
3 Ethnic entrepreneurship: a theoretical framework

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1 Introduction

With the recent growth of new ethnic populations in Western societies, ethnic business is no longer a matter of strictly historical interest; neither is it parochial American concern. Because new ethnic populations have grown at a time when Western economies are in a phase of slow growth and massive technological challenge, ethnic adaptation and mobility are central issues to economic research (Waldinger et al., 1990a: 13). In Europe, businesses run by persons from minority ethnic groups have always been present, but three changing historical circumstances have increased their salience and visibility over the past decades. Firstly, massive immigration from former colonies, southern Europe and North Africa has led to a considerable migration flows. Secondly, three decades of economic restructuring have led to a fundamental transformation of the labour market and a general shift away from employment in large firms to self-employment in small ones. This trend has hit certain immigrant groups much harder than indigenous populations, which is reflected by the higher unemployment rates among immigrants (Barret et al., 1996). Thirdly, the opportunity structure for ethnic business has become more favourable as Europe's changing industrial structure has led to a resurgence of small and medium-sized enterprises (Blaschke et al., 1990).

The main objective of this chapter is to develop a framework for understanding the dimensions in ethnic entrepreneurship. Factors influencing the establishment of an ethnic enterprise are multifaceted and include education, generation, the local population, the economic situation, job opportunities, location, cultural and religious differences, and the origin. The result, viewed from a macroeconomic perspective, presents a very complex and dynamic mosaic, which usually moves too fast for statistics to keep up.

This chapter begins with a conceptual consideration of the topic of ethnic entrepreneurship and examines the definition and evolution of ethnic entrepreneurship. We next discuss the different theories which can be drawn upon to frame the field. We conclude the chapter with the development of an enhanced model.

2 Defining ethnic entrepreneurship

Ethnic entrepreneurship is 'a set of connections and regular patterns of interaction among people sharing common national background or migration experiences' (Waldinger et al., 1990a:3). Since the emphasis for theoretical explanations of this phenomenon is based upon those patterns of interaction, the focus of the majority of studies in this area is the ethnic group. Various definitions for the term 'ethnic group' have been suggested. According to Yinger (1985:27) for example, an ethnic group is 'a segment of a larger society whose members are thought, by themselves or others, to have common origin and to share important segments of a common culture and who, in addition, participate in shared activities in which the common origin and culture are significant ingredients'. An alternative term used to 'ethnic' is 'immigrant entrepreneurs', which in turn would only

include the individuals who have actually immigrated over the past few decades. This definition excludes, however, members of ethnic minority groups who have been living in the country for several centuries, such as Afro-Americans in the USA, Jews in Europe or aborigines in general. 'Ethnic' on the contrary, does not exclude immigrant or minority groups. The term 'immigrants' will nevertheless be used hereafter when speaking specifically of the early stages in the process of ethnic entrepreneurship, that is, when an ethnic group is new in a host society and its members can clearly be considered as 'immigrants'.

Light and Gold (2000:3) for their part speak of 'ethnic economy', which they define as 'any ethnic or immigrant's self-employed group, its employers, their co-ethnic employees, and their unpaid family workers'. They further introduce the concept of ethnic ownership economy to distinguish between an ethnic economy that is based on property right and ownership and an 'ethnic economy whose basis is de facto control based on numbers, clustering, and organization, the ethnic-controlled economy'.

Whereas ethnic ownership economy consists of small and medium-size businesses owned by ethnic or immigrant entrepreneurs and their co-ethnic helpers and workers, ethnic control economy refers to industries, occupations, and organization of the general labor market in which co-ethnic employees (not owners) exert appreciable and persistent economic power. This power usually results from their numerical clustering, their numerical preponderance, their organization, government mandates, or all four. The 'ethnic-controlled' economy is completely independent of the 'ethnic ownership' economy. The participants in the ethnic controlled economy exert control rather than ownership authority. The authors believe that the ethnic-controlled economy permits fellow migrants to secure more and better jobs in the mainstream economy, reduce unemployment and improve working conditions.

3 Evolution of the concept

Ethnic entrepreneurship is by no means a new phenomenon, as it is a firm part of any migration, most obviously observed in the United States, where the foreign born have been overrepresented in small businesses since 1880 (Barret et al., 1996). The long history of ethnic entrepreneurship in the USA also explains why research in this subject has its roots there. An early and very prominent theory suggested that ethnic businesses are an obvious reaction to blocked opportunities in the labor market, which in many instances still holds true today. Europe, on the contrary, was at the turn of the century an emigration continent and remained very homogenous until after World War II, when large labor forces were needed by ever-growing industrial companies. Initially, the immigrants came as a temporary workforce, fulfilling jobs which required no skills and which could easily be replaced by a succession of sojourners (Waldinger et al., 1990a). As the immigrants started to settle down over time, the preconditions for ethnic businesses slowly started to evolve. In most cases, it was the ethnic community which created the demand for specific ethnic goods and services in the first place and which could only be fulfilled by co-ethnics with knowledge of tastes and buying preferences.

Markets occupied by ethnic entrepreneurs are typically characterized by low barriers of entry in terms of required capital and educational qualifications, small-scale production, high labor-intensity and low added value, while cutthroat competition reigns. This leads to the emergence of a large number of start-ups and, in turn, a high rate of failure. In order to stay ahead and remain competitive under such conditions, the temptation to

apply informal practices with respect to taxes, labor regulations, minimum wages and employing children and immigrant workers without documents is quite large (Rath and Kloosterman, 2002).

The opportunities offered by the environment of a host society have a strong influence on the propensity of immigrants to turn to self-employment as a way of absorption and upward economic mobility. These external factors influence different ethnic and immigrant groups in different ways (Razin, 2002). The decision regarding business entry, being a central part of entrepreneurial behavior, is certainly a prime object of interest. Generally speaking, individuals who have no real chance of becoming employed are 'pushed' into self-employment in contrast to individuals who are 'pulled' into self-employment, possibly from an employee status, attracted by the rewards and independence that it offers (Borooah and Hart, 1999).

The business entry decision has had a strong impact on the development of theories in ethnic entrepreneurship. Much attention has been given to the question whether cultural or structural factors influence the business entry decision and therefore are responsible for the rise of ethnic entrepreneurship. Supporters of the culturalist approach believe that immigrant groups have culturally determined features leading to a propensity to favor self-employment (Masurel et al., 2004). The structuralist approach, on the other hand, suggests that external factors in the host environment, such as discrimination or entry barriers on the labor market due to education and language deficits, pushes foreigners into self-employment. More recent approaches, which attempt to combine these two perspectives, show that a differentiated view is necessary to understand this complex phenomenon.

Today, a gradual shift away from the stereotypical ethnic-run corner shop towards more diversified sectors can be observed (Freitas, 2003). Even though these types of self-help firms persist, new sectors such as computers, global trade, leisure and recreation management, real-estate agencies and cultural enterprises are developing as well.

4 Theoretical framework

Sociology, anthropology and labor economics literature have each contributed to the development of theoretical frameworks addressing the effect of ethnicity and race on entrepreneurship. Research into ethnicity and entrepreneurship can be traced back to classic works such as those of Weber (1930), Sombart (1914) and Simmel (1950). These scholars' concept of the stranger as trader, combined with the social structure of societies and pervasive religious canons, have influenced subsequent literature about and study of ethnic entrepreneurship. Enclave theory and middleman theory are two of the primary explanatory frameworks. Ethnic business typically starts when an entrepreneur begins serving other members of the ethnic community and satisfies their specific ethnic needs (Greene and Owen, 2004). This process is facilitated when larger ethnic groups live in geographically concentrated areas. Despite being widely recognized, this theory is itself insufficient to explain the entire phenomenon.

Most initial theories on ethnic entrepreneurship stem from sociology. The disadvantage theory and the cultural theory are two major theories that can be drawn from this field to explain ethnic entrepreneurship. Disadvantage theory suggests that most immigrants have significant disadvantages hampering them upon arrival but which at the same time steer their behavior (Fregetto, 2004). Firstly, they lack human capital such as language skills,

education and experience, which prevent them from obtaining salary jobs, leaving self-employment as the only choice. Secondly, a lack of mobility due to poverty, discrimination and the limited knowledge of the local culture can lead ethnic minorities to seek self-employment. This theory sees entrepreneurship not as a sign of success but simply as an alternative to unemployment. Therefore, it is probably more adequate to explain the development of informal and illegal activities, rather than to explain the widespread creation of immigrant businesses. This is because immigrant policies deny newcomers becoming legally self-employed in the first years of their stay, when the disadvantages would be the greatest.

The cultural theory suggests that ethnic and immigrant groups are equipped with culturally determined features such as dedication to hard work, membership of a strong ethnic community, economical living, acceptance of risk, compliance with social value patterns, solidarity and loyalty, and orientation towards self-employment (Masurel et al., 2004). These features provide an ethnic resource which can facilitate and encourage entrepreneurial behavior and support the ethnic self-employed (Fregetto, 2004). Ethnic people often become aware of the advantages their own culture might offer only after arriving in the new environment: 'Whether one is English, Albanian or Mongolian, the very act of transferring to a new society with alien customs and incomprehensible language is in itself likely to heighten awareness of one's own cultural and national identity' (Jones and McEvoy, 1986: 199).

The differences in ethnic resources act also as an explanation for the different rates of self-employment between equally disadvantaged ethnic groups (Waldinger et al., 1990a). For example, cultural aspects are particularly popular for explaining the propensity of Asian people, for example, to become self-employed. The strong presence of Chinese people in the catering sector has many observers believing that a certain predisposition of the Chinese culture determines their participation in such economic sectors (Leung, 2002). New studies, however, have attempted to illustrate that these assumptions fail to consider other critical aspects of the complex phenomenon, such as employment alternatives, immigration policies, market conditions and availability of capital.

Among economic explanations, middleman minority theory is the primary explanation for ethnic entrepreneurship. Ethnic enterprises rapidly pop up with the expansion and growth of an ethnic community and include businesses such as travel agencies, garment shops, specialized grocery shops, tearooms and fast-food stands. An important prerequisite for the broad emergence of ethnic businesses within a community is a sufficient number of potential consumers of ethnic products on the one hand, but also their aim of a permanent stay in the host country; that is, the immigrants have to bring their families along. Not only is the community otherwise too small to develop the necessary demand for ethnic goods, but an additional factor hindering business creation is the large sums of money sent home to families and relatives and thus not available for start-up capital. This phenomenon was discovered at the turn of the twentieth century when comparing Jewish and Italian immigrants in New York, with the latter group not having sufficient funds for new investments (Waldinger et al., 1990b).

After a while, ethnic businesses can start to grow by engaging in trade with entrepreneurs from other ethnic groups. After reaching a critical mass and gaining acceptance within the indigenous population, they can become a viable and respectable business by expanding into the high-volume trade with the local population.

5 Models

Many of the theories previously described have been integrated into models attempting to explain the phenomenon as whole. Two commonly used models will be discussed in this section. We will then develop an enhanced model, which attempts to position the ethnic dimension into the classic entrepreneurial context.

5.1 *The interactive model*

The interactive model, conceptualized by (Waldinger et al., 1990a), suggests that the development of an ethnic business cannot be traced back to a single characteristic that is responsible for the entrepreneurial success of an ethnic group. Instead, the success of an ethnic enterprise depends on a complex interaction between opportunity structures and group resources, as displayed in Figure 3.2. These two dimensions steer the strategies an ethnic entrepreneur has to implement in order to create a viable business in an alien environment. The opportunity structures are made up of market conditions, access to ownership, job market conditions, and legal and institutional frameworks. Typically, opportunities emerge from the development of a new ethnic community. These communities have specific needs which only co-ethnics are capable of satisfying. The greater the cultural differences between the ethnic group and the host country, the greater the need for ethnic goods and the bigger the potential niche market. But no matter how big the niche market is, the opportunities it offers are limited. Access to open markets, which are typically occupied by local entrepreneurs, is often blocked through high entry barriers, either on a financial or on a knowledge basis. But not all industries in Western economies are characterized by mass production or unattainable know-how. Especially markets with low economies of scale, such as the taxi industry, can offer opportunities which immigrants can successfully pursue. Further potential lies in markets either underserved or completely abandoned by the locals, because of insufficient returns and strenuous working conditions.

The second dimension focuses on the resources shared by immigrants and ethnic people of the same origin. Here, ethnic people can draw on the resources provided by their cultural

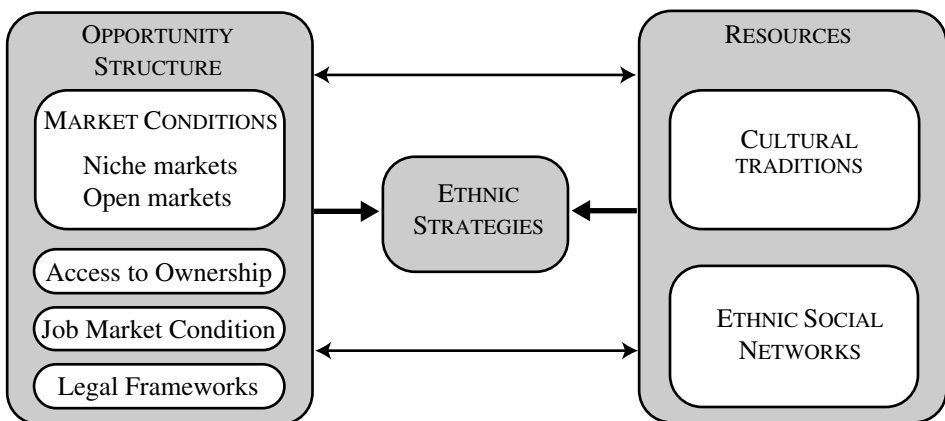


Figure 3.1 *Interactive model of ethnic entrepreneurship development; adapted from Pütz (2003) and Waldinger et al. (1990)*

traditions and ethnic social networks. The explanation of cultural traditions is based on assumptions that self-employment of certain groups is the result of their specific cultural predisposition (Pütz, 2003). The importance of cultural traditions needs nevertheless to be considered with caution and should not be overemphasized. The significance of family and ethnic networks as resources is, however, undisputed. Such interrelational connections play a crucial role in the success of an ethnic enterprise and can compensate for many disadvantages foreigners face in an alien environment.

Opportunity structures and ethnic resources constantly interact. In this sense, some aspects of the opportunity structure can be influenced and improved with the help, for example, of a strong ethnic network. Ethnic strategies are the solutions to the specific problems ethnic entrepreneurs encounter as a result of the interaction between the opportunity structures of the host society and the characteristics of their group. The problems ethnic entrepreneurs must contend with include the gathering of information, capital, training and skills, human resources, customers and suppliers, competition, and political attacks (Boissevain et al., 1990).

5.2 The mixed embeddedness model

The concept of mixed embeddedness is a further development of ethnic resources and opportunity structure. It recognizes that the structures of a local economy and legal–institutional factors exert a strong influence on the creation and existence of the small business economy in general. The influence of these factors on the access of immigrants to small business is even greater (Razin, 2002). The economic environment, however, differs widely on a national scale, offering substantially different opportunities from one region to another. This phenomenon was emphasized by Razin and Light (1998), who provided evidence for spatial variations among the same immigrant groups and variations between different ethnic groups in the same economic milieu. The local influence depends not only on the local economy structure, but also on the characteristics of the local ethnic community, such as the specific location of ethnic networks. A further attribute is discrimination through the absorbing environment but also through the local community. Opportunities should therefore be analyzed on a national, regional and local level (Boissevain et al., 1990).

The mixed embeddedness model is based on three assumptions:

1. Opportunities must not be blocked by too high barriers of entry or government regulations;
2. an opportunity must be recognized through the eyes of an potential entrepreneur as one that can provide sufficient returns; and
3. an entrepreneur must be able to seize an opportunity in a tangible way.

The main weakness of this model is that it is still in an experimental phase. The validation of the phenomenon has not yet gone beyond descriptive case studies (see, for example, Collins, 2002; Jones et al., 2002; Peters, 2002).

5.3 Merging the interactive model with the entrepreneurial process

The model depicted in Figure 3.2 is an attempt to capture the factors influencing an ethnic entrepreneur by recognizing two essential aspects: that the individual is from a different

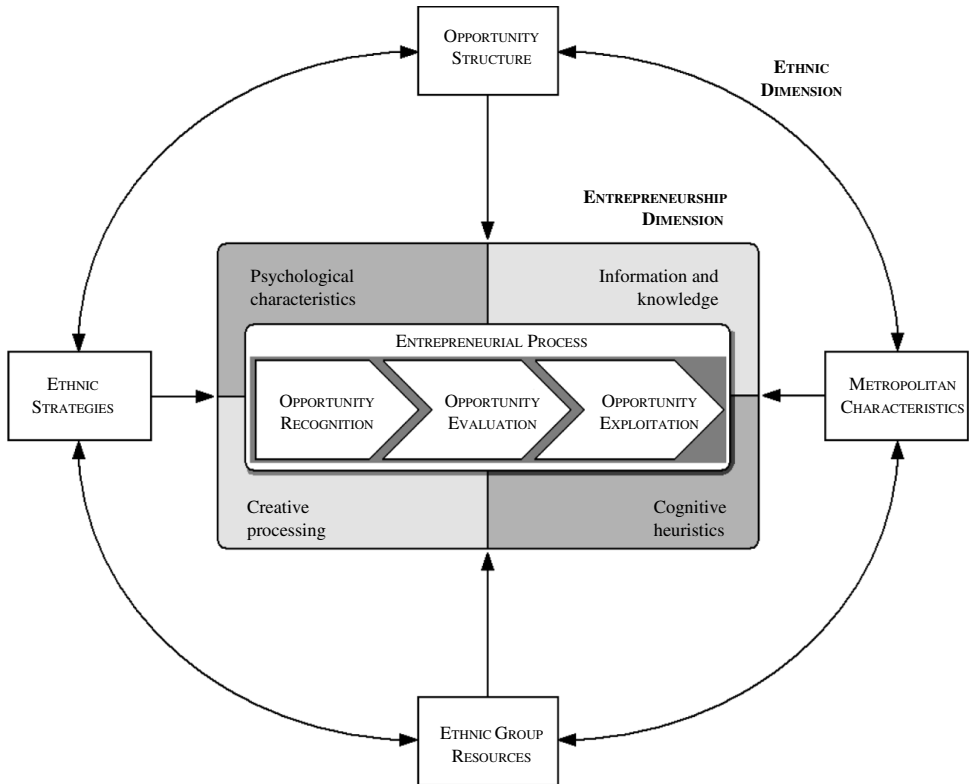


Figure 3.2 *Enhanced interactive model in the context of entrepreneurship*

ethnic group, and that this individual is an entrepreneur. As shown in Figure 3.2, the *entrepreneurship dimension* exists independently of a potential entrepreneur’s ethnic, cultural or religious background and influences the pursuit of entrepreneurial opportunities. Even people with the same nationality or from the same ethnic group have differences which affect the way they recognize and pursue opportunities.

This does not mean that the entrepreneurship dimension is not influenced by the factors present in the ethnic dimension. Schaper and Volery (2004) remarked that people can be differentiated on the basis of four aspects: firstly, specific psychological characteristics, such as the need for achievement, the belief in control over one’s life, and a propensity to take risks, typically characterize the classic entrepreneur; secondly, information and knowledge not available to others can motivate an individual to search for and exploit opportunities in a specific domain. Furthermore, networks and social relationships play a decisive part in gathering information and gaining access to important resources; thirdly, the ability to analyze an opportunity and transform it into a commercially exploitable business idea implies special skills, aptitudes, insights and circumstances, related to creative processing; fourthly, an inevitable part of being an entrepreneur is the recurrent confrontation with new problems which require quick and efficient judgements and decisions. The ability to find and develop simplifying strategies

to facilitate this crucial process is known as 'cognitive heuristics'. These four aspects influence the entrepreneurial process, which includes the recognizing, evaluating and exploiting of opportunities.

Conversely, the *ethnic dimension* encompasses the factors only relevant for ethnic entrepreneurs. The influence that the ethnic dimension exerts on the entrepreneurship dimension can vary tremendously, depending on how big the cultural differences are between host and home country, the discrimination the entrepreneur is subjected to, the progression of the social integration of the concerning ethnic group, the experience gained in the new environment, age and gender, and the education level of the entrepreneur. In the case of a highly educated and very well integrated individual, the influence of the ethnic dimension can shrink to a level where it is no longer relevant. As shown in the interactive model, the opportunity structures and the ethnic group characteristics determine the ethnic strategies and these three factors have an influence on the entrepreneurship dimension. When observing specific ethnic or immigrant groups, studies have often focused on the behavior of groups in only one particular location and have not thoroughly investigated the influence of the urban milieu on the prospects of entrepreneurship (Razin and Langlois, 1996:704). Results show, however, that spatial variations exist and are due to different metropolitan characteristics. Especially the size of communities, varying widely from one milieu to another, has an impact on the self-employment rates.

5.4 *Ethnic strategies*

It is common for ethnic entrepreneurs to set up a business which is easily portable and allows them to return to their homelands. This can be accomplished by acquiring skills or assets that can readily be transferred across geographic regions. Ethnic business is usually characterized by rather low innovativeness. Commonly, immigrants acquire the skills and capital needed to start an enterprise while employed. Subsequently, when the time is right and they feel confident about their capabilities, they take the step of establishing their own business. This stereotypical path represents a case of entrepreneurial reproduction; that is, the entrepreneurs perform a familiar activity and attempt to bring added value to their services or products through operational efficiency (Iyer and Shapiro, 1999:95).

Do ethnic entrepreneurs have any advantages over indigenous entrepreneurs? While considering the risks which can typically face an entrepreneur – financial risks, career risks, health risks and social and family risks (Schaper and Volery, 2004:38) – one notices that the career and social risks are much less distinct for an ethnic entrepreneur. Firstly, a failed ethnic entrepreneur, because of the difficult circumstances he had to begin with, will probably be accorded more understanding than his local counterpart. Secondly, the jobs many immigrants practice do not require very high standards and are thus easy to regain. Thirdly, if family members work in the enterprise, as is commonly seen among Asian entrepreneurs, the entrepreneur will still be able to spend enough time with his loved ones and not risk social exclusion.

5.4.1 *Ethnic communities and networks* Virtually all ethnic entrepreneurs make extensive use of their social networks because these are a central source of 'social capital'. Such migration networks can be defined as 'sets of interpersonal ties that link migrants, former

migrants, and non-migrants in origin and destination areas through the bonds of kinship, friendship, and shared community origin' (Massey, 1988:384). The influence of an ethnic network is often intense and reaches further than is normally presumed. The decision to migrate or to stay, the selection of a destination, and the adjustment process at the destination are massively influenced by ethnic kinship and friendship networks in which people participate (Light et al., 1993). Having restricted opportunities, a good social structure can enable or at least facilitate a job search, hiring, recruitment and training, and, more importantly, organizing the information flows between newcomers and settlers (Waldinger, 1994). Networks can substantially improve the efficiency of searches, enabling immigrants to find jobs and housing faster. The community surrounding an ethnic entrepreneur is capable of delivering a number of crucial resources for the launch and the growth of the business, such as cheap and loyal labor and capital. However, even the strongest community support can only help improve (but does not guarantee) the survivability of the enterprise when confronted with the harsh conditions of the market (Jones and Ram, 1998).

Ethnic networks can reduce the economic risks related to the creation of a new business, thus rendering the decision to become self-employed more attractive from a risk-diversification perspective. It is often the social support network of an ethnic community and the cultural background that give the required impulse to start a business. But if a successful entrepreneur seeks to grow and break out of the ethnic market serving the community's needs, these same factors can present a serious limitation (Masurel et al., 2002). In general, firm survival and growth are explained in terms of the entrepreneur's ability to acquire skills through learning-by-doing and to innovate (Jones and Ram, 1998:57). In addition, Waldinger et al. (1990a) suggest that cultural and social factors take up a central position in explaining growth in ethnic enterprises. More recent studies dismiss this idea. Basu and Goswami (1999) used a multivariate model including economic, cultural, social and managerial variables to identify the determinants of entrepreneurial growth in South Asian ethnic firms in Great Britain. Their results suggest that some individual cultural characteristics can hinder growth. The ability to overcome the inhibition to delegate responsibilities to non-family employees is just one example. The commitment to work hard, a virtue typical of Asian people, is crucial during the start-up process. Human capital factors, however, such as the entrepreneur's educational attainments and employee training in the long run have a more important effect on growth.

5.4.2 Financing ethnic businesses Gathering the necessary capital to start a small business is indisputably one of the biggest challenges in the process of business creation. This is also true for ethnic entrepreneurs. Factors such as inner-city locations, highly competitive market sectors, the absence of a 'track record', language difficulties and discrimination, often comprise difficult conditions for a bank loan (Jones and Ram, 1998). Still, ethnic businesses would not develop and prosper in such numbers if ethnic entrepreneurs were not capable of raising formal or informal equity. Contrary to conventional expectations that an ethnic business is usually a small corner shop with little capital need, the capital required to establish an enterprise can quickly surpass \$300 000 in the case of a restaurant. Several studies have shown that most ethnic entrepreneurs accumulate the bulk of their start-up capital through their own savings, some through arranged loans from relatives or within the ethnic community, whilst only a small number may acquire a

bank loan (Basu and Goswami, 1999). This is surprising, since immigrants usually arrive with only a few savings and often earn their living with unskilled labour paying barely enough to survive. Enduring long working hours, spartan living and multiple employments for a few years are usually the only conceivable methods to amass necessary savings (Boissevain et al., 1990).

A popular method for accumulating financial resources among Chinese and Korean ethnic entrepreneurs across the globe is via the rotating credit associations (RCA) (Bates, 1997). 'These methods facilitate the birth of innumerable businesses globally, because they break through red tape, facilitate capital efficiency, and allow for quick business geneses in contexts in which people lack credentials to acquire loans from traditional channels' (Iyer and Shapiro, 1999:97). RCAs typically flourish where formal financial institutions fail to satisfy the needs of large sections of the population, but also where ethnic groups are either subjected to discrimination, or cannot meet the demanded criteria. In general, RCAs can be defined as a 'a voluntary grouping of individuals who agree to contribute financially at uniformly-spaced dates towards the creation of a fund, which will then be allotted in accordance with some prearranged principle to each member of the group in turn' (Calomiris and Rajaraman, 1997:208). At periodic intervals, a member can withdraw the cash accumulated in the fund and use it for commercial purposes. Once a member has received a fund, he is excluded from the distribution of future funds, but has to continue paying until the end of the RCA period.

Concluding that the variations in the rates of self-employment among ethnic and immigrant groups can be traced back to the intensive and widespread use of RCAs among Asian entrepreneurs would, however, be inexact. Despite being a good example of a social resource, solid evidence is missing as to whether RCAs really represent a major source in financing immigrant-owned firms (Bates, 1997).

Conclusion

Ethnic entrepreneurship has become an important aspect of modern urban life and fulfills a key economic and social role for ethnic communities. The restructuring of the Western economies has changed the situation for foreigners for the worse, but at the same time has given rise to businesses with low economies of scale. This presents a new chance for immigrants to regain lost ground, but only if they are not held back by immigrant policies or subjected to invisible barriers, such as discrimination. The influence of the socio-economic context, or 'opportunity structure', will continue to affect the decision to enter self-employment.

The aim of this model was to provide a mental aid which can help position and understand the ethnic factor within the broader context of entrepreneurship. Using it as a template for the empirical analysis would, however, prove to be a very difficult task.

As shown in this chapter, a standalone theory is capable of explaining the business entry decision of a single ethnic entrepreneur and maybe of small groups with a similar immigration history and entrepreneurial activity. However, no theory can explain the phenomenon as a whole. The two models presented attempt to combine the 'culturalist' and 'structuralist' approach into an interactive concept. The theoretical frameworks described in this chapter offer guidance in investigating differences in entrepreneurial behaviors between ethnic groups, but perhaps more importantly in focusing upon different paths and strategies of the business creation process.

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