ENTREPRENEURIAL DISCOVERY OR CREATION?
IN SEARCH OF THE MIDDLE GROUND

Nicolai J. Foss
Copenhagen Business School and Norwegian School of Economics
njf.smg@cbs.dk

Peter G. Klein
Baylor University and Norwegian School of Economics
peter_klein@baylor.edu

18 March 2016

Academy of Management Review, forthcoming

Introduction

Stratos Ramoglou and Eric Tsang (2016) propose a middle-ground position in the long-standing debate on whether entrepreneurial opportunities are best understood as objective, existing independent of entrepreneurial action, or as subjective and constructed by the entrepreneur. Controversy about exogenous discovery versus endogenous creation go back at least four decades in the economics of entrepreneurship (e.g., Kirzner, 1971; Casson, 1982). In the management literature on entrepreneurship the extreme positions are the “individual/opportunity nexus” (or “discovery”) view associated with Shane (2012; Shane & Venkataraman, 2000) and the “creation” view associated with Alvarez and Barney (2007, 2010). Those positions are central to ongoing discussions about the ontological, epistemological, and explanatory status of the opportunity construct (Short, Ketchen, Shook, & Ireland, 2010; Dimov, 2011). Ramoglou and Tsang (2016) suggest a “realist” alternative occupying a middle-ground position between the discovery and creation views. Key to their approach is the analytical separation of opportunities and profits: while market outcomes are uncertain and unknown at the time of action, opportunities—conceived as *propensities* for profits—exist independently and prior to action.

We applaud Ramoglou and Tsang’s effort to reconcile the discovery and creation views, as we also find the extreme positions in the debate unsatisfactory. However, we think that Ramoglou and Tsang’s contribution muddies the waters. First, they largely neglect two existing middle-ground perspectives that are more straightforward and intuitive than their complicated and difficult exercise, the *effectuation/bricolage* approach (Sarasvathy 2008; Baker & Nelson, 2005) and the *judgment-based view* (McMullen & Shepherd, 2006; Klein, 2008; Wood & McKinley, 2010; Foss & Klein, 2012; Alvarez et al., 2014). In doing so, they misconstrue the current controversy over entrepreneurial opportunities, which is not only about the realism of opportunities, but the usefulness of the opportunity construct itself. We think their argument confuses the ontological, epistemological and explanatory/methodological issues involved in the debate, leading them to offer a proposed solution that is unnecessarily cumbersome and potentially misleading.

Middle-Ground Views: Judgment and Effectuation

Both the judgment and effectuation/bricolage views deny the existence of opportunities exogenous to entrepreneurial action. However, this does not imply radical subjectivism or social constructivism; these views see entrepreneurship as enabled and constrained by objective factors such as resource availability, technology, consumer preferences, and institutions that shape entrepreneurial imagination and ultimately determine success and failure. Entrepreneurial action unfolds over time as entrepreneurs experiment with resource combinations, attempt to circumvent constraints, revise initial plans, and so on. The interaction of internal cognitive factors and external constraining and enabling factors constitutes the mechanisms that produce observable events, such as whether entrepreneurs realize profits, achieve personal satisfaction, or meet other objectives. Entrepreneurship research is about theorizing and testing these mechanisms. Because our contributions lie within the judgment view, we concentrate here on this theory of entrepreneurship as it speaks to the issue of entrepreneurial opportunities.

In our attempts to update the entrepreneurship theory associated with classical writers such as Knight (1921) and Mises (1949), we have criticized the idea that entrepreneurial value creation can be separated into clearly delineated discovery, evaluation, and exploitation phases (Foss & Klein, 2012; Klein, 2008). In our perspective, opportunities for entrepreneurial profit do not exist, objectively, waiting to be discovered and exploited, but neither are they created at will. Rather, “opportunity” is a metaphor, a shorthand for the entrepreneur’s beliefs, or judgments, about the uncertain future. (Kirzner [1999] makes it clear that entrepreneurial discovery is a metaphor or analytical device, not an ontological claim.) The essence of entrepreneurship is the actions undertaken to bring about the future and the outcomes that result, not the imagined future itself. This approach may be construed as a middle-ground perspective because we do not deny that objective *indications* of future profits may exist, such as marketing research revealing that customers value certain attributes not currently offered on the market. But these do not constitute opportunities in the literal sense, or even in Ramoglou and Tsang's (2016) sense of probabilistic tendencies toward particular outcomes. First, the objective indicators require *interpretation;* survey results and similar metrics are data, but the knowledge embodied therein contains an essential subjective element. Second, unmet market demands, once perceived, do not generate profits without resource commitments, including the entrepreneur's own labor. Third, the results of entrepreneurial action cannot be known *ex ante*, but only come into being *ex post*, when consumers, rivals, and other market participants have had their say.

Thus, entrepreneurial action begins with the entrepreneur's interpretation of current (objective) conditions, his beliefs about possible future states of the world (e.g., a profitable product or venture), and his expectations and confidence in his ability to bring about that possible future—all these constituting what Knight (1921) famously called judgment. The entrepreneur then acts (or doesn't act), with success or failure determined ex post, largely by objective factors. In this perspective, the language of "opportunities" is redundant at best, misleading at worst. The discovery view mistakenly implies that opportunities exist independent of human belief and action. The creation view rightly emphasizes human belief and action, but mistakenly implies that profit opportunities, once the entrepreneur has conceived or established them, somehow come into being. We too think entrepreneurship is a creative process but say that what entrepreneurs create (or attempt to create) are not opportunities, but new firms, new products, or new markets. When they are successful, their efforts may be recast in opportunity language. But little or no additional insight is produced by doing so.

Redefining opportunities as propensities strikes us as an improvement, but still implies a general, implicit movement toward entrepreneurial success. Why not use the term "possibilities" or—even better—simply drop the opportunity construct altogether (cf. also Davidsson and Tonelli, 2013)?

The Explanatory and Methodological Status of "Opportunity"

Ramoglou and Tsang (2016: 30) characterize our critique of the opportunity-discovery view (Klein, 2008; Foss and Klein, 2012) as epistemological: because opportunities cannot be known ex ante, opportunity is not a useful construct. They argue instead that opportunities can be real even if unknown at the moment of action. "Profits relate *epistemologically* to opportunities: when profits are realized we know that the related opportunities exist. However, opportunities are *ontologically* irreducible to profits and, therefore, it does make sense to discuss opportunities as propensities prior to the realization of profits." But our critique is not ontological or epistemological, but *methodological*. What we question is the explanatory value of talking about opportunities independent of the entrepreneur's beliefs and actions, market outcomes, and subsequent processes of learning and adjustment.

Our position is that all the important phenomena of interest to entrepreneurship scholars—entrepreneurial cognition, founder characteristics, the acquisition and combination of resources for new products and ventures, the choice of individuals between self-employment and paid employment, the organization of innovation, the effect of institutions and the competitive environment on entrepreneurial outcomes, and so on—can be explained with reference to the entrepreneur's beliefs, actions, results, and adjustments. There is no *need* to invoke the nebulous and elusive concept of opportunities when what we mean are expectations, plans, efforts, and outcomes.

Ramoglou and Tsang devote considerable effort to distinguishing among realized opportunities, unrealized opportunities, and what they call "non-opportunities," i.e. propensities toward profit that "lack[] the objective conditions necessary for profit actualization." We find this exercise cumbersome and unnecessary. When an entrepreneur's beliefs about the future are mistaken, and she takes actions that lead to losses rather than profits, what is gained by saying she "pursued a non-opportunity"? Why not simply say that she exercised poor judgment, and hence the venture did not perform up to her expectations? The idea of pursuing non-opportunities violates the ordinary-language notion of "opportunity" and hence tends to mislead researchers, students, practitioners, and policymakers.

REFERENCES

Alvarez, S. A., & Barney, J. B. 2007. Discovery and Creation: Alternative Theories of Entrepreneurial Action. ***Strategic Entrepreneurship Journal*** 1(1–2): 11–26.

Alvarez, S. A. &. Barney, J. B. 2010. Entrepreneurship and Epistemology: The Philosophical Underpinnings of the Study of Entrepreneurial Opportunities. ***Academy of Management Annals*** 4(1): 557–83.

Alvarez, S. A., Barney, J. B., McBride, R., & Wuebker, R. 2014. Realism in the Study of Entrepreneurship. ***Academy of Management Review***, 39: 227-233.

Baker, T. & Nelson, R. E. 2005 Creating Something from Nothing: Resource Construction through Entrepreneurial Bricolage. ***Administrative Science Quarterly,*** 50: 329-366.

Busenitz, L. W., & Barney, J. F. 1997. Differences between Entrepreneurs and Managers in Large Organizations: Biases and heuristics in Strategic Decision-Making. ***Journal of Business Venturing,*** 12(1): 9-30.

Casson, M. 1982. ***The Entrepreneur: An Economic Theory***. 2003 ed. Aldershot: Edward Elgar.

Davidsson, P., & Tonelli, M. 2013. Killing Our Darling: Why We Need to Let Go of the Entrepreneurial Opportunity Construct. In Davidsson, P., ed., ***Conference Proceedings: Australia Centre for Entrepreneurship (ACE) Research Exchange Conference 2013***, Australia Centre for Entrepreneurship, Queensland University of Technology, Brisbane, QLD

Dimov, D. 2011. Grappling with the Unbearable Elusiveness of Entrepreneurial Opportunities. ***Entrepreneurship Theory and Practice,*** 35: 57–81.

Forbes, D. P. 2005. Are Some Entrepreneurs More Overconfident than Others? ***Journal of Business Venturing,*** 20(5): 623-640.

Foss, N. J. & Klein, P. G. 2012. ***Organizing Entrepreneurial Judgment.*** Cambridge: Cambridge University Press.

Kirzner, I. M. 1971. Entrepreneurship and the Market Approach to Development. In Hayek, F. A., Hazzlitt, Read, L. R., Velasco, G. & Harper, F. A., eds. 1971. ***Toward Liberty: Essays in Honor of Ludwig von Mises on the Occasion of his 90th Birthday, September 29, 1971***. Menlo Park: Institute for Humane Studies.

Kirzner, I. M. 1999. Creativity and/or alertness. ***Review of Austrian Economics*,** 11: 5-17.

Klein, P. G. 2008. Opportunity Discovery, Entrepreneurial Action, and Economic Organization. ***Strategic Entrepreneurship Journal***, 2: 175-190.

Knight, F. H. 1921**. *Risk, Uncertainty, and Profit***. Reprinted (1965), New York: Augustus M. Kelley.

McMullen, J., & Shepherd, D. A. 2006. Entrepreneurial Action and the Role of Uncertainty in the Theory of the Entrepreneur. ***Academy of Management Review***, 31: 132–52.

Mises, Ludwig von. 1949. ***Human Action: A Treatise on Economics***. New Haven: Yale University Press.

Ramoglou, S. & Tsang, E. 2016. A Realist Perspective of Entrepreneurship: Opportunities as Propensities. ***Academy of Management Review*** (forthcoming).

Sarasvathy, S. D. 2008. ***Effectuation: Elements of Entrepreneurial Expertise***, Northampton: Edward Elgar Publishing.

Shane, S. 2012. Reflections on the 2010 *AMR* Decade Award: Delivering on the Promise of Entrepreneurship as a Field of Research. ***Academy of Management Review***, 37: 10-20.

Shane, S. &Venkataraman, S. 2000. The Promise of Entrepreneurship as a Field of Research. ***Academy of Management Review*,** 25: 217–226.

Short, J. C., Ketchen, D. J. Shook, C. L. & Ireland, R. D. 2010. The Concept of "Opportunity" in Entrepreneurship Research: Past Accomplishments and Future Challenges. ***Journal of Management,*** 36(1): 40–65.

Wood, M. S., & McKinley, W. 2010. The Production of Entrepreneurial Opportunity: A Constructivist Perspective. ***Strategic Entrepreneurship Journal***, 4: 66-84.

Nicolai J. Foss (njf.smg@cbs.dk) is Professor of Strategy and Organization at the Copenhagen Business School (CBS), Department Head, Department of Strategic Management and Globalization at CBS, and Professor of Knowledge-based Value Creation at the Norwegian School of Economics. He received his Ph.D. from CBS. His interests lie in the theoretical and empirical aspects of microfoundations for strategic management theory and in the intersection of organizational economics and strategic management.

Peter G. Klein (peter_klein@baylor.edu) is Professor of Entrepreneurship at the Hankamer School of Business, Baylor University, and Professor of Strategy and Management at the Norwegian School of Economics. He received his Ph.D. from the University of California, Berkeley. His research and teaching focus on the relationship between entrepreneurship and firm strategy and organization, with applications to diversification, health care, and public policy.