Understanding entrepreneurship in the local context
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CHAPTER 1.

Introduction
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1.1 Motivation
The notion of growth, both economic growth and population growth, continues to dominate in research and policy. A growing population is strongly associated with economic growth: classic economic theory explains that as long as more people can be employed, production will also grow – given that labour is one of the major inputs of production. The rate of population growth, however, is slowing down in most developed countries. The world population has increased by nearly 13 per cent in the first decade of the 21st century, while Europe only grew about 1.5 per cent over the same period (UN, 2013). Population decline is now a reality for most countries in the EU. Even those countries with overall growth have regions already experiencing population decline, requiring a different approach. There are three main causes of regional population decline: low fertility rates, out-migration and ageing (Mai and Bucher, 2005). These three processes of decline are linked very closely: an ageing population can in itself cause regional population decline, as ageing leads to fewer births and more deaths (Verwest, 2011). The process of ageing is the result of selective outmigration of young people and families, low inflow of migrants and a low birth rate, which in its turn causes population decline (De Jong and Van Duin, 2011). Natural population growth, the number of births minus the number of deaths, has been the traditional cause of population growth until well into the 20th century (van Steen and Pellenbarg, 2006; NIDI, 2009). Within Europe, the Netherlands was unique in its long continued growth due to natural population growth after the second world war, but has now stabilized in the last 30 years at a fertility rate below the replacement level (NIDI, 2009).

Population decline is a complex issue with many social and economic implications; with mainly young people leaving, fewer children are born and the ageing population is left with fewer employment opportunities, and fewer retail and care facilities (Haartsen and Venhorst, 2010). Social expenditure is put under strain because of a shrinking labour force and declining purchasing power, a direct consequence of young people migrating out. This process makes it difficult for small communities to maintain
adequate infrastructure, educational and medical facilities and other public services, which in turn can make it difficult to attract new immigrants or prevent current residents from relocating (Fésüs et al., 2008; Haartsen and Venhorst, 2010; Mai and Bucher, 2005; Polèse and Shearmur, 2006; Simmie and Martin, 2010), thereby creating a negative spiral. Furthermore, social ties are disrupted by continuous out-migration, causing a decrease in support systems and social capital, which can have detrimental effects on liveability. At the same time, population decline strengthens the effect of population ageing. People are getting older, but also, people are getting older in greater numbers. Ageing is the most imperative example of selective population decline. It causes a relative decline in the population of working-age and the labour force will consist of more and more older people (Börsch-Supan, 2002). The potential labour force is expected to continue to decrease in the future (OECD, 2013).

Population decline can thus, depending on the intensity, constitute a deeply rooted problem. It can, however, also be interpreted as a positive development as population decline could relieve congestion, improve environmental quality or reduce noise pollution (van Dalen and Henkens, 2011). It is still unclear what this new trend means for our society and economy, what the possible consequences are and how we should deal with this. Population decline and ageing are noticeable trends in several Dutch regions. Although decline in the Netherlands has not yet taken on dramatic proportions as it has elsewhere in Europe (Barca, 2009; European Commission, 2010), the change is structural and incremental and there is a challenge in keeping these declining regions viable in the future (SER, 2011). In order to deal with the consequences of demographic change, we turn to entrepreneurship as an adaptation mechanism. Entrepreneurship can play an important part in keeping these regions viable, both in economic and in social terms. This thesis looks into the connection between the decline, ageing and density of the population, and the level and the form of entrepreneurship, in order to determine whether there is a causal relationship between these variables.

The relevance of this research and it contribution to existing literature is threefold. The first contribution relates to the context of the study as it addresses the challenges of dealing with the complex problems that potentially accompany population decline and the effects of it that are still unclear (SER, 2010). This research contributes to the relatively limited scientific work done on regions facing a declining population. Secondly, the role of entrepreneurship and the way it develops within a declining context has yet to be uncovered, see paragraph 1.2. The third category of contributions made in this thesis concerns the way entrepreneurship can impact its environment in both economic and social terms, which is dealt with in paragraph 1.3.
1.2 Entrepreneurship in different contexts

Traditional views regard entrepreneurship as being formed by only the qualities of the individual, ignoring the context, but factors influencing entrepreneurship can be both personal characteristics and environmental (Eliasson and Westlund, 2013). The link to the environment is of equal importance to the individuals characteristics, given that the entrepreneurial process depends on the available opportunities in the environment and on the individual’s identifying and exploiting these opportunities. New business creation is then the result of interaction between an individual’s traits and their environment, which means it is very likely that entrepreneurship differs in various environments. Regions in transition can provide additional challenges for new businesses, making the start-up decision and process more challenging.

Entrepreneurship has traditionally been seen as a mechanism of growth. Regional macroeconomic research continues to place emphasis on the analysis of economic growth (Hill et al., 2008) and research on the role of entrepreneurship in a non-growing context seems to be lacking (Liñán and Javier Santos, 2007). Population change can create more demand as new and bigger consumer markets emerge because of the growing population (Armington and Acs, 2002; Wennekers et al., 2005), stimulating new business creation by providing opportunities for new economic activity. Needless to say, this positive effect will be missing in the case of population decline.

Ageing and decline interact, such that the former will increasingly impact firms, too. An ageing and declining population involves changes in the demand for consumption goods, housing and services (Euwals et al., 2009). On the supply side, labour is the ultimate resource. If the ageing and decline of the total population translates into the ageing and decline of the labour force, firms might resent this. Ageing changes the labour market, possibly making it more difficult to find the right employee, but it also affects the pool of potential new entrepreneurs themselves (Bönte et al., 2009). The capability of the labour force is of utmost importance in order to remain competitive. One characteristic of declining and ageing regions is that skilled and higher educated people are among the first to leave (Astrom, 2001). In addition, the likely reduction in support systems caused by out-migration might also have an impact on the nascent entrepreneur. Starting a new firm is a highly social process, as information, new ideas and resources are predominantly acquired via personal networks (Aldrich et al., 1998; Davidsson and Honig, 2003). Start-up risk will be higher in a declining region given the challenges for entrepreneurship that accompany decline.

Population change is not a homogenous process. Growth and decline occur side by side and in different types of regional contexts. Regional differences in degree of population change can be the result of region-specific characteristics, opportunities or limitations.
An important regional characteristic is the distinction between urban and rural regions. Urban and rural regions differ in various aspects. Urban regions usually include more modern and better infrastructure. They also differ in terms of the number of available jobs and education opportunities, both usually fewer in rural regions (Eliasson and Westlund, 2013). The most obvious difference between urban and rural regions is population size and density which is most relevant within the aims of the study. Population decline in a low density region will have a relatively bigger impact; the critical mass for maintaining the same level of public services and local businesses is reached earlier in rural regions. Rural areas are therefore expected to experience the effects of population decline differently and perhaps more intensely than high density regions (Haartsen and Venhorst, 2009; NIDI, 2009). Whether and to what extent they are actually affected differently is uncertain.

Population density is considered to be positively correlated with entrepreneurship (Audretsch and Keilbach 2005; Becker et al., 2010; Fritsch and Mueller 2008). Urban areas have important advantages for entrepreneurship: conditions for entering a market are thought to be more favourable in more densely populated regions (Audretsch and Fritsch, 1994), as the consumer market is in closer proximity and the business infrastructure is better developed (Bruderl and Preisendofer, 1998; Fritsch and Mueller 2008). Spatial density also improves the likelihood of recruiting a more skilled workforce and enables ideas and knowledge to flow faster. Moreover, the risk of starting a business in urban areas is considered relatively low due to the rich employment opportunities, which function as a safety net in the case the firm fails (Stam, 2009). Finally, the establishment of businesses in a certain area is likely to attract other businesses because of the opportunities of cooperation and spillover effects (Audretsch and Fritsch, 2002). There is, however, also a flipside of the coin. Higher population density can lead to the pursuit of economies of scale. Economies of scale enables firms to be more efficient, needing fewer employees and leaving fewer opportunities for new small start-ups (Verheul et al., 2001). Policy makers often invoke the idea of entrepreneurship when dealing with population decline. Entrepreneurship policies are frequently designed with urban regions in mind and might be less effective when implemented in the same manner in rural areas due to the different characteristics, requiring a place-based approach (Eliasson and Westlund, 2013).

1.3 Impact of entrepreneurship on the context

Regions confronted with population decline face potentially complex problems. Entrepreneurship could play a role in dealing with issues that arise as a result of population decline. It could be part of the solution. Therefore, in addition to assessing how the context influences entrepreneurship, this thesis also considers the question from the other way round; the potential impact of entrepreneurship on its
environment. Entrepreneurship can have many positive effects on a region such as driving competition and innovation, and consequently GDP and employment growth. It also contributes to a more diverse economy and diversity helps to create a stable community (Steiner and Atterton, 2014). Entrepreneurship affects both economic and non-economic features within a region. It can also contribute to aspects of quality of life, such as the level of social capital, in that it creates trust, maintains social relations and provides meeting places (Morris and Lewis, 1991; Westlund, 2003).

Particularly for declining regions, new business creation is often seen as a means to secure current and future employment opportunities (c.f. Andersson and Noseleit, 2011; Armington and Acs, 2002; Stam, 2010). Given the likely declining labour supply, population decline is strongly associated with economic decline, although it does not automatically lead to less economic growth (Gáková and Dijkstra, 2010). Whether a new business contributes to regional employment growth or not depends on the type of firm and its regional context, including population dynamics.

The effects of entrepreneurship should be assessed beyond the economic impact only, in particular in the context of population decline or low population density (Ahmad and Hoffman, 2008). The way entrepreneurship can impact its environment in a non-economic manner represents an important contribution made in this thesis. Entrepreneurship influences the level of social capital and has a positive impact on the liveability of a region (Morris and Lewis, 1991). Maintaining and building social capital is important in addressing the social challenges that population decline and ageing can cause (Bærenholdt, 2002). Particularly in a rural context, small businesses often create a distinctive aesthetic and add to the personality that characterizes the local high street. This distinctive aesthetic attracts residents and tourists to shop there, leading to a more convivial place and improved community cohesion (Henderson, 2002; Steiner and Atterton, 2014).

This study provides new insights from the wider community regarding entrepreneurship as a mechanism for building social capital and enhancing quality of life, where others have focused on the perspective of the entrepreneur. Social capital has been the topic of a vast and growing stream of literature; however, in combination with entrepreneurship it mainly focuses on how social capital can contribute and affect the level of entrepreneurship, not the other way around. Entrepreneurship can be as much a creator of social capital as a result of it, but few empirical studies have addressed the reciprocal relationship.
1.4 Research questions and thesis outline

This thesis takes two different perspectives of entrepreneurship into account. To begin with the context in which we study entrepreneurship, which itself has an impact on entrepreneurship. The form and the extent of this impact are thus far unknown. The impact of the context on new business creation is approached in a quantitative way (Chapter 2) but also studied from a more individual perspective (Chapter 3) to develop a better understanding of start-up motivations and how the context influences the decision making process. Secondly, entrepreneurship itself has effects on the region, both economically and socially. Starting from an economic point of view, Chapter 4 studies the way in which new business creation exerts its influence on employment growth in the context of population change, disentangling long and short term effects. The social impact is dealt with in Chapter 5.

In Chapter 2, entitled ‘Population change and new firm formation in urban and rural regions’, we look into the relation between population decline, and the rates of new businesses creation. Although it is clear that fewer people will eventually lead to fewer (new) firms, the central question of this chapter is whether this negative relationship differs with different rates of population change and across regional contexts. Population decline occurs in different types of regional context, which could also lead to different outcomes. In this chapter we therefore distinguish not only between declining and growing regions, but also between urban and rural areas. We apply a quantitative method to this problem by estimating a spatial Durbin model on a municipal level in the Netherlands and observe a relative high rate of new business creation in declining rural regions.

The next Chapter continues with the question of who these new entrepreneurs are and what their motivations are for start-up in adverse circumstances. Chapter 3, entitled ‘Why start a business in a declining rural area with an ageing society? A UK-NL case study’, concerns the impact of the (changing) regional context on the creation of new businesses on the individual level by looking into start-up motivation. Firms are set up by individuals and individuals are influenced by their environments, which means that adverse circumstances could lead to different motivation for start-up, such as necessity driven. The positive impact of population decline on new business creation, as measured in Chapter 2, could possibly be the impact of necessity-driven entrepreneurship. We chose two rural, ageing case studies; one in Drenthe, in the Netherlands, and one in Northumberland, England. The case studies reveal that necessity-driven entrepreneurship is actually a rare occurrence and they underline the importance of a specific lifestyle choice which leads to business creation in these regions. The results from the second Chapter raise questions regarding the Dutch countryside: can one speak of ‘real rurality’? the answer according to the Dutch is in the affirmative (Haartsen, 2002), but focusing on population density one could argue
the opposite. The secondary aim of both Chapter 3 and Chapter 5 is therefore to compare the two case study regions in terms of their rurality and accessibility.

In Chapters 4 and 5, the focus is on the impact of local businesses on their environment. First, in Chapter 4, entitled ‘The effect of new business creation on employment growth in regions facing population decline’, we aim to disentangle the economic consequences of new business creation in different regional contexts. Beside knowing that the quantity of new businesses in declining and rural regions is relatively high, what is their impact on regional employment growth? Intuitively, one would expect a positive relation between new business creation and economic growth. However, new firms can have a negative impact on employment change, known as destructive entrepreneurship (Baumol, 1996). The interesting question is how regional employment growth differs depending on the changing demographics. We find that start-ups in regions declining in population generate less employment growth compared to other regions, but they do have a positive and significant impact on regional employment change.

The impact of local entrepreneurship is, however, not limited to economic aspects. Particularly in the case of small, rural towns, local businesses can play an important role in creating or maintaining community quality of life. Chapter 5, entitled ‘The impact of local businesses on community quality of life: “a village without a shop doesn’t have a heart”,’ deals with this issue. It applies a qualitative research method, using the same two case study regions as in Chapter 3. The Chapter shows that local businesses contribute to the building of bridging social capital and that they are an integrated part of the community’s identity and quality of life. Finally in Chapter 6 we present a summary and general conclusions are drawn based on the analyses in Chapters 2 to 5. Furthermore, Chapter 6 presents the main conclusions, limitations, and suggestions for future research and policy implications.

1.5 Research challenges

Population decline takes place at different aggregation levels, from neighbourhood to country level. Capturing decline is spatially challenging; what is the appropriate unit to consider? Using a higher aggregation level will cause regions to become more alike, as outliers are levelled out. A low level of aggregation on the other hand could mean that observations become too dependent on the specific choice of sometimes rather random administrative borders.

For the quantitative chapters of the thesis, there are three aspects that need to be taken into consideration, namely population change, new business creation and to a lesser extent also degree of urbanization. Population decline is visible on the low level of
neighbourhoods, occurring side by side with growth within one city or municipality. Such a low level however, will be too finely grained from the perspective of new business creation, their local markets and location choices are highly likely to cross neighbourhood borders. The opposite option would be to look at labour markets, which in the case of the Netherlands is the NUTS 3 level. The NUTS 3 level divides the country into 40 regions which will cause the nuances of both population dynamics and degree of urbanization to disappear.

The municipality level is therefore preferred. First because a small spatial scale allows us to identify the declining regions and to understand specific local issues in the Netherlands including urban and rural differences (OECD, 2008). Second, as new business creation is often a local phenomenon (Dahl and Sorenson, 2012; Sternberg, 2011), new businesses are likely to be located in the home region primarily serving local and regional markets and are therefore heavily influenced by local conditions (Bosma et al., 2008; Stam, 2009). Finally, the low aggregation level is needed in order to understand specific local issues, such as identifying urban and rural regions. Spatial econometric techniques allow the analysis of the influence of neighbouring municipalities in order to take account of larger spatial scale effects.

References


