

Education, not funding, key to success of microenterprises

In countries with high unemployment rates, spending public money on learning rather than supporting entrepreneurs may be best for long-term impact.

October 6, 2014

What best predicts whether a very small business will thrive or not?

Here's a hint: public funding does not seem to be the answer. At least not in Argentina. There, an entrepreneur's level of education and dedication tended to be better predictors of business success, even as public funding flowed.

[Pascual Berrone](#) of IESE and co-authors from the National University of Cordoba in Argentina studied 300 microenterprises with five or fewer employees. They set out to identify the determinants of performance, and found some surprising results.

Published in the [Journal of Small Business Management](#), the preliminary evidence from this study suggests that education, drive, commitment and the application of innovations are the factors that best predict business success.

In contrast, when an entrepreneur starts a business because he or she has no other job, the chances of that business succeeding tended to be lower than when an entrepreneur starts a business because he or she sees a product opportunity or a market niche to fill.

Microenterprises with macro importance

Microenterprises can be important players in a country's economic growth and development. In Latin America, more than 80 percent of businesses are microenterprises, and they are

often recipients of public money to spur growth and reduce unemployment. In fact, many believe that "all you need is funding" to make a go of a small enterprise.

However, using public money to finance microenterprises as a means to reduce unemployment and alleviate poverty may just be a short-term solution. Berrone and co-authors write: "Public funds may be better invested in aspects that have proved to be beneficial for the success of microbusinesses, such as education or innovation, in order to provide sustainable prosperity."

Predictors of success

Based on their surveys of a sample of 300 microenterprises in Cordoba, Argentina, the authors identified a number of factors as important to a small company's performance.

- The level of formal education of the entrepreneur
- The level of dedication to the enterprise, which was determined by the number of hours invested in the venture
- The use of the entrepreneur's own capital
- The application of innovations, resulting in improvements to the value chain and differentiation from the competition
- A voluntary decision to start the enterprise, perhaps motivated by a perceived niche in the market. (In contrast, ventures motivated by unemployment did not perform as well.)

There were other factors that the authors did not find to be significant.

- The gender of the entrepreneur
- Family participation in the venture
- Whether or not the business operated formally or informally

Potential to alleviate poverty

In Argentina, an unstable economy with a high unemployment rate, financing microenterprises is seen as a means of poverty alleviation. But that thinking may be too short-term.

The study indicates that involuntary entrepreneurs, motivated by unemployment, underperform those motivated by a wish to improve their circumstances or reach a new niche in the market (voluntary entrepreneurs). If the aim of financing microenterprises is to

spur economic growth, financing "involuntary" entrepreneurs may not be the way to go. They may be better served by an unemployment subsidy.

Meanwhile, the positive relationship between formal education and business performance suggests that policymakers with the long view in mind might look to education and training as investments in the future.

www.iese.edu/insight