



WORKSHOP REPORT

Introduction

This workshop was aimed at officials of the European Commission and was stimulated by presentations from three European Employment Observatory experts:

- Ari Hyytinen, EEO Thematic Expert, University of Jyväskylä, Finland;
- Udo Brixy, EEO Thematic Expert, Institute for Employment Research (IAB), Germany; and
- Lubos Vagac, EEO SYSDM Thematic Expert Slovakia, Centre for Economic Development.

The workshop was chaired by Frédéric Lagneaux, Unit D/1, DG EMPL and by Roger Sumpton, EEO Core Team, GHK Consulting.

The workshop aimed to reflect upon three main aspects to self-employment within the EU labour market:

- The extent to which self-employment can be regarded as a valid alternative for paid employment (and exit from unemployment);
- Successful practices for the promotion and take-up of *–sustainable–* self-employment (and the monitoring of such practices);
- Assessment and improvement of the quality of self-employment.

The presentations gave, in turn, an overview of movement into and out of self-employment (Ari Hyytinen), a reflection on start-ups and self-employment in Germany (Udo Brixy) and the position of self-employment in the labour market, and more generally the economy, in Slovakia (Lubos Vagac).

The background

Self-employment plays a very significant part in the EU labour market, as elsewhere in the global economy. Both self-employment, and entrepreneurship in general, have a particular role in business creation; as such, they are key to the success of the EU 2020 Strategy. Micro-firms (of less than 10 people) account for 95% of newly-created firms and, in total, account for 30% of total employment in the EU.

In 2009, 32.5 million people in the EU were self-employed, accounting for 15% of total employment. There are concentrations of self-employment in the services sector and in agriculture (explaining the relatively high levels of self-employment in southern European countries and in Poland). Whilst self-employment in itself accounts for a much smaller proportion of total employment than dependent employment (accounting for over 80% of total employment), self-employment generates a significant number of dependent jobs given that almost a third of the self-employed employ other workers.

Between 2004 and 2007, self-employment grew by about 1.3 million; this was in the context of a relatively favourable business environment and facilitated by the expansion of more readily accessible communication technologies. However, self-employment took a declining share of total employment,



as shown by the self-employment rate (the percentage of self-employment in total employment) which fell from 16 % to 15 % from 2000 to 2009. This is a reflection of the steady and high growth in dependent employment over the same period.

These overall trends mask some interesting differences between Member States. In reality, most Member States have seen a fall in self-employment rates since 2000. Those that have seen growth in the rate are Austria, Czech Republic, Denmark, Malta, Slovakia, The Netherlands and the UK.

In looking to the future, and as the economy emerges from recession and from the economic crisis, it is clear that self-employment will continue to play a significant role. Indeed, self-employment is set to continue as a policy priority. It is supported in the European Employment Recovery Plan through the micro-finance facility and with flexibility on state aid for micro-companies. The EU 2020 Strategy presents entrepreneurship as a key element in achieving smart, sustainable and inclusive growth and, under the Inclusive Growth Pillar, it aims to encourage Member States remove measures that discourage self-employment.

Workshop presentations

The workshop presentations can be found at:

<http://www.eu-employment-observatory.net/en/documents/Meetings-Workshops.aspx?year=2010>

1) *Selection into and out of self-employment (Ari Hyytinen)*

This presentation firstly reviewed the distinction between self-employment and entrepreneurship. Many people who become self-employed are not entrepreneurs aiming systematically to grow and develop their firms. Amongst any given cohort of new firms, a minority survives and could be classified as a high growth entrepreneurial firm (HGEF). In general, businesses which are able to develop their productivity survive and become HGEFs; other less productive firms, cease trading. All of this points to several issues:

- Why do people enter and exit self-employment and entrepreneurship? There are both 'push' and 'pull' factors, as well as monetary and non-monetary motivations. Two types of human capital can be identified – that which is useful to all enterprises and that which is useful in specific firms only.

Evidence on the outcomes (wage and non-wage) for people returning to the labour market after a spell of self-employment was analysed for a sample of over 25,000 individuals covering the EU15 (minus Sweden), between 1996 and 2001. In terms of wage outcomes, there is some evidence for negative selection into self-employment (given that the initial wages of those entering self-employment is lower). For more highly educated males, the self-employment spells appear to be unemployment 'in disguise' (e.g. looking for a new job whilst self-employed). In relation to non-wage outcomes, it appears that attachment to the labour market is weaker after the spell of self-employment and there is some evidence that financial circumstances are worse after re-entry to employment.

- What determines the duration of a self-employment spell? A large proportion of self-employment spells are very short, with many of the self-employed returning to the labour market as employees. Does this mean that there is excessive entrepreneurial churn, e.g. in comparison with worker flows and excess churn?



There is an emerging consensus in the literature that entrepreneurs are overly optimistic. They appear to underestimate the probability of failure and are more likely to run ventures that 'more rational' individuals would not undertake. These points have been reinforced both by indirect and direct empirical evidence. Further analysis shows, however, that entrepreneurs are not all overly optimistic; they are a heterogeneous group. In general, it seems that those who think they will not fail are, on average, less likely to fail.

There are several policy implications associated with the above research and conclusions. It cannot, on the basis of the evidence, be argued that European entrepreneurship or self-employment is constrained by the prospect of having to face a hostile labour market after a spell of self-employment. Given that there is evidence of negative self-selection into self-employment, it would be valuable to see the development of policies aimed at encouraging positive selection; this, it could be argued, would have positive implications for market experimentation and productivity. Also, it may be that entrepreneurial over-optimism partially accounts for the excessive churn in entrepreneurship and in self-employment.

Finally, in relation to the quality of self-employment, it appears to be more satisfying to be self-employed, given the relative independence from bureaucracy and organisational routines. Interestingly, the evidence does not suggest that the greater levels of satisfaction derive from greater autonomy in use of time; indeed, self-employed people tend to work longer days, have less leisure time, and are less frequently absent from work.

2) Start-ups in Germany: sufficient or too few? (Udo Brix)

This presentation reviewed the extent of entrepreneurial activity in Germany and examined the significance of entrepreneurs out of unemployment, in order to draw conclusions about policies aimed at supporting unemployed people to move into self-employment.

There are substantial differences in the self-employment rate between European countries. Italy has a very high rate, much higher than that in Germany, which is amongst the five countries showing the lowest self-employment rate in 2009. However, examination of 'total early-stage entrepreneurial activity' (TEA) reveals a different picture, for example, that the current entrepreneurial attitude itself is very similar in Germany and in Italy.

By considering the motives for entering self-employment, nascent entrepreneurs can be classified as either 'opportunity entrepreneurs' or 'necessity entrepreneurs'. The former are motivated into self-employment by 'pull' factors, whereas the latter are mostly influenced by 'push' factors (e.g., entering self-employment whilst searching for alternative dependent employment). It is arguable that opportunity entrepreneurs are those who are most likely to be motivated to make a success of their ventures, to grow their business and maximise profits.

In Germany, policies to promote start-ups and self-employment for unemployed people have been widely used:

- For 20 years, Bridging Allowances were the single instrument used to promote start-ups.
- In 2003, through the Hartz Reforms, an additional measure was introduced, aimed especially at small start-ups by lower qualified people – the 'Me Inc.' ('Ich-AG') programme.



- In 2006, the programmes were integrated into a single measure – the Start-Up Subsidy (Gründungszuschuss).

Evaluation of the programmes revealed that they worked well for less qualified people; the self-employed who received support had higher incomes (than those in a matched control sample) and were less likely to be unemployed after four years.

However, further analysis of the impact of the programmes by regions reveals a more complicated picture. In particular, the evidence shows that there is a greater number of subsidised start-ups in areas where labour markets are strong. Conversely, in areas with a weaker labour market (e.g. in the north east of Germany), there is much lower take-up of subsidies.

In considering the policy implications of the evaluation of these programmes, it is important to distinguish between social policy goals – aiming to achieve social inclusion - and economic policy goals – focussing more on macro-economic effects. The latter may lead to an emphasis on reducing unemployment, without a full consideration of the social policy implications, e.g. support to become a self-employed entrepreneur will not be appropriate for all unemployed individuals.

Furthermore, as demonstrated clearly in the case of Germany, regional differences need to be taken into account; the same active labour market policy will not have the same effects in all regions.

3) Self-employment in Slovakia: a country perspective (Lubos Vagac)

This presentation reviewed the trends of self-employment in Slovakia, the impact of labour and other policies upon self-employment and discussed the challenges in terms of quality of self-employment.

In 2000, self-employment in Slovakia was amongst the lowest in Europe. However, there has been a very large increase in self-employment since 2000; the rate almost doubled from 2000 to 2009 (from 8 % to 15.7 %). The profile of self-employment currently is mostly male (72 %), aged between 30 and 39 (29 %), conducting business in trade (28 %) or construction (18 %), and with full secondary education. There are many instances of self-employment as a secondary job (in addition to dependent work and/or a main self-employment role, or pension, or study). In addition, there is evidence of undeclared self-employment.

There are several factors which have contributed to the extensive growth in self-employment in Slovakia in recent years.

- The initial situation means that self-employment started from a very low base. However, there was a tradition of entrepreneurship which facilitated the trends in self-employment, coupled with the structure of the economy (a prominent state sector with under-developed service sector provision provided opportunities for self-employment).
- Structural reforms between 2003 and 2005 affected the tax and pension regimes, giving a boost to the economy and to new jobs. There were also increased incentives to work and to declare work, alongside simplified conditions for conducting business.
- Labour legislation has seen frequent changes in this period; in particular, revision of the Labour Code in 2007 increased employee protection, with a decrease in recruitment and an associated shift of workers to self-employment.



- There have been substantial changes to the tax and social security regime. These have included a 2 % lump-sum income tax (in 2001 – 2003) for small entrepreneurs and 40-60 % lump-sum tax deductible expenses (since 2004). These changes mean that the self-employed pay much lower taxes and social security contributions than employees. This has been a key driver in stimulating the increase in self-employment.

In addition to the above, there have been active labour market policy developments which have contributed to the increase in self-employment. From 2004, policies to support self-employment start-ups were introduced. These were successful in supporting exit from unemployment and job creation; data show that more than half of new self-employment jobs, since 2004, have been supported by start-up incentives.

The government's employment recovery package, as a response to the economic crisis, included two temporary measures to support self-employment (from March 2009). However, these have failed to attract any interest, perhaps an indication of the strong impact of the existing self-employment support measures.

Other measures introduced recently have also had an impact on the operating context for the self-employed. For example, administrative burdens on business have been reduced (e.g. one-stop shops for entrepreneurs), with reduced periods for VAT reclaims, and simplified tax records.

In terms of the quality of self-employment, small businesses continue to be concerned about the burden of the social security system and its complexity. Improvements in quality of self-employment could be achieved by stabilising business-related legislation, further reducing administrative and financial burdens and by promoting a fair and clear social security regime for all types of employment. The sustainability of self-employed businesses could be enhanced through several measures, such as: improving law enforcement and speeding-up resolution of disputes; combining start-up support and training programmes; involve small businesses in future skill needs identification; and support entrepreneurship education.

Workshop discussions

This section provides a brief summary of the discussion which followed the keynote presentations.

Cost-effectiveness of start-up incentives

Although it does not clearly appear in all countries, some, such as Germany, post a high correlation between the amounts invested in these labour market policies (expressed as percentage of GDP) and the self-employment rate recorded in the following year. But it is harder to ascertain whether this eventually has a positive impact on total employment figures...

'Crowding-out' and competition

In some sectors, there are concerns that schemes, like Me Inc in Germany, are a form of unfair competition, moving dependent employment into self-employment. Whilst there may be a cost to such policies, it is arguable that the main competition is likely to be between the newest start-ups, and that such competition could result in more sustainable firms in a stronger sector.



Productivity effects

Another dimension to the 'crowding-out' effect, is that public support for self-employment may have a negative impact upon productivity dynamics. In particular, subsidised firms may stay in the market longer than they would have done without support; they then compete, for longer, for resources that more efficient and productive firms would otherwise use. The net result is that there are more inefficient firms in the market, affecting overall sector productivity in a negative way.

Productivity may also be undermined in a more general sense by supporting 'lower quality' entrants (newly self-employed people) into the market. However, the examples of support for self-employment – from Germany and from Slovakia – include a requirement for approved business plans. Nevertheless, there is an implicit assumption that private start-up finance will not be available for many start-ups, thus requiring public support as an alternative. Questions remain as to whether the same qualifying conditions are applied to start-ups supported by public and by private funds.

With regard to the *quality of self-employment*, it is clear that there is a relative lack of evidence. In part this is because of the absence of generally agreed measures of the quality¹.

Financial markets' failures and public financing of start-ups

It is assumed, in line with a common understanding in state aid literature, that financial markets are often affected by "failures" (e.g. informational problems, externalities, etc.) vis-à-vis small undertakings, which are indeed less financed than they would / should be in a more optimal market. Therefore public intervention appears to be necessary. Such policies are probably not only socially desirable, but also economically useful.

However it should be noted that it does not necessarily follow from the existence of market failures that public intervention can improve the outcome. After all, if the private financiers suffer, we have to critically ask how this same informational constraint affects the ability of the government to allocate capital in an efficient and effective manner.

More information about other EEO activities can be found at:

<http://www.eu-employment-observatory.net>

¹ For some discussion on measures of quality, see 'Working Poor in Europe', European Foundation for the Improvement of Living and Working Conditions, 2010, Dublin.