A survey on institutions and new firm entry: How and why do entry rates differ in emerging markets?

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1. Introduction

Entrepreneurship and the process of new firm entry is recognized as an important element in economic development (Baumol, 1990; Wennekers and Turik, 1999). Mechanisms whereby the entry...
of new firms might contribute to economic growth and development include the generation, dissemination and application of innovative ideas enhancing efficiency and productivity (Nickell, 1996), increasing competition and providing diversity among firms (Cohen and Klepper, 1992). However, as Baumol (1990) shows, the various rules of the game through the system of respective rewards may divert entrepreneurial effort either to productive uses or to unproductive uses, which may even be destructive. De Soto (1990) has also highlighted the critical role of institutions – both formal and informal in the sense of North (1990) – in the process of entry in developing economies. In this paper, we survey the literature about the relevance of institutions for the entry of new firms in emerging markets. We draw in particular on the findings from a cross-country study in four major emerging markets – Brazil, Russia, India and China, the so-called BRIC economies.

1.1. What we know about entry and institutions

A large literature has developed to analyse the entry of new firms in developed and developing economies, including Geroski (1995), Caves (1998), Tybout (2000), Djankov et al. (2002), Klapper et al. (2006), and Bartelsman et al. (2004). From these, we know that gross entry rates in developed countries are generally high in most industries, that entry and exit rates are correlated in mature industries, and that net entry rates are generally low, reflecting structural and strategic barriers. For developing countries, the evidence on new firm entry is less well established. Tybout (2000) stresses the importance of regulatory barriers and Aw et al. (2003) finds that entry rates are relatively high in some developing countries but low in others.

It is now commonplace to argue that institutions matter for the development process and that they exert a strong determining effect on aggregate incomes in the context of developing countries (Hall and Jones, 1999; Acemoglu et al., 2001a; Rodrik et al., 2004). An innovative and important strand of this literature has attempted to quantify institutional barriers to new firm entry, using indices about the complexity of starting and doing business in different national contexts as well as about contract enforcement (Djankov et al., 2002). These data, available in the World Bank Doing Business, necessarily represent largely “formal” measures of institutions because they are constructed in a comparable fashion across 85 countries so as to facilitate the use of cross-country econometric methods. However, though it is widely recognized that institutions are complex and heterogeneous, these indicators are at best very coarse measures of the factors influencing entry in developing economies. This complexity of institutions in the literature includes a focus on property rights and historical legacies in their establishment (Acemoglu et al., 2002, 2003); on the political power of the elite and the relationship between the state and entrepreneur (Acemoglu and Robinson, 2000); and on the constraints on the elite and safeguards on state intervention and the independence of the judiciary (La Porta et al., 1999; Acemoglu et al., 2001b). All this work stresses the importance of clear property rights and legal framework and the independence of the judiciary from the political executive in the growth of countries. Easterly and Levine (1997) and Rodrik (1999) have also established the harmful effects of domestic social and ethnic conflict on the growth of developing countries. The literature on the grabbing hand of the state emphasizes the negative influence of state regulation and corruption, which is argued to motivate the growth of the informal sector (Mauro, 1995; Friedman et al., 2000; Johnson et al., 2000).

Regulatory barriers represent an important example of formal institutions. Djankov et al. (2002) find that higher regulation is not associated with positive outcomes such as better product quality but with higher levels of corruption and a greater relative size of the unofficial economy. In addition, there is a literature on the effect of regulatory conditions and bureaucracy on entry behaviour. Klapper et al. (2006) find that costly regulations hamper the creation of new firms, especially in industries with higher entry rates in the US and entry barriers. Moreover, regulations hinder entry more in countries with lower levels of corruption. Finally, there is a tradition concerned with lack of access to capital as a potential entry barrier. This stems from Bain’s (1956) argument that capital requirements pose barriers for potential entrants. In the context of institutional development, one would include access to capital markets, access to bank loans and overdraft facilities as well as the importance of informal sources of finance through access to networks of family and friends (Aidis et al., 2008).
1.2. Informal institutions and effects on entry

Informal institutions are defined in various ways in the literature. If we take as our starting point North’s (1990) definition, ‘the rules of the game .. the humanly devised constraints that shape interaction’, this includes formal rules and enforcement mechanisms and implicit rules that can take the form of taboos, customs, codes of conduct, routines and so on (North, 1990, pp. 6, 43, 83). Rules, following Ostrom (1986), need to be commonly known and the result of human action, but are not necessarily of deliberate design; private rules do not count as institutions. Voigt (2009) labels rule-breaking that is punished by the state as external institutions, which approximates to what we denote as formal institutions, and rule-breaking punished by members of society as internal institutions, which one might broadly equate with informal institutions. Alternatively, one can think about informal institutions in terms of social capital. Stiglitz (2000) interprets informal institutions in the context of social institutions or social capital and asks about the extent to which they make up for deficiencies in the market economy. Social capital is seen as tacit, productive knowledge, as part of the social glue, as a collection of networks and as an aggregation of reputations and a way to sort out reputations. He is interested in the relationship between these social institutions and market institutions, especially when market institutions are dysfunctional.

A further important distinction in this literature is that between de jure institutions, which we equate with formal institutions, and de facto institutions, which we pick up under the umbrella of informal institutions, signifying how things play out on the ground. It is acknowledged in the literature (Glaeser and La Porta, 2004; Voigt, 2009) that these are often worlds apart. It is more straight-forward although not easy to find objective measures of formal de jure institutions, such as judicial independence measured through the tenure of court judges (Persson and Tabellini, 2003), than to find objective measures of informal institutions. There are also differences in measures of institutions between ‘political’ institutions and ‘economic’ institutions. Political institutions are often focused on as the type of institutions that affect economic processes (Glaeser and La Porta, 2004) rather than specifically economic institutions. However, there are a number of differences between them: political institutions such as elections are more likely to specify procedures than economic ones, which may be more flexible for instance in the procedures associated with contracting. Punishments for non-compliance are more likely to be specified in economic institutions such as in contracting than in political institutions (Voigt, 2009).

1.3. Measuring the impact of informal as well as formal institutions on entry

A group of papers which attempted to analyse the impact of both formal and informal institutions on entry processes were published mainly in Economic Systems in 2007. The country studies are Aidis et al. (2008), Aidis and Adachi (2007), Bhaumik et al. (2007), Bruno et al. (2008), Campos and Iootty (2007), and Tian (2007), reviewed in Campos and Estrin (2008). The approach was to analyse in detail four country case studies, looking at the BRIC economies (Brazil, Russia, India, China) because of their increasing significance on the global economic stage. The disadvantage in terms of generalisability of this method was offset by the ability to analyse institutional characteristics and their interaction with entry processes in greater depth. In these papers, data on entry rates in each country is reported, as well as data on formal institutions, material on informal institutions, and their interaction. The concentration was on the four most significant dimensions of institutions in the literature in terms of effects on the creation of new firms: (a) property rights and contracting, (b) regulation and especially labour regulation, (c) access to finance and credit, and (d) infrastructure. The framework allowed an assessment of how the interaction between formal and informal institutions, for each of the four types of institution, affected entry rates and conditions in each country. We compare and develop these findings in the remainder of this paper.

It was argued that for each aspect of institutions, the interaction between formal and informal could in principle make matters better or worse for entrants. The results across the studies can be combined in order to place the BRIC countries for each aspect of institutions according to whether the formal/informal interaction has a positive or negative effect on entry. On this basis one can derive empirical regularities and comparisons that contrast China and India on the one hand, for the way that
the informal mechanisms compensate for formal institutional deficiencies, with Brazil and Russia on
the other, where over certain dimensions of institutions the informal interaction either undermines
relatively decent formal institutions or where compensating positive informal mechanisms are
entirely absent.

Before proceeding, we provide contextual data against which to consider the subsequent study of
institutions and entry. Entry rates in developed, transition and developing economies are reported in

Table 1.

It can be seen that gross entry rates in various studies of developed countries averaged around 6%
apa, compared with higher rates for transition economies of around 8% pa and even higher rates of
around 10% pa for the few developing country studies. Table 2 summarises the World Bank Doing
Business data for the BRIC countries, placing the BRIC countries in a wider context. We will use these
data in greater detail when discussing the countries individually below. Table 3 reports on
entrepreneurial activity, income distribution, number of firms per capita and the size of the informal

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<tr>
<td>Developed</td>
<td></td>
<td></td>
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</tr>
<tr>
<td>Canada</td>
<td>4.0 (1971–1979)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Italy</td>
<td></td>
<td>3.5 (1998–1999)</td>
<td></td>
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<tr>
<td>Average</td>
<td>6.0</td>
<td>12.3</td>
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<td>Developing</td>
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<td>Chile</td>
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<td>8.5 (1979–1986)</td>
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<td>Colombia</td>
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<td></td>
<td>11.9 (1977–1989)</td>
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<tr>
<td>Korea</td>
<td>3.3 (1976–1978)</td>
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<tr>
<td>Average</td>
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<td>Transition</td>
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<td>Bulgaria</td>
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<td>8.6 (1998–1999)</td>
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<td>Czech Republic</td>
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<td>11.6 (1998–1999)</td>
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<td>Poland</td>
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<td>12.0 (1998–1999)</td>
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<td>Romania</td>
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<td>18.0 (1998–1999)</td>
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<td>Average</td>
<td></td>
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<td>15.7 (1998–1999)</td>
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Table 2

Djankov data across countries: (World Bank Doing Business data).

<table>
<thead>
<tr>
<th></th>
<th>Brazil</th>
<th>China</th>
<th>India</th>
<th>Russia</th>
<th>Senegal</th>
<th>SA</th>
<th>Chile</th>
<th>Poland</th>
<th>US</th>
</tr>
</thead>
<tbody>
<tr>
<td>World Bank, Doing Business Report: starting a business, no of days (January 2004)</td>
<td>152</td>
<td>41</td>
<td>89</td>
<td>36</td>
<td>57</td>
<td>38</td>
<td>27</td>
<td>31</td>
<td>5</td>
</tr>
<tr>
<td>Starting a business, cost as % of income per capita (January 2004)</td>
<td>11.7</td>
<td>14.5</td>
<td>49.5</td>
<td>6.7</td>
<td>112.9</td>
<td>9.1</td>
<td>10</td>
<td>20.6</td>
<td>0.6</td>
</tr>
<tr>
<td>Enforcing a contract, cost as % of debt (January 20 0 4)</td>
<td>15.5</td>
<td>25.5</td>
<td>43.1</td>
<td>20.3</td>
<td>23.8</td>
<td>11.5</td>
<td>10.4</td>
<td>8.7</td>
<td>7.5</td>
</tr>
<tr>
<td>Closing a business, cost as % of estate)</td>
<td>8</td>
<td>18</td>
<td>8</td>
<td>4</td>
<td>8</td>
<td>18</td>
<td>18</td>
<td>18</td>
<td>8</td>
</tr>
<tr>
<td>Difficulty of firing index</td>
<td>70</td>
<td>40</td>
<td>90</td>
<td>20</td>
<td>70</td>
<td>60</td>
<td>20</td>
<td>30</td>
<td>10</td>
</tr>
<tr>
<td>Firing costs (weeks)</td>
<td>165</td>
<td>90</td>
<td>79</td>
<td>17</td>
<td>38</td>
<td>38</td>
<td>51</td>
<td>25</td>
<td>8</td>
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</table>
sector across our countries. Table 4 presents national data relevant to the entry process: GDP per capita, education levels and infrastructure. One notes the wide variety across the developing countries in all these measures.

The rest of the paper is structured as follows. In the following section we provide an overview of the findings, Section 3 outlines the methodology used in the studies and surveys the findings country by country. Section 4 concludes.

2. An overview of the findings

Fig. 1 summarises the entry and exit rates – both gross and net entry – and therefore survival conditions across our four countries. Details of how these were determined are given in Section 3.

Fig. 2 summarises our interpretation of the situation in each country in terms of the net effects of interaction of formal and informal mechanisms on entry rates in each of our four spheres of institutions. We argue that the effects on entry could be positive and large; in the top right-hand quadrant formal institutions and informal institutions can operate in a symbiotic way to facilitate entry. In the top left-hand quadrant, they are also positive but reliant on informal mechanisms counteracting weak formal institutions. In the lower right-hand quadrant, informal mechanisms undermine positive formal institutions and in the lower left-hand quadrant informal and formal institutions have a negative reinforcing effect on the entry process.

Except for infrastructure, we have evaluated India and China in a broadly similar way, with deficiencies in formal institutions compensated by positive informal mechanisms on entry. For India, this applies only in some states; in others the effects on entry of a lack of formal structures is aggravated by informal corruption, lawlessness and bribery. Brazil on some measures is in some areas
Fig. 1. Entry and exit rates.

<table>
<thead>
<tr>
<th></th>
<th>Gross entry</th>
<th>Gross exit</th>
<th>Net entry</th>
<th>Therefore survival of firms</th>
</tr>
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<tbody>
<tr>
<td>China</td>
<td>High</td>
<td>Low</td>
<td>High (6%)</td>
<td>Ability survive and grow – excessive – exit barriers high</td>
</tr>
<tr>
<td>Brazil</td>
<td>High (14%)</td>
<td>High (10%)</td>
<td>Medium (4%)</td>
<td>Survival of firms – on par with developed country rates?</td>
</tr>
<tr>
<td>India</td>
<td>Medium in high entry states (3-4%)</td>
<td>Low</td>
<td>Medium in high entry states 3-4%</td>
<td>Excessive survival in high entry states with exit blockages</td>
</tr>
<tr>
<td>Russia</td>
<td>Low</td>
<td>Low</td>
<td>Low</td>
<td>Entry blocked at gross entry stage</td>
</tr>
</tbody>
</table>

Fig. 2. Effects on entry of various aspects of institutional structure – showing interaction of formal and informal effects in Brazil, Russia, India and China.
institutionally closer to a more developed country in its lack of constraints on entry. However, its formal deficiencies with respect to labour regulations and finance are not compensated by informal mechanisms. This phenomenon holds more generally in Russia, where the interaction between formal and informal institutions places emphasis on weak de facto property rights and contract enforcement as being the strongest deterrent to new entry.

Fig. 2 shows that in China and India, the fairly weak formal institutional structures are compensated by informal institutional mechanisms. In three areas – property rights, access to finance and labour regulation – formal potential obstacles to entry are overcome through informal mechanisms – microfinance and access to illegal credit, support for enterprises from state-owned banks, lack of enforcement of labour regulation (in most areas in China and in some states in India), and weak property rights and contract enforcement are strengthened by the force of the state or local government in both China and some Indian states. Infrastructure has a negative effect on entry in India, affecting location decisions between states, but less so for China where there are sufficient compensating informal mechanisms to support entry into most localities.

This contrasts with Russia, where on all measures of institutions formal structures have been set up or have been reformed which on paper aspire to western standards, but entry is often blocked through informal mechanisms, chiefly various forms of corruption, in the way that enforcement is implemented that supports incumbent companies at the expense of new entrants. Corruption has allowed the capture of state processes by incumbent companies that make it very difficult – due to uncertainty and arbitrariness in the way that laws and regulations are interpreted – for new enterprises to come into existence. This undermining of formal structures runs across all the major areas of institutions – property rights and contract enforcement, labour regulation, access to finance – although the effects on entry through infrastructure are less pronounced. The blocking of entry into the formal sector thus pushes new firms into the informal sector.

The picture for Brazil is diverse, with strengths of both formal and informal mechanisms in their effects on the creation of new enterprises in two areas – property rights/contract enforcement and infrastructure – but serious weaknesses in terms of labour regulation and access to finance. In these, informal mechanisms do not compensate for the effects of overregulation and the insufficient quantity of credit and lack of savings that limits particularly new firm survival. So whilst gross entry is fairly robust, exit is also quite high and net entry is around western levels at 4% per annum, but with wide variation across industries and regions. This combination of tightly enforced excessive regulation and insufficient access to credit drives firms and new entrants into the informal sector. Thus, while Brazil and Russia are both characterized by large informal sectors, their causes are different. China and India have informal sectors (around 17% of GDP and 26% of GDP, respectively) which are more in line with OECD levels, which suggests that obstacles to entering the formal economy in those countries are not insuperable.

3. Country by country analysis

We first look at the methodology employed before considering the impact of institutions on entry processes in each country. The papers surveyed in this study use a cross-country case study approach with a template outlining methods to use, the kind of material to gather, and questions to pose in interviews. This ensured the adoption of a common framework, with comparable data collection, interviews and gathering of institutional material. Material was collected on the institutional environment and on gross and net entry and exit rates. Both formal processes and regulations on the one hand and informal processes on the other were considered.

World Bank Doing Business data (see Table 2) were provided as a starting point and researchers were asked to deepen this enquiry to gain a better understanding as to how representative these data were or whether practices differed substantially from this aggregate picture. The teams were invited to probe further into the formal barriers and to provide examples and illustrations of how they worked in practice in each country. Two formal processes were selected to explore in further detail: bankruptcy and exit procedures, because important differences between developed and emerging markets were apparent in these procedures, and contract enforcement, to establish whether the aggregate data fully reflected the differences in formal procedures relating to enforceability of contracts.
In terms of informal practices attention was focused on various aspects of corruption – the distortion of procedures, the extent of bribery, and how it worked. Given the difficulties in establishing evidence in this area, the objective was to gather illustrative and circumstantial evidence via newspapers and interviews. The other area of informal practices was network linkages, which might replace markets and, in particular, capital markets in our countries (Khanna and Yafeh, 2005; Estrin et al., 2008). The questions asked related to finding out whom entrepreneurs approached within their network, whether these were familial linkages, how extensive these networks were, and how the specific network practices differed, for example between Chinese guanxi and Russian blat. In particular, it was explored whether these networks were conducive to entry or acted as additional obstacles to new entrants, potential entrepreneurs being treated as outsiders threatening incumbents’ rents.

We now consider the country by country findings – for Brazil, China, India and Russia – of the effects on the entry process of the four types of institutions outlined above.¹

3.1. Brazil

We find in Fig. 1 that gross entry and exit rates in 100 3-digit industry level 1996–2002 are 14% and 10% pa, giving net entry of 4% pa. There is substantial variation across industries, with lower rates in the textiles and electronics industries, for example. There is greater entry into those sectors that are more protected through exporting into the Mercosur area.² The Global Entrepreneurship Monitor data suggest substantial entrepreneurship rates of 13.5% and there are 0.079 firms per capita, compared with the US figure of 0.052.

3.1.1. Labour regulation as a significant constraint on entry, particularly net entry

Labour regulation in Brazil is very onerous, increasingly so since the mid-1990s. The World Bank data indicate that hiring and firing indices are worse than for our other countries and Investment Climate indicators indicate that labour markets are highly regulated. Labour regulation acts as a deterrent to hiring skilled labour, encouraging labour turnover and acting as a disincentive to training (World Bank Investment Climate Assessment, Brazil 2003) and these disincentives apply particularly to smaller, younger and less technologically advanced firms. Labour regulations are seen as an obstacle to growth by a much higher proportion of firms in Brazil (57% for 2003) than in India – 17% (2002) – or China – 19% (2002). Labour regulation affects survival and net entry through discouraging innovation and labour legislation affects firms’ human resource decisions, impeding technology adoption and affecting skill composition and labour productivity (Scarpetta and Tressel, 2004). In Brazil we find firms shifting workers from formal to informal arrangements to avoid compensation for dismissals or legal suits attendant on non-payment of benefits. Thus 30% of formal sector workers have worked for less than 1 year in the same firm, compared with 20% in the US (Menezes-Filho and Rodrigues, 2003). Closing a business is thought to be over-regulated because redundancy is not grounds for dismissal, with high severance pay and strong rights to job security. The Brazil ICA also points out that firms citing labour legislation as a constraint to hiring and firing employ more informal sector workers so that labour legislation affects the skill level and formality of the labour force and this affects higher R&D firms disproportionately. This underlines the linkage between formalism, regulation and the size of the unofficial economy which is borne out in Brazil where the informal economy is 42% of GDP.

3.1.2. Finance as another significant constraint on entry and net entry

Lack of access to finance and underdevelopment of financial markets is the other major area of constraint on entry in Brazil. This operates because of the weak development of capital markets, which is not mitigated through informal access to capital.

The evidence for this comes from a number of indicators reported in Table 5. There are comparable levels of access to bank loans or credit as in our other countries overall, but worse access for smaller

¹ Our data on gross entry and exit and net entry rates come from a variety of sources which are reported more fully in Tian (2007), Campos and Iootty (2007), Bhauimik et al. (2007), Aides et al. (2008) and Bruno et al. (2008).
² This contrasts with China where there are lower entry rates into more protected sectors.
than for larger firms. The role of capital markets overall is limited for the private sector, especially for small firms. This weakness relative to China or India is probably because the public sector squeezes out the private as the main borrower, and access to long term finance through international capital markets is restricted to larger firms.

The levels of reliance on retained earnings are similar in Brazil, India and China, but there is less access to informal sources of finance. Moreover, more than half of Brazilian firms that need loans do not apply for them because of the complex requirements, compared with a figure of 32% for China and 16% for India. The problem is especially severe for microfirms where the Brazilian level is three times that of Chinese or Indian firms (World Bank Investment Climate Assessment, 2003). Weak access to finance combines with regulatory requirements to tighten this constraint. Our industry case studies indicate that access to credit was harder for SMEs with low volumes of credit given, high interest rates and high default rates. There is greater protection of incumbents, with the influence of industrial policy particularly strong in electronics for instance. Thus, we find Development Bank disbursements going to expansion rather than to the setting up of new firms in this sector; entrants are largely foreign firms (Campos and Iootty, 2007). All of the above leads to a much higher proportion of firms in Brazil citing access to external finance as being an obstacle to growth.

In terms of macro constraints, shortage of finance also has an effect on entry and growth of firms. Rodrik (2004) argues that high return opportunities exist but there is a lack of domestic savings, so Brazil is constrained by deficits and the inability to get access to foreign savings due to macroimbalances and the threat of depreciation from borrowing. This concurs with the major obstacles as perceived by firms, based on the survey by Campos and Iootty (2007) where macro variables such as inflation and the exchange rate are seen as significant obstacles to new entrants. There are also high interest rates and wider spreads between lending and deposit rates in Brazil compared with Russia and China. Wide spreads probably reflect the poor legal framework with a lack of guarantees for creditors and weak creditor rights.

3.1.3. Infrastructure and property rights not a constraint on entry

There is little evidence in Table 4 that poor infrastructure or lack of property rights act as a constraint on entry in Brazil, either formally or informally. For example, the measures of electricity as a constraint on growth are lower than in China and India, although above Russia, and telephone mainlines were on a par with Russia and well above China and India, whilst its mobile telephony and internet users were well above our other countries. Brazil’s legal rules and property rights are clear, although procedures are lengthy and numerous.
3.2. China

Using the available data for net entry rates and covering only larger firms, we find entry rates in Fig. 1 to be high in China, although variable between industries and across regions (Tian, 2007). Between the late 1980s and 1992, 28 out of 38 industries had net entry of over 10%, between 1993 and 1997 it was 14 out of 37 and between 1998 and 2002, 21 out of 37. Thus, entry has been strong since the late 1980s, with a correlation between entry and growth (Tian, 2007). Net entry rates in the eastern region 1988–2002 were over 6% pa compared with 1.1% in the central region, 1.3% in the western region and around 3% in the north-eastern region. In terms of net entry rates over time, in the eastern region they ranged from 11% in the late 1980s to 16-17% in the mid-1990s, slowing to 5% in the late 1990s. There is great ease of entry and importance is given to entry by policy makers, whilst protecting incumbents from exiting.

3.2.1. Property rights and contract enforcement are weak, but state power compensates

Formal property rights in China are weak and legal independence of the judiciary is poor. There is a lack of legal infrastructure, shaky Intellectual Property Rights (IPR) and weak contract enforcement (Cao, 2004), although things are gradually improving (Hu and Jefferson, 2009). Yet in practice Chinese entrepreneurs and indeed foreign companies feel that their property rights are protected. This view has evolved gradually through the state holding residual rights in town and village enterprises and increasing recognition that private property is not at risk of expropriation (Rodrik, 2004). More formal legal rights have also more recently been extended, with the recognition of private property in 2004. The pattern in China has been of extending rules following from accepted practice on the ground, an example of the dual-track nature of reform (Lau et al., 2000). The law on IPR, for example, has been strengthened and amended in response to the growing need, as China’s patenting increases, for greater formal protection (Hu and Jefferson, 2009).

The role of the state is to complement and bolster the weak formal legal infrastructure and compensate for it. Generalized belief in the power of the Chinese state underwrites the functioning of property rights. As Rodrik puts it: ‘In a system where courts cannot be relied upon to protect property rights, letting the government hold residual rights (as they did in TVEs) in the enterprise may have been a second-best mechanism for avoiding expropriation. In such circumstances the expectation of future profits can exert a stronger discipline on the public authority than fear or legal sanction. Private entrepreneurs felt secure not because the government was prevented from expropriating them, but because sharing in the profits, it had no interest to expropriate them’ (Rodrik, 2004).

3.2.2. Labour regulation: formal regulations contrast with lack of enforcement but overstaffing and firing indices indicate obstacles to exit

There is a similar discrepancy between the stance of the Chinese government with respect to labour regulations on paper and regulatory enforcement in practice. There is a framework of employment law, with Labour Dispute Arbitration Committees around China dealing with 7000 cases between 1993 and 2001 and over 2.4 million workers (Tian, 2007). According to World Bank surveys, senior management time spent dealing with regulation has been falling and compares favourably with other emerging market economies (Table 6). This has fallen in China from 9% in 2000 to 8.1% in 2003 (Table 7). However, the labour market is intensely competitive and the government turns a blind eye in favour of employers when it comes to flouting labour law. Thus, advertisements for hiring labour show no regard for labour codes of regulation and advertised jobs have long working hours, a lack of holidays or weekends and no social care, pension or health benefits (Tian, 2007). These conditions probably help to foster a positive entry environment. However, difficulties in firing may be leading3 to overemployment; overstaffing appears to be higher in China than India or Brazil (Table 6).

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3 This picture is confirmed by Tian’s study (2007) contrasting the effect of government protection on entry and exit between the automobile sector (government protected) and the computer sector (liberalized), which finds higher entry rates in the liberalized sector, although comparable exit rates in both types of sector. Government protection has therefore been largely withdrawn in affecting entry conditions but its effects still linger over exit conditions.
Johnson et al. (1998) argue that excessive regulation leads to higher levels of corruption and to a larger informal sector seeking to avoid the grabbing hand of government. Chinese regulation by these measures does not look excessive. The size of the informal sector is relatively small (17% GNP against the OECD average of 18% (Table 3)) and the number of firms per capita is high. In addition, Global Entrepreneurship Monitor (GEM) indicators of entrepreneurship are high (Table 3) and the importance of ‘returnees’ as entrepreneurs has been encouraged by state policies and is thought to have had significant effects particularly in high-tech sectors (Prevezer and Tang, 2006). All these indicators suggest that the \textit{de facto} institutional environment for entrants is positive and that ‘informal’ forces, in this case largely attributable to the practices of the state, are counteracting weaknesses in the formal structures of property rights and contract enforcement.

3.2.3. \textit{Weakness in exit procedures leading to high net entry}

There is no formal bankruptcy code in China. The costs of exit are high and priority runs in favour of employees, then government and then creditors. Losses are therefore borne by creditors, especially banks and central government. The state is reluctant to close firms as this creates unemployment, so it allows an increase in non-performing loans on (typically state-owned) banks’ balance sheets. Firms have to go to court to establish bankruptcy. Courts have the final say in determining bankruptcy but are influenced by the Communist Party and government, and corruption in this area is high (Tian, 2007). However, the stance taken by local governments varies from province to province. The risk of bankruptcy is transferred away from the entrepreneur towards the state; the process is not market driven and this prolongs the inefficiency of incumbents and dampens the contribution of entrants towards growth and productivity. When comparing the relatively protected automobile sector with the more liberalized computer sector, the entry rate is higher in computers than in automobiles (3.8% compared with 2.6%, 1998–2002). However, entrants in both industries have higher productivity than incumbents and firms that have exited in both industries, with productivity rising over time. This is more accentuated in the computer sector, with higher productivity of entrants and lower productivity of exciters. The government tends to support the inefficiency by funding loss-makers in automobiles (Tian, 2007).

3.2.4. \textit{Access to finance – formal access via state banks, bolstered by strong informal networks}

Lack of access to credit does not act as a formal barrier to entry or survival though the formal institutions of credit and selection mechanisms for targeting productive opportunities are poorly developed. The influence of the state is strong in this area too.
There has been progress in the development of credit institutions but with severe restrictions for certain types of businesses, especially privately owned and riskier enterprises. Table 5 reports on access to formal bank loans and bank credit, which is not very high, especially for smaller firms. Firms’ reliance on either internal finance or retained earnings is correspondingly high and their reliance on informal sources of finance is also reportedly high. Entrepreneurs go to unofficial and illegal credit institutions. State-owned banks, who decide who receives loans, favour strategically important firms at the expense of SMEs. Private credit and illegal and underground credit unions, which rely on personal connections and reputation, flourish. As a small business owner said “Yes, I borrowed from a gang and I must pay them back at a high rate. However, what can I do? The door of the official banks is not open to me”.

3.2.5. Infrastructure’s effects on entry

There is no evidence to suggest that infrastructure acts as a constraint on entry in China. The proportion of firms using own generators is much lower in China (27%) than in India (61%), although higher than in Brazil (17%). Telephone mainlines per 1000 people were above the levels for India although below those of Brazil (see Table 4) and cellular subscribers and internet users were also well above Indian and Russian levels in 2002, although again below Brazil’s, and may be thought to compensate for inadequacies in landline services. Thus, in China, positive informal infrastructure outweighs the negative effects of formal deficiencies in infrastructure.

3.3. India

For India, the distinguishing feature of our definition of entry is that it is based on the establishment of new plants, not on new firm registrations. A new plant may be associated with the expansion of existing firms or the establishment of a new firm but we are unable to distinguish between those categories. Hence our measures of entry rates differ between India and the other countries.

The influence of policy changes have been particularly marked in India from 1991, with the liberalization of entry procedures and delicensing, an easing of restrictions on FDI and a move towards decentralization shifting control from the federal to state-level governments (Bhaumik et al., 2007). We note in Fig. 1 that net entry (in terms of establishment of new plants) at the national level increased from 1.4% pa in the 1980s to 2.9% in the 1990s. However, entry rates in terms of units per million population show no increase when comparing the mid-1970s with the early 1990s and 2000/2001; the level remains constant at around 150 units per million population. But the picture is more varied at the state level. One can identify higher entry/expansion states with entry rates of 3–4% pa, including in the 1980s Rajasthan, Tamil Nadu, Uttar Pradesh and Andhra Pradesh and in the 1990s Rajasthan, Tamil Nadu, Kerala, Haryana and Gujarat. There is some continuity between the periods in terms of high entry states but some new states also have high entry in the 1990s. The higher entry states for new units per million population include Tamil Nadu, Haryana, Kerala and Rajasthan (from low base), with no increase in Karnataka. There were big declines in Delhi, Maharashtra, West Bengal and Bihar, so that the low entry or declining states in the 1990s were Delhi, Bihar, Uttar Pradesh and Andhra Pradesh (Bhaumik et al., 2007).

3.3.1. Indian exit procedures

Exit procedures are poorly developed in India, so net entry rates are boosted by low exit. The main bankruptcy law and court (BIFR) emphasises restructuring rather than closure, with a reluctance to close due to the effect on unemployment. Judges decide on closure of firms at the state level, but the financial costs of bankruptcy are borne at the federal state level, passing the risk and financial costs onto central government. This is gradually changing as judges are

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4 As a banker said: “We do not have the money and only take care of it for the government. If the government wants us to lend to the loss-making SOEs we simply do it. If the government wants us to generate profits, we just lend it to the cash cows. If the government wants us to control risks, we do not lend it to the small or risky firms. Taking bribes is not unusual, but I must be careful.”

5 Rodrik and Subramanian (2004) argue that reform in the early 1980s was tilted towards favouring expansion of incumbent firms rather than new entry, whereas from the 1990s reforms were geared towards encouraging new entrants.
becoming more prone to declaring closure of firms and with harder budget constraints at state level. There is nevertheless great variation in the number of cases with the BIFR by state. High exit states include Maharashtra, Andhra Pradesh, Gujarat and Tamil Nadu, which shows some overlap with higher entry states.

Entrepreneurship is high in India: GEM data give 17.5% of its sample as entrepreneurs, compared with 10.5% in the US, which is higher than in Brazil and China. There is a high number of firms per capita (0.116 compared with 0.052 in the US) and the number of factories per million people increased in the high entry states. The informal sector is fairly small for this sample, at 26% of GDP in 2002/3, but employment in agriculture is high at over 65%.

Regional differences highlight the role of regional distinctions in the entry process. Although national legal structures and policies apply in all states, there are sufficient differences in the implementation of the legal system and security, for example of land rights, between states as to make a discussion of these issues mainly about the variation between states and the differential effect that this has on entry. The gap between India’s rich and poor regions, in per capita incomes for example, is wider between Maharashtra and Uttar Pradesh or Punjab and Madhya Pradesh than the average income between India and China.

3.3.2. Labour regulation as a bottleneck on entry/expansion in some states

The formal laws would suggest that labour regulations pose a significant constraint on entry, but business perceptions rate it much lower – 17% of the Indian sample of the World Bank Investment Climate Survey identified labour regulation as an impediment to growth – comparable to China and much below Brazil. However, the constraint is viewed as a severe bottleneck in Delhi (69%) and Karnataka (52%). Labour unionization is higher in Kerala and West Bengal, where left-wing parties are stronger, while other state governments are viewed as being pro-industry. This is in line with Besley and Burgess (2004), who found that states which introduced stricter labour regulation had lower manufacturing output, investment and productivity.

There is also considerable regional variation in the enforcement of regulations with light enforcement of laws in some states and more heavily left-leaning states tending to protect workers more overtly. State inspectors are the chief enforcers and have the power to suspend plant operations for inspections. Inspection visits may be arbitrary or excessive and can be veiled demands for bribes which are often seen as worth paying to avoid disruption to production plans. The number of inspections a year is lower in India than in China and Brazil (see Table 6). There are more inspections in low-tech sectors, whereas in China and Brazil higher tech sectors are inspected more frequently. This is improving over time, with fewer inspections in 2003 than in 2000, as is the case in all our countries. In terms of senior management time spent dealing with regulation, Table 6 shows that India fares worse than our other countries.

It is not clear whether labour regulations greatly deter new entrants: the proportion complaining of regulation and of corruption associated with it are equivalent in our ‘positive’ entry states as in the more hostile entry environments. Likewise, skill shortages are perceived as serious in a mix of high and low entry states. This may be in part because corruption has relatively benign effects in our ‘positive’ states, greasing wheels and having positive associations with profitability (World Bank ICA, 2003). Regulatory compliance involves interaction with inspectors, which provides likely openings for demands of irregular payments, but this is nevertheless positively associated with profitability and thereby location decisions: firms perceive informal payments as a transaction cost and would rather pay these amounts than undergo further inspections.

3.3.3. Property rights – unclear access to land rights affects location of entry between states, but is not a major obstacle overall

Property rights are not well developed in India, notably those concerning land ownership. This leads to unclear land ownership, widespread institutional ownership, inflexible land use and property rights, and high transaction costs (e.g. stamp duties). Land costs relative to per capita incomes are 80% higher in New Delhi or Mumbai than in Tokyo, Singapore, Jakarta or Seoul (World Bank ICA, 2003). Unclear property titles impede transactions, with ambiguity leading to litigation and supply constraints. Institutional ownership causes underutilization of prime land and inflexibility, due to
zoning difficulties and land conversion regulations, creates “dead land”. High stamp duties discourage land transactions; there is an incentive to underdeclare the value of land which adversely affects the use of land as collateral for financing. Again, this is variable by state, being particularly severe in West Bengal. Poor access to land has a negative impact on location decisions and local policies have an impact for example on zoning changes from industrial to commercial or from residential/agricultural to industrial, and this varies from state to state.

3.3.4. Infrastructure as a deterrent to location of entry

Only in India of our four countries is infrastructure a serious obstacle to growth, affecting location decisions on entry between states. This is partly because poor infrastructure is bound up with other problems of bureaucracy, regulation and excessive corruption. Table 8 reveals all measures of infrastructure in India to be significantly worse than in China, Brazil and Russia. Power supply outages are more frequent with higher proportions of firms running their own generators, it takes longer to have a phone line connected, longer to be connected to the electricity grid and transport infrastructure is worse. There have been improvements, but it remains likely to be one of the factors affecting location decisions between states on firms entering or expanding plants, according to the World Bank ICA.

Location of firms within India depends partly on the benefits of particular regions and in particular on the investment climate, which depends considerably on infrastructure and varies markedly between states in India. Firms weigh up the relative costs of business regulation, the costs of corruption, the cost and reliability of power supply, the intrusiveness of industry regulation enforcement and the ease of gaining land rights for business premises when choosing locations for entry. The better investment climate states – Maharashtra, Delhi, Gujarat, Andhra Pradesh, Karnataka, Punjab, Tamil Nadu and Haryana – also have higher entry rates and better infrastructure. Variations in access to electricity are bound up with political issues concerning the balance between urban and rural areas affecting other problems of access to land and property rights between urban and rural areas. The variation across cities in what firms pay for electricity is in part due to a complex system of

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6 For example, obsolete cotton mills in Mumbai and Ahmedabad dominate huge land parcels. The businesses cannot sell assets, and new firms cannot build in these desirable locations.

7 In particular, infrastructure is worse for small cities compared with metropolitan areas, whereas the reverse is true for China and Brazil. This is probably an indicator of underdevelopment – with inferior services in rural areas or smaller cities than in big cities – and it is worse in the low entry states with delays in power connection being particularly poor in Andhra Pradesh, Kerala and the Punjab, for example. For China and Brazil, services are worse in metropolitan areas, an indicator of congestion effects.

8 The World Bank ICA (2003) argues that things such as delays in phone connections or in shipping materials through customs have major effects on regional disparities.

9 Though it is still a major constraint in some better entry states; for instance in Karnataka, 61% of firms rate infrastructure, particularly power supply, as a major to severe bottleneck.
cross-subsidy punishing urban and rewarding agricultural users. Differentials in infrastructure between cities, e.g. in landline telephony, are highly correlated with land and electricity problems.

3.3.5. Access to finance as a major obstacle in higher entry states – especially high in Tamil Nadu, Gujarat and Haryana

Overall, access to external finance in India is adequate, with quite good access to external credit and overdraft facilities, especially compared with China, and particularly for small and microcompanies. Just over a quarter of Indian firms rate access to external finance as a severe obstacle, roughly on par with China, and much lower than Brazil’s 85%. Over half of small businesses have active bank credit lines or overdraft facilities. There is a lower reliance on retained earnings than in China and a considerable reliance on informal credit facilities, as in China, especially for SMEs (Table 5).10

3.4. Russia

Fig. 1 shows that entry rates in Russia are low by emerging market standards. Aidis and Estrin (2006) report data on the entry of new firms and entrepreneurial activity in Russia 1998–2002. The Amadeus dataset, which is restricted to firms with more than 50 employees, provides a record of formal entry and shows gross entry rates from 1999 at below 1% pa. An alternative measure that is taken from GEM indicates that the proportion of individuals creating an active firm represents 2.2% of the population in 2001. Aidis et al. (2008) use GEM data to explain rates of entrepreneurship in a cross-country sample. They find that entry rates are significantly lower in Russia than even in other former socialist economies, and even these are (negative) outliers by developed economy standards.11 This compares with gross entry rates in Brazil of 14% and net entry rates in China and India of over 6% pa and 3–4% pa, respectively. Table 1 reports gross entry rates in the 5–15% range for Europe and somewhat higher rates for developing and transition economies (Cable and Schwalbach, 1991; Klapper et al., 2006).

3.4.1. Property rights formally good but the effectiveness of legal system and judiciary weak and corruption seen as an important deterrent to entry

On paper, Russian property rights and contract enforcement are on a par with those in OECD economies. Universal property rights were granted by the 1993 Constitution and regulated by the 1994 Civil Code. However, serious issues remain in practice because of lax enforcement and failure in the protection of minority shareholder rights, creditor rights and the balance between debtors and creditors in bankruptcy hearings, plus a lack of transparency in bankruptcy and company law. Reforms in 2000 led to an improvement in transparency and the implementation of international accounting standards for many firms, and competition law in 2002 strengthened the norms and rules governing contracts. The independence of the judiciary was improved through a law of 2001 on the status of judges, which removed regional legislatures from the realm of judicial appointments, and bolstered by a new Criminal Procedure Code of 2002 strengthening the power of judges. The security of property rights came under the scrutiny of parliament in October 2003 and some issues relating to minority shareholder rights were addressed in 2004 (Granville and Leonard, 2006). The Russian Federation is classified as a ‘high compliance country’ in terms of the level of compliance with international standards for corporate governance, indicating a sound legal framework in line with OECD principles (EBRD, 2005, p. 24). Formal data on entry costs (Table 2) puts Russia as the best performer of the BRIC countries in terms of days for starting a business and on a par with Brazil for contract enforcement. Time needed to resolve overdue payments fell from 7 to 6 weeks between 2002 and 2005. Formal exit barriers are relatively lower in Russia compared with our other emerging economies.

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10 Again this is variable by state. Lack of access to finance is worse in Kerala, Karnataka, Gujarat and West Bengal than in other states – reflecting complaints about the cost of finance as much as access to external finance.

11 However, using the Ruslana dataset, which includes almost all Russian firms, including very small ones, Bruno et al. (2008) find Russian entry rates to be more similar to those observed elsewhere. They suggest that the inconsistency between the Amadeus and Ruslana findings indicates problems of small firm survival and growth in the Russian context.
3.4.2. Corruption of various sorts undermines formal property rights and contract enforcement

Corruption in Russia appears to be worse than in our other emerging market countries, worse than average for the transition countries, and worsening since 2002. Thus, Transparency International’s Corruption Perceptions Index places Russia as having much worse levels of corruption than Brazil, China and India for 1998–2004, improving somewhat to converge with Indian levels in 2002. The BEEPS survey reports a statistically significant deterioration in the perception of corruption between 2002 and 2005 in Russia compared with an overall improvement amongst transition countries (EBRD, 2005, p. 11). The percentage of contract paid to secure a government contract was around 1.5% in 2002 and increased to 1.99% in 2005, comparing favourably, however, with 2.2% for China in 2003 and 12.2% for Brazil in 2003. However, the frequency of bribery measured as a percentage of respondents who agreed to pay irregular payments or gifts appears to have been increasing from 30.6% in 1999 to 38.7% in 2002 to 39.3% in 2005, compared with 8% in Germany or South Korea or a 21% average for transition countries in 2005. Losses due to crime as a share of sales appear to be higher in Russia at around 3% for 2002 and 2005 compared with estimates for Brazil of 0.64% and for China of 0.3% in 2003.

Far from being wheel-greasing, Russian corruption is linked with deficiencies in law enforcement, whereby legislation can be interpreted in multiple ways and applied selectively by the authorities. Radaev (2002) found that over 80% of Russian entrepreneurs had suffered from broken contracts. In a survey of foreign investors, half reported substantial losses due to intellectual property violations. Industrial concentration has increased, with the largest 23 Russian business groups responsible for around 35% of industrial output and 16% of industrial workers (World Bank, 2004) and the influence of incumbents increasing alongside this concentration (Guriev and Radinsky, 2004).

In certain regions, the governor’s influence has protected incumbents who are members of the family. The region of Oryol, for instance, has been governed by Yegor Stroyev for over 16 years and critics claim that he has protected his family and friends in the running of the local economy and crushed opposition (Aidis and Adachi, 2007). Kursk has similarly been dominated by its governor Rutskoi, whose family runs local businesses and the administration (Krystanovskaya and White, 2005, in Aidis and Adachi, 2007). These forms of corruption deter entry and swell the informal sector, which measures 49% of official GDP. The number of firms per capita is much lower than in our other emerging market economies (Table 3).

3.5. Infrastructure: formally not an obstacle to entry

Russia’s infrastructure is fairly good (ratings of 3 out of 4+ in the EBRD Transition Report, 2005), especially in comparison with other transition countries. This is particularly so for electric power, railways and telecommunications, with roads and water services getting a slightly worse rating. This accords with the World Bank Doing Business and Investment Climate Assessment, where only 4.6% of firms in Russia indicated that electricity was a major constraint compared with almost 30% in India and China. Likewise, Russia has telephone connections equivalent to Brazil’s and much superior to those in India and China.

3.5.1. Labour regulation – formally low but informal practices and arbitrary nature of inspections deter entry

According to the EBRD Transition Report (2005), labour regulation is less onerous in transition economies than in developed countries. This accords with the World Development Report (2005) investment indicators, where Russia has lower proportions of firms (3%) reporting labour regulation as a constraint than India (17%), China (21%) or Brazil (57%). Djankov et al. (2002) also show Russia’s firing and exit costs to be below those of Brazil, India and China (Table 2).

On the other hand, Aidis and Adachi (2007) argue that the implementation of regulation in general through tax and inspection agencies constitutes an entry barrier. For example, the inspection

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12 An example of the deterring effects of arbitrary regulatory enforcement is in the implementation of the ‘back tax law’, which allows tax inspectors a free hand in collecting back taxes from any existing business for up to a 10-year period. It has mainly been implemented for large businesses such as Yukos but fear that it may be targeted at smaller businesses in an arbitrary fashion to boost government revenues is thought to deter entrepreneurship.
agencies have independent powers to inspect businesses at any time and there are no limits to the
duration or frequency of inspections. On average, a small enterprise was inspected 7 times a year, and
this also increases the likelihood of corruption (OPORA, 2005).

Of 80 regions covered in a survey of SMEs in Russia, conducted by OPORA in 2005, businesses in
Moscow were hardest hit by tax and sanitary inspections. As a result, business owners in Moscow
spent around 11.5% of monthly earnings on kickbacks, compared with a national figure of 8.9% (Aidis
and Adachi, 2007). Moscow is seen as a particularly hostile environment for the implementation of
regulation.

3.5.2. Access to finance – formally quite good and has improved, but in practice favours larger firms

A number of studies have identified capital constraints as a major obstacle to both starting up and
expansion of businesses in transition economies and in Russia specifically (Pissarides et al., 2003;

Finance is reported by many firms in the 2005 BEEPS survey (of transition countries) as one of the
major constraints on entrepreneurship, though this is thought to have lessened since 1999. The
obstacle is greater for locally owned than for foreign firms, for private than for state-owned ones and
for micro than for larger firms. The costs of starting up are estimated to have increased, requiring
$10,000–$20,000 compared with per capita GDP of $9800 (Aidis and Adachi, 2007). Use of external
finance for start-ups is relatively low: the OPORA survey of SMEs stated that only 16% of small
businesses across Russia use bank loans (OPORA, 2005).

As in India and China, Russian entrepreneurs rely on informal networks as sources of financial
capital (Aidis and Estrin, 2006). Such networks or ‘blat’ existed in the Soviet regime as a way of
obtaining scarce resources, but have not evolved into a substitute for the weakness of the institutional
environment in ways that networks appear to do in India and China. Rather, blat has devolved into a
sophisticated form of corruption available only to the elite (Hsu, 2005). It was always seen as antisocial
and a way of cheating the system and never acquired the moral legitimacy that such systems appear to
have acquired in India and China. Blat favours incumbent holders of power over newcomers in that it is
based on supporting existing power groups and gives disproportionate gains to elite groups (Aidis and
Estrin, 2006). Puffer and McCarthy (2001) argue that commitment and trust amongst network
members in this region are low, ties weak and network knowledge poor, with relatively few
participants.

4. Conclusions

The entry of new firms is an important aspect of the development process, influencing both the
pace and character of economic growth. The literature has recognized that in emerging markets,
institutions and regulations are a particularly significant factor determining both the entry rate
and the prospects of new firm survival and growth. This has motivated important new work
seeking to quantify the quality of institutions and their impact on entry. However, this method of
necessity loses some fineness of classification and interpretation to gain cross-country
comparability. In this paper, we have sought to supplement the approach by using a comparative
case study method. Our findings considerably enrich the literature on the impact of institutions on
entry. We confirm the importance of institutions for entry, but in contrast to the view that
different aspects of institutional quality tend to be highly correlated (see Aidis et al., 2008, for a
survey), we find different institutions to have significant impacts in different contexts. Moreover,
we identify that informal institutions can work either to undermine or substitute formal ones.
Thus, in China and India, we observe a significant degree of substitution, while in Russia, and to a
lesser extent Brazil, informal processes lead to outcomes that conflict with the objectives of the
formal arrangements. This suggests that researchers should be cautious in the interpretation of
studies that rely only on formal measures.

Our work also casts some light on the interpretation of corrupt practices and informal sector
development in emerging markets. It is too simplistic to argue that either are inherently damaging
to new firms’ entry; the impact depends on the nature of the interaction between formal and
informal institutions, notably with respect to property rights, regulation and finance. In China,
high levels of corruption act to some extent as a counter to inefficiencies in formal structures, while in Russia, corruption acts instead to debilitate those structures. In the former case, policies to eradicate corruption could in fact be damaging; instead, the institutional weaknesses underlying the corruption should be eradicated. In Russia, however, the effectiveness of the formal structures has to be strengthened at the expense of informal ones. Similarly, one suspects that part of the informal sector in Brazil might shrink on its own as formal institutional arrangements improve. In Russia, however, the large size of the informal sector is related to failures to enforce the existing regulations as intended, and it is necessary to bring informal structures in line with the formal ones.

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