Public Policies and New Business in Brazil: Motivation and Innovation

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1 Introduction

Worldwide, inequality is rapidly decreasing as people are taking themselves out of poverty at unprecedented rates. Illustratively, the percentage of global citizens living in extreme poverty went from over 40% in 1980 to about 10% in 2015 (The World Bank, 2020). Technological progress happens at escalating speeds while software development is 'eating the world' (Andreessen, 2011), allowing many to get more access to the physical infrastructure. For entrepreneurs, the need for large upfront capital diminishes with increasing standards of living and the advent of the 'sharing economy' (Munger, 2018).

The research question is to verify if there is a relationship between public policies to improve entrepreneurship and behavioral aspects of entrepreneurs in Brazil, as it will be seen in the conclusion section. The article has been divided into two parts. In the first part, a review was made of the different views of entrepreneurship held by Joseph Schumpeter and Israel Kirzner. A literature review was also conducted on the layers of entrepreneurship and the influence that institutions have on entrepreneurial activity. In the second part, the empirical test was carried out, using data available from GEM, and the Pearson Correlation Analysis method was used. It was found a correlation between public policies directed to entrepreneurship (support, taxes and

bureaucracy, stimulus programs) with entrepreneurial activity, the motivation to undertake and the rate of innovation of new enterprises. This result can be useful for theoretical and practical reasons, which means that it opens up possibilities for more research analysis about entrepreneurship and institutional variables and allows entrepreneurs to understand and handle challenges that affect their everyday situations.

2 Literature Review

Economic Causes of the Entrepreneurial Blind Spots

Entrepreneurial action can be the Schumpeterian "creative destruction" type (Schumpeter, 1983), the disruptive innovations that shape or create new markets, or Kirznerian "arbitrage" (Kirzner, 1973, 1979) type, that spreads ideas/innovations and thus tend to equalize their effect across markets and segments. Historically, Kirznerian entrepreneurship dominated markets, while the Schumpeterian type was comparatively rare. This usual feature facilitates the diffusion of innovation and growth but lacks the capacity to disrupt the normal way of doing things and create large growthfast. In the modern economy, however, in many cases the problem is opposite —entrepreneurialdisruption tends to outpace equilibration (Lachmann, 1986).

The Layers of Entrepreneurship

Entrepreneurship occurs and will primarily affect markets and resource allocations on at least two *layers*: the *upper layer*, comprising the early adopter market in which innovation is first introduced, and *lower layer*, comprising the laggard market, in which innovation becomes widespread and reaches the larger part of the population. That reality is more complex, however, and the boundaries between layers are blurry, so, there could be an enormous number of observables, interdependent, "layers" with different actors and dynamic allocation of actors

across time. Among others, the relevance of the geographic areas, for example, different layers can occur on the global level, in the supranational one, nationally, regionally, and locally.

The basic argument is premised upon the relationship between Schumpeterian and Kirznerian entrepreneurship as discussed in Packard and Bylund (2018): the former are innovations that successfully offer consumers the possibility of enjoying completely new value and, therefore, leave producers acting within the status quo comparatively inefficient; the latter consists primarily of the imitation of pre-existing solutions that followers engage in as the disruption is already apparent, which includes both protection of one's previous competitive ability within a market and the introduction of a novel innovation to new markets (thereby causing equalization between those markets). This second part spreads the benefits of the new value facilitation over a much greater part of the market. The same concept is seen in strategic management with different labels. The entrepreneurs or organizations that look for the introduction of solutions capable of allowing the consumers to access new value are consideredas adopting an explorative approach, while the exploitative approach reproduces what has already been proved successful (Almahendra & Ambos, 2015; March, 1991; Sinha, 2015).

These definitions imply an interdependence between layers, as Kirznerian entrepreneurship can be the simple act of following a first mover to maintain competitiveness and market share, but can also imply the diffusion of innovations through their introduction into new market segments. From within the upper layer, this latter type is a matter of Kirznerian diffusion or imitation whereas, from the viewpoint of the lower layer or the market to which the innovation is introduced, this Kirznerian imitation appears to be Schumpeterian market disruption. What disrupts and disequilibrates from the perspective of the lower-layer market at the same time *equilibrates* from the viewpoint of the upper-layer market. When Schumpeterian

entrepreneurship dominates an economy, then the upper layer is serviced while the lower layer is neglected. Because of the low payoff relative to the high uncertainty, Kirznerian entrepreneurship becomes uninteresting for the actors in a setting like that.

The Effects of Imbalance between Schumpeterian and Kirznerian Entrepreneurship

An imbalance between the rates of Schumpeterian and Kirznerian entrepreneurship would tend to retard or even *bypass* lower-layer economic growth for several reasons. Including: (1) differences in the temporal requirements between Kirznerian equilibration and Schumpeterian disequilibrium; (2) higher consumer uncertainty for low-wealth consumers in the face of high levels of market disruptions; and (3) higher uncertainty for Kirznerian entrepreneurscreated by the constant wave of Schumpeterian entrepreneurs and innovations.

First, the price reduction process of Kirznerian entrepreneurship whereby new technologies become accessible to the masses is expected to be time-consuming, production processes take time, even if they are imitative. As technologies become both increasingly more frequent and more disruptive (more distant from the current standards), the rate of disequilibrium may outpace the rate of innovation diffusion and equilibration (Lachmann, 1986). As a result, a tentative diffusion may not even be started or abandoned prematurely as new technologies, superior to the still-diffusing solutions, emerge and may become the new target for Kirznerian entrepreneurs. This can leave the lower-layer economy—the comparatively poor and inaccessible—unreached for extended periods of time.

Second, consumers face uncertainty regarding the value of new innovations (Bee & Madrigal, 2013; Castaño, Sujan, Kacker, & Sujan, 2008; Kalish, 1985). This "uncertainty chasm" (Packard, 2016) slows the adoption of innovations and, therefore, their diffusion, and

causes many new products not to reach a critical mass to break even or become successful. The imbalance of Schumpeterian and Kirznerian entrepreneurship, and the previously noted effects of temporal differences in the two processes, exacerbates this consumer uncertainty within the lower-layer economy. This is because by the time that diffusion reaches, or might have reached the lower layer, a new Schumpeterian upper layer innovation may have already arrived, or may be forthcoming, such that lower layer consumer investment in the solution (coming from often limited funds) is unwarranted where the prospect of some better solution soon arriving and the opportunity cost of purchase are high.

Third, comparatively high rates of disequilibrating entrepreneurship create uncertainty for equilibrating entrepreneurs, who might find themselves in the process of diffusing a new technology only to face a new disruption, creating sunk cost on the previously made investments. As a result, Kirznerian equilibration entrepreneurship is retarded, exacerbating the problems of the previous two sources. The process of lower layer diffusion is further delayed (or avoided altogether) as a result of the uncertainty, and consumers are even more hesitant to purchase under such conditions, causing (would be) Kirznerian entrepreneurs to delay or avoid their tentative diffusion even more.

The result is a vicious cycle that retards Kirznerian equilibration into the lower layer while pushing entrepreneurs more and more toward pursuing upper-layer Schumpeterian entrepreneurship, where, in spite of the higher uncertainty, the payoff for success is much higher, thereby widening the imbalance.

Political Causes of Entrepreneurial Blind Spots

The vicious economic cycles would, left alone, create new entrepreneurial opportunities

for Kirznerian arbitrageurs to correct the imbalance and profit by better diffusing recently obsoleted upper-level technologies at reduced cost to the lower layer economy. In that situation, one would expect the inefficiency to self-correct through entrepreneurial alertness seen in exploitative strategies. It does not happen as much as it, perhaps, means either that something does not sound with the theory, or else, more likely, that there are other, unnatural to the market process, features causing these entrepreneurial blind spots to persist.

Regulation and Entrepreneurship

Entrepreneurial activity always takes place within a specific regulatory and institutional setting — the rules of the game (North, 1990) — and that this setting usually differs across markets and geographical locations. As institutions also are scaffolded and occur on different levels, their misalignment may cause institutional uncertainty for entrepreneurs and thereby subject their actions to additional costs (Bylund & McCaffrey, 2017), to the point that they may even seek extra-institutional actions by evading or seeking to alter institutions (Oliver, 1991).

The literature on political/institutional entrepreneurship deals with this fact. (Boettke & Coyne, 2007; Dau & Cuervo-Cazurra, 2014; Sine & David, 2010).

High regulatory burdens on entrepreneurship tend to impact the lower layer far more than they do the upper layer, those burdens will be much more difficult to respond to by the exploitative entrepreneurs that have to obey the rules already in place, while explorative entrepreneurs often act in an environment that has not yet been institutionalized in legislation.

This is because the costs of adhering to regulations either must be passed on to consumers or else absorbed within the profit margin, in both cases it reduces the exploitative entrepreneurs' possibilities to compete because passing costs on to price when trying to attract price sensitive

consumers tends to have a large negative impact on sales, limiting profitability, product diffusion and, of course, entrepreneurial attractiveness. The alternative, eating the cost of compliance within the margins has a similar effect, limiting the attractiveness of Kirznerian entry where margins are comparatively thin. Moreover, regulations such as licensing and registration rules, erect entry barriers that protect upper layer incumbents from lower layer entrants (Carpenter II, Knepper, Erickson, & Ross, 2012), which have two exacerbating effects: (1) it inhibits lower layer consumers from the productivity gains that might allow them to escape into the upper layer, and (2) it artificially curtails the Kirznerian entrepreneurship that such entrants would provide.

As Packard and Bylund (2018) explain, in the absence of the Kirznerian entrepreneur, the possibilities for the emergence of the Schumpeterian type will be reduced, individuals will have harder times accumulating wealth that will allow them to escalate in the direction of the upper layer in which the explorative entrepreneurs act. As far as the regulations make it harder for entrepreneurs to act, they reduce the incentives and the possibilities of action, initially for the equilibrating entrepreneurs and, as time passes, and for the aforementioned reasons, for the disequilibrating ones as well.

Local regulation influences entrepreneurship

The theoretical framework recognizes that, to an important extent, the environment will influence the amount and type of entrepreneurship that happens in a given location. In particular, the formal regulations, the local laws, will undermine or potentiate entrepreneurial action.

As Baumol (1990) suggested, the proportion of entrepreneurs in a given society is relatively stable. More specifically, the two aforementioned sets of predictors will, to a fair part, determine if there will be entrepreneurship in that location and, in case there will be, if it will be of

the explorative or the exploitative kind.

Research on the impact of institutional setting on entrepreneurship is not new. Reports such as the "The Heritage Foundation's Index of Economic Freedom" (Miller, Kim, & Roberts, 2020) consider institutional factors as antecedents to liberty and consequent freedom of enterprise and entrepreneurship. International studies on the topic such as the Global Entrepreneurship Monitor (GEM), also consider the importance of the institutional environment, in the specific case of local institutions they say:

> any decision to start and run a new venture will be taken in a specific context, encompassing a wide range of local and national conditions that may facilitate or hinder that new venture. […] a city or region […] may discourage that same [entrepreneurial] activity by having exorbitant business registration fees or a heavy burden of local regulation and bureaucracy […] there is likely to be a positive relationship between the quality of entrepreneurship- specific conditions and the frequency and nature of entrepreneurial activity (Bosma et al., 2020, p. 68).

Relationship between public policies and entrepreneurship

Economic growth is considered as an important objective for national governments. It is considered that higher economic growth reduces unemployment and increases social welfare of the community (Da Silva e Silva 2019). Public policy is recognized as a fundamental instrument that the governments around the world uses to improve the entrepreneurship behavior and economic prosperity of the countries (Halabí & Lussier, 2014). In this sense, policies on economy, taxation, education, legislation, industry, employment, technology and government subsidies may have a marked influence on the processes and outcomes of new and established businesses (Zerbinati and Souitaris 2005; Michael and Pierce 2009). Murdock, 2012 performed an empirical analysis that has been carrying out for the case of 19 European Union member countries using OLS regression. The results show that business regulation has a negative impact

on entrepreneurship activity and the location of the policy has not a significant impact.

To Aldrich & Cliff (2003), opportunity is a fundamental aspect to entrepreneurship.

Research shows that people are motivated by opportunity or necessity. In the same way, some trials and case studies show that sometimes the reasons are beyond these causes and may be related with both reasons together (WILLIAMS et al., 2009; WILLIAMS; ROUND, 2009).

According to Da Silva e Silva (2019) the motivation of new entrepreneurship (TEA) shows that the proportion or necessity entrepreneurship reduced 9% between 2015 and 2016 suggesting an increase in entrepreneurship motivated by opportunity. Furthermore, Barboza et al (2017) concluded the network of public policy agents can contribute strongly to the breaking down of barriers and resistance to the generation or incorporation of innovations by micro and small companies - both traditional and technological.

3 Methodology

After reviewing how public policies can positively or negatively affect entrepreneurial action on a given locality, it was proposed to conduct a correlation analysis taking into account the variables that stimulate individuals to become entrepreneurs. The division was made between individuals who initiate entrepreneurship due to an intrinsic motivation, and individuals who initiate entrepreneurship because of the need to obtain a brief financial return. Data was collected from the GEM database from 2002 to 2016. The Global Entrepreneurship Monitor (GEM) research program happens worldwide and evaluates the yearly entrepreneurship activity national level. GEM started in 1999, with 10 countries in a partnership between London Business School (England) and Babson College (USA). The program is growing year by year and has more than 80 countries now.

The behavior variables were collected from the Adult Population Survey (APS) and the sample was between 1.997 and 10.000 respondents according to the year. The focus is not only on business characteristics, but also on people's motivation for starting a business, the actions taken to start and run a business, as well as entrepreneurship related attitudes. Government variables were collected from the National Expert Survey (NES). NES consists of carefully chosen experts who are asked to respond to a series of statements on a Likert scale, rating them from completely false to completely true. In our research, the number of experts was between 35 and 105.

Variables

Table 1 - Behavioral variables chosen

Behavioral variables of entrepreneurship	
TEA	Total early-stage Entrepreneurial Activity Rate: Percentage of 18-64 population who are either a nascent entrepreneur or owner-manager of a new business;
Motivational Index	Opportunity: Percentage of those involved in TEA that are improvement-driven opportunity motivated; Necessity: Percentage of those involved in TEA that areimprovement-driven necessity motivated;
Innovation Rate	Percentage of those involved in TEA who indicate that their product or service is new to at least some customers AND that few/no businesses offer the same product.[1]

Note: by authors.

[1] It was considered for de variable the sum of TEAnewpr (% within TEA: product is new to all or some customers) and TEAnewmk (% within TEA: new market (few/no businesses offer the same product).

Table 2 - Government policies

Government Policies	
Governmental Support and Relevance	The extent to which public policies support entrepreneurship - entrepreneurship as a relevant economic issue;
Government Taxes and Bureaucracy	The extent to which public policies support entrepreneurship - taxes or regulations are either size-neutral or encourage new and SMEs;
Government Entrepreneurship Programs	The presence and quality of programs directly assisting SMEs at all levels of government (national, regional, municipal).

Note: by authors.

Statistical analysis

It was used Pearson Correlation Analysis performed with the *R* software package Hmisc - HarrellMiscellaneous (Harrell, 2019), to calculate Pearson's coefficient (*r*) and the asymptotic P-values (*p*) (Hollander; Wolfe, 2013). Before analysis data were tested by Shapiro-Wilk Normality Test for normality distribution. Variables TEA, opportunity and innovation have non normal distribution, and because of this a logarithm analysis was used. Pearson's correlation coefficient could have significant advantages for continuous non-normal data which does not have obvious outliers. The shape of the distribution should not be a sole reason for not using the Pearson product moment correlation coefficient (Chok, 2010).

Table 3 - Achieved results

Results	References
- There is a positive relationship between entrepreneurial activity and public support policies, fees and bureaucracy and public support programs;	Murdock, 2012 Lecuna, Cohen & Mandakovic, 2020
- The growth of entrepreneurial activity was more supported by the motivation of opportunity for most of the period, except in the end, between 2015 and 2016;	Da Silva e Silva (2019)
- There is a relationship between the innovation rate of entrepreneurial activity and public support policies and public support programs.	Barboza et al (2017)

Note: by authors.

Table 4 - Descriptive statistics and correlation analysis between variables

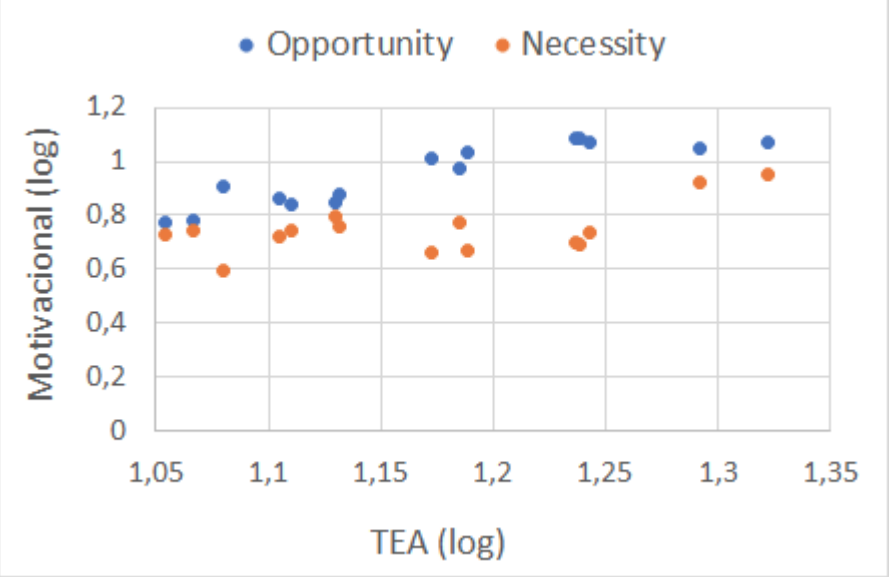
Variable	**Mean**	**SD**	**n**	**1**	**2**	**3**	**4**	**5**	**6**
1. TEA	15.06	2.94	15						
2. Opportunity	9.23	2.37	15	0.89****					
3. Necessity	5.70	1.33	15	0.63*	0.22				
4. Gov. Support	2.28	0.56	15	0.88****	0.66**	0.79***			

Variable	**Mean**	**SD**	**n**	**1**	**2**	**3**	**4**	**5**	**6**
5. Gov. Taxes	1.57	0.28	15	0.80***	0.59*	0.74**	0.96****		
6. Gov. Programs	2.42	0.43	15	0.75**	0.49	0.79***	0.92****	0.94****	
7. Innovation	55	13.02	7	0.79*	0.19	0.84*	0.76*	0.64	0.80*

Significance level: p < .0001 = ****. p < .001 = ***. p < .01 = **. p < .05 = *; n = 15 (2002-2016); Innovationsample only available from 2010 to 2016.

Note: by authors.

Picture 1 - Scatterplots between TEA and motivational variables



Note: by authors.

Results from de data analysis

The correlations of governmental policies and entrepreneurship activity are presented

in Tables 3, 4 and 5 and in Picture 1. Statistical analysis shows that the relationship between the rate of innovation of the entrepreneurial activity and governmental support ($r=0,76$; $p<0.05$) andpublic support programs ($r=0,80$; $p<0.05$). Furthermore, the innovation rate of the entrepreneurial activity is strongly related to TEA, especially for entrepreneurship motivated bynecessity (Picture 1).

TEA is more correlated with opportunity ($r=0,89$; $p<0.0001$) than necessity ($r=0,63$; $p<0.05$) in the entire period but there is no correlation between both entrepreneurship motivations($r=0,22$). Although, TEA is influenced by governmental support ($r=0,88$; $p<0.0001$), taxes ($r=0,80$;$p<0.001$) and programs ($r=0,75$; $p<0.01$).

4 Discussion

The entrepreneurial activity is affected by governmental policies such as public support programs and bureaucracy. In Brazil, the motivation for starting a new business by opportunity isincreasing constantly. There is an exception for years 2015 and 2016 that could be explained by internal governmental crises. Furthermore, innovation rate is related to both motivations, opportunity and necessity. The differences in the type of entrepreneurship are as having both economic (endogenous, within-economy) causes, through the absence or lack of structural balance between types of entrepreneurship, and political causes. The research thus offers scholars and policy makers insights into how it would be possible to begin to solve some of the challenges of reasons why people become entrepreneurs and leaves as a future research agenda studies which could help entrepreneurs to identify scenarios and external variables on its country/region that could potentially help them to strive. The weaknesses of the work are that, for a larger volume of data and for more robust inferences, a more elaborate statistical method is required, such as multiple regression or panel data analysis

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