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DOES MONEY MAKE THE ENTREPRENEURIAL WORLD GO ROUND? (SUMMARY)

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DOES MONEY MAKE THE ENTREPRENEURIAL WORLD GO AROUND?

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Principal Topic
Lack of capital (liquidity constraints) is one of the oldest explanations advanced to explain lack of firm entry, performance, and survival. In this paper, we model each of these business steps in a causal chain by testing the liquidity constraints theory.

Method
We probe the relationships between capital, and firm entry, size, and survival by computing an exogenous measure of liquidity (historical earnings), calculating measures of human capital, and developing instruments to cope with the difficulty of measuring business quality. With this approach, we are able to distinguish more precisely the capital and business-quality effects on firm size and survival. We analyze these issues using a unique Portuguese database that traces the mobility of the founders across firms and matches founders with their ventures' characteristics.

Results and Implications
Our results indicate that capital is important to some extent in the entrepreneurial world, but not so much as previous work has argued. We find only weak support that individuals with more earnings are more likely to attempt entrepreneurship, except in the professional industries. However, founder earnings are an important determinant of start-ups financial capital. Entrepreneurs contribute more of their own capital when they accumulate larger earnings, which enable founders to obtain larger funds from external institutions. Start-up size is positively determined by financial capital, but whether the latter affects the survival rate is questionable.

Overall, lack of earnings inhibits individuals from raising the desired amount of financial capital and establishing firms with the desired scale. Nevertheless, after excluding alternative theories, we find support for the liquidity constraints hypothesis (capital market imperfections) only in the funding decisions and not in entry or size decisions.

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