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PLANNING FOR FAILURE AS DE-BIASING STRATEGY FOR ESCALATION OF COMMITMENT AT MARKET EXIT (INTERACTIVE PAPER)

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Principal Topic

Business failure is common. However, there is a tendency in the literature to focus much more on entrepreneurial success and to avoid failure as a deserving research topic (McGrath, 1999). Furthermore, while much attention is devoted to studying market-entry decisions, very little is known about market-exit decisions (Khavul et al., 2009). To the extent that such “exit” research exists, studies have primarily focused on economic barriers and strategic factors (Covin & Slevin, 1990).

Method

In this study, we investigate behavioral factors in an entrepreneurial context that affect one’s decision to “delay” exit during a failing course of action. More specifically, we focus on escalation of commitment – the time entrepreneurs take from when they decide to exit until they actually exit. An orderly and timely exit is important since it determines the level of sunk cost and ultimately the total cost of failure. It carries critical implications for how entrepreneurs recover from their failures for future entrepreneurship. What determines the extent to which entrepreneurs persist on a failing course of action in the form of delaying their exit? More importantly, under what conditions are entrepreneurs able to de-bias their escalation of commitment at market exit?

Results and Implications

We find that longer time and larger amount of financial resources invested into the venture can lead to longer time to exit after making the decision to exit. It appears; however, that greater investment in human-resource leads to shorter time to exit. Our findings suggest that time and money encourage more escalation, whereas the level of employment discourages escalation.

Our findings also suggest that contingency planning reduces the hazard and the cost of escalation of commitment, thus can be beneficial for the entrepreneur. We find that planning can be a valuable activity especially in an uncertain and ambiguous situation like market exit. While the main compelling reason for writing a business plan has been identified as an external purpose to raise funds (Lange et al., 2007) it can also be useful for internal purposes for entrepreneurs to reduce their escalation of commitment to a failing course of action. Overall, we deliver an explicit message that entrepreneurs can improve their strategic decision-making by planning for failure.

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