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Social networks and self-employment

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Abstract

This article applies social network concepts, developed in sociology, to the analysis of the self-employment decision. Theory suggests that if one's social network provides social support so as to reduce the costs of self-employment, those with more effective social networks may possess a greater incentive to attempt self-employment, *ceteris paribus*. Empirical investigation of this hypothesis is conducted using a unique new data set, the Wisconsin Entrepreneurial Climate Study, which allows analysis of self-employment in a social context. Results illustrate that the individual self-employment choice is highly influenced by the size and composition of the social network and that women receive less influential social support for entrepreneurial activity than men receive, a finding that may provide an explanation for gender differences in self-employment likelihood. © 2000 Elsevier Science Inc. All rights reserved.

1. Introduction

Why do some people choose self-employment over more traditional wage-employment? Why do so *few* make this choice? After all, as Aronson (1991) documents, only seven to eight percent of the labor force make such a decision. Some attributes of the self-employed are coming into focus. Education, earnings, business cycles, liquidity constraints, discrimination, and a host of personal characteristics help explain the decision to attempt self-employment, but few doubt that there is more to discover.¹ This paper pursues a different aspect of this decision by considering the immediate social environment surrounding the potential entrepreneur. In particular, we investigate the effect of an individual's social network—the depth and breadth of family, friends and acquaintances—on the self-employment choice. A social network may plausibly be a source of venture capital, initial customers,

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information, and psychological support. In these ways it may have a significant impact on the net benefits of self-employment and may be the critical factor that convinces someone to become his or her own boss.

This study proceeds as follows. First, the concept of social networks is borrowed from the sociological literature and reworked to fit more comfortably into a formal neoclassical economic model. This analysis lays a theoretical foundation for the paper's central hypothesis, that a more effective social network increases the likelihood of self-employment, *ceteris paribus*. Empirical analysis is then conducted using data that allow analysis of entrepreneurial activity within a social context. The paper concludes with a discussion of the results, which in general suggest the importance of several factors relating to social networks and the broader social environment, and more specifically suggest that commonly observed differences in male and female self-employment may be partially explained by differences in social networks between the sexes.²

2. Conceptual foundation

Walker, MacBride, and Vachon (1977) have defined a *social network* as the “set of personal contacts through which [an] individual maintains his social identity and receives emotional supports, material aid and services, information and new social contacts (p. 35).” In practice, a person's social network generally consists of his or her family members, friends, and acquaintances. To describe social networks, analysts commonly invoke three elemental concepts. The *size* (or *range*) of a social network refers to the number of individuals in the network. The *composition* of a social network typically refers to the degree to which the network is made up of either family members or friends. Thus, a social network in which the majority of members are family might be said to have a “kin-centered” composition. The notion of *frequency* in a social network refers to the regularity of contact between the individual and members of the network.

As the above definition indicates, social networks are thought to provide two types of social support: emotional and material. Emotional support takes the form of “resources which protect [someone] from the negative effects of stressful situations (McLanahan, Wedemeyer and Adelberg 1981, p. 602).” Material support involves more objective benefits, directed at finding solutions to specific problems. Much of the research into social networks has been conducted by sociologists interested in how the various elements of social networks change following a marital disruption, and how such change affects the divorced individual's well-being. In this context, emotional support might take the form of verbal encouragement for a newly divorced mother, while material support might involve loaning her money or giving her information about child day care availability. This analysis serves as a useful foundation for a further extension of social-network concepts to self-employment activity; like reactions to stress or major lifestyle changes, major labor-market decisions may also be influenced by material and emotional support from the people around us.

Previous research strongly suggests that the effectiveness with which a social network provides social support increases when the network is larger and when contact is more frequent, but social network composition appears to play an important role as well. Empirical

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