STIGMATIZATION OF FAILED ENTREPRENEURS: PREVALENCE AND SOLUTIONS

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Recommended Citation

Available at: http://digitalknowledge.babson.edu/fer/vol34/iss5/2
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Abstract

This paper investigates why entrepreneurs experience stigma after firm failure and what can be done to reduce it. We use attribution theory as an overarching theoretical framework and hypothesize that entrepreneurs are held more accountable than employees for their unemployment after firm failure irrespective of the circumstances causing the failure. To test this hypothesis we conduct a between group, 2x2 full factorial experiment where the cause of the failure is manipulated. We find that entrepreneurs are held more accountable for firm failure irrespective of the circumstances causing the failure and that respondents who view failure as an inherent risk of firm ownership are less likely to stigmatize failed entrepreneurs.

Introduction

Entrepreneurs and employees who become unemployed because of firm failure often suffer from lowered self-esteem and financial strain (Singh, Corner, & Pavlovich, 2007). Entrepreneurs, however, are likely to experience stigma in this situation and suffer from a loss of reputation, image and status, and experience diminished labour market opportunities (Wiesenfeld, Wurthmann, & Hambrick, 2008). In contrast, employees are often referred to as victims and the (un)fairness in which they lost their job is focused on (Bennett, Martin, Bies, & Brockner, 1995).

Underlying this difference in responses to unemployment is the extent to which the individual is perceived to have control over the events that led to their unemployment (Wiesenfeld et al., 2008), whereby the extent of stigmatization is directly related to how closely the firm and individual are linked by time, proximity and accountability for the failure (Simmons & Wiklund, 2011). As firm failure is often associated with failure of the entrepreneur (Shepherd & Haynie 2011), entrepreneurs are frequently singled out as causing the failure and experience stigma as a result (Wiesenfeld et al., 2008). Main stream media contribute to this process by focusing their reporting of corporate failures on the stigmatization of the entrepreneurs involved (Cardon, Stevens, & Potter, 2011).

To date, however, the entrepreneurship literature has predominately focused on the macro level implications of stigma by investigating how regulatory frameworks and cultural perceptions influence start-up rates and re-entry after failure (e.g. Landier, 2005; Armour & Cumming, 2008). Stigma associated with firm failure is symbolized formally in the regulatory environment (Landier, 2005). For example, lenient bankruptcy laws increase the start-up rates of new firms (Armour & Cumming, 2005) while a general fear of failure decreases start-up rates (Arenius & Minniti, 2005) reflecting, in part, the risks and stigma associated with this occupational choice. Research on the implications of stigma at the individual level, however, is limited (Simmons, Wiklund, &
Levie, 2013). Recent research has started to investigate whether entrepreneurs have personally experienced stigma after failure (Cope, 2011). However, there has been no systematic investigation to the extent that entrepreneurs experience stigma after firm failure nor whether society in general place stigma markings on failed entrepreneurs and the nature of these markings.

To further understand the extent of stigmatization of entrepreneurs who experience failure and what can be done about it we investigate (1) how the extent of controllability for the cause of the failure influences the extent of stigma directed towards entrepreneurs and employees and (2) what can be done to reduce the extent of stigmatization. To do this we draw on Weiner’s (1985; 1995) attribution framework and develop hypotheses to explain why entrepreneurs are more likely to experience stigma when entering unemployment than employees, even in seemingly similar circumstances. We also then develop and test a set of hypotheses to show what can be done to reduce the extent of stigma faced by entrepreneurs.

We aim to make two contributions with this study. First, the study will help to identify underlying mechanisms explaining why entrepreneurs experience stigma after firm failure. As stigma can push entrepreneurs into a cycle of low self-confidence, discredited relationships with stakeholders, and loss of future labor market potential (Shepherd, 2003) understanding stigma after firm failure and what can be done to reduce it has implications for the well-being of failed entrepreneurs and their motivation to re-enter self-employment.

Second, the findings are relevant for the development of policies related to both helping failed entrepreneurs to re-enter the labor market (in paid or self-employment) and cope with the implications of failure. This also has broader implications at a societal level. Reducing the stigma associated with failure can encourage more individuals to start firms as the costs of failure are reduced.

Stigma is the outcome of having an attribute or reputation that is socially discrediting causing an individual to be classified by others as undesirable (Goffman, 1963). What is stigmatized is the outcome of a process whereby social audiences form collective judgments about the consequences of bearing a particular marking and whereby persons who bear that marking are socialized to incorporate the judgments of the wider society into their conception of self (Goffman, 1963). Stigma originated with the Greeks who branded slaves that tried to escape with the letter F, for fugitive. Other forms of stigma then emerged that were associated with any mark or sign that was perceived by others as inferior or discrediting.

Historically firm failure, and in particular bankruptcy, has been stigmatized (Efrat, 2006). Bankrupts have faced public humiliation as part of their punishment and language used in the public discourse has been disapproving referring to them as deceivers and frauds (Efrat, 2006). Not being able to pay debts went against commonly accepted social norms of acting honestly and was viewed as engaging in reckless and deviant behavior (Efrat, 2006). Punishment included being sold as a slave and having to wear identifiable clothing in public.
This negative image of bankrupts was widespread across American and Europe through the Victorian era and into the 20th century. Although the negative public perception of bankrupts has eased, there is still substantial stigma associated with bankruptcy (Landier, 2005). For example, bankruptcy is still associated with shame and mistrust in Sweden despite only 4% of corporate bankruptcies being associated with improper conduct (Sannesson, 2011).

Firm failure often triggers a sensemaking process whereby observers stigmatize individuals they perceive as causing the failure (Wisenfeld et al., 2008). Observers use information to arrive at causal explanation for why the firm failed. Individuals with a legitimate platform to make judgments about the cause of the failure play a key role in determining the extent that an individual is stigmatized and disseminate this information. Wiesenfeld et al. (2008) call these individuals arbiters and divide them into three categories: social arbiters who have legitimate platforms for influencing the public opinion such as press, academics and activists; legal arbiters are who can make decisions on the legal side of the failure such as regulatory officials, judges and prosecutors and economic arbiters who have the option of going into economic exchange with the stigmatized individuals such as venture capitalists and employers.

Cardon et al., (2011) found in the reporting of corporate failures in newspapers, the most frequent form of reporting was to create a sense of stigma around the entrepreneurs. This is one mechanism in which the failure of the entrepreneur is made public increasing the likelihood that the entrepreneur experiences stigma. Research on start-up rates and bankruptcy law has found that in countries with stricter bankruptcy laws there is lower start-up rates. This reflects how the regulatory environment influences the stigma associated with firm failure.

**Attributional Theory Of Stigma**

We draw on Weiner, Perry, and Magnusson (1988) attributional analysis of reactions to stigmas to investigate the extent entrepreneurs and employees experience stigma when becoming unemployed after firm failure. This theory focuses on the nature of the attributions people make for stigmas and how this influences the extent of pity and aid they afford the stigmatized individual. Underlying the extent of aid offered depends on the extent that the observer attributes the cause of the stigma to factors under the control of the individual (Sakalli, 2002). For example, the decision to help another individual often depends on the perceived cause for why the individual needs help (Weiner et al., 1988). Help is offered more frequently when it is perceived that the individual has low ability and this is outside of their control, or the help is required due to an external barrier or circumstances (Schmidt & Weiner, 1988). In contrast, aid is often withheld when the help required is due to lack of effort or other causes under the individual’s control.

Support for this relationship between responsibility and negative reactions has been found in a range of stigma contexts including HIV/AIDS (Cobb & deChabert, 2002; Steins & Weiner, 1999), mental illness (Corrigan et al., 2001), physical illness (Crandall & Moriarty, 1995), obesity (DeJong, 1980) and homosexuality (Armesto & Weisman, 2001). For example, in the context of excess weight and reactions to overweight people, research has found that individuals are more willing to derogate a person who is overweight from overeating (controllable cause) than a person who is overweight from biological factors (uncontrollable cause) (DeJong, 1980). In studies of emotional reactions to stigmatized individuals, sympathy, pity and aid are more likely to be afforded to individuals who have an uncontrollable stigma.
To determine the extent of controllability social observers use information to arrive at causal explanations. As already outlined, in the case of firm failure, this information can be sourced from public opinion such as media and the press, the regulatory framework such as laws and regulatory officials and the extent that individuals are willing to engage in economic transactions with stigmatized individuals (Wiesenfeld et al., 2008). Drawing on this research on stigma and failure, and the attribution framework for understanding responses to stigma, we develop a set of hypotheses that relate the extent of controllability over the causes of the firm failure and the extent that entrepreneurs and employees are held accountable for their lack of employment. Underscoring our hypotheses is that entrepreneurs are held more accountable for the failure of the firm than employees independent of the circumstances causing the failure.

H1: Entrepreneurs are held more accountable than employees for their unemployment after firm failure irrespective of the circumstances causing the failure.

H2: The greater the accountability for the failure, the greater the stigmatization in terms of (a) lower empathy and (b) lower assistance afforded to the unemployed individual.

As our aim is to not only understand why entrepreneurs are stigmatized after firm failure but to also understand what can be done to reduce the extent of stigmatization, we also hypothesize that individuals who are more aware of the challenges faced by entrepreneurs are less likely to stigmatize against them. Specifically, we suggest that individuals who believe that owning and running a firm by its nature involves risk and that this risk is difficult to avoid, are less likely to stigmatize failure. As they view failure as an expected outcome from entrepreneurial endeavors they are less likely to stigmatize unemployment that results from firm failure. This leads to the following two hypotheses:

H3: The greater the belief that failure is an inherent risk of owning and running a firm, the lower the stigmatization in terms of greater (a) empathy and (b) assistance afforded to the unemployed individual.

H4: The relationship between accountability for failure and (a) empathy and (b) assistance afforded is moderated by the extent that the respondent believes that failure is an inherent risk of firm ownership, such that the extent of the relationship is reduced.

**Method**

To test our hypotheses we conduct a between group, 2x2 full factorial experiment where the cause of the failure is manipulated. The company that was created for these experiments does not exist. The experiments were conducted in May 2013 on third year business students. A student sample is used as it is a relatively homogenous group and thus we minimize the error variance and increase our ability to detect significant relationships (Calder, Phillips & Tybout, 1981; Lynch, 1999).

Participation in the experiments was voluntary and the experiments were administered at the start of a lecture. In total, 82 useable booklets were returned (100 percent response rate). Due to sample size a control group was not included in the design.
The four different experiment packages were randomly assigned to participants in each experiment. The booklets were identical with the exception of the short description for why the firm failed. These descriptions were very similar in length and were presented in the same way.

**Instructions**

The participants were given an oral presentation with instructions on how to read and fill in the questionnaire. They were also provided with a short written instruction, see first part of the questionnaire (Appendix 2), to ensure they understood the scales. In order to reduce the risk of affecting respondents' preferences, we did not reveal that they were part of an experiment. Instead, they were informed that the survey was part of a study on unemployment.

**Manipulation**

The two treatment conditions were varied on two levels and consisted of (1) the cause of failure being due to an internal cause (i.e., loss of major customer) or an external cause (i.e., weak conditions in the external economic environment) and (2) where the individual was portrayed as either an owner/manager or employee. A vignette of each treatment can be found in Appendix 1.

**Measures**

*Accountability* was measured using six items. Inspiration for the items was taken from experiments on stigma and obesity. Respondents indicated on a 7-point Likert scale (1 = completely disagree; 7 = totally agree) the extent to which each accountability item reflected their perception of Annie's (the name given to the unemployed individual) role in the failure. The stem of the question read as follows “To what extent do you think Annie” and examples of the items are: (1) was responsible for the failure of the firm? (2) had control over the events that led to the failure of the firm? (3) contributed to the failure of the firm? And (4) is to blame for the failure of the firm? The Cronbach Alpha for the measure was .846.

*Empathy* was measured using three items. Inspiration for these items was also taken from experiments on stigma and obesity. Respondents indicated on a 7-point Likert scale (1 = completely disagree; 7 = totally agree) their response to each question. The stem of the question read as follows “To what extent do you” and the three items were: (1) feel sympathy toward Annie in her current situation? (2) feel concerned for Annie in her current situation? (3) feel sad because of the situation Annie currently is in? The Cronbach Alpha for the measure was .787.

*Assistance* was measured using a single item. Respondents indicated on a 7-point Likert scale (1 = completely disagree; 7 = totally agree) their response the following question: To what extent do you think Annie is entitled to unemployment benefits.

*Inherent risk* was measured using a single item. Respondents indicated on a 7-point Likert scale (1 = completely disagree; 7 = totally agree) their response the following question: To what extent do you think the failure was an inherent risk of owning and running a firm that is difficult to avoid?
Control variables were included in the model. We controlled for (1) whether the respondent had prior self-employment experience, (2) worked for a small business owner, (3) whether family members or close friends had been self-employed and (4) whether they, family members or close friends have been unemployed for an extended period of time (longer than six months) and (5) the sex of the respondent.

Results

Our first hypothesis states that entrepreneurs will be held more accountable than employees for their unemployment after firm failure irrespective of the circumstances causing the failure. To test this hypothesis we analyzed our data using a one-way ANOVA. We found that there was an overall significant difference ($p < .001$) in the between group means. However, we found that there was no significant difference between the condition entrepreneur, economic environment and entrepreneur, sale account. Nor did we find a difference under the condition Entrepreneur economic environment and Employee sale account. Thus we found partial support for Hypothesis 1. The results are presented in Table 1.

We then use regression analysis to test Hypothesis 2, 3 and 4. Hypothesis 2 stated that the greater the accountability for the failure the lower the (a) empathy and (b) assistance afforded the individual. The results are presented in column 3 in Tables 2 and 3. We found that accountability had a significant negative impact on the amount of empathy afforded to the individual ($\beta = -.354 p<0.01$) and a marginally significant impact on the amount of assistance afforded to the individual ($\beta = -.286 p<0.10$). Thus we find support for Hypothesis 2. Hypothesis 3 stated that the greater the belief that failure is an inherent risk of owning and running a firm, the lower the stigmatization in terms of greater (a) empathy and (b) assistance afforded to the unemployed individual. The results for this hypothesis are presented in column 4 of Tables 2 and 3. We found that inherent risk has a significant positive influence on the empathy afforded ($\beta = .307 p<0.01$) but did not have an influence on the assistance afforded to the individual ($\beta = .148 p>0.05$). Thus we receive partial support for Hypothesis 3.

Hypothesis 4 stated that the relationship between accountability for failure and (a) empathy and (b) assistance afforded is moderated by the extent that the respondent believes that failure is an inherent risk of firm ownership, such that the extent of the relationship is reduced. The results for this hypothesis are presented in column 6 of Tables 2 and 3. We found that the moderation term had a significant negative influence on empathy ($\beta = -.179 p<0.05$) but did not have an influence on the assistance afforded to the individual ($\beta = -.165 p>0.05$). To determine the nature of the interaction between inherent risk and accountability (Hypothesis 4), we plotted the effect of accountability on empathy for values of inherent risk set at one standard deviation above and below the mean, as suggested in the literature (Cohen & Cohen, 1983). Our results are plotted in Figure 1. We found that individuals who believe that failure is an inherent risk of firm ownership are more sensitive to the extent that they believe that the individual was accountable for the failure when considering the amount of empathy to afford the individual. Thus we did not find support for Hypothesis 4.
We found that entrepreneurs are held accountable for the failure of their firms irrespective of the extent of controllability they had over the cause of the failure. Specifically, we did not find a mean difference regarding the perceived extent of accountability the entrepreneur had over the cause of failure between our two experimental conditions: (1) a downturn in the economy was the cause of the failure and (2) a loss of a major sales account by the entrepreneur was the cause of the failure. In contrast, we find that there is substantial variation in the extent that employees are held accountable for the failure of the firm depending on the cause of the failure. In particular, we find that entrepreneurs are held more personally accountable for the firm failure than employees in all experimental conditions, even when information is present that the situation was the culpable factor. In turn, we found that the extent of accountability for the failure has a negative influence on the amount of empathy afforded to the individual. Thus, our findings help explain why entrepreneurs can experience stigma after firm failure.

We also found that respondents who believed that failure was an inherent risk of owning and running a firm that is difficult to avoid were more likely to afford individuals who become unemployed as a result of firm failure empathy. In particular, respondents were more likely to afford these individuals empathy when they also believed that individuals had limited accountability for their unemployed state. An outcome of this finding is that it provides a starting point for understanding how to reduce the extent of stigmatization experienced by failed entrepreneurs. By increasing awareness that failure is an inherent risk of owning and running a firm that is difficult to avoid, entrepreneurs are likely to be held less accountable for their failures and, in turn, experience less stigma as a result.

Our findings have important policy implications. At a macro-level the extent of stigmatization influences the relative risks of choosing self-employment or paid employment and thus the number of individuals who are willing to engage in entrepreneurial ventures (Armour & Cumming, 2005). This is through a signaling effect regarding the attractiveness of self-employment as a career choice, perceptions of stigma towards failed entrepreneurs and the motivations of failed entrepreneurs to re-enter self-employment (cf. Baumol, 1990). In turn, the relative risks to self-employment and paid employment impacts the overall economic growth in the economy (Landier, 2005).

In this paper we investigated why entrepreneurs experience stigma after firm failure and what can be done to reduce it. We found that entrepreneurs are held accountable for the failure of their firms irrespective of the circumstances causing the failure. This finding suggests that the reason why the firm failed has little influence on the experience of stigma; rather it is failure per se that is stigmatizing. We also found that respondents who viewed failure as an inherent risk of firm ownership that is difficult to avoid were less likely to stigmatize failed entrepreneurs. This finding suggests that a greater understanding of the risks involved in firm ownership is one mechanism that can help reduce the stigmatization of failed entrepreneurs.

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Reference List


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**Table 1: Mean Comparison: Accountability**

<table>
<thead>
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<th>Treatment</th>
<th>n</th>
<th>Mean</th>
<th>S.D</th>
<th>Comparison</th>
<th>Significance</th>
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<td>3.79</td>
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<td></td>
<td></td>
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<td>Employee, Sale Account</td>
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<td>.90</td>
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<td></td>
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<td></td>
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**Table 2: Regression results Empathy**

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<th>Empathy</th>
<th>Empathy</th>
<th>Empathy</th>
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<td>.579*</td>
<td>.517</td>
<td>.422</td>
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<td>Prior Self-employment</td>
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<td>-.078</td>
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<td>-.239</td>
<td>-.244</td>
<td>-.290</td>
<td>-.202</td>
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<tr>
<td>Family, friends self-employed</td>
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<td>-.580</td>
<td>-.467</td>
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<td>-.762*</td>
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<tr>
<td>They family friends unemployed</td>
<td>.199</td>
<td>.125</td>
<td>.174</td>
<td>.083</td>
<td>.114</td>
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<tr>
<td>Constant</td>
<td>4.135***</td>
<td>5.171***</td>
<td>2.963***</td>
<td>4.598***</td>
<td>1.761</td>
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</table>

**Research variables**

| Accountability | -.354** | -.412** | .392 |
| Inherent risk   | .307*   | .361**  | .987**|
| Inherent risk x Accountability | -.179* |

N 82

| Adjusted R Square | .057+   | .131**  | .124*  | .229*** | .265*   |
| F                 | 1.942+  | 2.957*  | 2.841* | 4.306** | 4.511***|
### Table 3: Regression results Assistance

<table>
<thead>
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<th></th>
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<td>Constant</td>
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<td>2.963***</td>
<td>5.291***</td>
<td>2.674</td>
</tr>
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</table>

**Research variables**

|                     |          |            |            |            |            |
|---------------------|----------|------------|------------|------------|
| Accountability      | -.286+   |            |            |            | .425       |
| Inherent risk       |          | .148       | .190       | .767+      |            |
| Inherent risk x Accountability |      |            |            |            | -.165      |

|               |          |            |            |            |            |
| N               | 82       |            |            |            |            |
| Adjusted R Square| .017     | .048 +     | .018       | .059+      | .077       |
| Change Adj. R Square |        |            |            |            |            |
| F                | 1.270    | 1.660      | 1.240      | 1.697      | 1.813+     |

**Figure 1: Interaction – Accountability and Inherent Risk**

![Graph showing the interaction between Accountability and Inherent Risk](attachment:image.png)
Appendix 1: The four different experiment treatments (vignettes)

Entrepreneur, internal cause of failure (lost large and important customer)

Annie Day, the founder of Nordic Designs, is currently unemployed.

She owned and operated Nordic Designs, a Scandinavian design store specializing in the product development and sales of classic and contemporary designs for the home.

Since Annie started the business nearly ten years ago it has experienced steady growth and a healthy profit until recently when Annie lost a major sales account after months of negotiation.

The lost account has resulted in a substantial drop in sales. The business has subsequently struggled to meet its financial obligations and was placed in bankruptcy.

The firm failure has left Annie unemployed.

Employee, internal cause of failure (lost large and important customer)

Annie Day, a former employee of Nordic Designs, is currently unemployed.

She was employed at the firm Nordic Designs, a Scandinavian design store specializing in the product development and sales of classic and contemporary designs for the home.

The business experienced steady growth and a healthy profit for nearly ten years. Recently Annie lost a major sales account after months of negotiation on her part.

The lost account has resulted in a substantial drop in sales. The business has subsequently struggled to meet its financial obligations and was placed in bankruptcy.

The firm failure has left Annie unemployed.

Entrepreneur, external cause of failure (financial crisis)

Annie Day, the founder of Nordic Designs, is currently unemployed.

She owned and operated Nordic Designs, a Scandinavian design store specializing in the product development and sales of classic and contemporary designs for the home.

Since she started the business nearly ten years ago it has experienced steady growth and a healthy profit until recently when the effects of the recent financial crisis resulted in a steady decrease in sales.

As a consequence of the decrease in sales, the business struggled to meet its financial obligations and was placed in bankruptcy.

The firm failure has left Annie unemployed.
Employee, external cause of failure (financial crisis)

Annie Day, a former employee of Nordic Designs, is currently unemployed.

She was employed at the firm Nordic Designs, a Scandinavian design store specializing in the product development and sales of classic and contemporary designs for the home.

The business experienced steady growth and a healthy profit for nearly ten years. Recently the effects of the recent financial crisis resulted in a steady decrease in sales.

As a consequence of the decrease in sales, the business struggled to meet its financial obligations and was placed in bankruptcy.

The firm failure has left Annie unemployed.