THE VALUE OF POVERTY AND INFORMALITY: HOW ENTREPRENEURS CREATE INFORMAL INSTITUTIONS TO TRANSFORM POVERTY SETTINGS INTO MARKETS

Informal markets are critical for the economic growth of developing countries (Chen, 2006; Hart, 2006; Schneider, 2002, 2012). Entrepreneurs who live in poverty are their main actors (Webb, Kistruck, Ireland, & Ketchen, 2010). Their endeavors are mainly forced into existence by the necessity of survival in weak or non-existent formal institutional settings (Dencker, Bacq, Gruber, & Haas, 2019). Street vendors, handicraft manufacturers, and retail sellers and distributors of consumer goods through small, neighborhood shops are examples of entrepreneurs that emerge in informal markets in developing countries (Webb, Bruton, Tihanyi, & Duane Ireland, 2013).

One of the shortcomings of academic research on informal markets in developing countries is that, until now, these markets have been studied in isolation, without conceiving their connection with formal markets. Neither the literature on informal markets nor that on collaboration between actors from informal and formal markets has explored how informal markets are connected with formal markets and how this connection affects the creation and characteristics of informal institutions. In fact, developing countries are not entirely configured by formal institutional voids (Khanna & Palepu, 1997). Rather, they are configured by less developed areas in which poverty and the lack of formal institutions makes it difficult for markets to perform under formal contracts, property rights, and the enforcement of law and, therefore, function due to the existence of informal institutions, in conjunction with more developed, geographically adjacent areas where formal institutions function (Webb et al., 2010). Another underdiscussed issue is that less-developed areas in developing countries cannot always be considered markets. In many poor and informal settings configured by people who lack access to the resources that allow them to meet their most basic needs, market activity is completely absent (Karnani, 2007).

Linking a) the theoretical lens of institutional work (Lawrence & Suddaby, 2006) and b) the current literature on informal markets and informal institutions, proves useful in understanding the agency of entrepreneurs (who are poor and whose endeavors are mainly driven by the necessity) to transform poverty settings into informal markets. Following the definition that informal markets are markets that function due to informal institutions, we focus our study on the institutions created at the cognitive and normative levels. We define cognitive institutional work as creating, maintaining or disrupting cognitive institutions, which are assumptions, values, shared meaning frames, and schemas for making sense of reality and coping with it; and normative institutional work as creating, maintaining or disrupting normative institutions, which are rules of behavior, procedures, and networks (Fligstein, 2001; Lawrence & Suddaby, 2006; Scott, 2001). This leads us to the research question: *How do entrepreneurs in poor and informal settings create informal institutions at the normative and cognitive levels in order to transform poverty settings into markets?*

To answer this question, we executed an empirical case study in La Carpio, a slum in Costa Rica near the capital city of San José. During our first field visits and interviews, we realized that one of La Carpio's main economic activities was the "*Ropa Americana*," or used "American clothing," stores that have been founded by poor entrepreneurs who purchase used clothing in the formal market of San José and then sell it in the slum. We focused our analysis on a triangulation of biographical interviews, expert interviews, participatory observations, document analyses, and informal discussions. Our research design was based on 54 interviews with entrepreneurs who sell used American clothing in the urban slum of

La Carpio, consumers of these clothing, the slum's founders and leaders, importers of used American clothing, and other types of entrepreneurs.

We were able to theorize from our results that the daily practices developed by entrepreneurs in order to survive created informal institutions at the cognitive and normative levels, which connected them with local formal companies (importers of used American clothing) located in formal markets to obtain clothing products that were then sold informally within La Carpio. In this way, the entrepreneurs were able to transform poverty settings into informal markets that functioned due to the existence of informal institutions that connected them with formal markets. In our study, we introduce a process model that highlights the creation of *cognitive institutions* (the positive valuation of informality and poverty through connection with formal markets) and *normative institutions* (inter-institutional networks for importing products and intra-institutional networks for selling these products) that facilitated the emergence of an informal market within the La Carpio slum along four phases: 1) community building, 2) financial inflow, 3) product inflow, and 4) competition. The institutional work of entrepreneurs takes place in the third and fourth phases and is built upon the first two phases, which are carried out by the entire population living in the poor and informal setting (including the entrepreneurs themselves). In this sense, the first two phases of institutional work act as a precondition for the entrepreneurs' subsequent institutional work, which is necessary for market building.

We propose two theoretical contributions that aim to contribute to the literature on informal markets, collaboration between formal and informal markets, and institutional work. First, we extend the literature on informal markets and informal institutions, as well as that on collaboration between formal and informal markets, by introducing *connection with formal markets* as a key institutional characteristic of informal markets in poverty settings. These results contradict the literature that proposes that informal institutions—which includes both cognitive and normative institutions—in poverty contexts are negative for market activities (Mair, Marti, & Ventresca, 2012; Shantz, Kistruck, & Zietsma, 2018) or that informal markets are isolated (Shantz et al., 2018). Our study shows that informal markets are, rather, a complex phenomenon (Godfrey, 2011, 2015) that is marked by entrepreneurs who intend to give value to their contexts of little economic resources and weak or non-existent formal institutional settings by relating with formal market actors such as local companies—but not necessarily formalizing. This is a much more subtle relation between formal and informal markets than the formalization proposals suggest. Our study aligns with emerging studies that propose a link between the literature focusing on entrepreneurship in informal markets and that focusing on collaboration between formal and informal markets (Branzei & Abdelnour, 2010; Seelos & Mair, 2007) to better understand their connections and the nature of informal markets.

Second, we theorize that collaboration between formal and informal markets emerges from the institutional work of entrepreneurs who reside in poor and informal settings. We introduce two types of cognitive work (defining positive value of informal and poverty settings, and defining positive value of formal markets) and four types of normative work (constructing intra-institutional networks based on community ties, constructing inter-institutional networks based on work relations, constructing inter-institutional networks based on product transactions, and constructing intra-institutional networks based on competition), which unfold along the four phases of a slum's development (*community building*, *financial inflow*, *product inflow*, and *competition*) to allow collaboration with formal markets to emerge from the works of entrepreneurs residing in poor and informal settings. These different forms of institutional work reinforce one another across the four phases (Perkmann & Spicer, 2008), interact constantly, and build upon one another throughout the process of market building (Leblebici, Salancik, Copay, & King, 1991).

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