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IMPACT OF SHADOW ECONOMY ON PRACTICAL ENTREPRENEURS IN ONDO STATE

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ABSTRACT

This study investigates the influence of the shadow economy on practical entrepreneurs in Ondo State, Nigeria. The target population comprised 291 shadow economy entrepreneurs, from which a sample size of 169 participants was selected using purposive sampling based on specific criteria related to active entrepreneurial engagement. A descriptive survey design was adopted, and quantitative data were collected through a structured questionnaire. Multiple Linear Regression Analysis was employed to examine the relationships between the independent variables (market share, growth, and welfare) and the dependent variable (performance of practical entrepreneurs). The findings reveal that market share, growth, and welfare each have a positive and statistically significant influence on practical entrepreneurs operating within the shadow economy. Specifically, growth and welfare were found to significantly impact entrepreneurial success, contrary to initial null hypotheses. Based on these findings, the study recommends strategic efforts to enhance entrepreneurs' market share, promote sustainable growth practices, and improve stakeholder welfare. Furthermore, policy interventions aimed at formalizing shadow economy activities, providing skills development opportunities, and facilitating access to financial resources are imperative to support the long-term success of practical entrepreneurs.

Keywords: Shadow Economy, Practical Entrepreneurs, Market Share, Welfare, Entrepreneurial Growth, Informal Economy

INTRODUCTION

The shadow economy, also known as the informal or underground economy encompasses a wide range of economic activities operating outside official government regulation and taxation (Bello, Dandago & Samaila, 2023a). These activities include both legal but unreported transactions, such as cash payments for goods and services, and illegal enterprises involving the production and sale of illicit goods. Globally, the shadow economy remains a substantial component of economic life, representing up to 37% of GDP in many developing countries (Schneider & Enste, 2021).

The persistence and expansion of the shadow economy are often driven by economic underdevelopment, high unemployment rates, regulatory inefficiencies, and elevated poverty levels (Williams & Nadin, 2020; World Bank, 2021). In contexts where formal employment opportunities are scarce, many individuals resort to informal economic activities as a means of survival. The size and impact of the shadow economy are further influenced by institutional quality: nations characterized by weak governance, corruption, and low public trust tend to have larger informal sectors (OECD, 2022; IMF, 2023).

From a fiscal perspective, high tax burdens and perceived inefficiencies in public service delivery often incentivize entrepreneurs to operate informally to minimize their tax liabilities (Asian Development Bank, 2024; Bello, Dandago & Samaila, 2023b; Smith, 2021). Conversely, stronger tax morale, where citizens feel a social responsibility to pay taxes has been shown to mitigate participation in informal economic activities (Bello, Dandago & Samaila, 2023b; Johnson & Lee, 2022).

For practical entrepreneurs, particularly small business owners and startups, the shadow economy offers both opportunities and risks. On the one hand, informal markets reduce bureaucratic obstacles, lower operational costs, and provide flexible avenues for income generation (Garcia et al., 2023; Thompson, 2024). On the other hand, entrepreneurs in the informal sector face significant challenges, including limited access to financial services, vulnerability to regulatory crackdowns, lack of legal protections, and restricted opportunities for sustainable growth (Williams & Martinez, 2023).

Against this backdrop, this study investigates the impact of the shadow economy on practical entrepreneurs in Ondo State, Nigeria. Specifically, it aims to examine how informal economic activities affect entrepreneurs' market share, business growth, and welfare.

Statement of the Problem

The shadow economy plays a pivotal but complex role in the entrepreneurial landscape of many developing economies, including Nigeria. While it offers critical income-generation opportunities for practical entrepreneurs, it also exposes them to significant risks and limitations. Entrepreneurs operating within the shadow economy often enjoy reduced operational costs and flexibility but are simultaneously deprived of formal sector advantages such as access to legal protections, credit facilities, and formal market opportunities (Williams & Nadin, 2021; Kaufmann & Kaliberda, 2023).

Competition from unregulated businesses intensifies pressure on entrepreneurs, particularly those striving to maintain compliance with formal regulations. Informal competitors, often offering lower-priced goods and services, erode the market share of formal businesses and create an uneven competitive environment (Baker et al., 2022). Moreover, the shadow economy influences entrepreneurs' growth trajectories; while informality may initially facilitate rapid expansion by bypassing bureaucratic barriers, it also introduces long-term vulnerabilities due to limited scalability and exposure to regulatory risks (Brown et al., 2023).

The welfare implications are equally profound. Informal entrepreneurship often serves as a critical livelihood strategy in contexts of high unemployment and poverty (Johnson, 2024). However, entrepreneurs and their workers are frequently excluded from social protection schemes, healthcare benefits, and retirement security (Williams & Garcia, 2025). Additionally, large shadow economies reduce government tax revenues, impairing the provision of essential public services and infrastructure, thereby indirectly affecting entrepreneurs' operating environments (Bello, et al, 2023b; Smith, 2021; Johnson & Lee, 2023).

Understanding the nuanced impacts of the shadow economy on practical entrepreneurs in Ondo State is essential for informed policymaking. Without adequate insight, efforts to regulate, formalize, and support entrepreneurial activities may inadvertently stifle innovation, limit income opportunities, or exacerbate inequality. Therefore, this study seeks to fill a critical gap by analyzing the multiple dimensions through which the shadow economy influences market share, business growth, and welfare among practical entrepreneurs in Ondo State.

LITERATURE REVIEW

Concept of Shadow Economy

The shadow economy, also known as the underground or informal economy, refers to the transaction of goods and services that are not reported to the government and therefore evade taxation and regulatory oversight. It encompasses both illegal activities, such as drug trafficking, smuggling, and illegal gambling, as well as legal activities conducted without the necessary licenses or tax payments, including unreported income from self-employment (Maastricht, 1993; Olufemi, 2017). Shadow economic activities often flourish in environments characterized by excessive taxes, stringent regulations, price controls, and inefficient property rights enforcement. When individuals perceive that formal market participation is overly burdensome, they may opt for participation in the informal sector.

Concept of Market Share

Market share represents the percentage of an industry's total sales controlled by a particular company over a specified period. It is a critical metric for evaluating a firm's competitiveness and position within its industry. Businesses increasingly emphasize expanding their market share, employing strategies such as product innovation, aggressive marketing campaigns, and strategic partnerships to gain an edge (Stern NYU, 2024; Toan, 2023). In today's dynamic environment, leveraging digital marketing techniques has become particularly instrumental in achieving substantial market share increases, as firms can efficiently reach broader audiences.

Growth of Practical Entrepreneurs

The growth of practical entrepreneurs within the context of the shadow economy can be understood by examining how informal economic activities influence overall entrepreneurial development. The shadow economy, consisting of activities unreported for tax purposes, often grows due to factors such as high taxation, inefficient social security systems, bureaucratic bottlenecks, and weak enforcement of legal frameworks (Akinlo & Akinlo, 2018). In periods of economic stagnation or rising unemployment, individuals frequently resort to informal entrepreneurial activities as alternative sources of income and employment (Colin & Sara, 2023; Gorana & Banko, 2021).

Theoretical Framework

Modernization Theory (MT)

This study is anchored on the modernization theory, introduced by Walt Rostow in his seminal work *"*The Stages of Economic Growth: A Non-Communist Manifesto *(1960)"*. Rostow's model outlines a linear progression of societal development across five stages: Traditional Society, Preconditions for Take-off, Take-off, Drive to Maturity, and Age of High Mass Consumption. Modernization Theory posits that societies transition from traditional economic structures to modernized, industrial economies through technological advancement, social transformation, and economic growth. Applying this lens to the shadow economy allows for a comprehensive analysis of how informal entrepreneurial activities emerge and evolve within transitional economies. It also highlights how such activities might either support or hinder broader national development goals.

Empirical Review

Toan, (2023) conducted a study on institutional quality, shadow economy, and entrepreneurship intermediate evidence, using quantitative methods on a sample of 79 economies from 2006 to 2018. The study employed fixed effects and the Generalized Method of Moments (GMM) estimation techniques. Findings revealed that improved institutional quality boosts entrepreneurial activity, and that expanded entrepreneurship contributes positively to economic growth. The study recommends strengthening institutional frameworks and controlling the size of the shadow economy.

Gorana and Banko (2021) examined the relationship between the shadow economy and business development. Utilizing a survey design and quantitative data analysis, their findings showed that 30.7% of businesses operate within the shadow economy, compared to 23% operating formally. The study concluded that more individuals engage in informal businesses due to economic pressures, recommending economic reforms aimed at mitigating the negative impacts of the shadow economy on formal sectors.

Schneider and Enste (2020) analyzed the size, causes, and consequences of the shadow economy across various countries. Adopting a quantitative research design, the findings identified high tax rates, excessive regulations, and labor market rigidities as major drivers of shadow economic activities. The study emphasized that the shadow economy adversely affects public finance and economic growth and suggested policy interventions such as reducing tax burdens, simplifying regulatory frameworks, and enhancing labor market flexibility.

John (2016) observed that informal sectors, often characterized by illegality or non-compliance with governmental regulations, significantly impact national economies. According to John, the grey market or shadow economy is typified by unregulated transactions that bypass official taxation and reporting structures, thereby weakening formal economic institutions and policies.

Akinlo and Akinlo (2018) described the black market economy as comprising economic activities outside the formal rules and regulations of the state. These transactions, whether legal or illegal, evade formal registration, taxation, and protection. The study extended the traditional view of the informal sector to include not only self-employed individuals in small enterprises but also wage earners in unprotected labor markets.

Collins and Sara (2023) investigated the contributions of shadow economy businesses to social welfare in the United Kingdom. Using a qualitative approach involving interviews with 43 informal business operators, the study found that many such businesses positively impacted citizen welfare despite their unofficial status. The research called for a nuanced understanding of the shadow economy's role in society, acknowledging its potential to support livelihoods while recognizing the risks of informalization.

Conceptual Framework

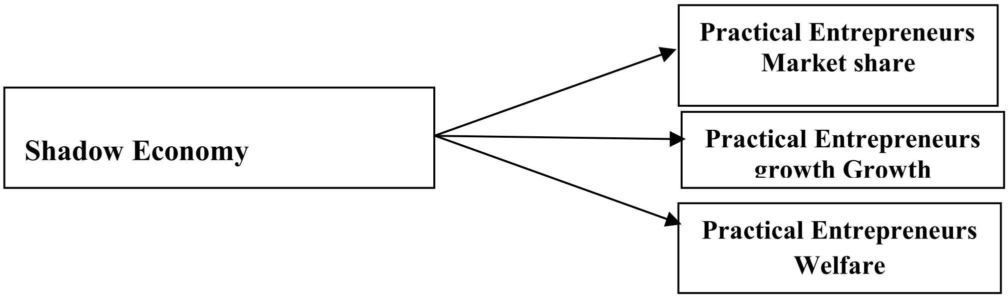

Figure 2.1: Conceptual framework
Source: Author Design, 2025

The figure above shows the relationship between the independent variables and the dependent variables. The relationship between practical entrepreneurs and the shadow economy can be analyzed through the lens of market share, growth, and welfare. Practical entrepreneurs often contribute to formal market growth by increasing their market share, which can lead to enhanced economic welfare. As these entrepreneurs thrive in a regulated environment, they may reduce the size of the shadow economy by providing legitimate alternatives to informal markets. Conversely, when growth is stifled or welfare is low, individuals may resort to the shadow economy for survival. Thus, a positive correlation exists where increased entrepreneurial activity leads to reduced shadow economy participation. Practical entrepreneurs positively influence market share and growth, enhancing welfare while reducing the shadow economy's size. (Chearlers, 2013).

METHODOLOGY

This study adopted a descriptive survey design to investigate the influence of shadow economy operators in Ondo State. A descriptive survey is appropriate for this research as it enables the systematic collection of quantitative data that can be statistically analyzed, providing insights into the characteristics, behaviors, and patterns of entrepreneurs operating within the shadow economy.

The target population for this study comprised active entrepreneurs across the three senatorial districts of Ondo State who are engaged in shadow economy activities. The total population was identified as 291 shadow economy entrepreneurs. These individuals represent a diverse range of informal business operations that exist outside the purview of government regulation and taxation. To determine the appropriate sample size, Taro Yamane's formula for sample size calculation was employed. This statistical technique ensures that the selected sample is both representative and sufficient to draw generalizable conclusions from the study population. The study employed a purposive sampling method. Participants were selected based on specific criteria: Active involvement in entrepreneurial activities within the shadow economy and based on operation of informal businesses within the past five years. This targeted approach ensured that only entrepreneurs with relevant and recent experiences were included, thereby enhancing the validity and relevance of the collected data.

Data was gathered using a structured questionnaire specifically designed to capture critical dimensions of the shadow economy's impact on entrepreneurship. The instrument was carefully constructed to ensure clarity, coherence, and alignment with the research objectives.

The collected data was analyzed using Multiple Linear Regression Analysis. This statistical technique enabled the exploration of the relationships between several independent variables (such as factors influencing participation in the shadow economy) and the dependent variable (entrepreneurial performance and sustainability). The use of regression analysis provided a robust framework for identifying the strength and direction of associations among the variables under study.

RESULTS AND DISCUSSION

Results

Table 1: Coefficients

Model	Coefficients (B)	Standard Error	t	Sig.
(Constant)	1.090	1.509	0.022	0.041
Growth	0.580	1.337	11.145	0.003
Market Share	0.482	0.120	5.305	0.004
Welfare	0.450	0.201	13.021	0.001

Source: Field Survey, 2025

a. Dependent Variable: Practical Entrepreneurs

Table 1 presents the results of the multiple regression analysis, providing information on each predictor's coefficients and significance levels in the model predicting the performance of practical entrepreneurs. Specifically, the table reports the unstandardized coefficients (B), standard errors, standardized coefficients (Beta), t-statistics, and significance levels (Sig.).

Market Share

The unstandardized coefficient for market share is B = 0.482 with a standard error of 0.120. The standardized Beta coefficient is 0.108, the t-statistic is 5.305, and the p-value is 0.004. These results indicate a positive and statistically significant effect of market share on practical entrepreneurs' performance at the 5% significance level ($p < 0.05$).

Growth

The predictor for growth has an unstandardized coefficient of B = 0.580 with a standard error of 1.337. The standardized Beta is 0.502, the t-statistic is 11.145, and the p-value is 0.003. This suggests that growth has a statistically significant positive impact on entrepreneurial performance. The high t-value and low p-value confirm the strength of this relationship.

Welfare

The unstandardized coefficient for welfare is B = 0.450 with a standard error of 0.201. The standardized Beta coefficient is notably high at 0.870. The t-statistic is 13.021, and the p-value is 0.001. This implies that welfare has a strong and statistically significant effect on the success of practical entrepreneurs operating in the shadow economy.

In summary, the multiple regression analysis indicates that market share, growth, and welfare each have a positive and statistically significant influence on practical entrepreneurs' success in Ondo State.

Discussion of Findings

The findings from the regression analysis demonstrate that all three predictors (market share, growth, and welfare) have significant effects on practical entrepreneurs engaged in the shadow economy.

Market Share and Entrepreneurs (H01)

The results support the hypothesis that market share has a significant positive influence on practical entrepreneurs. The positive relationship indicates that an increase in market share within the shadow economy enhances entrepreneurial performance and sustainability. This aligns with previous research that emphasizes market expansion as a catalyst for business success.

Welfare and Entrepreneurs (H02)

The second hypothesis tested whether welfare has a significant effect on practical entrepreneurs. Contrary to the null hypothesis, the study finds that welfare has a statistically significant and positive effect. This suggests that when entrepreneurs' welfare needs are adequately addressed (such as through better access to healthcare, education, and social services) their productivity and entrepreneurial drive increase.

Growth and Entrepreneurs (H03)

The third hypothesis examined the effect of growth on practical entrepreneurs. Findings indicate a strong and positive association, affirming that business growth opportunities (including access to new markets, customer base expansion, and increased revenue) significantly boost entrepreneurial performance among shadow economy operators.

Overall, the study challenges the initial null hypotheses, concluding that market share, growth, and welfare each significantly and positively affect practical entrepreneurs operating in the shadow economy in Ondo State. These findings emphasize the need for targeted interventions and policies aimed at improving the operating conditions of entrepreneurs in informal sectors, ultimately fostering economic inclusion and sustainability.

CONCLUSION AND RECOMMENDATIONS

Emanating from the findings of this study, it is concluded that market share, growth, and welfare significantly influence the success of practical entrepreneurs operating within the shadow economy in Ondo State. Specifically, the study affirms that market share plays a vital role in enhancing profitability and overall business success. A strong market presence facilitates greater customer engagement, competitive advantage, and improved operational efficiency.

Similarly, growth is identified as a fundamental component that contributes to entrepreneurial success. The findings reveal that prioritizing sustainable growth strategies significantly fosters profitability and long-term business viability. Furthermore, welfare emerges as a critical determinant of entrepreneurial success. The study emphasizes that improving the welfare of all stakeholders within the entrepreneurial ecosystem (including employees, customers, suppliers, and the community) directly enhances business productivity, reputation, and sustainability. Overall, this research concludes that a focused improvement on market share, growth, and welfare is essential for the prosperity and sustainability of practical entrepreneurs operating within the shadow economy.

Based on the conclusions drawn, the following recommendations are proposed:

Practical entrepreneurs should prioritize strategies aimed at expanding their market share. This can be achieved through competitive pricing, innovative marketing strategies, product quality improvement, and strong brand positioning. Capturing a larger market share will enable entrepreneurs to benefit from economies of scale, leading to reduced operational costs and increased profitability.

Entrepreneurs are encouraged to implement growth strategies that are sustainable and adaptable to market changes. Efforts should focus on customer base expansion, operational efficiency, diversification of product and service offerings, leveraging technology, and continuous investment in employee development. A culture of innovation and adaptability will ensure long-term business success.

It is crucial for entrepreneurs to prioritize the welfare of all stakeholders involved in their businesses. This includes implementing fair labor practices, ensuring customer safety, maintaining supplier relationships, and engaging in corporate social responsibility initiatives. A commitment to stakeholder welfare enhances business reputation, employee morale, customer loyalty, and overall productivity.

Policy Implication of the Findings

The findings of this study highlight the significant impact of the shadow economy on practical entrepreneurs, necessitating comprehensive policy interventions to mitigate its negative effects and promote greater formal economic participation. Specifically:
Entrepreneurs operating informally often face unfair competition from those evading taxes and regulations. This undermines fair market dynamics and restricts access to financial resources like loans and grants that require formal business documentation. A thriving shadow economy distorts economic data, leading to policy misalignments that fail to address the real needs of businesses. Excessive regulation may inadvertently push entrepreneurs into informality, while streamlined regulations could encourage formalization. Informal entrepreneurs are often excluded from social safety nets such as healthcare, pensions, and unemployment benefits, increasing their vulnerability during economic downturns.
To address these challenges, policymakers should consider the following strategies:
Reducing bureaucratic hurdles and making registration processes more accessible will encourage informal entrepreneurs to transition into the formal sector. Tax breaks and financial incentives should be offered to small businesses that formalize their operations, making compliance more attractive than informality. Educational programs should be developed to increase awareness of the benefits of formal operations and to enhance entrepreneurs' business management skills. While avoiding over-regulation, strategic enforcement against severe shadow economy violations can level the playing field without discouraging legitimate entrepreneurial activities. Establish mentorship programs, microfinance access, and other support systems to assist informal businesses in formalizing their operations while maintaining competitiveness. Developing more accurate methods for measuring shadow economic activities will provide better insights for crafting effective and targeted policy interventions.
By implementing these policy measures, governments can foster a more conducive environment that supports the growth and sustainability of practical entrepreneurs, while simultaneously addressing the root causes driving the expansion of shadow economies.

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