross-section of individuals and not a longitudinal survey—inquires about the respondents and their parents and can therefore be used as a panel, with some caveats. One of the limitations is that income cannot be measured in a reliable way for both generations in this way. For this reason, the survey relies on data about the assets held by the respondents and their parents. The authors use this information to construct asset indexes, which are used as proxies of permanent income, to assess absolute mobility.

The study on Colombia and another study on Uruguay (Gandelman and Robano, 2014) assess another form of intergenerational mobility where entrepreneurship may make a difference: education. Gandelman and Robano analyze whether the children of entrepreneurs attain more years of education than the children of non-entrepreneurs. Mejía and Meléndez, in their study on Colombia, look at the issue from the opposite angle, which is whether entrepreneurs' education levels are less influenced by the level of education reached by their parents than is the case for non-entrepreneurs.

All the studies coincide in that entrepreneurship is associated with higher social mobility, whether within or across generations, and in the case of intragenerational mobility, whether it is absolute or relative. Evidence of higher intergenerational social mobility is revealed as well when looking at education rather than income or assets.

Table 4. Income (or asset) persistence coefficients for entrepreneurs and non-entrepreneurs

	Entrepreneurs	Non-entrepreneurs		
		Total	Self-employed	Employees
Colombia (Mejía and Meléndez)				
Intragenerational absolute income persistence				
	All	0.270	0.510	
Intragenerational relative income persistence				
	All	0.340	0.500	
Ecuador (Ordeñana and Villa)				
Intragenerational absolute income persistence				
	Male	0.524	0.774	
	Female	0.227	0.477	
Mexico (Vélez-Grajales and Vélez-Grajales)				
Intergenerational asset persistence				
	Born 1942-1964	0.552	0.602	0.511
	Born 1965-1981	0.720	0.676	0.590
Uruguay (Bukstein and Gandelman)				
Intragenerational absolute income persistence				
		0.934	0.917	0.893, 0.953 ^a
Source: Authors' compilation.				
a: The first number refers to self-employed with a fixed location, while the second refers to self-employed without a fixed location.				

A summary of the point estimates of income (or asset) persistence coefficients is provided in Table 4 (values closer to 1.0 imply lower mobility). Intragenerational persistence of entrepreneurs' absolute income is substantially higher in Uruguay (0.934) than in Colombia (0.27) and Ecuador (0.524 for males, 0.227 for females). Income persistence is lower among entrepreneurs than non-entrepreneurs, and the differences between both are statistically significant in all cases. However, in the case of Uruguay, self-employed workers with a fixed work location exhibit lower income persistence than entrepreneurs. Women face less income persistence than men whether or not they work in entrepreneurial jobs, as is shown by the case of Ecuador. The study on Colombia presents estimates of relative income persistence whose coefficients are substantially larger than absolute income persistence.

Surprisingly, in Mexico, for those born between 1965 and 1981, the intergenerational persistence of asset ownership with respect to their parents is higher among entrepreneurs (0.72) than among self-employed workers (0.676) or wage earners (0.590). However, for the generation born between 1942 and 1964, the persistence coefficient of the entrepreneurs was lower (0.552), and was below that of self-employed workers (0.602) and similar to that of waged workers (0.511). Although strict comparability of the two sets of coefficients may be limited by the nature of the data and the computation of the asset indexes, the results suggest that social mobility has declined in Mexico, and especially so for entrepreneurs.

That intragenerational social mobility among entrepreneurs is higher than among other workers is not surprising since entrepreneurship implies more risk taking and therefore higher income variability than other work options. Thus, a central question is whether that additional risk is compensated by higher incomes. Using propensity score matching to compare entrepreneurs with non-entrepreneurs, the study on Mexico reaches the conclusion that the earning premium for entrepreneurs is 12-22%. The premium differs markedly by socioeconomic origin. For entrepreneurs from the poorest quintile (in terms of their parents' asset ownership), the premium is 35-57%, while for those from the richest quintile, it is 27-32%, and for those from the middle quintiles, it is 5-14%. Since the estimation procedure allows the comparison of entrepreneurs with non-entrepreneurs of similar family background (in addition to other characteristics), it is less subject to the potential bias problem resulting from the omission of variables that are known to influence the probability of success of entrepreneurs, such as

early exposure to the values and decision practices associated with entrepreneurship (Kantis, Federico, and Trajtenberg, 2014; Anchorena and Ronconi, 2014), and access to social and professional networks (Ordeñana and Arteaga, 2014).

5. OTHER FINDINGS

Entrepreneurship does not occur randomly among individuals. Entrepreneurs are more often found in higher-income groups, as mentioned. In Colombia, entrepreneurship is more common among older, male, and more educated individuals. Entrepreneurs are more likely to have experienced intergenerational social mobility, as measured by years of education they attain in comparison to their parents. In Uruguay, the children of entrepreneurs attain more years of education than the children of non-entrepreneurs, irrespective of parents' education. Combining the two findings suggests that entrepreneurs are both the result and cause of higher social mobility. In Mexico, the probability of becoming an entrepreneur increases when the respondents' father was also an entrepreneur, suggesting that there is a strong role model effect. The father's occupation turns out to be a more important explanatory factor than initial wealth or education. As mentioned, a family-transmission effect of occupational *values* (to become an entrepreneur) seems to be operating.

Self-employment is often seen as an incipient form of entrepreneurship. However, the characteristics of self-employed workers and entrepreneurs are markedly different, and so are their responses to changes in opportunities. In Mexico, the father's occupation is the variable that most increases the probability of sons choosing the same occupation, which is also the case for the self-employed. But, in addition, having a father who belonged to the middle class or was an entrepreneur decreases the probability of being self-employed (but not the probability of becoming an employee). The probability of becoming self-employed instead of an entrepreneur falls with years of education attained and increases if the individual comes from an indigenous group or lives in a rural area. The study on Colombia confirms that self-employment is an occupational choice of individuals whose characteristics are significantly different from those of entrepreneurs, on average. Women are more likely to become self-employed than entrepreneurs. The number of years of schooling decreases the probability of being self-employed rather than being an entrepreneur, as does parents' maximum schooling

attainment. Finally, the study on Uruguay finds that income from self-employment is more stable than income from entrepreneurship, as entrepreneurs assume more risks. While entrepreneurship tends to flourish during periods of rapid economic growth and to shrink during recessions, self-employment without fixed location behaves counter-cyclically.

6. DISCUSSION

Taken together with previous empirical literature on the role of entrepreneurship in fostering social mobility, the findings reported in this issue indicate that entrepreneurial activity is a channel of social mobility both within and across generations. Although the income persistence coefficients do not indicate the direction of such mobility, the estimates of income differentials between entrepreneurs and non-entrepreneurs lend support to the hypothesis that upward mobility dominates.

Although the literature for the United States indicates that entrepreneurial activities open avenues of economic progress, especially to minority groups, the studies included in this issue do not shed much light on this issue. Women in entrepreneurial activities do seem to have lower income persistence than their male counterparts, but only the study on Ecuador finds a substantial effect.

From a public policy perspective, a central issue in the design of policies to promote social mobility and reduce inequality is whether to focus on policies that benefit specific socio-demographic groups or to facilitate mobility in general. Policies to promote entrepreneurial activities also face that dilemma. Mejía and Meléndez (2014), after considering the evidence for Colombia, take the position that instead of promoting entrepreneurship among middle- or low-income groups, public policies should aim to facilitate firm creation and growth and foster education and formation of productive capabilities among those groups. These and other arguments against policies to promote entrepreneurship are made forcefully by Shane (2009).

The studies in this issue point to the need to deepen our knowledge in several respects. Since entrepreneurship cuts across different fields, an interdisciplinary approach to the topic is required. Joint research among business experts, economists, psychologists, venture capitalists, talent specialists, and experts in the labor market and industrial relations could yield relevant insights.

Better ways of measuring entrepreneurship are necessary to improve our understanding of how entrepreneurial activities contribute to mobility. The use of proxies such as measures of ownership, self-employment, firm size, and business creation to gauge entrepreneurship demonstrates that the topic is still in an early phase from an empirical viewpoint.

The lack of longitudinal studies in Latin America that track the family and occupational history of individuals over long periods of time limits the study of entrepreneurship and its role in promoting intergenerational mobility. Although the studies in this issue deploy diverse empirical methods to overcome this limitation, they are still limited by the lack of panel data.

More research is needed in areas such as the values of the entrepreneur. The classic depiction of a frugal individual willing to postpone consumption and endure sacrifices to make his or her vision of a business a reality may remain valid, but the role of sophisticated capital markets and family inheritance changes the picture somewhat.

The theme of how to manage risk and embark on productive ventures in uncertain contexts remains a critical topic. More work is needed in understanding and measuring the intergenerational transmission of values at the family level, given the importance of parental and family roles in the propensity for entrepreneurship. It is also important to study the importance of role models outside the family in shaping entrepreneurship.

Finally, understanding the gender component of entrepreneurship is an emerging subject. Entrepreneurship is predominantly a male activity in Latin America. The importance of family factors, exclusion patterns, and low female labor participation rates in shaping the role of women in entrepreneurial activities and in social mobility is still poorly understood.

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