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The Liability of Poorness: Why the Playing Field is Not Level for Poverty Entrepreneurs

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Entrepreneurship is increasingly emphasized as a pathway out of poverty. However, the complex, multi-faceted nature of the poverty experience has important implications for the ability to launch and sustain viable businesses. All entrepreneurs must overcome the liabilities of newness and smallness, as reflected in a lack of legitimacy with stakeholders, inadequate resources and capabilities, an unclear identity, misunderstood roles and unclear role definitions, few established routines and procedures, and little bargaining power. However, poverty entrepreneurs face an additional barrier, which we term the liability of poorness. Four underlying dimensions of the liability of poorness are identified: literacy shortcomings, a scarcity mindset, significant non-business distractions, and the lack of financial slack or a safety net. The manner in which each of these interacting elements exacerbate the entrepreneur's ability to address the liabilities of newness and smallness is explored. It is argued that, as the liability of poorness becomes greater, the vulnerability and fragility of the poverty entrepreneur's venture are apt to increase. Under such circumstances, significant external shocks and unexpected occurrences, such as the economic shutdown resulting from the COVID-19 pandemic, typically have a more devastating impact on the ventures of the poor. Policies are needed to level the playing field.

KEY WORDS: entrepreneurship, poverty, liability of poorness, fragility, policy

Introduction

When major crises occur, the citizens of a nation do not equally share the burden. Almost always, it is the poor who are most adversely impacted. The economic crisis growing out of the COVID-19 pandemic represents a case in point. While we know the poor have borne a disproportionate amount of the cost in terms of infections and death (Sumner, Hoy, & Ortiz-Juarez, 2020), the economics of the crisis also have overwhelming implications for those in poverty. When there is any sort of economic downturn, the vulnerability of the poor means they are more significantly affected (Lustig, Fishlow, & Bourguignon, 2000; Mendoza, 2011). And when it is a dramatic downturn, such as an unprecedented economic shutdown, the

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impact is more immediate, significant, and lasts for a considerably longer time period.

Perhaps the greatest tragedy is the potential of these crises to erase any progress a person has made toward getting out of poverty. Quite simply, those in poverty that have the most to lose are often the ones who lose the most. Consider the low-income person that has managed to start a business. Venture creation represents a source of empowerment as this person creates their own job and jobs for others (Amorós & Cristi, 2011; Banerjee, Banerjee & Duflo, 2011). It can also enable him or her to create their own identity, wealth, future, sense of pride and self-worth, presence in the world, and abilities to give back and make a difference (Morris, Santos, & Neumeyer, 2020; Shantz, Kistruck, & Zietsma, 2018). Further, when the poor create sustainable enterprises, there can be positive spillovers in terms of transforming families, neighborhoods, and communities (Abraham, 2012; Amorós & Cristi, 2011; Clark, Blair, Zandiniapour, Soto, & Doyle, 1999).

The COVID-19 response and its lingering long-term economic effects will disempower many low-income entrepreneurs. A large number of these ventures will fail, while those that survive will struggle to recover the lost ground (Bekele & Worku, 2008; Fairlie & Robb, 2008; McMullen, 2011). The question is why. What is it that puts the poverty entrepreneur at a relative disadvantage? It has been noted that all entrepreneurs confront significant challenges when launching a business, as reflected in the liabilities of newness and smallness (Hannan & Freeman, 1984; Stinchcombe, 1965). Here, newness and/or smallness result in a lack of legitimacy, inadequate resources and capabilities, misunderstood roles and unclear role definitions, few established routines and procedures, an unclear identity, and little bargaining power in early stage ventures. As such, the entrepreneur is at a disadvantage, especially relative to incumbent organizations.

In this paper, we argue that the poor face an additional challenge, which we shall label the "liability of poorness." It centers on literacy gaps, a scarcity mindset, intense non-business pressures, and lack of a safety net. The collective impact of these elements has profound implications for the nature of the ventures created by the poor, how the liabilities of newness and smallness are addressed, and the performance and sustainability of these businesses. Critically, each of them contributes to the fragility of the enterprises created by the poor. This fragility, in turn, explains why these ventures are more significantly impacted by external shocks and major setbacks. It is argued that, to level the playing field, policy and community support efforts to facilitate venture creation by the poor should be re-designed to explicitly address the liability of poorness.

Difficulties in Successfully Launching a Business

Launching a business is a difficult undertaking regardless of who is involved, but is especially challenging for those in poverty (Alvarez & Barney, 2014; McMullen, 2011). Failure rates differ internationally, but it is generally estimated that between 45 and 55 percent of new ventures fail within the first five years of operation (Lowe, McKenna, & Tibbits, 1991; Stangler; 2010; Watson & Everett,

1999). With the ventures of the poor, we know less about their outcomes, but there is anecdotal evidence to suggest a significantly higher rate of failure (Bekele & Worku, 2008; Fairlie & Robb, 2008).

Two major reasons for new venture failure are the liabilities of newness and smallness. The liability of newness is concerned with inherent disadvantages new firms have when compared to incumbent organizations (Stinchcombe, 1965). Newness suggests that those involved must learn new roles with which they are unfamiliar. The organization lacks the routines, standardized procedures, and problem-solving strategies that could increase efficacy and ensure consistency in operations (Baum, 1996; Gong, Baker & Miner, 2004). Externally, new firms lack an established identity and struggle to establish legitimacy with customers, suppliers, financing agents, regulators and competitors. Here, legitimacy refers to "a generalized perception or assumption that the actions of an entity are desirable, proper or appropriate within some socially constructed system of norms, values, beliefs and definitions" (Suchman,1995, p. 211).

The liability of smallness refers to the vulnerability of an entrepreneurial venture based on its limited resources and capabilities (Aldrich & Auster, 1986; Hannan & Freeman, 1984). The business has a paucity of internal resources and difficulties in accessing resources (Santos & Morris, 2017). Smallness makes it harder to attract and retain skilled employees (Aldrich & Auster, 1986). It limits the bargaining power of the entrepreneur in dealing with resource suppliers and makes it difficult to achieve the economies necessary to be competitive (Crook & Combs, 2007; Wilson & Summers, 2002). Limited working capital hinders operations and results in missed opportunities (Lefebvre, 2020). Anderson & Ullah (2014) conclude that the condition of smallness results in attitudes and behaviors that serve to reinforce smallness.

We know little regarding how the liabilities of newness and smallness affect those who come from a poverty background. This is due, in part, to our failure to consider the unique nature of poverty and how it informs the entrepreneurial experience.

Poverty and the Liability of Poorness

While all entrepreneurs must overcome the liabilities of newness and smallness, and most start with little in the way of resources, the ability of the poor to deal with these liabilities is complicated by the enduring effects of the poverty experience. It is an experience that transcends a lack of income or wealth and can be characterized by a complex web of interacting conditions. The poor suffer more food insecurity and less healthy diets (Bhattacharya, Currie, & Haider, 2004), higher crime rates and physical insecurity (Pare & Felson, 2014), more chronic medical conditions and higher levels of childhood mortality (Van Agt, Stronks, & Mackenbach, 2000). They encounter fewer and less attractive job opportunities and demonstrate higher unemployment and underemployment rates (Morris, Santos, & Neumeyer, 2018). Their housing conditions are more sub-standard (Morland et al., 2002), while they frequently lack dependable transportation alternatives (Wachs, 2010). They

attend lower quality schools and demonstrate above-average school drop-out rates (Orfield & Lee, 2005). Teenage childbearing and single parenthood are both common (Maldonado & Nieuwenhuis, 2015) as are high stress levels and constant fatigue (Banerjee et al., 2011). They tend to be segregated from much of society (Abramson, Tobin & VanderGoot, 1995), with limited social networks (Matthews & Besemer, 2015).

Conditions such as these suggest the poverty entrepreneur must overcome a third liability, which we label the liability of poorness. It can be defined as *the potential for failure of a new venture due to difficulties encountered that are traceable to the characteristics and influences deriving from a poverty background*. In effect, the liability of poorness puts the individual at a relative disadvantage compared to other entrepreneurs.

The liability of poorness has four underlying dimensions that contribute to heightened risk and vulnerability (see Figure 1). These include literacy gaps, a scarcity mindset, intense non-business pressures, and the lack of a safety net. Let us consider each of these elements.

Literacy Gaps

UNESCO (2005, p. 21) defines literacy as “the ability to identify, understand, interpret, create, communicate and compute using printed and written materials associated with varying contexts. Literacy involves a continuum of learning in enabling an individual to achieve his or her goals, develop his or her knowledge

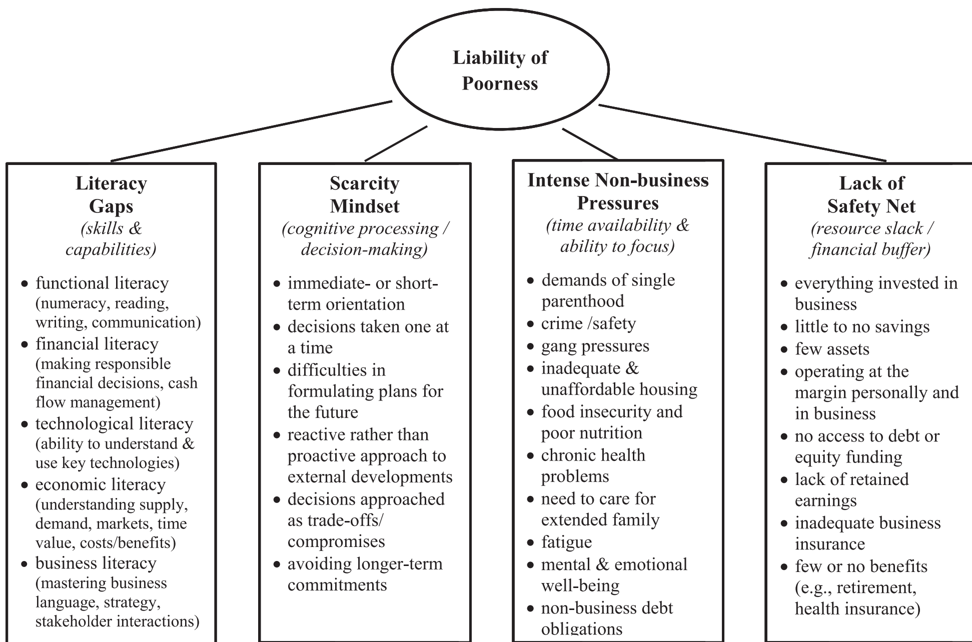

Figure 1. The Concept of Liability of Poorness and Its Components.

and potential, and participate fully in community and wider society." Morris et al. (2018) emphasize the roles of five inter-related literacies when considering the poor and entrepreneurship: *functional* (reading, writing, numeracy, communication); *financial* (understanding how to budget, save, manage credit and debt obligations, make financially responsible decisions); *economic* (understanding economic incentives and disincentives, supply and demand conditions, and the costs and benefits of alternative courses of action); *business* (mastering the language of business and how to effectively interact with various stakeholders); and *technological* (appreciation for the significance of key technologies impacting a business, how they are used, and issues raised by their use). Arguably, these five literacies are more important than any other resource when starting a business. Yet, the evidence is clear that, across the globe, the poor suffer from low literacy levels (Ahmed, 2011; Hernandez, 2011; Wilson, 1996).

Scarcity Mindset

An endemic characteristic of poverty is scarcity. Lack of resources forces the poor individual to make trade-off decisions in determining which bills to pay, such as whether to buy medicine for a sick child or cover this month's rent. Beyond this, the poor face a scarcity of options and choices, and can also experience scarcity of time and energy, such as when attempting to work two part-time jobs while also launching a venture. Shah, Shafir, and Mullainathan (2015) demonstrate that those with limited resources will more exclusively focus on accomplishing the most pressing tasks at hand and ignoring other critical tasks—even where doing so takes away from the ability to achieve larger goals. Immediate problems, those where scarcity is most salient, consume a disproportionate amount of their time, effort, and limited financial resources (Mani, Mullainathan, Shafir, & Zhao, 2013). By allocating attention to immediate needs, the individual frequently ignores other needs and engages in actions that prove to be costlier or detrimental in the longer term. Shah, Mullainathan, & Shafir (2012, p. 682) argue that "resource scarcity creates its own mindset, changing how people look at problems and make decisions." In an entrepreneurial context, this mindset can undermine the ability to plan or think strategically, especially in a manner that anticipates and prepares for unexpected occurrences and emerging threats. Attentional shifts and reliance on locally convenient responses can serve to harm the long-term potential of the venture.

Intense Non-Business Pressures

The ability of a poor individual to run a business is also compromised by constant and occasionally extreme personal (unrelated to the business) demands placed on the entrepreneur. Time pressures on the poor have been explored by various authors (e.g., Chatzitheochari & Arber, 2012; Dermott & Pomati, 2016). If one's family is exposed to more chronic medical problems, difficulties paying for basic needs, threats of foreclosure or eviction, high crime rates and gang violence,

unexpected job losses, and similar everyday pressures, large amounts of time can be consumed. Such developments can distract the entrepreneur from addressing critical business needs. The ventures of the poor are frequently labor-intensive operations heavily dependent on the entrepreneur to both manage the business and also perform the core work (e.g., construction, cleaning, cooking) of the business. A major personal or family problem can require that operating hours be reduced, key decisions be compromised or deferred, and resources be taken out of the business. Similarly, the quality of business decisions may suffer as the entrepreneur is distracted by these outside developments.

Lack of Safety Net

The final contributor to the liability of poorness is the lack of any sort of safety net or financial slack when major obstacles are encountered or unexpected developments occur. The entrepreneur has typically put all of his/her financial resources into the business, and there are no remaining savings to draw upon (Barr & Blank, 2009). Friends and family members lack resources to help out should the business get in trouble. Beyond this, the entrepreneur's limited social network contributes to the lack of a safety net. He or she struggles to qualify for any sort of bank debt or outside finance, and if they have credit cards, these are at their limit (Littwin, 2008). The business fails to contribute to the entrepreneur's safety net, as it frequently operates at the margin (Morris et al., 2018). Capacity is limited, as the entrepreneur may work from home or a stall, and is not able to employ much equipment or technology in operations. Competitive conditions keep prices low, and when combined with relatively high unit costs, result in little to no profit. Marginal operations limit the ability to build cash reserves or generate retained earnings that can be reinvested in the business or flow back to the entrepreneur.

The four dimensions of the liability of poorness interact. For instance, the short-term focus and struggle to plan or think strategically that result from a scarcity mentality are reinforced by the distractions posed by intense non-business pressures. Failure to plan can also contribute to the lack of a safety net, which in turn leads to more conservative and short-term decision making. Literacy shortcomings are likely to encourage a focus on the immediate while hindering the ability to create slack in the organization through investments in equipment and technology. When combined, these four factors can impose a burden on the entrepreneur that influences the ability to address the liabilities of newness and smallness, the kind of venture that emerges, and venture outcomes.

Others who have not experienced poverty can encounter aspects of each of these dimensions. However, for the person in poverty, the likelihood of all four factors operating in tandem is high. They are conditions in which the poor tend to be immersed prior to the launch of a venture, often for all of their lives. As a result, overcoming them once the business is operating places unique demands on the entrepreneur, and for some can represent an insurmountable challenge.

The Liability of Poorness and Venture Fragility

The underlying components of the liability of poorness can make the poor especially vulnerable when confronting adverse circumstances (e.g., Payne, DeVol, & Smith, 2006; Van Ginneken, 2005). A concept related to vulnerability is fragility. While the former term suggests a potential weakness that could result in loss, the latter concerns how easily (the likelihood that) something can be damaged or broken and a loss incurred (Porter, 2015). A venture is fragile when it is vulnerable to bad decisions and external threats, and there is a high likelihood of loss of value or outright failure. Without a buffer that allows them to withstand the adverse impact of shocks, the organization becomes unable to fulfill its core functions.

Let us consider the direct effects of the liability of poorness dimensions on the entrepreneur's ability to address problems of newness and smallness, and how this can result in greater venture fragility. Gaps in functional and business literacies can make it difficult to communicate effectively with prospective employees, suppliers, distributors, and others, increasing the difficulties in establishing legitimacy with stakeholders. Even fundamental tasks such as obtaining permits, registering the business, and tax compliance can seem overwhelming. Organizational learning and the entrepreneur's understanding of how to develop routines and procedures can be hindered. A person with less functional, technological, and financial literacy may have limited capabilities when it comes to particular organizational tasks, less familiarity with roles, and an inability to incorporate basic technologies into operations, all of which can produce inefficiencies in operations. These and economic literacy gaps can make it harder to realize how to achieve economies in procurement, production, and distribution.

With a scarcity mindset, the entrepreneur is focusing on immediate problems and short-term needs, in effect ignoring or putting off other business decisions. The result can be inefficiencies in the areas not receiving attention, particularly if deferring things results in higher unit costs. A lack of strategic thinking can lead to legitimacy problems, especially when stakeholders are aware of emerging challenges for which the entrepreneur appears unprepared. A preoccupation with immediate problems can also mean the entrepreneur is not developing knowledge and capabilities associated with key roles that must be filled within the enterprise, particularly when these roles are unrelated to the problems at hand. Without the planning that comes with a longer-term focus, the firm cannot begin to achieve economies in procurement and production. Such planning is also critical for the development over time of effective routines and procedures.

When intense personal (non-business) pressures distract the entrepreneur from attending to the needs of the venture, legitimacy can suffer as stakeholders question the entrepreneur's dedication to the enterprise. Lack of complete focus on the enterprise is likely to produce inefficiencies in operations, less learning, reduced planning, and reduced bargaining power with external stakeholders. Activities associated with key roles in the enterprise may not receive attention. In addition, such distractions suggest the entrepreneur is less able to ensure that key routines have been formalized and are being adhered to.

The lack of a safety net can make it more difficult to attract financial resources, particularly when the organization has had to under-invest in assets, and financial statements indicate little in the way of owner's equity. Without any cushion in terms of personal savings or cash on hand, stakeholders become more aware of the financial vulnerability of the enterprise, especially with regard to a major threat or setback, which can detract from its legitimacy. Suppliers may use such vulnerability as a reason to impose more restrictive terms on purchases. Operating on a thin margin with no reserves, the entrepreneur can be forced to limit inventory levels and make smaller purchases. Overly conservative spending then reduces bargaining power and limits the firm's ability to achieve economies in operations.

The burden posed by the liability of poorness varies. The poor differ in terms of the extent to which they experience lower levels of literacy, an immediate-term orientation, personal pressures that are not business-related and little safety net. Additionally, certain types of businesses may perform adequately in spite of one or more of these risk factors. However, for most new ventures started by the poor, as this burden increases so too does their fragility. They become more vulnerable to major setbacks, their ability to provide core functions declines, and the likelihood of failure increases.

An example can be found in the high vulnerability of these businesses during the COVID-19 economic crisis. Orders quickly dry up, contracts are canceled, and sources of support disappear. Fragility is then reflected in their inability to afford inventory, pay bills, meet payroll demands, serve customer needs, hold on to employees, maintain marketing efforts, and sustain relationships with external stakeholders. Lack of cash flow ultimately forces the business to reduce capacity, sell off assets, and otherwise lessen the venture's ability to create value. The firm becomes less competitive and less economically viable. Even as the crisis passes and opportunities begin to appear, the firm is unable to capitalize upon them. Many poor entrepreneurs fail, and only a small percentage will ever regain ground that has been lost.

The Need to Level the Playing Field

As the liability of poorness places the poverty entrepreneur at a relative disadvantage, it is important that we find ways to ensure the poor have an equal opportunity when it comes to successful venture formation. Unfortunately, the unique context of poverty is not well-reflected in the design of public policies or community-based initiatives that seek to foster entrepreneurship (Morris & Tucker, 2020). Many of the available policies and programs are not designed in ways that reflect the characteristics of poverty and their implications for entrepreneurial behavior. Instead, they reflect the public at large and tend to prioritize the needs of those who are launching growth-oriented and scalable enterprises (Morris & Kuratko, 2020).

The initial challenge is to make venture creation by the poor a priority in terms of both policy formulation and the activities of local entrepreneurial ecosystems. Liability of poorness factors tend to limit the types of ventures created by low-income

entrepreneurs to struggling survival and lifestyle businesses (Morris et al., 2018). There are those who suggest such ventures should receive no support because of their inefficiencies, limited hiring potential, and failure to produce significant innovation (e.g., Shane, 2009; Stam, 2015). We need to highlight the critical roles played by the ventures of the poor in addressing unfilled market niches, enhancing competition, paying taxes, stabilizing neighborhoods, contributing to the fabric of the community, and providing a developmental experience for the entrepreneur (Morris & Tucker, 2020).

Addressing the relationship between the liability of poorness and venture fragility should serve as a central guide in the design of public policies and community programming. These efforts must be built around the risk factors associated with literacy gaps, an immediate-term focus, personal demands outside the business, and no safety margin. Further, they should consider the integrated needs of those in poverty in terms of training, incubation, mentoring, consulting, resource access, and financial support as they move from ideation to launch to stability and then growth of their enterprises.

It must start with literacy, and recognizing how shortcomings here limit both start-up rates and venture viability. The availability to the poor of literacy training programs varies considerably across nations and communities, with the greatest emphasis placed on basic functional and financial literacy. A more holistic approach would consider the interplay between functional, economic, business, financial, and technological literacies, particularly within an entrepreneurial context. It would also consider the roles of social structures and community contexts in fostering participation and achievement in literacy training efforts (Prins & Schafft, 2009).

With entrepreneurial training and development, a different mix of tools and training approaches are necessary to reflect the unique developmental needs of the kinds of ventures started by those in poverty. Unfortunately, many of the tools and concepts available to support venture creation (e.g., lean start-up methodology, business model canvas, business plan approach) are more effective in addressing the requirements of those launching growth-oriented, scalable and high tech ventures. The goal should instead be one of making survival and lifestyle businesses more economically viable and sustainable. Specifically, greater emphasis is needed on tools that help those in poverty expand their opportunity horizons, assess markets at the base of the pyramid, access community resources through bootstrapping and leveraging, differentiate what are often commodity ventures, expand their social networks to enable collaborations with existing businesses, improve their profit models, and incorporate guerilla techniques in penetrating markets.

The intense non-business pressures and demands and lack of a safety net experienced by those in poverty might be mitigated with income subsidy programs that provide payments to the poverty entrepreneur tied to progress in advancing their ventures. Vouchers to help low-income entrepreneurs address personal demands in such areas as child care, transportation, health services, and rent can also help them concentrate their attention on their emerging businesses. Both the legitimacy and bargaining power of poverty entrepreneurs can be increased through

a number of vehicles. Examples include making them eligible for set-asides built into the procurement efforts of government, universities, and local companies; mentor-protégé programs that match low-income entrepreneurs with established firms in their industries; and joint buying arrangements between ventures of the poor and established companies.

Microcredit programs, government guaranteed loans, crowdfunding platforms, and community grants can be targeted to very early stage ventures of the poor, where payouts are linked to meeting activity-based metrics over time. In this manner, they encourage the entrepreneur to think beyond immediate needs. Alternative types of financing schemes should be encouraged, such as community-based financing schemes and rotating savings and credit associations (ROSCAs). Funding programs might also mandate that some percentage of monies provided be placed into savings accounts that are only accessible in crisis conditions. Consistent with the notion of a sharing economy, local communities can build pools of a range of different types of resources that poverty entrepreneurs can draw upon when their ventures are struggling.

These are but a few illustrations of ways in which efforts might be re-focused to address the liability of poorness and overcome venture fragility. It is not enough to simply recognize the potential of entrepreneurship as a pathway out of poverty. Morris and Tucker (2020, p. 17) have noted that "while poverty programs largely ignore entrepreneurship, efforts to encourage entrepreneurship largely ignore the poor." For entrepreneurship to become a truly viable part of the poverty-fighting toolkit, we must fundamentally rethink how the poverty experience can be reconciled with the nature of the entrepreneurial process. Such a reconciliation requires that we systematically address the liability of poorness while simultaneously capitalizing on the creativity, tenacity, adaptability, resilience, and other qualities that are often endemic to the experience of poverty.

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