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SPECIFIC KNOWLEDGE AS A KEY TO LAUNCHING SUCCESSFUL NEW VENTURES

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ABSTRACT

We pit assumptions from informational economics against those from human capital theory in the context of repeatedly successful entrepreneurs versus discontinued entrepreneurs launching new ventures. We find that repeat entrepreneurs rely more on knowledge specific to a prospective new venture than discontinued entrepreneurs. In other words, they rely more on specific knowledge than they do on some generalized notion of human capital such as would be acquired through a college education.

INTRODUCTION

Several scholars have argued that specific knowledge is a key for entrepreneurs to earn above average economic returns (Hayek, 1945; Jenson & Meckling, 1995; Fiet, 2002, 2007; Soriano & Castrogiovanni, 2012). It is the recollection of information about people, places, special circumstances, timing and technology (Fiet, 2007). It is potentially valuable because it is non-tradable to other economic actors and can be used to create a quasi monopoly in time and space, resulting in the gaining of a temporary competitive advantage. However, other scholars have implied in their work that previous experience is all that is necessary, perhaps even to the point where they can enjoy a competitive advantage (Shane, 2000; Shane & Venkataraman, 2000). If previous experience consists of general knowledge related to previous start-up experience, this would be in juxtaposition to the arguments advanced by others about the desirability of specific knowledge.

General knowledge is codifiable into rules and procedures, which can be appropriated by others meaning that no monopoly in time and space is possible with only previous experience based on general knowledge. Once general knowledge is reduced to rules and procedures, it is quite inexpensive to publish for others to access. However, many scholars have related general knowledge even more broadly to industry experience or even to launching a venture in another industry (Coad, Frankish, Hightengale & Roberts, 2014; Colombo & Grilli, 2010; Hsu, 2007). Specific knowledge of particular elements in time and space can be aggregated or accumulated statistically (Jensen & Meckling, 1992). However, aggregation alone does imply that it can be codified because the elements themselves could be of ephemeral duration or entirely independent and unrelated to each other. This suggests that specific knowledge may only be valuable to the person who possesses it, but not to someone else who would proactively need to acquire it, once its value was already known. Thus, we expect that those who possess specific knowledge will have a competitive advantage compared with those who only possess general knowledge.
Despite these insights from informational economics, we do not know whether entrepreneurs actually rely on specific knowledge, nor if they do, their degree of reliance on it. Nor, do we know whether the degree of reliance on specific knowledge affects the success of entrepreneurs when it comes to discovering a venture idea and actually launching an on-going, successful venture. If reliance were related to one's previous successful experience using specific knowledge, one would expect to see a monotonically increasing relationship; however, in practice, we do not know whether this actually occurs.

This research extends what we know by addressing the question of the reliance of repeatedly successful entrepreneurs on either specific or general knowledge. It examines this reliance as a function of the actual success of entrepreneurs, which it compares across four different categories of entrepreneurs. Secondarily, we investigate whether initial entrepreneurial success is a function of the use of specific knowledge in preference to general knowledge and whether this success, again, is a function of entrepreneurial experience with success. Finally, we intend to test whether entrepreneurs are aware of the advantages of acquiring and using specific knowledge as they launch their ventures, which could provide evidence that specific knowledge is much more than a theoretically interesting construct.

This research will proceed in the following manner. First, it will compare various theoretical versus practical arguments for reliance on specific knowledge. Second, it reviews an experience-based argument that suggests which types of entrepreneurs would prefer specific knowledge to general knowledge, presumably resulting in the launching of more durable and successful new ventures. As it develops this argument, it will also develop hypotheses (one of which we report here) to extend our understanding of the relationship between the successful creation of new ventures and the type of knowledge employed to identify a potential venture opportunity. Third, it will describe the implementation of a relatively new qualitative technique for testing the hypotheses, together with more conventional methods. Finally, it will discuss the results and their implications for both theory and practice.

**Theoretical Versus Practical Reliance on Specific Knowledge**

The purpose of this study is to investigate whether actual entrepreneurs acquire and use specific knowledge as informational economics suggests that they will and ought to do (Fiet, 1996; Stigler, 1961). The arguments that follow review these relationships and develop testable hypotheses.

The previous-experience argument is similar to a human capital argument, which suggests that entrepreneurs who have certain types of human capital are likely to be more successful (Bhagavatula, Elfring, van Tilburg, van de Bunt, 2010; Colombo & Grilli, 2010; Gimmon & Levi, 2010; Hsu, 2007; Unger, Rauch, Freese & Rosenbusch, 2010). Human capital consists of practical learning, non-formal education and formal education (Davidsson & Honig, 2003), as well as knowledge and skills (Unger et al, 2010). In other words, human capital is similar to general knowledge that can likewise be reduced to rules and procedures. In essence, we can understand the specific/general knowledge dichotomy to be very similar to the specific knowledge/human capital dichotomy.

The question that remains is whether entrepreneurs benefit more from investing in specific knowledge or from the acquisition of human capital. A recent meta analysis of human capital indicates that entrepreneurs benefit more from knowledge and skills than they do from education.
and experience (Unger et al., 2010), suggesting that if the knowledge and skills were particularized to an opportunity that such a finding could favor specific knowledge over general knowledge/human capital. These Unger et al. (2010) findings do not relate exactly to the specific versus general knowledge question, so we cannot conclude by this study alone that entrepreneurs should favor specific knowledge.

The conceptual tension between specific knowledge and general knowledge or human capital is more than an abstract debate with limited impact. Acquiring specific knowledge could lead to above normal returns based on a valuable competitive advantage that was costly for others to access and copy; whereas, general knowledge could lead to only a distinctive competence and normal economic returns because the distinctive competence was more common than rare, based on the assumption that it would not be costly for others to acquire and copy. Clearly, this tension has important implications for how entrepreneurs can launch successful new ventures.

If entrepreneurs could be successful by merely acquiring human capital that could be redeployed to other ventures, they could likely avoid investing in a way that could become a sunk cost. However, it is less clear that human capital alone can lead to a sustainable competitive advantage, given that its re-deployability and resulting greater availability will equilibrate much more rapidly to earning normal economic returns.

If it were necessary for an entrepreneur to acquire specific knowledge in order to generate a sustainable competitive advantage and above normal returns, then only acquiring human capital would be insufficient. Nevertheless, the resolution of this tension is an empirical question to be addressed by this research. If specific knowledge were essential to earning above normal returns, one would expect that those who have a record of launching repeatedly successful ventures would understand its value and would typically seek to acquire it, albeit somewhat reluctantly, perhaps, due to its greater risk.

Let’s assume that there really is a difference in the competence to discover and launch a new venture that is conferred by possessing either specific or general knowledge/human capital, but that this difference only exists in the minds of some scholars. In fact, the difference could be meaningless because it is conceivable that entrepreneurs do not know anything about it. On the other hand, entrepreneurs are not equally successful in their start-up efforts.

**Hypothesis Development**

Some entrepreneurs are repeatedly successful in launching new ventures. Several scholars have referred to those who launch three or more ventures without a failure as repeatedly successful entrepreneurs (Fiet, 2007; Ucbasaran, Westhead & Wright, 2010). Although past success may not be predictive of future success, the fact that they have launched three successes without a failure means that they have beaten the odds against success.

One explanation is that they have learned something that average entrepreneurs do not know. Perhaps, this learning has come because they have acquired specific knowledge related to the prospects of launching a venture. For example, in our research of successful venture capital investors, we learned that they do not see this high-risk activity as risky because their specialized investing criteria, they claim, effectively shields them from the risks that impact non-specialists.

Now, if this specialization-based protection were typical of repeat entrepreneurs, it would suggest that they could sort out those ventures with less potential and decide not to launch
them. Instead, they would launch ventures relying on their specific knowledge of the particular circumstances of time and place that pertained to each venture (Hayek, 1945). Assuming that repeat entrepreneurs are more successful than others because of their reliance on their specific knowledge, we would expect that they would rely more on it than other groups, which leads to the first hypothesis:

\[ H1: \text{Repeatedly successful entrepreneurs will have a higher degree of reliance than other entrepreneurs on launching a venture using their opportunity-specific knowledge.} \]

Relatedly, we also examine university education as a substitute for specific knowledge; the use of specific knowledge by nascent and aspiring entrepreneurs. Due to space limitations, we do not discuss or report those results here.

**Method**

**Sample**

We conducted this research study in a Midwestern city in the United States with a population of more than 750,000. We identified a purposive sample of willing participants from several local entrepreneurial networks. The networks themselves include: startup incubators, venture club members and both community and university entrepreneurship startup education programs.

**Data Collection**

We utilized a mixed methods research design, which used both quantitative statistical information and qualitative interviews. We interviewed 61 entrepreneurs and determined that 41 of them met the criteria for the study. We recorded and transcribed each of the interviews. We developed 21 questions, which included 15 follow-on sub-sections. The interviewers followed two to three questioning threads, depending on the responses to the 21 interview questions. The interviews were primarily conducted in person, with the exception of a few interviews that were conducted by telephone due to scheduling conflicts. We utilized interviews as the primary source of evidence for this study. As recommended by Yin (2009), we developed a semi-structured guide for the interviewers to use during the interviews. Most of the questions and the interview guide are contained in Table 3.

**Data Analysis**

We followed the data analysis protocols recommended by Miles and Huberman (1994). Two interviewers conducted every interview together, which were recorded and later transcribed by a third party. Because no one else has previously used the interview questions in Table 3, we wanted to ensure that they would be effective in capturing the entrepreneurs’ intended responses. To identify any themes, two interviewers independently coded them, which were then checked for agreement and entered into NVivo. We also used NVivo to identify patterns in the themes. We further refined and modified the interview category themes as we completed more interviews.

The first order coding relied on structural codes derived from the interview questions (Saldana, 2009). The initial codes enabled categorization that allowed for frequency counts (Miles & Huberman, 2002).
We read and re-read the transcripts to locate and compare constructs. As themes emerged, we used a second order coding system that focused on whether or not the participant had a business plan. In a sense, we can say that we use NVivo to provide a robustness check for the variables and constructs used in this study. Once the categories (nodes) were established we used NVivo to summarize the basis for each category node listed as: people, places, special circumstances, timing and technology.

We returned several times to check the depictions of the data and to determine whether the thematic development of the findings was a valid reflection of the interviewees’ true thoughts (Rocco, 2003). We eventually developed major themes to describe the key findings from the data analysis. As recommended by Lincoln and Guba (1985) and Rocco (2003), we established trustworthiness by demonstrating: credibility, transferability and dependability.

**Results**

We tested the hypotheses using ANCOVA with the overall model being significant at the .05 level (p value = .032) while controlling for age and years of specific industry experience. The pairwise comparison for hypothesis 1 was significant (.05; p = .037). We also examined qualitative data using NVIVO, however we do not report the results here for the qualitative analysis.

**Discussion and Implications**

This research has examined the use of either general or specific knowledge on a success continuum between repeatedly successful entrepreneurs and discontinued entrepreneurs. We also used acknowledged attributes of specific information as contributory indicators of which type of information repeated entrepreneurs and others used to start a venture. We determined that repeat entrepreneurs invested in specific information; whereas, discontinued entrepreneurs had not made significant investments in specific information (t (36) = 2.72, p<0.05).

This finding is consistent with the prediction of informational economics, which posits that because specific information is not tradable it can be used as the basis for developing at least a temporary competitive advantageous. Whether the advantage would be sustainable would depend on whether others were able to imitate the resource investments of those who had invested in venture specific information.

The resource investments are those that support a fit between the resource requirements of a venture in order for it to survive its competitive threats and those that an entrepreneur actually allocates for this purpose. As Porter (1996) notes, successful strategy depends on recognizing and taking advantage of a venture's resource positions, which represent unavoidable tradeoffs. Not every entrepreneur is willing to make these resource tradeoffs because they come with the risk of assigning unneeded and costly resources to a strategy that will fail. One way to mitigate these resource risks is to acquire specific information related to placing good bets on how the resources will be used by a particular venture idea. Risk adverse entrepreneurs often prefer to hedge their resource bets. Investments in specific information can reduce the risk of resource misallocation but there is no time to delay in making them if they are to prove to be informative.

Despite the cost and risk of placing bad bets on acquiring specific information, it is vital to realize that acquiring specific information normally costs much less than placing bad bets on allocating resources to strategies that will fail, solely because one was ill informed and unwilling to invest in specific, risk-reducing information. Compared with placing bad resource bets, placing
bad bets on specific information is a real bargain. In other words, the tradeoff between placing a risky bet on specific information favors the entrepreneur when compared with placing a risky bet on the misallocation of resources that will become a sunk cost.

Alternatively, an entrepreneur could rely on less costly general information to make resource allocations, information that would not become a sunk cost. However, if an entrepreneur relies only on trends and general tendencies (general knowledge), it is less likely that he or she will be able to guess how best to make resource allocations, meaning that such a decision could lead to an entrepreneur being forced to discontinue a venture.

Although we cannot say with certainty that the discontinued ventures failed because they did not acquire specific information because other non-competitive forces could have been in effect, our main finding at least leaves open the possibility that this was the cause. It is interesting to realize that these same non-competitive forces were probably at work with repeatedly successful entrepreneurs. Nevertheless, it appears that their investments in specific information played an important role in starting at least three successful ventures in a row without a failure. The odds of this occurring three times in succession without a failure were less than 17%, so it is safe to say that their success was unlikely to have been due to luck.

The difference in their reliance on specific information between repeatedly successful entrepreneurs and discontinued entrepreneurs is important for theory. Contingency theory suggests that there are really no bad strategies, just strategies that would have worked in some alternative set of circumstances, given the appropriate investment in venture resources (Barney, 2011). The main finding of this study supports this contingency theory interpretation. However, it extends contingency theory by suggesting that what is important is not some general fit between a venture’s resource position and its strategy but a very specific one whose selection depends on possessing specific knowledge related to the circumstances of a particular opportunity.

Theoretically, we can also infer from these results that it is possible to measure venture success indirectly instead of directly by using such indicators as sales, return on investment, number of employees, or some measure of survivability. In this research we assumed that the track records of the entrepreneurs could be used as proxies for performance success. This relationship depends on the assumption that there is a relationship between an entrepreneur’s track record and what can be expected in the future. One basis for this relationship could be structural factors in the environment that are slow-to-change, which are known to repeatedly successful entrepreneurs, and which are used by them as strategic guideposts. Perhaps, these guideposts are used by repeat entrepreneurs as indicators of what type of specific information is necessary for strategizing about a venture’s future resource tradeoffs.

Entrepreneurship education often consists of exposure to information about what most entrepreneurs do. In other words, textbooks are replete with information about particular entrepreneurs (war stories), statistical or demographic information about typical entrepreneurs and admonitions about what authors think are important as they describe different parts of the entrepreneurship elephant. What students want to learn is how they can become very wealthy, as students and teachers often talk past each other. Teachers want to tell students about what they have learned studying what entrepreneurs do. This is somewhat puzzling because eighty percent of entrepreneurs launching new ventures fail after 5 years, so in effect, teachers taking a descriptive approach to pedagogy are often describing entrepreneurs who have already failed (Fiet, 2008). If teachers do not discriminate in what they teach about entrepreneurs between those who were
successful and those who have discontinued their ventures, their students will leave confused, and are likely to fail themselves more often for having taken time out to study what actual entrepreneurs do. This will become an unfortunate waste of student talent and enthusiasm unless their students’ real career objective is to become a social scientist, not an actual, successful entrepreneur.

This research makes several contributions to pedagogy. First, it suggests that if students want to copy entrepreneurs, they would do well to study what repeatedly successful entrepreneurs do, and the patterns that they follow. Second, repeat entrepreneurs have demonstrated in this study that they acquire specific knowledge more than entrepreneurs who discontinue their ventures. Because the acquisition of such knowledge could represent a sunk cost, it must be because they have learned to use it to succeed more than other entrepreneurs. Third, because specific information about prospective ventures cannot be found in textbooks, students must investigate the people, places, timing, special circumstances and technology of particular ventures. Fourth, this research should provide some encouragement to entrepreneurs who have invested in specific information against those who only use their own opinions or general information to be critical of a venture idea. Such critics are insufficiently knowledgeable of the specifics to know whether it will be successful.

Empirically, the current research can be improved by creating larger, more equally sized subsamples to ensure comparable comparisons across groups. In addition, this research can be improved by more effectively translating the concepts in informational economics to a language that is less abstract and more comprehensible to respondents.

Theoretically, there are many opportunities to extend Hayek’s (1945) insights into many related areas of study. For example, what relevance would his ideas have for intra-firm innovation, even in established organizations? How would his ideas translate when being adopted by entrepreneurial teams? Fiet (2007) suggested through his use of joint consideration sets, that teams ought to be able to increase the scope and competence to handle specific knowledge from multiple sources; however, no known research has accepted the challenge to explain how team members could combine their individual specific knowledge into a working amalgam that could not only increase a venture’s strategic responsiveness, but also strengthen its competitive advantage.

Pedagogically, we could develop and test in-class exercises that could sensitize students to the utility of and approach for acquiring specific knowledge for their projects. This could include ways to negotiate for specific information from outside information channels, as well as how to lessen the risk of cooperation when sharing specific knowledge with venture team members.

This study’s principle finding is that entrepreneurs who succeed the most often also base their venture decision-making on specific knowledge much more often than entrepreneurs who discontinue their ventures. As we have argued, this is a finding that has meaning implications for entrepreneurship research, practice, and pedagogy.

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