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Unemployment Compensations and Entrepreneurial Initiative: Does Entrepreneurial Motivation Matter?

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Abstract

People may choose to create a new business for different reasons, and theory distinguishes between opportunity-motivated entrepreneurs, “pulled” into entrepreneurship by good business opportunities, and necessity-motivated ones, who are “pushed” in by the lack of means to earn their living. The pool of unemployed individuals is an important source of entrepreneurial initiative, especially for necessity reasons. High unemployment benefits may, nevertheless, diminish unemployed individuals’ incentives to look for a job or enter entrepreneurship. A few studies found compelling evidence that generous unemployment insurance schemes inhibit entrepreneurial initiative; however, there is no evidence whether different forms of entrepreneurship, depending on the entrepreneur’s motivation, are equally affected by the design of unemployment benefit schemes. Our paper fills this gap and examines the effects of unemployment compensations on opportunity- and necessity-driven entrepreneurship for 23 EU countries and a timespan of 19 years (2001-2019). Our results confirm that generous unemployment benefits hinder entrepreneurial initiative in a country. However, against common belief, the negative impact is higher for opportunity-driven entrepreneurs, and only weaker and dependent on the estimation technique for necessity-driven ones. Moreover, opposite to the conventional view, more detrimental effects of high unemployment compensations are evidenced at short unemployment durations. These findings reiterate the need for a properly designed unemployment benefit system, which provides income replacement for the unemployed at a moderate level, and a more balanced time profile of benefits along the unemployment spell.

Keywords: European Union countries, necessity-driven entrepreneurship, opportunity-driven entrepreneurship, time pattern of benefits, unemployment benefits