

Agricultural entrepreneurship and informality in Sub-Saharan Africa: Insights from Benin

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Abstract

This paper investigates the degree of informality of agricultural entrepreneurship in Benin, using data from the follow up survey of 2011 of the General Census of Enterprises. Considering informality as a continuum, the enterprises are classified as completely informal (98.24%), mostly informal (0.95%), mostly formal (0.68%), and completely formal (0.14%). The characteristics of entrepreneurs and of businesses as well as institutional and structural environment related factors influence the degree of informality of the firms. Therefore, transforming structurally the agricultural sector could pass through better access to adequate formal education, sensitization on the benefits of entry the formal sector, and institutional reforms especially of judiciary and tax systems.

Key words: agricultural entrepreneurship; Benin; informality; structural transformation; Sub-Saharan Africa

Introduction

In Sub-Saharan African countries, an important challenge of policy makers and economists is to understand how to accelerate and support economic transformation. (Breisinger and Diao, 2008). A key characteristic of Sub-Saharan African countries is the low level of formal entrepreneurship (Benjamin and Mbaye, 2012a; Benjamin, Golub and Mbaye, 2014), although entrepreneurship is seen as an important driver of development, through the process of “creative destruction” (Schumpeter, 1947). According to the Lewis’ dual economy theory, there is the modern sector and the traditional one, which is large in Sub-Saharan African countries (Lewis, 1954; Lewis, 1979; Vollrath, 2009). From the perspective of the established theories of development, the process of economic development is characterized by a period of rapid growth per capita combined with structural change (Breisinger and Diao, 2008). Thus, transformation involves the modernization of a country’s economy, society and institutions (Breisinger and Diao, 2008; Vollrath, 2009; Chen, 2012).

Sub-Saharan African countries are lagging behind in terms of economic transformation. The evidence shows the limited success of economic development experiences in Sub-Saharan Africa compared to the successes of Asian and Latin American countries (Breisinger and Diao, 2008). Agriculture which is mainly traditional continues to be the main contributor to employment in Sub-Saharan Africa, and there are many informal production organizations. From the perspective of established theories of development, informal production organizations are transitory, and are expected to gradually disappear with the emergence and growth of large formalized enterprises, resulting from the technological and market compulsions of modern development (Papola, 1980; ILO, 2002).

Informal enterprises are seen as untapped reservoir of entrepreneurial vigor, which is held back by government regulations (De Soto, 2000; La Porta and Shleifer, 2014). Thus, an improvement of property rights or a reduction of entry regulations would lead to unleashing this energy, which would fuel growth and development (La Porta and Shleifer, 2014). As informal firms do not comply with regulations, they compete illegally with formal firms. Indeed, informality is bad and is seen as a trap for development and growth (Kanbur, 2011).

The concept of informal economy has been introduced at the beginning of the 1970s to shed light on the significant unregulated yet well-organized business activities that occurred in impoverished societies, although evidence revealed the occurrence of informal economic activities long before 1973 (Hart, 1973; Benjamin and Mbaye, 2012b; Webb, Ireland and Ketchen, 2014). Historically, the debate on the informal economy was about four dominant schools of thought in terms of its nature and composition, which are the Dualist School, the Structuralist School, the Legalist School, and the Voluntarist School (Chen, 2012). The informal sector is defined by the Dualist School as comprising marginal activities which are distinct and not related to the formal sector, and is source of income for the poor and of safety net when crises occur (Hart, 1973; Chen, 2012). According to the Structuralist School, the informal sector is composed of subordinated economic units and workers which help to reduce input and labor costs, leading to the competitiveness of large capitalist firms (Chen, 2012). As for the Legalist School, the informal sector is composed of brave micro-entrepreneurs who opt to operate informally to avoid the costs, time and effort of formalization and that need property rights in order to convert their assets into legally recognized assets (De Soto, 2000; Chen, 2012). The Voluntarist School considers the informal sector as comprised of entrepreneurs who voluntarily opt to run away from regulations and taxation (Chen, 2012). The difference between the Legalist and the Voluntarist Schools resides in the fact that the latter considers informal entrepreneurs as not blaming the cumbersome registration procedures.

There is a certain conceptual incoherence to the literature of informality, and therefore new and old definitions of the concept compete leading to a plethora of alternative conceptualizations (Kanbur, 2009). Kanbur (2009) suggested that informality and formality have to be considered in direct relation to economic activity in the existence of specified regulations. Four conceptual categories can help to frame the analysis relative to the regulations: “(A) regulation applicable and compliant, (B) regulation applicable and non-compliant, (C) regulation non-applicable after adjustment of activity, and (D) regulation non-applicable to the activity” (Kanbur, 2009: 41). He argued that it would be preferable if these four categories (or even more disaggregated as appropriate) are taken into account, instead of relying on the generic labels ‘informal’ and ‘formal’.

It is worth noting that the concept of informal economy is broader than that of informal sector. The Fifteenth International Conference of Labor Statisticians in 1993 defined the informal sector as a group of household enterprises or unincorporated enterprises owned by households (ILO, 2002). The informal sector is seen as the sum total of all income-earning activities outside of legally regulated enterprises and employment relations (ILO, 2002). As for the informal economy, it includes informal employment inside and outside informal enterprises (ILO, 2002).

Entrepreneurs operating in the informal economy are considered being within informal institutional boundaries (i.e., norms, values, and beliefs of large groups in a society) but outside of formal institutional boundaries (i.e., laws, and regulations) (Webb, Tihanyi, Ireland and Sirmon, 2009). A distinction between formal institutions which account for the codified laws, and regulations and informal institutions comprising norms, values, and codes of conduct is made by scholars which adopt institutional theory, and they consider informal sector entrepreneurs as operating outside of formal institutional boundaries but within the boundaries of informal institutions (Webb, Tihanyi, Ireland and Sirmon, 2009; Webb, Ireland and Ketchen, 2014; Williams and Vorley, 2014; William and Shahid, 2016). Thus, the motivations of entrepreneurs to operate in the informal sector reside in the asymmetry between formal and informal institutions (William and Shahid, 2016). Although from the institutional perspective it seems easy to partition entrepreneurs as formal or informal, in reality many entrepreneurs are neither wholly formal nor wholly informal (William and Shahid, 2016). Many entrepreneurs are somewhere between the two extremes, displaying various levels of formalization/informalization (Chen, 2012; de Mel, Mckenzie and Woodruff, 2013; William and Shahid, 2016). Indeed, three aspects characterized informal enterprises: (i) they are unincorporated, (ii) they do not keep formal accounts, and (iii) they are not registered with the authorities such as for tax purposes (ILO, 2012).

Recently, the analyses of the motivations of entrepreneurs to operate in the informal sector are gaining widespread attention (e.g., Adom and Williams, 2012; de Mel, Mckenzie and Woodruff, 2013; Adom, 2014; Williams and Shahid, 2016). In Ghana, it was found that the motivations of household informal entrepreneurs transcended the marginalization thesis and they were often motivated not by necessity or opportunity, but rather by an amalgamation of the two (Adom, 2014). In Pakistan, the three characteristics of informal enterprises of the International Labor Organization (ILO, 2012) were used to investigate the degree of informalization of entrepreneurs (Williams and Shahid, 2016). The decision of formalization of firms is supposed to depend on the costs and benefits of formality (Kanbur, 2009; Benjamin and Mbaye, 2012a; de Mel, Mckenzie and Woodruff, 2013; Benjamin, Golub and Mbaye, 2015). Based on field experiments in Sri Lanka, it was found that the net benefit of formalization is modest for most firms (de Mel, Mckenzie and Woodruff, 2013). These findings also suggest that most firms seem to be rationally refraining from formalizing, while it seems optimal for a few to formalize their activities.

This study aims to shed light on the degree of informalization of agricultural entrepreneurs as well as its determinants in Benin. Therefore, the specific objectives are to: (i) analyze the state of formalization of agricultural entrepreneurs, and (ii) investigate the determinants of the degree of formalization. This study focuses on agricultural entrepreneurship for several reasons. The countries mostly exclude agriculture from their measurement of the informal sector, while some countries measure only the urban informal sector (ILO, 2002). Agriculture constitutes the main source of livelihoods and employment in Sub-Saharan Africa. In Benin, 70% of the workforce is employed in this sector which contributes 35% to the gross domestic product (GDP), and 75% to export revenue (République du Bénin, 2014). Moreover, the structural transformation of the agricultural sector is necessary to improve the livelihoods of the population and to tackle climate change related issues.

The remainder of the paper is organized as follows. Material and methods used are exposed in section 1. Then, the results as well as their discussion are presented in section 2. Finally, there is the conclusion section along with policy implications and perspectives for future research.

1. Material and methods

1.1. Data

The study uses firm-level data collected by the National Institute of Statistics of Benin (INSAE). In 2008, Benin carried out the second General Census of Enterprises (Recensement Général des Entreprises – RGE), and the follow up survey has taken place in 2011. This paper makes use of the part of the dataset from the follow up survey relative to agriculture. The usable sample size involves 2,956 agricultural enterprises. The RGE covered all the enterprises that were in Benin. It concerned both formal and informal economic units including those that were operating in the markets of the countries. In urban centers, all the enterprises within all the neighborhoods were included. While in rural areas, only those that were found in the capitals of the districts were taken into account as in these areas, enterprises are mainly concentrated in the capitals. However, the economic units of a certain importance located in the villages that the administrative authorities drew attention on were also taken into account.

1.2. Model

The degree of informalization of enterprises is evaluated through three factors, namely: (i) registration in the trade register, (ii) Ownership of Unique Fiscal Identifier (Identifiant Fiscal Unique – IFU), and (iii) types of accounts kept. Keeping formal accounts are determined by formal or simplified accounts (Table 1). A score equal to 1 is attributed to the enterprises when there is evidence of a given factor. As three factors are used, the highest total possible score is 3, whereas the lowest is 0. Therefore, considering informality as a continuum, the agricultural enterprises are classified in four categories ranging from completely formal (3 as total score) through mostly formal (a total score equal to 2), and mostly informal (1 as total score) to completely informal (a total score equal to 0).

Table 1. Decision matrix of the degree of informalization

	Trade Register	Unique Fiscal Identifier	Formal Accounts	Score
Completely formal	Yes	Yes	Yes	3
Mostly formal				2
Option 1	Yes	Yes	No	
Option 2	Yes	No	Yes	
Option 3	No	Yes	Yes	
Mostly informal				1
Option 1	No	No	Yes	
Option 2	No	Yes	No	
Option 3	Yes	No	No	
Completely informal	No	No	No	0

Consider rational entrepreneurs, i aiming to maximize their profit. The rational entrepreneurs will decide to formalize their business depending on their personal characteristics, institutional and structural environment. To investigate the determinants of formalization, this paper relies on econometric analyses. In the econometric regression the score underlying the degree of formalization is used as dependent variable. The model is specified as follows:

$$y_i = x_i' \beta + \mu_i \quad (1)$$

where y is the degree of formalization which takes the values 0, 1, 2, and 3, x is the vector of independent variables, β is the vector of the parameters to be estimated and μ refers to the error term.

The independent variables used are reported in Table 2. The independent variables comprise the characteristics of entrepreneurs (sex, age, and education), the characteristics of enterprises (age of business, having fixed work-place or not, number of days per week of work, number of hours per day of work, and capital), institutional and structural factors [knowledge of the Chamber of Commerce (Chambre du Commerce et de l'Industrie du Benin – CCIB), knowledge of the Center of Arbitration, Mediation, and Conciliation of the CCIB (Centre d'Arbitrage, de Médiation et de Conciliation – CAMEC), confidence on justice, perception on the number of taxes, and perception on the amount of taxes). Given the ordinal nature of the dependent variable, estimating the regression by the Ordinary Least Squares (OLS) will lead to biased results. The appropriate estimation method should be an ordered probability model. Thus this paper estimates an ordered probit regression to shed light on the factors that determine the degree of informalization of agricultural enterprises.

Table 2. Independent variables used

Variables	Description	Mean	Standard Deviation	Minimum	Maximum	Expected signs		
Characteristics of entrepreneurs								
Sex	1 if male and 0 if female	0.95	0.21	0	1	+/-		
Age	In years	33.88	8.95	15	92	+		
Education (None taken as reference)	Primary Junior high school Senior high school University	1 yes and 0 if no 1 yes and 0 if no 1 yes and 0 if no 1 yes and 0 if no	0.51 0.16 0.02 0.002	0.50 0.37 0.13 0.04	0 0 0 0	1 1 1 1	1 1 1 1	+
Characteristics of enterprises								
Age of business	In years	6.81	6.65	0	61	+		
Fixed work-place	1 yes and 0 if no	0.40	0.49	0	1	+		
Number of days per week of work	In days	6.11	0.59	1	7	+/-		
Number of hours per day of	In hours	10.97	1.91	2	24	+/-		

work Capital	In local currency	537,305	7,413,414	0	4.0e+08	+	
Institutional and structural factors							
Knowledge of CCIB	1 yes and 0 if no	0.10	0.31	0	1	+	
Knowledge of CAMEC	1 yes and 0 if no	0.01	0.11	0	1	+	
Confidence on Justice (Very confident taken as reference)	Rather confident	1 yes and 0 if no	0.41	0.49	0	1	-
	Not really confident	1 yes and 0 if no	0.25	0.43	0	1	-
	Not at all confident	1 yes and 0 if no	0.08	0.27	0	1	-
Perception on the number of taxes (High taken as reference)	Acceptable	1 yes and 0 if no	0.35	0.48	0	1	+
	Indifferent	1 yes and 0 if no	0.30	0.46	0	1	+
Perception on the amount of taxes (High taken as reference)	Acceptable	1 yes and 0 if no	0.23	0.42	0	1	+
	Indifferent	1 yes and 0 if no	0.30	0.46	0	1	+

2. Results and discussion

2.1. State of informality of agricultural enterprises

Of the 2956 agricultural enterprises, 98.24% (2904) are completely informal, 0.95% (28) mostly informal, 0.68% (20) mostly formal, and 0.14% (4) completely formal. Thus, most of the agricultural entrepreneurs operate completely informal enterprises. However, agricultural entrepreneurship is not completely characterized by informality.

2.2. Informality and characteristics of entrepreneurs

Table 3 reports the characteristics of entrepreneurs per degree of informalization. Mostly and completely formal agricultural enterprises are led only by males. Thus, the females lead only the completely and mostly informal enterprises. The youngest prefer operating informally, while there is no clear difference in average year between the three remaining categories. It appears that most of them regardless of the degree of formalization of the enterprises have at most primary education level, except for those that operate mostly or completely formally. Indeed, 45% and 50% of those that operate mostly and completely formally have at most primary education level, respectively.

Table 3. Characteristics of entrepreneurs by degree of informality

	Completely informal	Mostly informal	Mostly formal	Completely formal
Sex (% - male)	95.49	89.29	100	100
Age (years)	33.75	41.43	41.7	41.75
Education (number None)	881	5	2	1

of enterprises)	Primary	1,499	11	7	1
	Junior high school	474	9	6	0
	Senior high school	48	2	3	1
	University	2	1	2	1

2.3. Informality and characteristics of enterprises

Completely informal agricultural enterprises are characterized by the lowest level of capital and are the youngest (Table 4). Those that are completely formal appear to be the oldest enterprises. Thus, the likelihood to formalize gradually entrepreneurial activities increases over years. At least six days per week are devoted to work in the enterprises. This may be explained by the agricultural nature of the activities, which require a lot of time depending on the period. Moreover, the average daily minimum number of hours of work amounts to 10.25, which is beyond the legal daily eight hours of work.

Table 4. Characteristics of enterprises by degree of informality

	Completely informal	Mostly informal	Mostly formal	Completely formal
Age of business (years)	6.72	11.54	11.20	15.25
Fixed work-place (%)	39.19	82.14	75	75
Number of weekly days of work	6.11	6.21	6.15	6
Number of daily hours of work	10.96	11.68	11.7	10.25
Capital (in local currency)	503,473	1,927,396	3,226,100	1,925,000

2.4. Informality, institutional and structural factors

The characteristics of enterprises per degree of informalization are reported in Table 5. Less than 10% of completely informal enterprises know about the CCIB, against 64.29%, 95%, and 100% for mostly informal, mostly formal and completely formal enterprises, respectively. Thus, complete informality is associated with being unaware of the existence of the CCIB. The same patterns holds for CAMEC. The large majority of the enterprises are unaware of the existence of the CAMEC. Indeed, even it is only 25% of the completely formal enterprises that are aware about the existence of the CAMEC. Although, most of the entrepreneurs operate informally, most of them have confidence on the judiciary system. In terms of the perception on the number of taxes, 32.33%, 39.29%, 30% and 75% of completely formal, mostly formal, mostly informal and completely formal enterprises perceive it as high, respectively. As for the perception on the amount of taxes, these percentages are 44.52%, 60.71%, 55%, and 100%, respectively. Thus, the few number of completely formal organizations perceive both the number and the level of taxes as high. This may be due to corruption which still constitutes a serious issue in the country. Indeed, Benin was the 83rd corrupted country out of the 168 classified countries in 2015, with a score of 37 above the Sub-Saharan Africa average score (33) but below the global average score of 40 (Transparency International, 2016). Moreover, there are a lot of inefficiencies in public administration which have to be removed.

Table 5. Characteristics of enterprises by degree of informality

		Completely informal	Mostly informal	Mostly formal	Completely formal
Knowledge of CCIB (%)		9.30	64.29	95	100
Knowledge of CAMEC (%)		1.10	7.14	20	25
Confidence on Justice (number of enterprises)	Very confident	687	10	7	2
	Rather confident	1,200	11	5	1
	Not really confident	731	6	3	1
	Not at all confident	286	1	5	0
Perception on the number of taxes (number of enterprises)	High	939	11	6	3
	Acceptable	1,015	13	11	1
	Indifferent	950	4	3	0
Perception on the amount of taxes (number of enterprises)	High	1,293	17	11	4
	Acceptable	659	8	6	0
	Indifferent	952	3	3	0

2.4. Determinants of the degree of formalization of agricultural enterprises

Multicollinearity among the independent variables were checked through the variance inflation factors (VIFs). It appears that all independent variables display VIFs less than 2.3 except the two binary variables ('indifferent' regarding the perception on the number of taxes and on the amount of taxes) which display VIFs of 8.60 and 8.95. Given that the VIFs of the two binary variables are lower than 10 and the low level of the remaining ones, multicollinearity does not constitute a strong issue in the estimations. The estimation results are reported in Table 6.

The characteristics of entrepreneurs are in some extent important in explaining the degree of formalization. The degree of formalization increases significantly with the age of entrepreneurs. Female entrepreneurs are found to be significantly willing to give up informality than male entrepreneurs. Entrepreneurs having either primary or junior high school formal education level are less willing to operate formally compare to those that do not have any formal education. However, the effect is not statistically significant. Having senior high school and having university formal education level lead to the willingness to operate formally compared with having no formal education level, with the effect being statistically significant in the case of university level. These findings relative to the characteristics of entrepreneurs are consistent with those of previous studies (e.g., Adom, 2014; Williams and Shahid, 2016). However, a significant relationship was not found between the gender of the entrepreneur and the degree of formalization (Williams and Shahid, 2016).

As for the characteristics of the enterprises, the age of business, and having a fixed work-place influence positively and significantly the degree of formalization. The positive relationship between the age of the business and the degree of formalization is consistent with the findings found elsewhere (Williams and Shahid, 2016). Although the remaining factors relative to the characteristics of enterprises influence positively the likelihood to operate formally, the influence is statistically non-significant.

The institutional and structural factors are also in a certain extent determinant in the process of formalization of entrepreneurships. Being aware of the existence of the CCIB increases significantly the degree of formalization. Although being aware of the existence of the CAMEC is positively associated with the degree of formalization, the influence is not statistically significant. Not being very confident on justice negatively influences the likelihood to operate formally, with the influence being statistically significant in the case of those that are not really confident on justice. Although perceiving the number of taxes as acceptable or indifferent compare to perceiving as high influences positively the degree of formalization, no significant effect is found. However, perceiving the amount of taxes as acceptable or indifferent lessens the likelihood to operate formally. In Pakistan, tax level is found to decrease significantly the degree of formalization (Williams and Shahid, 2016).

Table 6. Ordered probit model of the determinants of the degree of formalization

Variables		Coefficients	P-values
Characteristics of entrepreneurs			
Sex		-0.57*	0.05
Age		0.02**	0.04
Education (None taken as reference)	Primary	-0.04	0.82
	Junior high school	-0.12	0.59
	Senior high school	0.36	0.23
	University	1.87***	0.00
Characteristics of enterprises			
Age of business		0.02*	0.07
Fixed work-place		0.53***	0.00
Number of days per week of work		0.09	0.43
Number of hours per day of work		0.05	0.11
Capital		1.95e-09	0.38
Institutional and structural factors			
Knowledge of CCIB		1.40***	0.00
Knowledge of CAMEC		0.37	0.15
Confidence of Justice (Very confident taken as reference)	Rather confident	-0.13	0.40
	Not really confident	-0.34*	0.09
	Not at all confident	-0.27	0.30
Perception on the number of taxes (High taken as reference)	Acceptable	0.15	0.43
	Indifferent	0.10	0.71
Perception on the amount of taxes (High taken as reference)	Acceptable	-0.39*	0.06
	Indifferent	-0.67**	0.02
Observations		2956	
Log pseudolikelihood		-202.35	
Wald chi2 (20)		275.60	
Prob > chi2		0.00	
Pseudo R2		0.34	

***, **, * : Significance levels at the 1%, 5%, and 10%, respectively.

Conclusion

Modernizing the agricultural sector in Sub-Saharan African countries is very important to boost economic growth and development. Using data from the follow up survey of 2011 of the RGE in Benin, the paper investigated the degree of informalization of agricultural

enterprises and its determinants. The findings reveal that although most of the enterprises operating in the agricultural sector are completely informal, there are three other categories of firms, namely mostly informal, mostly formal, and completely formal. The characteristics of entrepreneurs and of businesses as well as institutional and structural environment related factors influence the degree of informalization of the firms. Therefore, the structural transformation of the agricultural sector could pass through better access to adequate formal education, sensitization on the benefits of entry the formal sector, and institutional reforms especially of judiciary and tax systems. As this paper does not focus on the extent to which formalization affects productivity, future research should investigate that aspect. The use of a single cross-section data does not allow to investigate the dynamic of the degree of informalization over time. Moreover, future research can address this aspect as well as the differences in terms of economic and environmental performances.

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