

Innovation, Constraints and Success

The Case of Visible Minority Women Entrepreneurs

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Dans le contexte des coûts de transactions d'une entreprise l'auteure met en valeur un esprit d'entreprise innovateur et elle fait certaines recommandations basées sur les données

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d'une étude canadienne concernant les femmes d'affaires immigrantes de minorités visibles.

In an era concerned with socio-economic equity, women are particularly disadvantaged, but entrepreneurial activity offers an avenue for individual advancement. In the United States, for example, according to relatively recent statistics, women are starting small businesses at twice the rate of men; and women-owned enterprises now account for 25 per cent of all small businesses (Hisrich and O'Brien). In Canada, the corresponding figure for 1985 was 27 per cent, and the growth in female self-employment nationwide for that year was 5.8 per cent compared 2.8 per cent for males (Cohen).

Women in general are disadvantaged, but visible minority women who emigrate to Canada are significantly more economically and socially disadvantaged by virtue of their culture and backgrounds. Although the Canadian environment affords unlimited opportunities for entrepreneurial talent, the question arises as to whether immigrant women, especially those whose linguistic and cultural backgrounds are different, can avail themselves of or have full access to these opportunities.

As we enter a post-industrial age, knowledge-intensive service-sector activities have become central to economic activity. Women entrepreneurs, with their limited access to capital, have found the service sector a safe haven in which to invest. It seems natural, therefore, that there is a high concentration of women entrepreneurs in the service sector.

Economic activity can be thought of as transforming goods and services (altering their nature, function, and location). Such activity involves transaction costs—"friction"—which reduce efficiency in transforming goods and services. These costs are called "the costs of running

the economic system." Entrepreneurs call them "the costs of doing business." These costs may be high and they may threaten the viability of the economy and/or the business.

Transaction costs represent a double-edged sword for the entrepreneur. On one hand, "frictions" from high transaction costs at the macro level of the economy may present "niche" innovative opportunities for small-scale entrepreneurs. On the other hand, transaction costs for small scale, entrepreneurial activity may constitute a significant hurdle, especially when the enterprise is undertaken by immigrants who have different cultural backgrounds and limited experience doing business in a Canadian environment.

To what extent can policy schemes to reduce transaction costs be targeted to the specific nature of the ventures undertaken by entrepreneurial (immigrant or other) Canadian women? Entrepreneurial activity depends upon insight and initiative. With minimal initial requirements for capital (fixed and working), small-scale entrepreneurial activity holds promise to the particularly disadvantaged. It can also advance the interests of society. The supply of entrepreneurial initiative and the "derived" demand for it are dependent upon the socio-economic milieu and policies influencing it.

In recent times, ideology and circumstances have combined to constrain funded social programs that deal with economic objectives, equity, and efficiency. Interest has grown in policies that minimize the direct role of government and shift much of the burden of overcoming adversity onto the individual. In other times, when ideology and economics sustain major government participation, the entrepreneurial option remains an important "safety valve," preserving elements of individual freedom and countering inefficiencies in the system.

Early views of entrepreneurship treated it as a distinct input into production, along with land (resources), labour, and capital. It was considered a relatively static input, a "fixed" input, seen to contribute to the "u-shaped," long-run cost curve. This approach says little about supply, demand, or those policies that can change conditions of supply and demand for entrepreneurship.

Later, with the writings of Joseph Schumpeter, entrepreneurship began to be regarded as a dynamic force in the operation of an economy. The post-mercantile focus on economic growth and job creation forced a review of the role of the entrepreneur. The shift was away from the traditional economic view of entrepreneurship as an input, to Schumpeter's view of entrepreneurship as the very lifeblood of economic growth and development.

Despite Schumpeter's efforts, there remains a general lack of understanding of the role of entrepreneurship in

economic development and growth. There is even less understanding of how social policies might shape and promote entrepreneurial activity. Schumpeter focuses on innovation, which he argues is responsible for economic growth through the reorganization of existing economic activities and the development of new ones. The process of innovation is perceiving opportunities and initiating activities before others realize the opportunity.

The process of innovation

The early economic literature presented the entrepreneur

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rather abstractly, as a figure spurred on by the profit motive and alienated from all external forces. Schumpeter, on the other hand, viewed entrepreneurs as "the leaders of modern economic life," describing the "characteristic entrepreneurial function as the carrying out of new combinations" (66). If cod fish, beaver pelt, and wheat could fuel an export-led engine of development, the entrepreneur was the sparkplug. Entrepreneurial innovation was described as "the spontaneous and discontinuous change in the channels of the flows, disturbance of disequilibrium, which forever alters and displaces the equilibrium state previously existing" (67).

Innovation is then seen as a key factor of change. The process is not driven by invention or technology. Innovators take advantage of technical changes but may not necessarily be inventors. What is important to entrepreneurial activity, in Schumpeter's view, is the entrepreneur's ability to perceive the opportunity for change, and the tenacity to pursue this change.

Innovative entrepreneurial activity can be partitioned into three stages: conception, feasibility, and profitability. The conception of an idea, in its most basic form, usually does not originate with the entrepreneur. The forces that drive human invention are not well understood, whether the invention is the product of a single mind or the collective effort of a research team. For the entrepreneur, the success of the idea depends on its feasibility and economic profitability.

For an idea to be feasible, it must be technically possible to carry out the production or provide the service. The idea must also be compatible with the limited resources at the command of the entrepreneur and with his or her goals and objectives.

Innovation starts with the exploitation of an idea. The idea then finds concrete expression in terms of produc-

tion, costs, revenues, and profitability. If the concept is to be viable, it must be something that brings a profit to the enterprise—above the competitive return in capital and which covers the opportunity cost of the entrepreneur time and effort.

Entrepreneurial innovation attains maturity through the feasibility and profitability stages. Successful maturity depends on the insights and organizational skills of the entrepreneur and the economic environment in which the effort is carried out. Sustained innovation, in turn, shapes the economy and subsequent entrepreneurial activities.

Minority women entrepreneurs and innovation

In examining the entrepreneurial behaviour of female visible minority entrepreneurs and how the material conditions of her undertaking impinge on continued growth and success, it is important to look at the ways in which gender and cultural history drive her or affect her success or failure? What sorts of obstacles are encountered? What types of policies and programs recommend themselves? It was to shed light on questions such as these that in September 1993 I conducted a survey of visible minority women entrepreneurs in the Metro Toronto area.

The survey was based on personal interviews of 40 visible minority women drawn at random from lists provided by ethnic, religious, cultural, and business associations. I chose a stratified sample of all those services representing the entrepreneurial efforts of the visible minority woman entrepreneur. Furthermore, I also attempted to include the different visible minority groups—South-East Asian, Asian, African, and West Indian.

Since the focus of the study was the growth and progress of the visible minority woman's undertakings, only those businesses that had survived for a minimum of three years were investigated.

The women in the survey were all born outside Canada and immigrated to Canada in their adult years. Their choice of sectors for innovation came as no surprise. Survey results showed that 85 per cent of respondents had concentrated their efforts in the service sector. This is similar to Ontario's Ministry of Trade and Technology figures, which estimate that about 76 per cent of women entrepreneurs were involved in the service sector.

Why does the service sector lend itself so well to innovation by entrepreneurial visible minority immigrant women? Is it the nature of the work, the effects of technological change, the scale of resource requirements, the skills these women bring to the tasks, the nature of the markets served, or other factors? A Statistics Canada survey carried out in 1985 canvassed a sample of 1,829 large, medium, and small companies to study research and development spending. Forty per cent of those involved in research and development were from the service sector. Obviously, this sector does lend itself to innovation brought about by technological change.

Innovation was expressed either in the offer of a scarcely

known service/product or in the establishment of the business in a new location, or both. Most of this entrepreneurial activity consisted of exploiting "niche" opportunities where capital requirements were low, but where the rate of return on entrepreneurial effort was low as well.

Study evidence showed that, despite her valiant struggle, the innovating visible minority woman entrepreneur's efforts to achieve profitability are fraught with hurdles—some of them insurmountable. In studying the profitability of these undertakings, we attempted first to create an acceptable definition of profitability. Profitability was thus defined as the sum of the following: the

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difference between the present salary of the entrepreneur and the salary she would have earned in an alternate occupation; equity contributions; car, fuel, and maintenance of car; and retained earnings. From the survey, we found that 50 per cent of those interviewed were not operating at a profit. The other 50 per cent were making an annual profit ranging from \$1,000 to \$4,000. This profit level generated a return of five to 20 per cent on an average investment of \$20,000. (Given the precarious nature of the activities in this sample of women entrepreneurs, it would have been useful to study the case histories of failed undertakings as well. Such a sample would be harder to collect, however.)

Why were these minority women so constrained in their opportunities? Although several reasons were offered, the primary causes for the limited profitability of these entrepreneurial ventures can be attributed to transaction costs—the "costs of doing business"—which act as a constraining factor on the ability of minority women's enterprises to grow and prosper.

The transaction costs framework

Research on entrepreneurship has focused predominantly on the entrepreneurial environment, and on entrepreneurial strategies. Unfortunately, very little has been done on the obstacles facing the enterprise from within. There is too little appreciation of the fact that the very nature of these enterprises and the environment in which they operate put constraints on the efforts of the entrepreneur, constraints which in turn are reflected in the small scale of the operation and the low return from the entrepreneurial effort.

A cynical view might be that an entrepreneurial "ghetto" exists in which capable entrepreneurs work under adverse

conditions to provide low-priced services to "niche" areas, services which lower the transaction costs of business to the more-established sectors. Insofar as visible minority immigrant women face a variety of obstacles to promising wage and/or salaried employment, there is scope for systemic exploitation. To the extent that this is the case, low returns signal not that entrepreneurial activity by immigrant women should be discouraged, but that remedial measures to unshackle the innovative activity of such women be introduced.

In the efficient operation of modern enterprise, size is important. The relationship between profitability and size "...depends on the balance between internal versus external transaction costs" (Coase 340). According to Coase, entrepreneurs may be involved in two different types of activity where size is a matter of importance. The two activities are: contracting, whereby entrepreneurs obtain the goods and services they require by contracting with other firms; and producing, whereby entrepreneurs obtain capital, hire employees, and produce the goods and services they require. The first type of transaction is between the entrepreneur and the contractor and is carried on outside the firm; the second is between the employer and employee and is confined within the firm. Both transactions involve costs. Coase observes that:

when internal transaction costs are smaller than external transaction costs, then entrepreneurs expand the size of their firm and produce [internally] a large number of the component parts and services they need themselves. When internal transaction costs exceed external transaction costs, then the rational entrepreneur does not expand his/her own firm but rather purchases the goods and services required from other firms. (338)

Oliver Williamson focuses on three factors that influence transaction costs and the comparative costs of internal versus external transactions costs. These factors influence the size of the firm which will develop. The first is the efficiency of the final product market. This entails the sales of completed products to consumers. An efficient final product market calls for lengthier product runs. Steady, predictable orders are the rule in this case and are therefore conducive to the creation of large firms.

The second is intermediate product market efficiency. If the intermediate market is efficient, then firms can easily buy and sell component parts and services to each other. Efficient intermediate markets lead to small firms.

The third is organizational skill. The more educated and literate an entrepreneur is, the greater his or her ability to negotiate transactions is. The entrepreneur becomes adept at the use of modern techniques of management, thus reducing uncertainty and risk.

James Acheson uses Williamson's three factors to develop a model whereby the size of a firm may be determined. When a firm is unable to gain access to an efficient

intermediate product market, the firm is defined as a small and general unit—general in the sense that the firm makes several complete products. Such types of firms abound in underdeveloped economies. A classic example is the small family-owned store in a rural economy that offers a range of goods and services. For immigrant woman entrepreneurs, this may be the type and scale of firm with which they are most familiar.

The large, vertically integrated firm (one that in producing a particular output also manufactures its required inputs—e.g., raw material), is characteristic of a developed economy. It is usually a conglomerate of small, specialized units. Economies of scale and scope (factors which cause costs to fall over the long-term as a firm's output increases) are possible here, allowing higher profits to be generated.

The small but specialized firm is also characteristic of a developed economy. Examples are found in the food-processing industry, clothing industry, etc. Such firms are capable of generating larger entrepreneurial incomes, provided that they grow. The firm's ability to generate income is constrained not by its "specialization" but by its "smallness." If this kind of firm continues to be small, its survival can be threatened by its faster-growing competitors. In our study, the bulk of the minority women entrepreneurs fell into this category. Their survival is threatened not by the nature of the service they render nor by their lack of production or service skills, but rather by the "smallness" of their operations relative to the scope of the market and their inability to benefit from economies of scale.

Women entrepreneurs and transactions costs

Eighty per cent of the firms we surveyed are small and specialized. They are specialized, in part, because of the nature of the service-sector "niches" they have been able to exploit, but this alone does not explain neither their "smallness" nor their poor returns.

Two-thirds of the firms surveyed were not yet profitable. The basic reason behind this inability to generate profits was the fact that firms were too small. The annual turnover of these "non-profitable" firms was in the range of \$50,000 to \$75,000. This small turnover provided only marginal earnings, in the range of \$12,000 to \$20,000 per annum.

From a preliminary analysis of the survey, we identified a number of reasons for the inability of enterprises run by visible minority women to grow, and consequently, to realize a larger income.

Adam Smith believed that transaction costs rise as the scale of the firm grows. This suggests that the problems arising from larger firms could be complex and hence outrun individual capacities, placing an effective "cap" on size and entrepreneurial profits. Today, of course, there is another way around this: the aggregating of individual capacities into larger organizations. In our survey, this latter possibility was never considered, even as a distant option for the minority woman entrepreneur. She tends to

operate predominantly in the service sector—delivering a "special" product or service to a clientele built up over a period of time. Rendering these "personalized" service forecloses the possibility of contracting to provide larger volume services to "depersonalized" institutions.

Minority women entrepreneurs showed a strong reluctance to combine their efforts with other women entrepreneurs. Their preference was to turn mainly to their own family members, even if the latter lacked the necessary entrepreneurial skills. Constrained by their inability to "network" and go beyond their cultural limitations, these women were confined to small business ventures.

The firms at the centre of this study also exhibited extreme dependence upon one outside person or firm (a supplier or customer). As a result they did not exploit external factors which could be internalized through vertical integration or economies of scale, either of which could decrease the cost of a service rendered or a good produced.

The firms surveyed rendered personalized service to a patronizing clientele, placing an additional obstacle to vertical integration and large-scale production. The individual entrepreneur, in most of these cases, knew her clients on a one-to-one basis and, as such, the services rendered by her firm were specifically geared to the needs of a small, select group. At best, the entrepreneur needed to employ only the services of an accountant, a maintenance person, and possibly a purchaser. These women entrepreneurs had little time available to expand beyond such efforts. This being the case, their firms remained small with no opportunity for growth through diversification. Vertical integration as a means of achieving growth was, on all counts, totally alien to them. Growth by other means looked no more probable.

Although spurred by the desire to innovate that created the endeavour in the first place, the visible minority woman entrepreneur is constrained in her efforts to grow—not so much by a lack of demand for her product but more by the high transaction costs that confront her should she try to expand or integrate production. What policies might be devised to remedy this situation? Is it possible to construct a policy environment such that the entrepreneurial efforts of visible minority woman entrepreneurs can evolve into large integrated firms? It is only when this evolution takes place that these women can realize higher incomes by way of greater entrepreneurial returns.

Policy implications

Williamson argues that, "[t]ransaction costs economizing is the previously neglected—but key—concept for understanding organizational innovation" (89). Transaction costs determine the type of niche in which the entrepreneur operates in the first place. The "niche" often profits from reducing transaction costs for others. As we have seen, this depends primarily on organizational skill combined with the efficiency of the component market

and the ability of the individual entrepreneur to integrate vertically and expand their operation. "Economic development involves, primarily, increases in organizational skill which allow the entrepreneur to take advantage of market efficiencies" (Acheson 75).

The women entrepreneurs in the survey were constrained by the limitations of their own organizational abilities. Further work on the survey data, and further survey work, using a transaction costs perspective, is expected to support our impression that the problem is one of binding constraints. The transaction costs involved in expanding the scope or scale of a firm, in working toward vertical integration, or in augmenting one's own human capital are considerable, given the limited resources and time available to the visible minority woman entrepreneur.

William Baumol argues that a theory of entrepreneurship can be promoted not by focusing on "the means which the entrepreneur employs or the process whereby he (sic) arrives at his decisions, but by examining instead the determinants of the payoff to his (sic) activity" (252).

Entrepreneurship, however, cannot be promoted if the constraints remain binding on the small specialized firm. Returning to our model of the small, specialized, and generalized firms operated by the minority woman entrepreneur, the payoff to her activity can be increased if public policy makes it possible for her to evolve from the small generalized firm to a larger more integrated firm.

When government plays a central role (i.e., by establishing government funded programs to help women develop their business skills) the woman entrepreneur can improve on her human capital in ways which allow her to exploit the opportunities at the edges of the "niche" where innovation started. [is this what you mean? I'm not sure this sentence makes any sense.] In this context, the entrepreneur should attempt to develop skills to allow her to reduce internal transaction costs or profit from reductions in external ones.

In this context, it was discouraging to note that of the 40 women entrepreneurs interviewed only 12 had heard of professional development courses and of these 12 only three had attended these courses. This calls for better coordination and dissemination of information about professional development courses sponsored by government or private agencies.

A second area in which policy could make a positive contribution to the expansion of efforts by these women entrepreneurs is in the provision of financing on reasonable terms. Most of the women surveyed seemed to have exhausted their ready sources of funds, and could obtain additional capital only at a tremendous cost. Herein lies the opportunity for (public or private) financial sources to make funds available on a "pooled risk," "soft loan," or similar basis, with rates and pay-back periods that reflect the realities faced by the women entrepreneurs.

Economic history is replete with the successes of "big" entrepreneurs. Is there room in today's history for the

efforts of these "smaller" entrepreneurs? The answer is yes. They are a benefit to the economy, to themselves, and their actions promote social equity. The challenge is whether or not society can fashion policies that allow them to attack the constraints that hold them back, constraints that are in part due to a lack of finance capital and in part due to a lack of human capital. These constraints, further aggravated by the element of transaction costs, set limits to the growth of female entrepreneurship. This study, it is hoped, has provided some evidence for the desirability of considering both economic and non-economic factors in determining the influences on entrepreneurship as a means for socio-economic change.

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