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CAN GOVERNMENT POLICIES PROMOTE ENTREPRENEURSHIP? EVIDENCE FROM COSTA RICA, URUGUAY AND CHILE

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EXECUTIVE SUMMARY

Governments around the world have begun to look to small- and medium-sized enterprises (SMEs) as sources of employment and economic growth for their domestic economies. However, neither public policy makers nor researchers have a solid understanding of which government policies are most likely to be most effective. We examined government policies towards entrepreneurship in three Latin American countries to identify the programs that appeared to be the most promising avenues for success.

Governments in each country implemented three types of policies toward entrepreneurship. They improved their regulatory environment for entrepreneurship by offering SMEs financial assistance and simplifying bureaucratic rules. They improved their cognitive environment for entrepreneurship by offering programs to teach would-be entrepreneurs the knowledge and skills necessary to run a small enterprise. And they strengthened their normative environment for entrepreneurship by working to improve society's perception of the entrepreneurial sector.

We conclude that the most effective policies were those that targeted all three of these dimensions. In particular, programs that brought SMEs together into a community of entrepreneurs helped them gain market power, obtain economies of scale, share knowledge, and achieve a range of other advantages. While specific policy prescriptions depend on a country's circumstances, we recommend that public policy makers and small business owners

consider forming communities of entrepreneurs to further their national and individual interests.

In 1993, several small wine producers in the Maule region of Chile were struggling for survival. They knew that some of the most successful wine producers in the world were growing large enough to achieve scale economies and devote substantial resources to process innovations and global marketing strategies. Unfortunately, these small Chilean firms lacked the resources to match this approach, and their own technology was becoming more obsolete by the day. These entrepreneurs lacked an understanding of the global market for wine, had little experience with managing growing business concerns, and were becoming increasingly afraid that they might begin to lose even the small level of export sales that they had already achieved, valued at approximately US \$83,000 a year. With such a small sales volume and so many global competitors, these winemakers had little chance of obtaining bank loans to improve their process technologies, build larger vineyards, or undertake strong marketing efforts on the world market (Cabrera Gajardo, 2001).

Firms in a wide range of industries and countries face dilemmas similar to the circumstances of these Chilean wine producers. National governments often profess an interest in aiding these small entrepreneurs, citing small firms' success as a source of economic development for their domestic economies. However, it is unclear what policies governments can implement that will truly improve the chances that these small enterprises have to survive and grow into thriving businesses. In this paper, we explore how government policies can contribute to national environments that promote small business entrepreneurship. We provide examples of programs that have been introduced in three Latin

American countries -- Costa Rica, Uruguay, and Chile -- to illustrate how both public and private programs have contributed to the performance of local entrepreneurs.

Policy makers have recognized that small- and medium-sized enterprises (SMEs) play a critical economic role, employing more than half of the working population in each of these three countries. Even so, these small firms display high mortality rates and rarely grow into thriving, innovative businesses. Government officials have made tacit or explicit decisions concerning policies toward their entrepreneurial sector. An understanding of the effects of these policies on domestic entrepreneurship holds clear relevance for government officials, executives of start-up firms, and owners of small businesses. In addition, managers of large enterprises often wish to partner with domestic entrepreneurial ventures, and multinational enterprises often prefer to locate in countries in which entrepreneurial firms will emerge to provide a strong infrastructure by marketing supporting goods and services. Therefore, even managers of larger, established companies have an interest in understanding how public policies influence the strategies and performance of entrepreneurial ventures.

NATIONAL ENVIRONMENTS FOR ENTREPRENEURSHIP

The volume and success of the entrepreneurial activity in a country depends on the independent economic decisions of each of its residents. The probability that residents will participate in entrepreneurial ventures is based on their individual motivation to become entrepreneurs, ability to undertake entrepreneurial activities, and perceptions about the opportunities that are available to them (Gnyawali & Fogel, 1994). National environments can influence each of these factors. Government policies that provide entrepreneurs with financial assistance via subsidies, preferential procurement, or favorable tax policies (we call

this a strong *regulatory* environment for entrepreneurship) increase the opportunities available for new ventures and small businesses. In countries in which business education and training programs are prevalent and residents understand *how* to found and manage a new business (we call this a strong *cognitive* environment for entrepreneurship), individuals are more likely to hold the ability to successfully manage their own company. Finally, in countries in which entrepreneurial activity is valued and admired (we call this a strong *normative* environment for entrepreneurship), more individuals are likely to be motivated to found a new business or manage a small business. These regulatory, cognitive, and normative environments form three pillars of support for a country's entrepreneurial activities (Busenitz, Gomez & Spencer, 2000; Kostova, 1996; Scott, 1995).

Governments vary in their preferences for promoting one sector of economic activity over another. Some governments may prefer to avoid interfering in their domestic marketplace by prioritizing one sector over another. And a few governments may even prefer to discourage entrepreneurship. For example, while imposing a tax on self-employment activity in Cuba, Fidel Castro declared, "We need a tax on robbery!" reinforcing an ideology that condemns those who put their individual interest over the interests of society (Miami Herald, 1995).

We suggest that governments that choose to *promote* domestic entrepreneurial activity will be best off if they implement policies to strengthen all three of the relevant pillars—regulatory, cognitive, and normative. Public policies targeting the regulatory environment can improve the opportunities available to entrepreneurs by offering small businesses financial incentives or preferential treatment in government procurement. Governments can strengthen the cognitive environment, and thus increase the abilities of entrepreneurs, by

offering government-sponsored training programs or consulting services. And by improving the normative environment for entrepreneurship -- for example, by using the bully pulpit to sway public opinion toward an admiration of entrepreneurs -- governments can increase the motivation of entrepreneurs.

----- Figure 1 About Here -----

The process by which a strong environment for entrepreneurship emerges in a country is incremental and cyclical (See Figure 1). An increase in the number of small businesses in a community will prompt new entrants or established businesses to invest in profitable ventures that support entrepreneurship. For example, small businesses are likely to patronize consulting services, law firms, accountants, and other business service providers who target their services toward the entrepreneurial sector. Likewise, as the number of new ventures increases, financing mechanisms such as venture capital and bank loans aimed at entrepreneurs, may emerge as potentially lucrative investments for financial organizations. Similarly, a growing entrepreneurial sector is likely to attract the attention of publishers, who may introduce magazines targeted at entrepreneurs, and schools and universities, which may begin offering courses and degrees in entrepreneurship. An increase in the number of entrepreneurs in a country also gives a stronger voice to small business interest groups, and therefore increases the chances that government officials will offer policies that promote new business development.

And the presence of these newly established support services and government programs, in turn, should facilitate the entry of the next generation of entrepreneurial

ventures. Therefore, countries that are able to provide an impetus for entrepreneurship in their domestic economies may be able to place themselves on a trajectory of increasing small business growth over time.

NATIONAL ENVIRONMENTS FOR ENTREPRENEURSHIP IN COSTA RICA, URUGUAY, AND CHILE

The national environments of Costa Rica, Uruguay, and Chile are similar along several dimensions. Each of these Latin American countries displays similar cultural values. All are relatively low on individualism, meaning that people in these countries value the interest of their group -- particularly their family-- over their individual needs. Each country scores relatively high on uncertainty avoidance, meaning that individuals in these cultures prefer to avoid ambiguous situations and have a relatively low tolerance for risk. Chile and Uruguay display high power distance, meaning that people in these cultures tolerate the fact that some people in an organization or in society, in general, hold power, while others do not. However, power distance appears to be smaller in Costa Rica.

Historically, the government of each country has looked to the development of large enterprises and foreign direct investment as its primary source of economic growth, often ignoring the entrepreneurial sector. Similarly, individuals in each of the countries have traditionally not valued employment in start-up ventures or small firms. In fact, economic experts in local Chambers of Commerce have noted that local residents historically preferred to work for a department or agency of the government rather than for a private business. More recently, as governments have begun to play a smaller role in the economy, individuals have displayed a preference for working in larger, established corporations. Although

residents are increasingly aware of the importance of the SME sector, experts report that most residents lack a real understanding of how to successfully manage an entrepreneurial venture. Experts have also noted that entrepreneurs have traditionally had a poor image, with a reputation for corruption and for pursuing their own profit at the expense of society. Therefore, while many programs' most immediate objective lies in helping entrepreneurs overcome tangible hurdles to founding and managing a business, their longer term goal rests in encouraging the local culture to become more receptive to entrepreneurial activity.

Despite similarities in the cultural and historical conditions for entrepreneurship in Costa Rica, Uruguay, and Chile, each of the countries' entrepreneurial environments is unique. The Costa Rican government has only recently started to promote domestic entrepreneurship. The government of Uruguay began programs to promote entrepreneurship in the early 1990s, and has relied on the efforts of business organizations such as Chambers of Commerce for some of their most important programs. Finally, although its focus on promoting entrepreneurship is fairly recent, Chile offers perhaps the most extensive collection of programs of all.

Costa Rica

Of the three countries studied, Costa Rica has the newest focus on promoting small business entrepreneurship. The Costa Rican government has pursued export-led development for the last two decades by providing incentives to firms that export products and services. The biggest exporters in Costa Rica have generally been large multinational enterprises with foreign investment in the country. As a result, for nearly twenty years Costa Rica has maintained one of the most thriving foreign trade zones in Latin America (Arino, 2001; Monge, 1998). At the same time, the government is aware that the majority of Costa Ricans

are employed by SMEs (Arino, 2001). In fact, estimates of SME employment go as high as 90% of the workforce. In addition, the Costa Rican government has made a commitment to the World Trade Organization to abandon export-related subsidies and assistance by 2003, placing smaller businesses in a more prominent position within the economy. Therefore, the government is becoming increasingly interested in promoting small and new businesses within Costa Rica.

Costa Rica does not maintain a specific government agency dedicated to promoting SMEs, but the interests of small businesses lie in the domain of the Ministry of Economy, Industry and Commerce. This ministry works with private business associations to offer industry fairs and training programs for small business owners. Entrepreneurs can access free business training on topics ranging from identifying and evaluating business opportunities to more specific topics such as accounting, marketing, capital budgeting, and sales. Some business associations also offer training at a cost. For example, the Center for Business Incubators (partly sponsored by the Technological Institute of Costa Rica, a public university), which fosters knowledge exchange and development of high technology start-ups, offers its own training programs for entrepreneurs. The National Bank of Costa Rica has agreed to analyze and consider financing the businesses that develop in this incubator.

Although the Ministry of Economy, Industry and Commerce does not offer its own financing programs for SMEs, multilateral development banks and state-owned banks provide credit lines with preferential interest rates for smaller businesses. Most policies toward SMEs focus on simplifying bureaucratic hurdles and providing business owners with clear information regarding the logistics of founding and managing a new business. The newly written *Manual for the Investor* spells out the steps, paperwork, and logistics of getting a

business started, providing entrepreneurs with extensive information about the bureaucratic process of founding a new company. The government has also tried to simplify the process of business registration. This is an ongoing process by which the government hopes to identify, revise, and sometimes eliminate, the paperwork and procedures that are most burdensome to entrepreneurs. In addition, tax regulations allow entrepreneurs to submit less paperwork and maintain simpler records than are required by larger businesses.

The Ministry of Economy, Industry and Commerce has also created an internet-based information program called the System of Information for Costa Rican Enterprises (linked through their website www.meic.go.cr, El Sistema de Información Empresarial Costarricense, www.seic.go.cr). The objective of this website is to simplify and expedite the distribution of information to the industrial sector to improve entrepreneurs' understanding of the domestic business environment. Ultimately, this system is expected to provide entrepreneurs with all the information they need to establish and operate a business within Costa Rica. Currently, the website provides information on credit lines, industry fairs, training programs, exporting and importing opportunities, trade law, government statistics, links to domestic and foreign business associations, and a link to the *Manual for the Investor*.

Uruguay

Historically, as one of South America's highest taxed countries, Uruguay has had a hard time fostering small business activity. One analyst concluded that excessive government intervention and high inflation have inhibited entrepreneurs from growing into lasting, innovative enterprises, and have instead promoted the establishment of smaller, informal micro-enterprises that barely achieve subsistence (Dana, 1997).

To address this weakness, the government of Uruguay has developed some programs intended to promote domestic entrepreneurial activity. The country launched its primary program to promote entrepreneurial activity, called DINAPYME (National Agency of Arts and Crafts and SMEs), in 1990. DINAPYME's objective lies in coordinating activities to promote micro-, small- and medium-sized enterprises that have fewer than 99 employees, annual sales of less than \$5,000,000 and assets under \$350,000. More than 90% of organizations in Uruguay's private sector fit this classification. However, according to economic experts, the mortality of these SMEs is quite high (Benavente, 2001).

DINAPYME, itself, does not provide financing. However, it does offer consulting services and training intended to help entrepreneurs in developing business plans, making presentations to investors and lenders, and presenting financial data appropriately.

DINAPYME develops many of its programs in close consultation with the private sector. The largest effort is called Red Propymes (The Network for Small and Medium Enterprises). This network integrates organizations that share the objective of promoting micro-, small- and medium-sized enterprises in Uruguay, including DINAPYME, chambers of commerce, banks, and other private and semi-governmental organizations. Red Propymes provides training for entrepreneurs, assists businesses' efforts to reach new markets and obtain new technology, expands firms' abilities to obtain capital, improves firms' access to information, serves as an incubator of ideas, and even increases the environmental conscience of budding entrepreneurs. For example, the network provides an award to the most innovative SMEs according to an annual theme such as environmentalism, employment-creation, or globalization, and works to improve the negative image of SMEs by conducting fairs and expos around the country.

Each member of Red Propymes also develops its own programs directed toward SMEs. For example, Uruguay's chamber of commerce launched a pilot program called the Industry Sector Nucleus program, with financial assistance from Germany's Agency for Cooperation (GTZ). This program is aimed at creating a nucleus of companies in a particular industry or regional area. By working together with a specialized consultant, these firms are better able to exploit synergies and overcome the difficulties inherent in being small. For example, thirteen butchers in a neighborhood of Uruguay's capital, Montevideo, joined forces to buy distribution truck and freezer. By working together, these entrepreneurs saved money on their capital investments and were able to gain leverage over their suppliers by buying in volume. In one year, the Industry Sector Nucleus program constructed 25 nuclei representing over 300 companies. Many of the participating SMEs have expanded their operations, and none have reduced personnel. Due to the program's success in maintaining and often increasing employment, even in the midst of an economic recession, the International Labor Organization as agreed to sponsor and finance an extension of this program into the future.

Another Red Propymes member, the Technology Laboratory of Uruguay (LATU), is a quasi-governmental organization that organizes industry fairs, assists with quality certification programs, and operates a business incubator for SMEs in the information and communication sectors. Although this incubator does not provide SMEs with direct financial support it does provide administrative support, business plan assistance, training, and other services to help new firms within the designated sectors.

In addition to the DYNAPYME program, Uruguay's tax system offers some basic assistance; SMEs qualify for tax breaks not available to the country's largest businesses, and micro enterprises are altogether exempt from some taxes. In addition, a new program allows

entrepreneurs to pay a small social security tax so that they qualify for government retirement benefits. Since these benefits are fairly extensive in Uruguay, this new tax provision is expected to benefit entrepreneurs substantially.

Chile

Finally, of the three countries, Chile has implemented the most aggressive policies towards entrepreneurship. Chile's National Training and Employment Service (SENCE) offers tax benefits to all Chilean firms who develop and train their employees, with special benefits accruing to smaller organizations whose employees tend to earn lower salaries. SENCE also helps SMEs finance training programs offered by other business associations.

In addition, Chile maintains two programs aimed at promoting success in entrepreneurial ventures. The *Solidarity and Social Investment Fund (FOSIS)* directs its efforts at self-employed individuals and micro-business, and the *Corporation to Promote Production (CORFO)* maintains fairly extensive programs that facilitate the development of small and medium-sized businesses (Segura, 2001).

The Solidarity and Social Investment Fund (FOSIS)

FOSIS was founded in 1991 with the goal of developing and financing projects that facilitate the social development of Chile. These programs are intended to increase domestic employment, improve Chile's quality of life, and help individuals work their way out of poverty. Within FOSIS is the "Program to Promote Productivity," which assists self-employed individuals and micro-businesses by offering training programs, as well as providing some financing.

Corporation to Promote Production (CORFO)

CORFO, a government-based organization founded in 1939, has historically played a strong role in Chile's economy. While its goals and structure have changed markedly over time (see the text box on the next page for a description of its changing role over the last sixty years), CORFO remains one of the most prominent organizations in Chile devoted to business development. While its goals and structure have changed markedly over time, shifting from an emphasis on state-run companies and the nationalization of private firms, to a focus on privatizing these state-owned businesses, to an emphasis on promoting SMEs, CORFO remains one of the most prominent organizations in Chile devoted to business development. Today, one of CORFO's main goals lies in assisting SMEs by facilitating access to financing, promoting collective efforts among small organizations, and helping small firms identify and employ the most modern technologies and management techniques.

CORFO provides a range of programs for SMEs. For example, CORFO offers direct and indirect financing to help SMEs invest in fixed assets, restructure debt, and overcome other obstacles. For example, CORFO recently announced plans to offer 100 SMEs "fast track" loans through a streamlined evaluation process, in order to support small firms that are struggling in the recent recession (Global News Wire, 9/26/2000).

Several of CORFO's programs are designed to help groups of firms work together to achieve a common goal. For example, the Program for Development of Suppliers (PDP), attempts to increase the competitiveness of production chains by establishing relationships between larger companies and a network of smaller suppliers. CORFO's program of technical assistance (FAT) will match investments made by firms or groups of firms who employ consultants to help them improve production, finance, design, marketing, or strategic

planning activities. CORFO is also working with private industry to create a website for SMEs to trade products and services, establish contacts, and gain access to industry-related services such as online training, financing, inventory auctions, and legal services (Global News Wire, 1/8/2000).

The history of CORFO parallels the turbulent history of Chile. Early on, some of Chile's biggest state-owned enterprises were founded under CORFO's watch, including the national electric company (Endesa), the national petroleum company (Enap), the national steel company (Cap), and the national sugar company (Iansa). CORFO was also responsible for providing credit lines, capital, and direct subsidies to many industries such as mining, agriculture, transportation, hotels, pharmaceuticals, fishing, tires, and films. During the socialist government of the 1960s and early 1970s, CORFO launched a new effort to create large enterprises, such as the national telecommunications company (Entel). During this time, CORFO also dedicated effort to nationalizing enterprises across critical sectors of Chile's economy.

In 1973, Chile's economic policies shifted dramatically towards free market reforms, and CORFO's objectives reversed themselves, focusing primarily on privatization of state-owned enterprises such as Endesa and Entel.

With the return to a democratic government, CORFO's role was redefined once again in the 1990s. Policymakers determined that the private sector in general, and SMEs, in particular, played a critical role in Chile's economic development. In addition, policymakers noted that public and private sectors require very different profiles for success. Therefore, the public sector component of CORFO's operations was transferred to a new agency called the Administrative System of Enterprise (Sistema Administrador de Empresas, SAE). And CORFO was asked to focus primarily on fostering a positive environment for the development of small and medium sized businesses in Chile.

Perhaps one of the most interesting programs started by CORFO focuses on Associative Projects of Promotion (PROFOS). CORFO completed a pilot program in 1993, and formally launched PROFOS in 1994. PROFOS aims to improve the competitiveness of SMEs by fostering interaction and association between groups of small businesses operating in similar or complementary industries. CORFO promotes the PROFOS program directly, and also recruits members through other organizations such as chambers of commerce,

SERCOTEC (Technical Cooperation Service), ASEXMA (Association for Manufacturing Exporters), and many others.

The PROFOS program focuses on priority sectors such as manufacturing, manufacturing services, tourism, fishing, arts and crafts, and agricultural industries. Figure 2 illustrates the process by which firms come together and coordinate action within the PROFOS program. SMEs progress from acting as a set of independent organizations with little knowledge about other participants, to a fairly cohesive co-operative that identifies common problems and works together to tackle them.

----- Figure 2 About Here -----

Through PROFOS, five or more SMEs team up to pursue a specific objective such as jointly purchasing capital equipment, coordinating export efforts, pursuing marketing campaigns, or overcoming technical hurdles. CORFO provides a network manager, who focuses on identifying appropriate members for a given PROFOS, diagnosing problems, and developing a collaborative project that can improve the performance of all member firms. CORFO subsidizes the collaborative project for up to three years, with the government paying 70% of project costs in the first year, 60% in the second year, and 50% in the third, and generally final, year.¹ While CORFO hopes that many of the associations will sustain activity beyond the three years of government assistance, some PROFOS are intended to be short-lived. For example, a PROFOS may well disband after it successfully completes a temporary project such as attaining ISO 9000 certification for member firms.

¹ In special cases where SERCOTEC believes the investment will lead to a unique economic opportunity for Chile, it will consider subsidizing a PROFOS for up to five years

PROFOS appears to be fairly successful. An early study provided evidence that many of the PROFOS that had been in existence for 20 to 30 months showed signs of becoming independent (Dini, 1993), and other data has suggested that many of these associations of SMEs have expanded their market share and gained access to markets within Chile and abroad (Humphrey & Hubert, 1995). For example, one PROFOS of small metalworking firms help members improve their performance and, together, these firms became regular suppliers to the state mining company. Externally, organizations such as the Institute of Development Studies and the United Nations have referred to PROFOS as one of the most successful associative programs in Latin America (Tilman, Qualmann, & Weller, 2001).

Private organizations also work to assist SMEs in Chile. Many government programs such as PROFOS are implemented in conjunction with private business associations. In addition, associations such as Chambers of Commerce work with money provided by the InterAmerican Development Bank, the European Union, and other foreign and multilateral organizations, to assist entrepreneurs with market studies, logistics, and other necessary activities.

WHICH PUBLIC POLICIES ARE MOST EFFECTIVE?

Figures 3, 4 and 5 summarize how the public policies implemented in each country contribute to regulatory, cognitive, and normative dimensions of their environments for entrepreneurship.

Regulatory Institutions for Entrepreneurship

Countries offering government support for entrepreneurship through tax breaks, loan guarantees, and other regulatory programs increase the chances that residents will perceive an

appealing business opportunity and, therefore, decide to launch their own business. For example, Chile offers financial incentives to micro-businesses and SMEs through the FOSIS and CORFO programs. Uruguay provides tax breaks to SMEs and offers some financing through the Industry Sector Nucleus program, and Costa Rica provides domestic SMEs with preferential credit lines in addition to the financial help available from the Center for Business Incubators.

----- Figure 3 About Here -----

Providing financial resources to SMEs is one of the most popular approaches to promoting entrepreneurship in countries around the world. For instance, financial support or preferential treatment for entrepreneurial ventures has come in the form of government procurement programs in Canada, tax incentives in Singapore, low interest loans and grants in the Virgin Islands, and business development assistance in the US (Doutriaux, 1998; Dana, 1987; Phillips, 1993).

This financial support may be particularly important for Latin American entrepreneurs, who regularly cite a lack of financing as a critical obstacle to starting a business. For example, a study conducted by the University of Chile found that, while PROFOS provided real benefits for SMEs, entrepreneurs still perceived a lack of financing as their number one obstacle (Benavente, 1998).

Costa Rica has also simplified the process of starting a business and articulated national bureaucratic requirements very clearly. This focus on bureaucratic details may be critical for entrepreneurial growth. Research in Saint Martin, the Cayman Islands, and China

has shown that burdensome procedural requirements may limit entrepreneurial activity, and that uncertainty and instability in government policies may reduce entrepreneurs' interest in developing long-term growth strategies (Dana, 1990; Tan, 1996).

Evidence from Costa Rica, Uruguay, and Chile demonstrates some success for programs designed to improve their regulatory environment for entrepreneurship. As an example, Cristián Cremaschi, a vineyard manager in Chile summarized how government loan guarantees and funding can help struggling entrepreneurs who lack the capital and collateral often expected from market institutions. "If I had not entered PROFOS, I would never have been able to make the investment that I did—nearly 100 million pesos, because I wouldn't have had the sales to make [a loan] feasible with the bank."

Cognitive Institutions for Entrepreneurship

Programs that focus on the dissemination of management knowledge and entrepreneurial skills focus on strengthening cognitive institutions, and this can improve the ability of local entrepreneurs to found and maintain their own private enterprises. Costa Rica has focused its efforts on making the steps required of entrepreneurs as widely understood as possible by maintaining a website and publishing a manual designed to improve individuals' understanding of the process of launching a new business. Costa Rica also offers some training programs for entrepreneurs. Uruguay's DINAPYME program provides consulting services to small businesses, and Red Propymes provides training to entrepreneurs. In addition, the Industry Sector Nucleus program helps firms work together to understand their industry environment. Finally, Chile offers training for SMEs and micro-enterprises, and its FOSIS and CORFO programs help firms develop the entrepreneurial skills necessary to succeed.

----- Figure 4 About Here -----

Other countries have also emphasized the importance of strengthening cognitive institutions. Studies in the US and Australia have pointed to the existence of business education and management training programs, as well as the availability of assistance with market research and other business development activities, as contributors to the entrepreneurial skill set of a society (Pennings , 1982; Dana, 1987; Hawkins, 1993; Phillips, 1993).

The Center for Business Incubators in Costa Rica demonstrates the importance of developing the cognitive skill set of entrepreneurs. The Center not only offers many administrative services for participants, but also provides extensive training and consulting to budding entrepreneurs. The Center has sponsored about 100 programs since 1994, resulting in viable high technology companies such as Fortech Quimica, which markets chemical products, and AEC Electronica, which provides technical support to the electronics sector. A recent study found that the average SME in the incubator directly or indirectly created eight new jobs for Costa Ricans (Centro de Incubación de Empresas. 2001).

Normative Institutions for Entrepreneurship

Finally, programs geared toward improving society’s view of entrepreneurs can influence a country’s normative environment, and thus improve individuals’ motivations to become entrepreneurs. Our economic experts suggested that normative institutions are perhaps the most difficult element of the entrepreneurial environment to change, and noted that it would take several generations to truly alter how people in a society view

entrepreneurs. One expert pointed out that his culture tends to perceive entrepreneurs skeptically because of years of public messages equating entrepreneurs with opportunists (Arino, 2001).

----- Figure 5 About Here -----

All three countries are engaging in strategies aimed at changing these societal perceptions. Costa Rica has offered fairs and expos to promote entrepreneurship. Uruguay has sponsored awards that highlight how local entrepreneurs contribute to the objectives of society, and has funded fairs and expos to draw attention to the entrepreneurial sector. Chile's community-building programs such as PROFOS strive to meet similar objectives. And government leaders have taken up the task of promoting Chileans' entrepreneurial spirit. The head of a Chilean brokerage firm summarized, "...Chilean management isn't entrepreneurial... Part of the problem is in Chilean culture. Fortunately, we have a [President] Lagos today who is smashing both political and social taboos" (Rudnick, 2000).

Research on other countries such as Japan has pointed to a relationship between public attitudes toward entrepreneurs and a country's level of domestic entrepreneurial activity. Some researchers have recommended that governments offer "entrepreneur of the year awards," and that national leaders regularly offer informal remarks praising the activities of local small business owners to change societal attitudes towards SMEs (Gnyawali & Fogel, 1994). We concur with these recommendations, and note that government can work to provide a positive environment that legitimizes entrepreneurship as a respected career in their domestic economy.

There is some evidence that individuals in the general population in Chile have begun to view entrepreneurship more positively. According to local economic experts, the Chilean population increasingly looks toward the private sector and entrepreneurship for national economic growth. While in the past, individuals aspired to work as government officials or employees in large, established firms, most people today seem to be interested in starting their own business (Segura, 2001). Further evidence of changes in how entrepreneurs are perceived comes from Costa Rica. Increasing interest in the topic of entrepreneurship has led private media firms to publish magazines, such as *Entrepreneurial Costa Rica*, that are aimed at SMEs.

Communities of Entrepreneurship:

Programs that promote all three dimensions of the institutional profile simultaneously should earn greater success than programs that focus on only one or two areas. Both the PROFOS program in Chile, and Uruguay's Industry Sector Nucleus program stand out as having particularly good probabilities of success because they contribute to each of the three pillars concurrently. These programs strengthen regulatory institutions by providing seed money and other financial resources for entrepreneurs. They also contribute to entrepreneurs' skill sets by providing a professional manager to guide member firms' activities, and encouraging firms to learn from one another. They help firms build a network of supporting industries that can provide both intellectual and tangible resources to small enterprises. And finally, by putting entrepreneurs in touch with one another, they help build legitimacy for entrepreneurship, both in the perceptions of entrepreneurs, themselves, and in the community at large.

By addressing all three dimensions simultaneously, improvements in one dimension can induce progress in the others. For example, a program that provides financing to an entrepreneur who lacks basic skills will likely be a waste of money, and may even worsen the standing of entrepreneurship, in general. Communities of entrepreneurship, on the other hand, can be designed to strengthen regulatory and cognitive dimensions directly, while slowly building the normative pillar of a country's entrepreneurial environment.

When founding a new business or managing a small enterprise, managers face challenges that are not necessarily present for executives of large, established firms. By nature of their size and age, entrepreneurial ventures often rely on an external support infrastructure for everything from mundane business tasks such as small-batch printing jobs, to more strategic activities such as market analysis and product distribution. Entrepreneurial firms are often too small to purchase capital equipment that lets them achieve an efficient scale. They lack the resources necessary to engage in extensive research and development or to market their product adequately.

By maintaining ties with other entrepreneurial firms, a small venture can increase its knowledge acquisition, pursue co-marketing strategies with other SMEs, and obtain financial and other resources that they may not have access to alone (Yli-Renko, Autio & Sapienza, 2001; Hartmann, 1993; Stuart; Hoang & Hybels, 1999). In addition, many new ventures require an infrastructure tailored the specific needs of their industry. Entrepreneurial ventures in high technology industries, for example, rely on an extensive infrastructure of materials and components, manufacturing equipment, and complementary products tailored specifically for their emerging technology.

Innovative firms in these technology-based industries also tend to make faster progress on commercializing a new product when they work together. A recent study on the wind turbine industry (Garud & Karnoe, forthcoming) found that some national technological communities approached innovation somewhat collectively, with firms working together to contribute their incremental advances to others in the technological community. Others approached innovation more individually, with firms working in relative isolation, pursuing unique and incompatible product designs. This study found that the community approach appeared to foster faster product development, and produced technological designs that had a greater likelihood of becoming accepted in the global marketplace. Therefore, entrepreneurial ventures pursuing new product commercialization appear to stand a better chance of success when managers build relationships with other organizations in their own industry community. (Garud & Karnoe, Forthcoming).

In sum, government policies that facilitate these community-building activities hold greater potential than policies that support firms' isolated efforts because a network of firms can internalize spillovers, achieve economies of scale, and attract the requisite industry infrastructure. Therefore, in many contexts, a consortium of small firms may leverage a given financial subsidy into greater success than would be achieved if the same funding went to dispersed SMEs. For example, none of the butchers in Uruguay's industry nucleus in Montevideo could afford to buy a refrigerated truck for their own small-volume business. However, these butchers, who were losing money prior to forming the nucleus, began to make a profit and grow within their first year of working together.

Several small toy manufacturers in Chile engaged in a similar effort through the PROFOS program. On their own, each firm lacked the capital and expertise to make

investments to increase labor productivity or engage in extensive international marketing activities. However, after coming together to form a co-operative, called Chilean Toys Manufacturers, these small companies were able to develop new products, adopt more advanced technology, and better promote their products at home and abroad. Sales, both within Chile and abroad, more than doubled within four years (Gajardo, 2001).

Policy makers in Chile are pleased with the success of the PROFOS program. They have concluded that the program has provided several specific benefits to participating firms. It has facilitated the use of quality control programs, factory automation, and production planning. It has also increased the availability of employee training programs, and given firms greater access to local technical and market knowledge. According to CORFO calculations, each US \$1 invested by a member company has, on average, generated US \$2.40 in additional sales (Benavente, 1998). CORFO managers are also pleased by the results from a public policy perspective, concluding that the program has led to an increase in national employment, and that every US \$1.00 invested by the government has produced an additional US \$3.20 in tax revenues from the VAT. Therefore, by bringing entrepreneurs together into a community, governments can leverage small investments into more significant strides in their promotion of entrepreneurship. Table 1 summarizes some of the advantages that can stem from building communities of entrepreneurs.

----- Table 1 About Here -----

LESSONS FROM LATIN AMERICA

Several basic conclusions from these cases can be instructive to policy makers, would-be entrepreneurs, and managers of small, medium, and large businesses.

Promotion of entrepreneurship is an incremental, cyclical process. As the number of SMEs increases in a country, a support system will arise to bolster that entrepreneurial activity. And this support system will motivate even greater entry into the entrepreneurial sector. For instance, the magazine, *Entrepreneurial Costa Rica* emerged to satisfy market demand from budding entrepreneurs, and offers articles that educate small business owners on topics such as organizing the SME, engaging in effective marketing strategies, dealing with business partners, and reaching international quality standards. This magazine's presence on newsstands, informative articles, and promotions, such as an *Entrepreneur of the Year* award, will also likely increase both the amount and success of entrepreneurship in the future.

Therefore, although a country's early efforts to promote entrepreneurship may be slow going, the pace of growth is likely to accelerate as institutions arise to support SME activity. Similarly, regulatory, cognitive, and normative institutions will not materialize at the same speed. While the regulatory environment toward entrepreneurship may emerge relatively quickly, it will take longer for knowledge and entrepreneurial skills to become widely distributed in society. And efforts to change the attitudes of a society toward an admiration of entrepreneurs will be slower, still. Therefore, even with a concerted effort by both public and private organizations, a country's progress toward building a thriving entrepreneurial sector may be incremental.

Public policies can target regulatory, cognitive, and normative pillars of a national environment. It appears that the most common public policies toward

entrepreneurship focus on the regulatory environment by offering entrepreneurs financial assistance of one sort or another. While there is evidence that these financial incentives may facilitate entry and growth of entrepreneurial ventures, they are rather blunt instruments that often do not address weaknesses in an economy's normative or cognitive environments for entrepreneurship.

A recent study reported that countries with a strong regulatory environment also had a large percentage of companies on their national stock market that were new listings, indicating that government regulatory and financial support associated with fairly advanced forms of entrepreneurship. However, the strength of the regulatory environment did not associate positively with domestic self-employment activity or the percentage of firms in the country's manufacturing sector that were SMEs. Instead, it appeared that countries with strong normative environments for entrepreneurship had a large number of local residents who chose entrepreneurial forms of employment such as self employment. And countries with a strong cognitive environment tended to have a large percentage of firms in the manufacturing sector that were SMEs, as well as many new listings on their domestic stock exchange (Spencer & Gomez, 2001). Together, these findings suggest that in addition to providing financial incentives, governments should consider policies that enhance the skill set of the country's residents, and that improve the status that entrepreneurs enjoy within the country.

Policies that bring firms together into a community may go farther. Countries may increase their likelihood of success by addressing all three pillars of the institutional environment simultaneously. In particular, by implementing policies that help SMEs form communities of entrepreneurs, governments may help firms overcome many of the obstacles

that result from their smallness or newness. Government support is not a prerequisite for such community efforts, however. Managers in SMEs may wish to coordinate community efforts on their own by identifying firms in similar circumstances and devising strategies that will yield market power, economies of scale, advancements in infrastructure, and opportunities to share knowledge.

Governments vary in their needs, as well as their capabilities to implement policies toward the small business sector. Countries launching efforts to promote domestic SME activity start with different institutional profiles for entrepreneurship. Therefore, the mix of policies that a country should pursue will vary cross-nationally. Countries vary in the relationship that exists between domestic business associations, such as industry associations and chambers of commerce, and the government. And countries vary in terms of their governments' abilities to sustain policies that support firms, industries, and sectors in their domestic economy. Some countries maintain reputations for sustaining such these policies over extended periods of time, while others are known for quickly abandoning policies that are not politically popular (Murtha & Lenway, 1994). Therefore, it is clear that a government's best strategy toward the entrepreneurial sector depends on its unique circumstances.

CONCLUSION

The small Chilean wine producers described at the beginning of this article recognized the challenges that lay before them. They needed to improve their technology, develop international marketing strategies, and manage production and human resource activities with growing sophistication. To meet these challenges, they designed a strategy to work together

within the PROFOS program in a co-operative that they named “Viñedos Valley of Maule S.A”. A PROFOS consultant assisted them in developing an export strategy. Member firms worked together to transfer technology among vineyards, set high quality standards, adopt quality control processes, and implement cost-saving technologies. Within four years, the value of the vineyards’ collective exports had increased from approximately US \$80,000 to about US \$4 million annually, and some wine labels began winning quality awards in international forums.

Government policies toward entrepreneurship have clear implications for the strategies and performance of small and new businesses within a national economy. They also have important implications for managers of larger firms. Established firms may prefer to locate foreign operations in countries that have the potential to provide an extensive supply infrastructure. For example, Intel’s manufacturing plant in Taiwan purchases about 80% of its supplies locally. In contrast, its newer plant in Costa Rica imports more than 90% of its supplies from abroad, since no domestic electronics industry yet exists (Stone, 2000). Intel’s ability to assess the likelihood that a domestic supply infrastructure will emerge to support its investment in a new country such as Costa Rica may contribute to the effectiveness of its international location decisions. Perhaps one of the reasons that Intel relies little on a local supporting infrastructure the lack of an entrepreneurial spirit in their host environment.

Policies to foster new business development and to strengthen small- and medium-sized enterprises top the policy agenda of governments across the world. More and more policy makers are looking to SMEs to spearhead technological advance, economic growth, and job creation in their national economies (Vives, 2000). Publications by multilateral organizations such as the International Monetary Fund, World Bank, International Labor

Organization, and Inter-American Development Bank have emphasized that promoting entrepreneurship can help a country foster economic development. And countries with high levels of entrepreneurial activity tend to display greater economic growth than less entrepreneurial countries (Reynolds, Hay & Camp. 1999). Clearly, public policy makers have a strong interest in understanding how to foster entrepreneurial activity within their borders. We hope that the lessons summarized here will help them with that endeavor.

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Table 1: Advantages to Community Efforts

Market Power

- ? Gaining power over suppliers by buying in bulk
- ? Shaping industry environment for new technology
- ? Building long-term relationships with buyers, suppliers, or makers of complementary products.

Building Infrastructure for Entrepreneurship or Specific Industry

- ? Building legitimacy for idea of entrepreneurship
- ? Building legitimacy for particular industry or technology
- ? Attracting supporting firms to the market (e.g., business service firms)

Economies of Scale

- ? Joint purchase/sharing of capital equipment
- ? Sharing marketing costs through co-marketing agreements
- ? Sharing administrative costs of bureaucratic activities such as ISO 9000

Knowledge Sharing

- ? Sharing knowledge about incremental advances within a new technology
- ? Sharing technical knowledge about manufacturing
- ? Sharing information about marketing issues

Figure 1: Emergence of Entrepreneurship as an Incremental and Cyclical Process

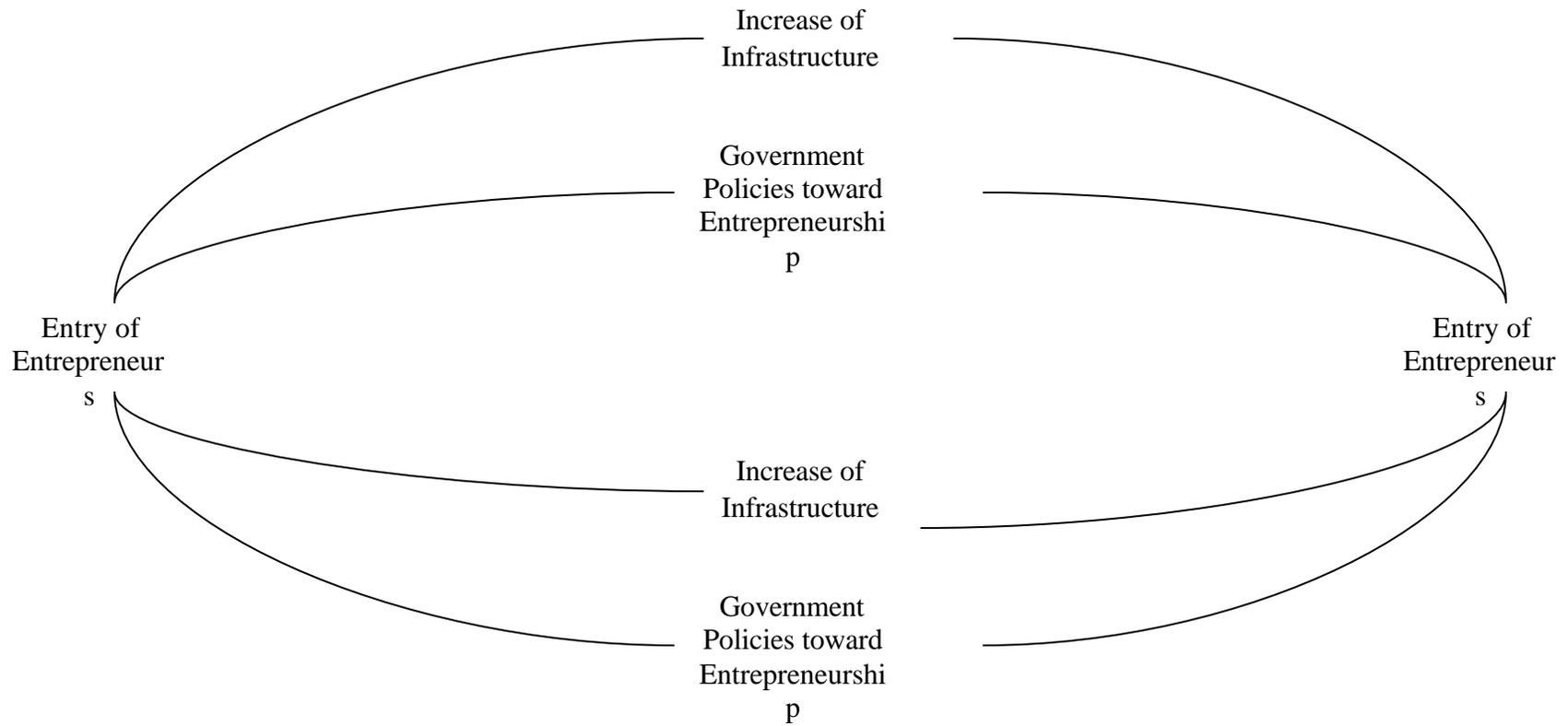
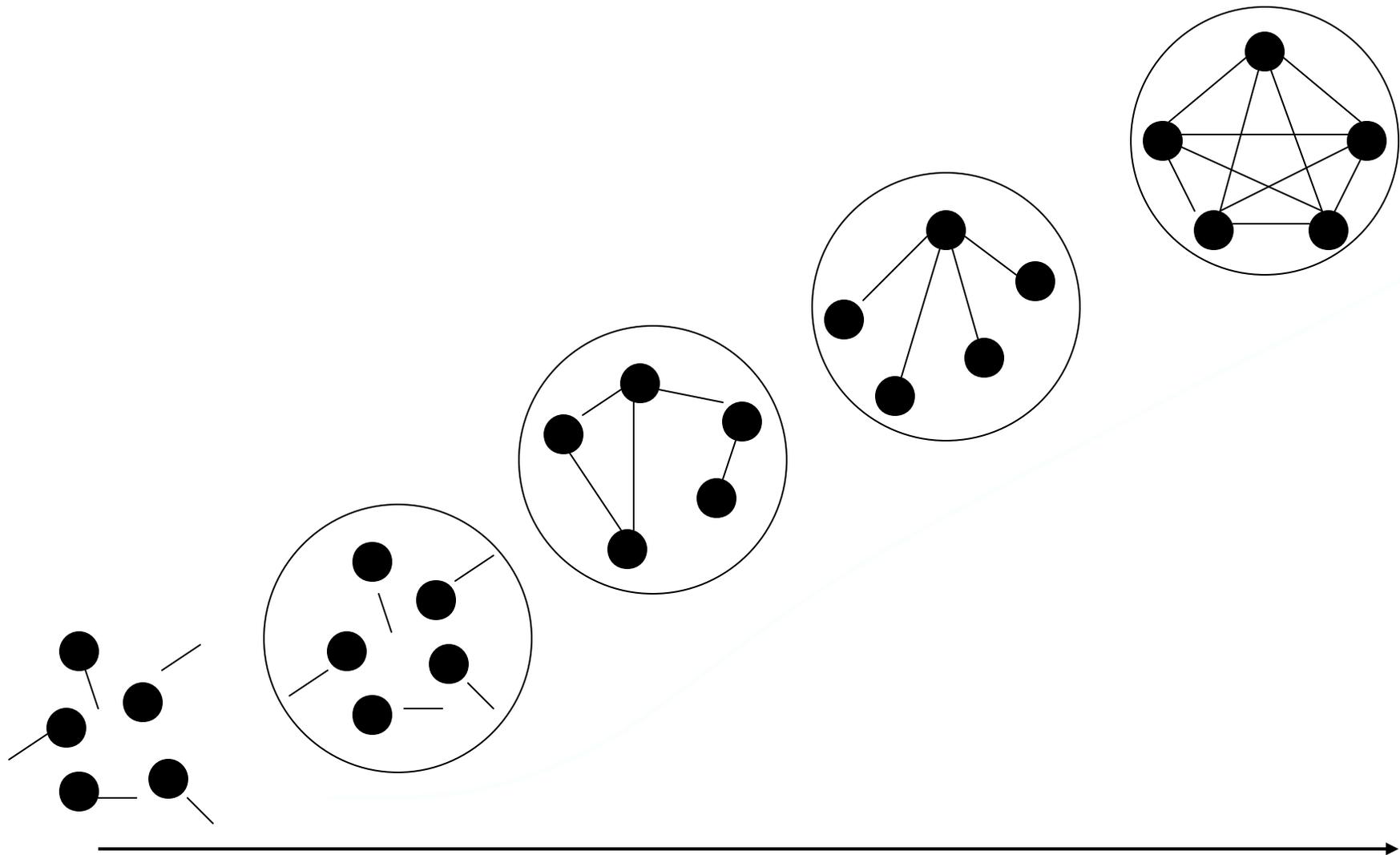


Figure 2: Objective of PROFOS



Source: PROFOS

TIME

Figure 3

Costa Rica

- Preferential Credit Lines for Small Business
- Program Simplification

Uruguay

- Tax breaks for SMEs
- Industry Sector Nucleus Program

Chile

- FOSIS Financing
- PROFOs
- PDP (Program for Development of Suppliers)

Regulatory
Environment
For
Entrepreneurship

Figure 4

Costa Rica

- Training programs
- Center for Business Incubators
- Website
- *Manual for the Investor*

Uruguay

- Assistance on applying for credit and developing business plan
- Red Propymes Training for Managers
- Industry Sector Nucleus Program
- LATU (Technological Laboratory of Uruguay)

Chile

- FOSIS training for the self-employed
- CORFO initiative to modernize technology and management
- PROFOs
- National Training and Employment Service
- PDP (Program for Development of Suppliers)

Cognitive
Environment
For
Entrepreneurship

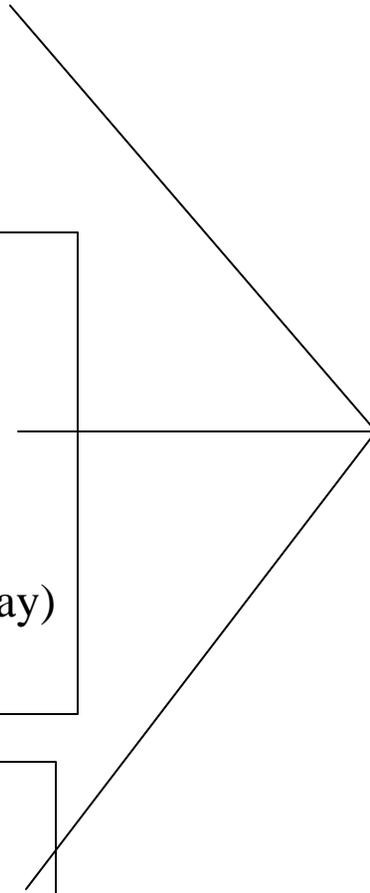


Figure 5

