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TOWARD A GREATER UNDERSTANDING OF ENTREPRENEURSHIP AND STRATEGY IN THE INFORMAL ECONOMY

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The informal economy consists of business activities that occur outside of formal institutional boundaries but within the boundaries of informal institutions. A large gap exists between the significant importance of the informal economy to commerce around the world and the small amount of informal economy research with which entrepreneurship and strategic management scholars have been involved. As a step toward filling this gap, this special issue includes four articles with the potential to significantly advance our understanding of business activities within the informal economy. In introducing these four articles, we discuss the myriad activities that fall within the boundaries of the informal economy and distinguish between the institutional foundations of informality in developed versus developing economies. The articles included within the special issue each offer a unique understanding of how entrepreneurs are influenced by and manage their institutional contexts in various informal economy settings, providing contributions that should give rise to a series of promising future research questions.

INTRODUCTION

Society establishes rules and structure that influence how entrepreneurs complete transactions for the purpose of operating their ventures (North, 1990). However, with the objective of achieving competitive success, entrepreneurs often break the rules and redefine existing frameworks of understanding. More specifically, entrepreneurs deviate from existing product offerings and depart from societal norms and beliefs. Such departures are a means to create value in society and to bring forth ideas previously unimagined, but at times, entrepreneurs operate outside of society's laws and regulations when doing so (Webb *et al*., 2009). When breaking rules, entrepreneurs also construct new rules by delivering new products, establishing more efficient and effective processes, innovating in ways that lead to the development of new markets, and shaping new norms and beliefs (Chiasson and Saunders, 2005). At the same time, because they break then-established rules, entrepreneurs create outcomes that vary in the extent to which they are productive, unproductive, or destructive to society (Baumol, 1990).

This depiction of entrepreneurship has provided a strong foundation for research for examining the interactions of entrepreneurs and their contexts. To some degree, though, this extant understanding provides a simplified view of society and how entrepreneurs act within it. This is because societies are

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composed of a plurality of rules and structures (Ostrom, 2005). Depending on the particular society, rules and structures can be more or less codified and tangible (North, 1990), consistent versus divergent in their definitions of social acceptability, and more or less characterized by qualities that facilitate market transactions (Meyer *et al*., 2009). Entrepreneurs choose the rules upon which they operate, opting to comply with certain rules and structures while simultaneously deciding perhaps that breaking other rules might facilitate actions that they take for the purpose of creating value.

Of particular interest to us in this special issue of *Strategic Entrepreneurship Journal* is the informal economy—the activities through which entrepreneurs operate and transact specifically outside of formal institutional boundaries yet remain within the boundaries of informal institutions (Webb *et al*., 2009). Formal institutions establish the codified laws and regulations and supporting apparatuses that define the legal rules of the game, provide incentives and controls to encourage legal compliance, and establish the infrastructure for facilitating market transactions and allocating society's scarce resources (Baumol and Blinder, 2008; North, 1990). In contrast, informal institutions include the norms, values, and beliefs that shape notions of social acceptability and can also provide some localized structures to support economic activity (North, 1990). Burgeoning scholarly interest points to the significant diversity of firm and entrepreneurial activities that occur in the informal economy (Webb *et al*., 2013).

As scholars begin to clarify the diversity and complexity of the informal economy, a finer-grained understanding of its benefits and costs may emerge. As such, the objective of this special issue is to *increase scholarly understanding of how and why entrepreneurs choose to and are able to manage activities outside of formal institutional rules and structures by drawing upon more informal rules and structures within society*. For example, realizing that scholarly inquiry has largely emphasized how entrepreneurs often can break certain rules while continuing to comply with formal institutional rules, we were motivated to uncover new insights that could be gleaned from the myriad activities of entrepreneurs operating illegally yet continuing to serve sizeable markets by drawing upon the boundaries associated with informal institutions. An additional motivation underlying our efforts was based on the consideration that scholars have predominantly addressed research questions related to entrepreneurship within largely developed contexts where formal institutions provide structures to support efficient market transactions, surfacing questions as to how entrepreneurial activities differ in lesser developed contexts characterized by formal institutional voids (e.g., lack of property rights, contract law, utilities, transportation/communication infrastructures—Khanna and Palepu, 1997; Webb *et al*., 2010) where entrepreneurs instead rely on more informally construed structures.

In devising this special issue, we hope to contribute to scholarly efforts being undertaken to develop a strong theoretical foundation for understanding entrepreneurship and strategy in the informal economy. More specifically, we viewed building, extending, and developing new theory regarding the informal economy as key outcomes of this special issue. We wish to acknowledge our appreciation to all of the reviewers who invested their time and efforts to provide constructive comments to the scholars who submitted their work to the special issue for publication consideration. We also appreciate the dedicated efforts of the authors of the articles appearing in the special issue. Our sincere appreciation also goes to *Strategic Entrepreneurship Journal's* Managing Editor Lois Gast for her help in managing the special issue's deadlines, organization, and other operational needs.

In the remainder of this introduction, we first briefly review the history and influence of the informal economy. We then distinguish key differences in informal economic activities across developed and developing economies. We then summarize the special issue articles and clarify how they contribute to a greater understanding of strategy and entrepreneurship in the informal economy.

HISTORY AND COMPLEXITY OF THE INFORMAL ECONOMY

The notion of the informal economy was introduced in the early 1970s to explain the significant unregulated yet well-organized business activities that occurred in impoverished societies (Hart, 1973). However, evidence can be provided suggesting that informal economic activities occurred long before the 1970s. Acemoglu and Robinson (2012) provide numerous examples of entrepreneurship that could be considered informal in nature. For example, in fourteenth-century China, given the fear of political

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destabilization that could potentially surface, Emperor Hongwu executed hundreds of entrepreneurs for attempting to commercialize international trade given that such activities were required to be organized by the government. In England during the late 1500s and early 1600s, despite potential significant gains in productivity, Queen Elizabeth and later King James I refused to allow William Lee to commercialize his stocking frame (i.e., the mechanization of textile production) given fears that this innovation would supplant human labor, thereby creating unemployment and political instability. In Austria-Hungary during the late 1800s, the Habsburgs prohibited the dissemination of new technologies, such as steam engine railways, that could lead to creative destruction and alter the position of the traditional elites (Acemoglu and Robinson, 2012). During the 1920s and 1930s Prohibition era in the United States, a time period during which the sale of alcohol was outlawed with the Eighteenth Amendment because of the social vagaries of drunkenness, speakeasies and organized bootlegging proliferated as underground entrepreneurial activities to address continued demand.

These various activities illustrate that throughout history, entrepreneurs have sought to break or alter formal institutional rules; and, at the same time, they highlight the tension that can exist between entrepreneurs and formal institutions. While the activities described previously had the potential to create significant value for society by addressing unsatisfied market needs and increasing productivity, they were rejected by formal institutions due to real or imagined societal costs.

Myriad informal economic activities are taking place in today's economies. The informal sectors of developed economies (i.e., the United States, Western Europe, Japan) can account for 5 to 15 percent of annual GDP and more than half of annual GDP in some developing economies (i.e., Latin America, Southeast Asia, Africa) (Schneider, 2002). Table 1 highlights various examples of informal economic activities. Some readers may disagree with our classification of certain activities as falling within the informal economy, instead viewing these activities as wholly illegal and unacceptable. However, large groups in society continue to view these activities as at least somewhat acceptable, as evidenced by their magnitude. Moreover, in some cases, informality is forced upon entrepreneurs given their exclusion from the formal economy. Thus, we do not suggest that Table 1's classifications are definitive; rather, we offer them as a framework around which additional scholarly analysis can be conducted.

Each of the activities listed occurs outside of formal institutional boundaries yet can be rationalized in accordance with informal institutions. Entrepreneurs can skirt general business regulations such as those requiring formal registration, licenses, and/or other mandated certifications (Nichter and Goldmark, 2009). Failure to comply with such regulations is often viewed as socially acceptable, especially in developing economies, because the impoverished conditions within these contexts force entrepreneurs to avoid what are relatively significant costs in time and capital needed to achieve compliance (De Soto, 1989; Grosh and Somolekae, 1996). Further, compliance could undermine entrepreneurs' ability to meet their daily subsistence needs, and realizing this, even enforcement agents may turn a blind eye or undertake a negotiated enforcement strategy in dealing with informal entrepreneurs (Bromley 1978; Stoller, 1996).

Beyond general business regulations, entrepreneurs can seek to skirt laws pertaining to taxes, trademark and other forms of property rights, labor, pollution, importation, and Internet commerce. The tension between formal and informal institutions related to these activities is evidenced by two considerations: (1) the magnitude of these activities within society, and (2) the rationalizations of these activities often highlighting pro-social values and beliefs that are restricted by laws and regulations. For example, an estimated 11.2 million illegal aliens are employed in the United States (Passel and Cohn, 2011). This informal economic activity represents a global concern; there are, for example, 2 to 4 million undocumented workers in the European Union (Dawar, 2012) and more than a quarter million in Japan (Friman, 2001).

Counterfeit products also are a global informal economy issue. According to official estimates, the annual value of counterfeit products has reached nearly $250 billion (Hargreaves, 2012); however, some suggest that this estimate is low and that the actual figure may be greater than $600 billion if illegal downloading and domestically consumed counterfeits are taken into account (Bialik, 2007). Highlighting the growth of informal economic activities, the International Chamber of Commerce predicts that the value of counterfeit goods sold in 2015 will be $1.7 trillion (Hargreaves, 2012). The magnitude of these various activities underlines their

Table 1. The diversity and magnitude of informal economy activities

Source of informality	Examples	Tension	Magnitude
Skirting of general business regulations	Entrepreneurs' decisions not to register their businesses, obtain the appropriate licenses for their particular type of business, and/or otherwise disregard specific requirements for operating within a specific industry	Registration and license requirements allow governments to keep track of entrepreneurial activities, ensure that entrepreneurs are operating in society's best interests (e.g., food vendors are meeting health requirements), and inform the efficient allocation of public resources. However, the cost in terms of time and money related to registering businesses and securing licenses can hinder entrepreneurs' ability to meet their families' subsistence needs. Requirements to operate within a particular industry are too constraining, favor the traditional elites, and have undermined the innovativeness of the industry and benefits for society.	Especially in developing economies where the relative costs of registration and licenses are high, significant portions of society (30 to 50% in some developing economies, but even higher in some) operate without them, creating ambiguities for policymakers and potential risks for society (Alford and Feige, 1989).
Skirting of tax laws	Entrepreneurs' avoidance of tax payments, social security, and other required disbursements facilitated by cash transactions, failure to record transactions, and other 'creative' accounting decisions	Tax and social security payments provide a revenue base for the government to make appropriate infrastructural investments and provide for the basic needs of society. However, the payment of taxes are often perceived not to result in any benefits in terms of formal institution infrastructural investments made by the government. The government is also often viewed as incompetent and/or untrustworthy for managing social security; therefore, individuals are better off managing for their own future security.	For 2001 to 2010, it is estimated that the United States lost $3.09 trillion in its federal revenue base due to tax avoidance. Of this amount, approximately 15 percent is due to business tax evasion (Cebula and Feige, 2012). Emerging and developing economies face similar challenges. For example, Brazil loses approximately $60 billion annually to tax evasion (Baer, 2007). Lost tax revenue undermines societies' abilities to deal with budget issues and address infrastructural needs.
Skirting of property rights laws	Counterfeit products and stores, software piracy, and services that facilitate unapproved downloading (i.e., Napster during the early 2000s)	Property rights laws seek to allow businesses to appropriate value from their investments in R&D and marketing. However, the exclusivity of property rights can be viewed as enabling the rightsholders to gouge prices and limit the availability of goods to certain markets, thereby excluding a significant portion of society from being able to secure desire goods.	Although estimates vary, the value of counterfeit goods sold globally in 2008 is $650 billion. The International Chamber of Commerce predicts that the value of counterfeit goods will exceed $1.7 trillion in 2015 (more than 2% of the world's total current economic output). More than CDs and designer handbags, counterfeiting spans electronics, chemicals, pharmaceuticals, and entire stores. In addition to lost tax revenues and lost sales for formal economy firms, it is estimated that 2.5 million jobs were lost to counterfeiting in 2008 (Bialik, 2007).

Skirting of labor laws	The use of undocumented workers, sweatshop conditions, the use of child labor, and disregarding minimum wage and maximum working-hour requirements	Labor laws seek to provide employees with minimum employment standards so they are not taken advantage of by employers. However, labor laws can be viewed as too constraining, overlooking the realities of global competition and the desire for employees to ultimately have a job to meet their daily needs even if the employment conditions are exploitative.	Approximately 10 million undocumented workers are currently employed in the United States, and roughly 2 to 4 million undocumented workers in the European Union. Undocumented workers are argued to represent a cheaper source of labor, but also take jobs of local citizens. Also, 250,000 workers are estimated to work in sweatshop conditions still today in the United States, suffering in unventilated areas for long hours without breaks or overtime pay and, at times, basically imprisoned. Finally, the International Labour Organization (1996) estimates that almost 250 million children worldwide work at least part time, leading to the loss of their childhood, undermining their potential for effective schooling, and putting them in contexts where they may more likely become injured or ill.
Skirting of environmental regulations	The use of banned chemicals and fuels, exceeding specified pollution limits, disregarding limitations on the trade of exotic animals, fishing regulations, and the destruction of forests	Environmental regulations seek to preserve the long-term viability of the environment by establishing appropriate standards. However, these regulations often ban low-cost options for fuels and other raw materials that create significant entry barriers to entrepreneurs. Environmental regulations also take a much longer-term outlook that dismisses short-term demand considerations. Environmental regulations can often influence the contexts of suppliers without any visible impact on the contexts of consumers, limiting societal backlash on the skirting suppliers.	Skirting environmental regulations poses significant deterioration to the environment, including the endangerment of species, destruction of natural resources, and unhealthy living conditions. It is estimated that the annual value of wildlife smuggling is $20 billion, illegal fishing is $16.5 billion, illegal logging is $15 billion, and illegal garbage/hazardous waste trafficking is $11 billion (Liddick, 2011). While a significant issue for developed economies, developing/emerging economies also face environmental woes. For instance, many small businesses, like brick kilns and tanneries, use inexpensive yet toxic fuels and dispose of chemicals in an unsafe manner (Blackman, 2000).
Skirting of other laws and regulations (i.e., *import laws, Internet regulations,* etc.)	Importation of pharmaceuticals that have not received regulatory approval domestically but have received international approval, importation of automobiles that fail to meet a country's regulations in terms of safety or exhaust limitations, Web sites that facilitate bartering and scalping beyond specified legal limits	Other regulations can be erected to ensure the safety and health of and fair marketplace for a society's citizens. However, these laws can limit products and services to one society that are viewed as acceptable in other societies. In terms of laws defining a fair marketplace and rules for transactions, these laws can be viewed as protecting buyers, although buyers might be perfectly willing to pay more or transact via alternative methods.	Various societies have different formal institutional frameworks. Therefore, entrepreneurs can take advantage of these differences by manufacturing products in one society where they are legal and then skirt other societies' import regulations that define the products as illegal, leading to potential significant health, fair market, and environmental concerns.

social acceptability within the broader society as various stakeholders such as customers and suppliers are willing to overlook their illegality.

The social acceptability of these activities within some quarters flows from the ability of individuals to rationalize the activities with their values and beliefs as to what is appropriate. For example, entrepreneurs skirting pollution regulations may be able to exploit stakeholders' short-term concerns for less expensive goods over long-term harm caused by pollution (Webb *et al*., 2013). Similarly, entrepreneurs employing undocumented workers may (1) emphasize that these workers perform jobs that legal employees do not want to perform or (2) draw upon nationalist values by suggesting that employing undocumented workers allows them to compete against low-cost imported goods. Unregulated work conditions can be rationalized by consumers as 'out of sight, out of mind,' a necessary evil for affordable goods, and the only way to compete (Paharia and Deshpandé, 2009). Counterfeit goods may be viewed as socially acceptable due to a perception of price gouging by branded products or a desire to gain status.

The various rationalizations paint a complex picture that illustrates the recognition that economic activities, whether in the formal or informal economy, create both societal benefits and costs. Formal institutions attempt to construct rules and structures through which an ideal balance between the benefits and costs of economic activity is specified. However, norms, values, and beliefs within society can view these formal institutions as too constraining, leading individuals who possess these conflicting views to potentially favor the creation of greater benefits despite increased societal costs.

In our conceptualization, informality should be viewed as distinct from wholly criminal activities that are illegal and illegitimate. Such wholly criminal activities are 'antisocial' in nature, increasing the potential value creation for the perpetrators, but at costs for others in society (De Soto, 1989). Criminal activities can lead to sizeable organizations as well, but unlike informality, these activities are facilitated by coercion, addiction, and clandestine operations (Webb *et al*., 2013). For example, 'Silk Road' was a $1.2 billion criminal marketplace on the Internet considered to be a black-market bazaar facilitating the sale and trade of illegal goods and services, such as money laundering, computer hacking, drugs, and assassination services (Leger, 2013). As another form of wholly criminal activity, mafias and gangs represent organized criminal activities that also draw upon antisocial means, such as extortion, theft, assault, and murder as a foundation for creating value for the perpetrators. The power structures of organized criminal activities can become institutionalized to the extent that they actually supplant formal and informal institutions, erecting obstacles to both formal and informal economic activities (Sutter *et al*., 2013).

As discussed, entrepreneurs have the ability to break rules while complying with other rules. Entrepreneurs' decisions in terms of how to navigate the rules within their environments may be viewed as individual strategic choices (Siqueira, Webb, and Bruton, 2013). In making these choices, entrepreneurs weigh the value of potential opportunities in the formal, informal, and criminal economies based on their understanding of formal and informal institutions (e.g., risks of enforcement and level of social acceptability perceived in society that might facilitate growth). In reality, significant interlinkages exist across the formal, informal, and criminal economies, as entrepreneurs realize the limited capacity to exploit opportunities in one economy then decide to exploit opportunities in other economies. These phenomena might manifest when formal entrepreneurs conclude that laws are too constraining, leading them to pursue activities in the informal or criminal economies (Neuwirth, 2011).

Alternatively, these phenomena might find criminal entrepreneurs recognizing that the risks of growing outside formal institutions have risen above their comfort levels, leading them to reinvest their crime-facilitated income into formal or informal activities. Interlinkages may also surface as entrepreneurs fully transition from one economy to another or as firms in one economy transact with firms in a different economy. For example, formal economy firms have been shown to outsource activities to informal economy firms (Beneria, 1989; Benton, 1989; Liddick, 2011). In doing so, the formal economy firms reduce their operational costs while limiting their own susceptibility to enforcement (although sometimes opening themselves to social backlash).

AN INSTITUTION-BASED VIEW OF THE INFORMAL ECONOMY: COMPARING DEVELOPED VERSUS DEVELOPING ECONOMIES

Formal institutions provide laws, regulations, and supporting apparatuses to structure economic activity (North, 1990). In doing so, formal institutions

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perform a number of important roles, one of which is defining the 'rules of the game.' Once established, the rules serve as guidelines as to what are legally acceptable behaviors and outcomes for firms and entrepreneurs (Suchman, 1995). In another role, formal institutions provide incentives and controls that seek to align the behaviors and outcomes with prescribed laws and regulations (DiMaggio and Powell, 1983). The intent is to facilitate efficient market transactions and the allocation of scarce resources among firms and entrepreneurs to provide for society's needs (Baumol and Blinder, 2008). Finally, with the realization that firms and entrepreneurs alone can overlook important opportunities or fail in their efforts, formal institutions also take on a complementary role in providing for society's basic needs (e.g., food, health, security, education).

Formal institutions, however, are imperfect in how they structure economic activity. In performing these roles, formal institutions can overlook opportunities, fail to provide structure that facilitates efficient market transactions and resource allocation, and otherwise ineffectively manage the complexities of often diverse, pluralistic, and demanding societies (Khanna and Palepu, 1997). These imperfections bring to light the tensions and unique interactions that can exist between formal and informal institutions (i.e., society's more intangible norms, values, and beliefs that can also define, monitor, and enforce social acceptability).

A few conditions may be highlighted to illustrate formal institution's imperfections that lead to a stronger role of society's informal institutions. First, while formal institutions can often represent an embodiment of society's informal institutions, the diversity and pluralism of norms, values, and beliefs that characterize many societies create contexts in which formal institutions can simultaneously stand in conflict with the values and beliefs of some large societal groups (Dowling and Pfeffer, 1975; Scott, 1995). For these opposing groups, their own norms, values, and beliefs can provide a more appealing framework for guiding their behaviors relative to the overarching formal institutions, especially if the formal institutions are viewed as unfair, untrustworthy, or otherwise incompetent (Maloney, 2004).

Second, formal institutions are often massive, dynamic, multilevel systems of myriad policies and supporting apparatuses (e.g., regulatory agencies) that focus on specific geographic and regulatory domains (Ostrom, 2005). The complexity of such systems can create conflict among regulatory agencies and uncertainty regarding the meaning of policies and which policies take precedent in which contexts. Rather than engage this complexity, some individuals simply rely upon informal institutions to guide their behaviors and transactions (Fernandez-Kelly 2006; Fernandez-Kelly and Garcia, 1989).

Finally, formal institutions rely on tax revenue to support infrastructural investments (Frey, 1989). For various reasons, ranging from ineffective tax collection efforts to a less-than-adequate tax base to incompetent/corrupt use of tax revenue (Baer, 2007; Maloney, 2004), formal institutions fail to provide effective infrastructures. In such cases, societies are left to rely on informal mechanisms (Mair and Marti, 2009), such as informal lending and insurance arrangements and interhousehold transfers of resources for the purpose of guiding and supporting economic activity (Lam and Paul, 2013).

The informal economy represents the manifestation of firm and entrepreneurial activity aimed at taking advantage of or filling the void left by the imperfections of the institutional environment. More specifically, the informal economy represents those economic activities that occur outside of formal institutional boundaries but within the boundaries of informal institutions (Webb *et al*., 2009). The much larger size of the informal sectors in developing economies relative to developed economies has generally led informality to be viewed as a possible hindrance to development (Hart, 2006; Rakowski, 1994). As such, the informal economy has been the target of numerous economic development efforts as policymakers have sought to construct policies that would encourage firms and entrepreneurs to formalize their activities. The logic, in turn, suggested that increased formalization would enhance the overall tax revenue base that could facilitate formal institutions' infrastructural investments, thereby supporting economic development.

The nature of the informal economy differs across developed and developing/emerging economy contexts, due in part to the level of formal institutional development across these contexts. In developed economies, societies are generally supported by clear and consistent property rights, well-defined contract law, regulations to promote fair competition, consistently and broadly available utilities, transportation and communication infrastructures, and efficient capital markets. Moreover, the laws and regulations (and common accessibility to the benefits provided by the supporting apparatuses) in

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developed economies tend to be supported by strong enforcement agencies and judicial systems.

While inevitably characterized by some imperfections, the formal institutional environments in developed economies create a relatively clear demarcation of legality. Laws and regulations are well defined. The benefits of complying with the laws are significant, as are the penalties for breaking laws (e.g., termination of venture activities, substantial fines, and imprisonment—DiMaggio and Powell, 1983). Certainly, the vast magnitude of all of a society's activities leads to potential weaknesses in enforcement that create opportunities for entrepreneurs (and criminals) to exploit outside of the legal framework (Webb *et al*., 2009). However, the efficacy of formal institutions in providing clear incentives for compliance and significant controls on defiance, alongside the enforcement apparatuses to provide these incentives and controls, generally lead to greater proportions of individuals within society believing that operating within the legal framework offers a greater potential for value creation.

Informality in developed economies becomes an issue of legality. Operating outside of formal institutional boundaries yet within informal institutional boundaries creates real legal concerns for entrepreneurs. Informal institutions continue to play a role in how these entrepreneurs are able to operate outside of formal institutions, yet why the entrepreneurs are willing to incur the legal risk and how they are able to grow ventures outside of formal institutions become more salient questions.

In comparison, developing economies are characterized by formal institutional voids (Khanna and Palepu, 1997). More specifically, these economies are characterized by some development, but these efforts are generally uneven, isolated to primary markets in urban areas, and heterogeneous, with some institutional centers (e.g., educational versus judicial versus capital market institutions) strengthening while others remain weak (Dhanani and Islam, 2002; Granville and Leonard, 2010). Therefore, significant regions within developing economies continue to deal with poorly defined property rights, limitations in contract law, rampant corruption, unreliable utilities, limited access to transportation and communication infrastructures, and inefficient legal systems and enforcement apparatuses (Kistruck *et al*., 2011). The lack of formal institutional development undermines market transactions, contributing to significant levels of poverty within developing economies (Sumner, 2012).

The demarcation of legality becomes blurred in developing economies. Even when laws are clearly formalized, enforcement apparatuses are often inefficient and corrupt. Therefore, the meaning of the laws becomes ambiguous as enforcement is inconsistent. Moreover, compliance with laws creates costs, and the effect of these costs is amplified within these highly impoverished settings. Registration costs in terms of both capital and time can be extremely burdensome (De Soto, 1989; Grosh and Somolekae, 1996). Labor laws strongly favor employees, imposing significant costs on the employers in terms of minimum wage, hours in a workweek, and termination of employment (Portes, 1994). Pollution regulations mandate that entrepreneurs use clean, yet more expensive, fuels (Blackman, 2000).

A significant proportion of individuals in developing economies undertake entrepreneurial activities not voluntarily, but rather because they have been excluded from formal economy opportunities, resulting in a view of entrepreneurship as a more effective alternative for them and their families relative to crime and unemployment (Kingdon and Knight, 2004). Complying with legal frameworks would greatly undermine individuals' abilities to subsist, especially given that there are limited benefits associated with compliance. To some degree, formal institutions in developing economies realize the plight within their societies and, therefore, take more of a negotiated enforcement approach by enforcing noncompliance primarily in the main marketplaces only (Bromley, 1978).

Informality in developing economies becomes less of an issue of legality and more about the role of informal institutions in facilitating organizing and transacting. Operating outside of formal institutional boundaries yet within informal institutional boundaries, from a developing economy perspective, concerns how entrepreneurs operate in formal institutional voids by drawing upon informal institutions as providing complementary, substitute mechanisms for organizing and transacting. Legality remains somewhat of a concern, especially as entrepreneurs are able to enjoy growth, but the role of informal institutions surfaces more salient questions.

This gives rise to important research questions. For example, how do informal lending and insurance arrangements (i.e., means through which to assemble resources given lack of access to formal institutions) influence informal entrepreneurs' performance? What relational governance mechanisms

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do informal entrepreneurs use to govern transactions given that they are not able to draw upon formal contract law to do so? How does the lack of property rights influence business investments of entrepreneurs, and how might entrepreneurs informally recognize property rights in the informal economy? How do norms, values, and beliefs shape entrepreneurs' business decisions and consumers' purchasing decisions in informal markets?

In short, the respective formal and informal institutional environments create unique conditions of informality within developed versus developing economies. The articles included in this special issue tackle research questions that contribute to our theoretical understanding of how formal and informal institutions shape the informal economy. We briefly discuss the contributions of each article next.

ARTICLES IN THIS SPECIAL ISSUE

Following a call for papers, 38 manuscripts were received. Table 2 presents the set of articles that were accepted for inclusion in the special issue based on a blind review process.

Each article in the special issue provides a unique perspective on how entrepreneurs navigate the formal and informal institutions within their contexts and how the characteristics of their formal and informal institutional environments facilitate and/or hinder their business activities. In the first article, Lee and Hung (2014, this issue) provide a case study of the *shan-zhai* mobile phone industry in China that evolved from informal to formal status over the decade from 1998 to 2008. As the authors discuss, the Chinese state sought to support 'national champions' in the mobile phone industry, providing licenses to a limited set of firms to restrict competition. This regulation created opportunities in the informal economy, as impoverished markets went unserved and technological advances lagged within the formal economy. Lee and Hung (2014, this issue) describe various mechanisms through which the *shan-zhai* entrepreneurs framed their activities and products as socially acceptable, gathered collective momentum within the informal economy, and bridged ties to external stakeholders as a means to solidify their position by diversifying their access to resources and increasing the breadth of support for their social acceptability. The Chinese state eventually abandoned its license control and thereby essentially recognized *shan-zhai* entrepreneurs as part of the formal economy.

Lee and Hung's (2014, this issue) study examines how governing bodies, responding to pressures originating within society, can alter formal institutions to open entirely new industries, shifting them from the informal to the formal economy by merely transforming laws and regulations. The legitimation of *shan-zhai* mobile phones provides a contrasting perspective to how the temperance movement in the United States during the late 1800s and early 1900s created social change that delegitimated alcohol consumption and ultimately led to the legislative changes that founded the Prohibition Era (Hiatt, Sine, and Tolbert, 2009). While conflicting views of social acceptability are common within societies, one likely avenue for future research is discerning why and how various societal factors gain momentum within society to the extent that they lead to broad and significant changes in formal institutions.

London *et al*. (2014, this issue) examine purchasing decisions within informal markets. Whereas informal norms can play a significant role in guiding activities among entrepreneurs in the informal economy, norms can also play a significant role in guiding consumer-related decisions in contexts of formal institutional voids. The informal economy and informal markets often go hand in hand in developing and emerging economy contexts, as these contexts can be characterized by formal institutional voids that undermine the efficiency of market transactions. Instead, entrepreneurs and consumers often rely upon informal norms and other supporting mechanisms to facilitate transactions, leading to informal economies and markets, respectively (Webb *et al*., 2013). At the same time, organizations in the formal economy, such as multinational corporations and non-governmental organizations (NGOs), have undertaken efforts to address the significant social and economic opportunities in these impoverished, informal markets (Webb *et al*., 2010).

Drawing upon a multidimensional view of poverty, London and his colleagues (2014, this issue) examine the extent to which poverty-based norms influence the decision to purchase eyeglasses provided by VisionSpring, a global NGO operating in the formal economy yet serving the informal, base-of-the-pyramid markets in India. More specifically, consistent with extant research (Alkire and Foster, 2011; Hulme and Shepherd, 2003), the authors view poverty as representing not only a function of the

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Table 2. Articles within the special issue

Article	Methodology	Theoretical lens	Study context	Main contributions	Future research questions
Lee and Hung	Case study	Institutional theory (a focus on institutional entrepreneurship)	China	In examining the influences underlying the transition to the formal economy, scholars have generally focused on firm-level considerations, such as the costs of complying with formal institutions and firm success as attracting enforcement risks. In comparison, the authors discuss how the *shan-zhai* mobile phone *industry* transitioned from the informal to the formal economy. This transition was facilitated by various stakeholders within and related to the industry, undertaking institutional entrepreneurship to broaden the legitimacy of these informal economy activities in ultimately leading the formal institutions to recognize their acceptability.	Is legitimacy building in the informal economy different from how formal economy entrepreneurs gain legitimacy? What was unique about the *shan-zhai* context from other informal economy enterprises in China that allowed *shan-zhai* to grow and gain legitimacy whereas other industries have remain regulated? How do entrepreneurs take advantage of conflicts across institutional centers to more effectively operate in the informal economy? Entrepreneurs within the *shan-zhai* mobile phone industry simultaneously competed in the marketplace and cooperated to build legitimacy; what informal norms facilitated this coopetition.
London *et al.*	Survey	Institutional theory (a focus on formal institutional voids and the role of informal norms)	India	Extant research has primarily focused on the informal economy. The authors provide a complementary focus on informal markets, focusing on consumer decisions governed by informal norms given formal institutional voids. The authors draw upon: (1) a multidimensional view of poverty to examine how various forms of poverty manifest in different informal norms; and (2) a view that formal institutional voids are heterogeneous across market contexts. The authors show how these poverty-based norms influence consumers' purchasing decisions, becoming more or less salient depending on the nature of the market's formal institutional voids.	How can poverty in base-of-the-pyramid markets be reduced through interactions with the formal economy, and how would such efforts influence local poverty-based norms? Given the various facets of formal institutional voids, is there a particular approach to filling these voids that would be more effective in addressing specific forms of poverty? To the extent that formal institutional voids are filled, does this alter the influence of existing informal norms, change the informal norms that shape market decisions, or wholly reduce the influence of informal norms altogether?

Uzo and Mair	Multi-case inductive study	Institutional theory (a focus on institutional ambiguity and defiance)	Nigeria	Scholars have predominantly discussed informality as a dichotomous variable in which entrepreneurs choose to operate in the informal versus formal economy. In comparison, the authors find that entrepreneurs deviate from overarching regulations on a selective basis, choosing to comply with some regulations while deviating from other regulations. The authors present evidence to suggest that the entrepreneurs are embedded within specific domains (i.e., based on family, religion, ethnicity, or friendship) that emphasize, to varying extents, social and economic rationales that influence the degree to which the entrepreneurs choose to deviate from regulations.	Entrepreneurs can be embedded within various domains, so how do entrepreneurs resolve conflicting views on acceptability with operating in the informal economy? What are the performance implications of selective versus consistent defiance? Does political embeddedness enable greater formality or facilitate informal economy activities? Do entrepreneurs differ in the organization of their ventures depending on their level of defiance/compliance?
De Castro *et al.*	Exploratory	Institutional theory (a focus on the role of meso institutions)	The Dominican Republic	Studies examining the motivations underlying informality have largely emphasized the costs of registration/licenses as a significant entry barrier to entrepreneurs entering the formal economy in developing and emerging economies. Providing a finer-grained understanding, the authors find that entrepreneurs consider the costs of formality alongside its resulting benefits. The authors find that entrepreneurs' perceptions of the costs/benefits of formality are shaped not only by considerations of the formal institutional environments, but also by beliefs within the entrepreneurs' local communities (i.e., meso institutions). The entrepreneurs' perceptions are further influenced by their success and their operating environment, as these factors can influence the pressures emanating from formal and meso institutions.	How can policymakers influence societal perceptions regarding the benefits of formality? Policymakers require a revenue base to provide formal institutional benefits, yet unregistered entrepreneurial activities reduce tax revenues, so how can policymakers move forward in providing meaningful benefits with limited capital? To the extent that meso institutions reflect local norms and beliefs within a community, what is the role of educational institutions in changing these meso institutions? How do meso institutions influence the transaction costs for entrepreneurs operating in the informal economy relative to the formal economy? What are the major sources of cost and benefit that are considered by entrepreneurs in terms of formalizing, and how do they differ across cultural and institutional contexts?

lack of income, but also the lack of relationships and basic capabilities (e.g., education). Individuals' poverty shapes behavioral and relational norms, such as the willingness to try new things and the understood hierarchy of status of individuals, respectively. London *et al*. (2014, this issue) find that poverty-based norms influence consumers' purchasing decisions and that the influence of these informal norms is moderated by the degree of formal institutional voids in the market. This research highlights the complementary roles of formal and informal institutions in structuring economic transactions, as well as the potential for organizations to undertake activities that span the formal and informal economy.

Uzo and Mair (2014, this issue) use a multi-case inductive study set in Nigeria's version of Hollywood—Nollywood—to examine why movie producers selectively versus consistently defy formal institutional prescriptions embodied in the Nigerian Copyright Act governing employment, ownership, and distribution. The authors find that institutional ambiguity encourages defiance and, consequently, operation within the informal economy. The prescriptions set forth in the Nigerian Copyright Act are ambiguous in the sense that they view movie production as a standardized process, thereby failing to capture complexities, such as the origination of movie ideas as a cognitive yet also collective process and the need to bootstrap when unexpected problems arise. Institutional ambiguity undermines the interpretation of the law, reducing the perceptions of the law's usefulness in guiding business decisions. The movie producers instead rely on informal institutions drawn from the social groups in which they are embedded. These social groups, defined by family, ethnicity, friendship, and religion, vary in the extent to which they balance social and economic considerations. Uzo and Mair (2014, this issue) find that stronger social considerations lead to more consistent defiance of the Nigerian Copyright Act.

These findings are consistent with Garcia-Rincon (2007), who found that inconsistent policies and limited coordination across state agencies introduced ambiguities that encouraged street vendors to operate informally. Roever (2006) also attributed institutional ambiguities and resulting informal economic activities in Peru to contradictions across national and local laws and the proliferation of *ad hoc* legislation. Taken together, this research suggests that a potentially fruitful line of inquiry may be to understand the various sources of ambiguity in formal institutions, whether some sources of ambiguity are more likely to increase informality, and how formal institutions can be more effectively constructed to promote transitions to the formal economy. Similarly, in societies such as Nigeria, which is characterized by many heterogeneous informal institutions, how can formal institutions provide prescriptions that are commonly accepted across society?

In the final article, De Castro, Khavul, and Bruton (2014, this issue) explore how entrepreneurs' macro and meso institutional environments influence their decisions to formalize their businesses. The authors distinguish between (1) the macro institutional environment as the formal institutions prescribed by both local and national governments and (2) the meso institutional environment as the rules taken for granted within an entrepreneur's community. The interplay of macro and meso institutional environments that De Castro *et al*. (2014, this issue) explore highlight the tension between the prescriptions set forth by formal institutions and the informal institutions in which entrepreneurs are more locally embedded (Uzo and Mair, 2014, this issue; Webb *et al*., 2009).

Whereas prior research has emphasized significant costs of complying with formal institutions in developing and emerging economies (De Soto, 1989; Grosh and Somolekae, 1996), De Castro *et al*. (2014, this issue) find that the costs of formalizing for street vendors in the Dominican Republic are actually not overly burdensome. Rather, the street vendors choose not to formalize their businesses because they do not see any benefits provided by the formal institutions. The authors find, however, that how street vendors weigh the costs and benefits of formalizing is shaped by their success and their operating environment. More specifically, street vendors' financial success can increase the awareness of formal institutions to the vendors' business activities, prompting the vendors to register some of their activities to some degree (i.e., at the local level). At the same time, the acceptance and disregard of vendors' informal status by key stakeholders, such as banks and suppliers, provides meso institutional support for the vendors' activities. In going forward, scholars may benefit from building greater understanding of the specific benefits and costs related to (in)formality that entrepreneurs consider and how these benefits and costs vary across different societies' macro and meso institutional environments.

CONCLUSION

In this special issue, we sought to advance the theoretical foundation for understanding strategy and entrepreneurship in the informal economy. We believe the four articles offered herein collectively take a significant step forward in this regard, especially in terms of how institutional theory may inform entrepreneurship and strategy in the informal economy. Our hope is that the special issue articles will stimulate future research to examine informal economy-related phenomena from various perspectives. We hope you enjoy the articles to follow!

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