How do human capital and pro-market institutions shape ambitious entrepreneurship in good and crisis times?

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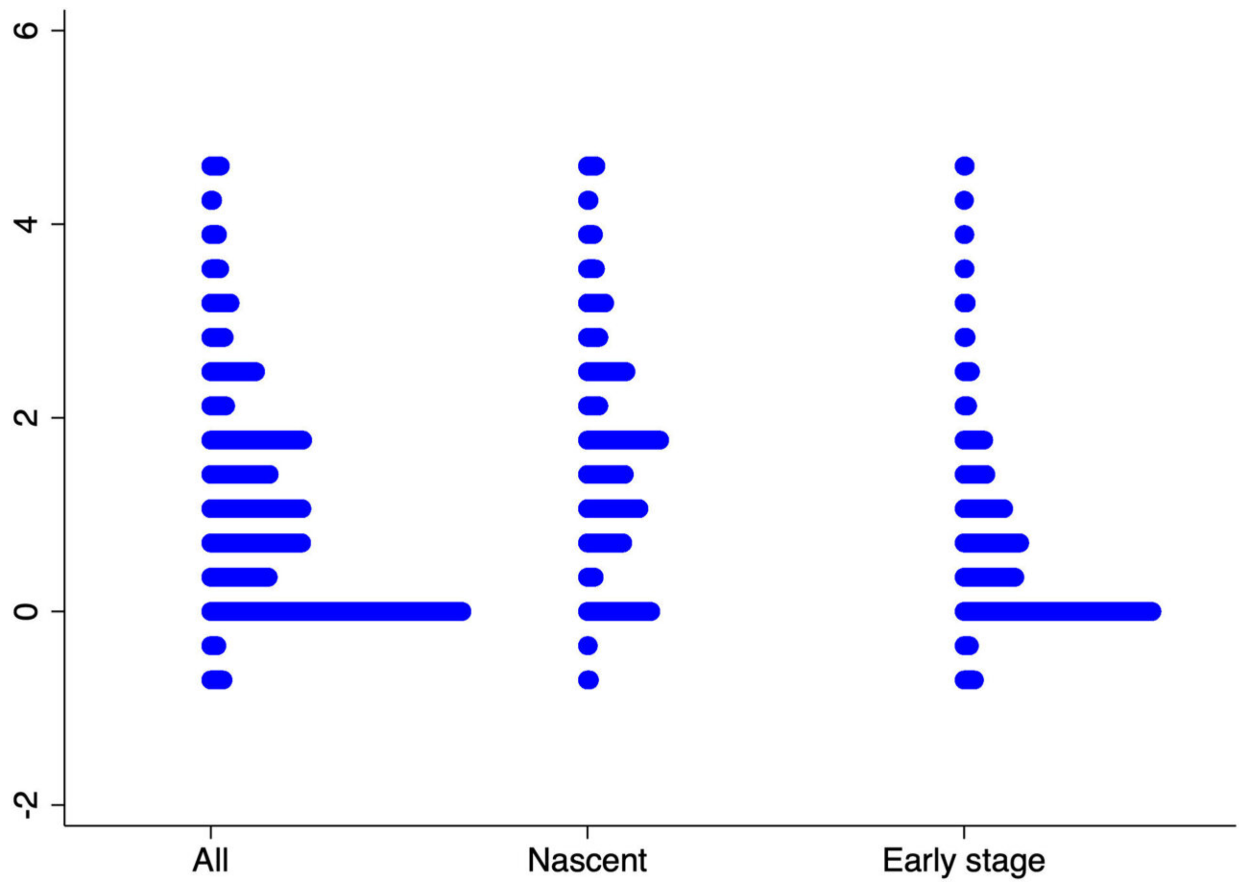

Entrepreneurial growth aspirations. This figure illustrates the distribution of entrepreneurial growth aspirations (EGA) computed as the difference between the natural logarithm of the entrepreneurs' expected number of employees in 5 years and the current number of employees (including the owner-manager in both expected and current employees). Credit: *Strategic Entrepreneurship Journal*

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Scholars and policymakers have highlighted the positive impact of human capital on entrepreneurial activity. Vast attention has also been directed to the beneficial role of pro-market institutions for entrepreneurship.

An article published in the *Strategic Entrepreneurship Journal* shows that the positive relation between pro-market institutions and growth aspirations is weaker for entrepreneurs with general human capital (higher education) but stronger for those with specific human capital (start-up or investment experience).

Interestingly, during the Global Financial Crisis (GFC) and the COVID-19 pandemic, the differential effect of pro-market institutions on growth aspirations exists only for entrepreneurs with specific human capital.

Why do institutions and human capital matter?

Institutions serve as "rules of the game," providing a context-specific nature to entrepreneurship. Such rules tend to remain stable over decades in their orientation toward more pro-market or more regulated organizations. Entrepreneurs take the institutional environment as a given when envisioning venture growth, which has been shown to be facilitated by pro-market institutions that reduce transaction costs.

Pro-market institutions promote economic liberalization, which requires bearing the opportunity cost of managing market uncertainty. Accordingly, in more liberalized markets (as compared to more regulated ones), entrepreneurs with specific human capital from start-up or investment (business angel) experience are expected to have higher growth aspirations.

In contrast, general human capital acquired through higher education can be at odds with liberalized markets and, thus, weaken growth aspirations. The reasoning is that general information transmitted via education is useful in more predictable markets, conferring an advantage to interpret regulation rather than to manage uncertainty.

Do predictions change in a crisis? When uncertainty spikes, and resources are scarcer, entrepreneurs with specific marketplace experience can have an even higher advantage in navigating a pro-market context. Conversely, there are mixed effects for those with general human capital.

Higher education may still be incongruent with pro-market contexts. However, it can provide an advantage of signaling future labor returns in a crisis such as the GFC and can serve to understand crisis-time regulations (e.g., COVID-19 relief packages to small firms).

An international dataset spanning good times and two crises

Entrepreneur-level data come from the Global Entrepreneurship Monitor and comprise 141,003 observations from 93 countries spanning the years 2005 to 2020. They confer two advantages: (1) country representativeness together with international comparativeness and (2) exogenous variation from the GFC and COVID-19 pandemic.

To gauge pro-market institutions, the study uses data from the Heritage Foundation and Fraser Institute. These measures provide a continuum of real institutional arrangements in which completely free or completely regulated markets do not exist.

What does the data say?

The results show that the positive relationship between pro-market institutions (measured through economic liberalization) and entrepreneurial growth aspirations is weaker for highly educated entrepreneurs (general human capital) but stronger for those with market experience (specific human capital).

During crises, this dynamic shifts: The negative interaction of pro-market institutions and general human capital vanishes, while the positive interaction with specific human capital becomes more pronounced compared to non-crisis periods.

This holds for start-up and business angel experience during the GFC and especially for start-up experience during the COVID-19 pandemic. One reason may be that during the GFC, investment experience was crucial for attracting funding, whereas in the COVID-19 pandemic, entrepreneurs could rely on government aid, and start-up experience took prominence.

These patterns are more robust for early-stage business owners (between three months and three and a half years of activity) compared to nascent entrepreneurs (first three months of activity), highlighting the significance of start-up experience, particularly in a crisis. Finally, potential complementarities emerge in more liberalized markets between higher education and business angel experience, mostly driven by non-crisis times.

Implications for policymaking

In the wake of the GFC and the COVID-19 pandemic, generous funding has been dedicated to business and education policies. Consistent with this study's results, recent proposals seek to increase complementarities between education and experience. An example could be to better integrate formal education with connections to lenders and equity investors.

Such policies could have higher returns in pro-market institutional contexts, which tend to feature economic growth through innovation. If education-based human capital serves as a precursor of growth, this research emphasizes the need to align theoretical training with real business experiences for aspiring entrepreneurs. This can enable entrepreneurs to scale up their ventures in institutional frameworks known to foster growth.

More information: Mircea Epure et al, Human capital, institutions, and ambitious entrepreneurship during good times and two crises, *Strategic Entrepreneurship Journal* (2023). DOI: 10.1002/sej.1492

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