



Buying Entrepreneurship: An Examination of the Drivers of Entrepreneurship through Acquisition

Justin Kent¹

¹ Assistant Professor, Department of Management, Walker College of Business, Appalachian State University, USA

Abstract

Entrepreneurship through acquisition represents a viable path to entrepreneurship, yet little is known about the characteristics of the individuals attracted to these types of opportunities. Using a unique dataset of aspiring entrepreneurs, we find that aspiring entrepreneurs with more experience are more likely to proceed with an ETA opportunity while those with experience working in bureaucratic organizations are less likely to proceed with an ETA opportunity. Finally, aspiring entrepreneurs who have stronger implicit motivations of status and recognition are also more likely to proceed with an ETA opportunity. Implications of the findings are discussed and directions for future research are offered.

Keywords: Entrepreneurship, Acquisition, Business, Ownership, Ecosystem

Introduction

Across the decades, scholars have offered a variety of definitions for entrepreneurship (Brockhaus, 1985; Carsrud, Olm & Edy, 1985; Gartner, 1990; Venkatraman, 1997). Some economists have defined entrepreneurship through the vehicle of the entrepreneurs themselves, who have been described as being risk takers (Mill, 1848), uncertainty bearers (Knight, 1921), innovators (Schumpeter, 1934), and arbitrageurs (Kirzner, 1973). Other researchers have interpreted entrepreneurship through its effects on economies (Acs & Szerb, 2007; Wennekers & Thurik, 1999) and communities (Barth, 1963; Austin, Stevenson & Wei-Skillern, 2006). Another scholarly stream of work has aimed to decipher entrepreneurship by parsing it into its fundamental activities, such as its discovery, evaluation, and exploitation processes (Bhave, 1994; Shah & Tripsas, 2007; Ahuja & Lampert, 2001).

Shane and Venkatraman (2000, p. 218) have integrated these variegated perspectives into a definition of entrepreneurship that has found reasonable consensus across the entrepreneurship community: “how, by whom, and with what effects opportunities to create future goods and services are discovered, evaluated, and exploited.” In spite of the wide berth that this definition affords, a typical premise regarding how opportunities to create future goods and services come to fruition centers on *de novo* entrepreneurship. Indeed, to date, a major thrust of entrepreneurship research has focused on new venture creation as being the primary mode of entrepreneurial entry. As a consequence, alternative paths to entrepreneurship – such as through the acquisition of an existing business – have been underexplored (Cooper & Dunkelberg, 1986; Parker & Praag, 2012).

We define entrepreneurship through acquisition (ETA) as the acquisition of an existing business by an individual (or group of individuals) with the intent to enact their entrepreneurial vision and actively manage the venture.¹ ETA is an important part of the entrepreneurial ecosystem because it involves the revitalization of existing systems of wealth and contributes to the well-documented interplay between entrepreneurship and economic growth (Hunt & Fund, 2012). To this end, estimates indicate that ETA transactions account for approximately five percent of the total annual business ownership transfers in the United States. These ETA transactions collectively represent \$25bn to \$40bn in total value – and it has been suggested that their associated economic impact well surpasses these statistics (Hunt & Fund, 2012).

¹This definition is similar to the one put forth by Hunt and Fund (2012) but does not restrict acquisition size to revenues greater than \$500,000 or less than \$50 million. Hunt and Fund argue that acquisitions with revenues less than \$500,000 should be excluded from the ETA classification because they would not be able to support a living wage for the entrepreneur, capital for transformational initiatives, or cover the debt maintenance associated with the acquisition. This overly narrow definition excludes entrepreneurs who are willing and able to take less than a living wage because they believe in the future prospects of an opportunity or entrepreneurs who self-fund an acquisition with sufficient resources to enact their vision for the acquired business.

ETA complements the new venture creation perspective in entrepreneurship. Exploiting opportunities to create future goods and services can be accomplished through both organic and inorganic means. For example, opportunities positioned in new industries that are surrounded with a high degree of uncertainty regarding demand and design would likely be attractive to start-up entrepreneurs. Entrepreneurs who are comfortable with uncertainty and prefer to experiment with different business models or product innovations stand to reap substantial financial returns if they are able to establish the dominant design and become a market leader (Murmann & Tushman, 2001). They also risk failure if their assumptions about the market are wrong. This high risk-high reward approach to entrepreneurship might not appeal to everyone. ETA offers an alternative path to business ownership where individuals can create future goods or services in an established context, thus avoiding much of the uncertainty associated with start-up entrepreneurship².

Notwithstanding the growing interest in ETA and its impact in the economy, little is known about the characteristics of entrepreneurs attracted to ETA opportunities. Some scholars have explored the factors that influence entrepreneurial entry mode decisions (Cooper & Dunkelberg, 1986; Parker & Praag, 2012) by comparing entrepreneurs who take over a business (either a family business they are associated with or an external takeover) with entrepreneurs who founded their venture. While these comparisons shed light on the differences between start-up entrepreneurs and takeover entrepreneurs, it is difficult to study these preferences after the decision to exploit has already been made. This project complements the research on entry mode preferences by using a risk set of potential entrepreneurs to explore the factors that influence their decision to proceed with or abstain from an ETA opportunity.³ Specifically, we seek to answer the following research question: how does an entrepreneur's prior work experience and motivation affect the entrepreneur's interest in pursuing ETA opportunities?

This study proceeds as follows. First, we position ETA in the finance and entrepreneurship literatures and consider the three primary entrepreneurial processes of ETA transactions. From there, we develop hypotheses that consider the relationships between key characteristics of the entrepreneur and the likelihood of their engagement in ETA. After describing our dataset and methodology, we share our results and analysis. Finally, we conclude with a discussion of the theoretical and practical implications of the study.

Background and Theoretical development

The ETA Phenomenon

ETA is a discipline-spanning phenomenon that has roots in both finance and entrepreneurship. In the finance literature, ETA is categorized as a rare type of buyout that is undertaken for growth aspirations rather than as an efficiency tool to streamline organizational processes (Wright, Hoskisson & Busenitz, 2001). From an entrepreneurship perspective, ETA represents an alternative entry mode into business ownership that involves different opportunity discovery, evaluation, and exploitation processes but does not require starting a new firm. Entrepreneurs engaging in ETA search for potential targets rather than building them. Once a suitable business has been discovered, the entrepreneur evaluates both the terms of a purchase agreement and their ability to successfully enact their vision to grow the business. Finally, exploitation of the acquisition target is accomplished by creating new value from existing business systems and underutilized assets. In an ETA context, a lower level of operational uncertainty surrounds acquisition opportunities because the business is established and the challenges facing management are often apparent.

In finance, ETA is one of several forms of buyouts, yet research has focused almost exclusively on large, public company leveraged buyouts (LBO) despite their rarity (Harris, Siegel & Wright, 2005). For example, in 2020, 186 large cap LBOs were completed which represents a small fraction of the total number buyouts completed when management buyouts, management buy-ins, divisional buyouts and ETA transactions are taken into account (Latour, 2021).

ETA and LBOs both seek to identify and acquire undervalued assets but ETA differs from LBOs in several ways. First, the goal of an LBO is to improve efficiency and reduce costs to generate free cash flows sufficient to service the debt used to acquire the assets. Over time, value is created through paying down the debt and incrementally improving performance. Equity holders in an LBO will typically pursue an exit within 3-5 years through a sale to a strategic buyer, IPO, or recapitalization (Olsen, 2003). In contrast, ETA uses free cash flows to fund growth initiatives such as new products, services, and/or markets to increase value. Entrepreneurs who acquire an existing business have a longer time horizon than LBO funds to allow initiatives to come to fruition. LBOs and ETAs also differ in their governance. LBOs maintain a principle-agent structure with fund managers (agents)

² While Knightian uncertainty cannot be eliminated, established businesses benefit from reduced state, effect, and response uncertainty (Millikan, 1987) when compared to start-up ventures. Established businesses have prior experience that provides insight into the current trends of their business environment (State Uncertainty) and its potential effect on the business (Effect Uncertainty). Established businesses are also more likely to understand who their competitors are and how they might respond to potential actions by the business (Response Uncertainty).

³ Note that this study does not seek to compare start-up entrepreneurship with ETA; rather, it is focused on investigating ETA itself.

overseeing management. ETA is free from the monitoring and incentive alignment issues associated with principal-agent governance because the entrepreneur who acquires the business is both the principal and the agent (Jensen & Meckling, 1976).

The act of franchising could be considered a type of ETA, but we argue that franchising is fundamentally distinct from ETA. Franchising is a contractual arrangement between two independent entities, whereby the franchisee pays the franchisor for the right to sell the franchisor's product or service and/or the right to use his trademark at a given place and for a certain period of time (Lafontaine, 1992). Under the franchise agreement, franchisors are required to operate under the direction of the franchisor thus limiting their ability to make transformational changes. Moreover, most franchisees purchase a franchise for the express purpose of operating a business with a proven operating system that does not require implementation of new strategies for success. In contrast, implementation of transformational strategies are a key component of ETA. Franchising is also contractually limited in duration while ETA continues in perpetuity or when the entrepreneur decides to sell or close the business.

ETA and franchising also differ in their governance and strategy. Franchisees purchase a residual claim but do not have full decision rights and must operate within the boundaries outlined by franchisor to maintain trademark value. Some decision rights (e.g., menu selection, building design, etc.) are maintained by the central company. The central company has authority to monitor the franchisee for product quality and to terminate the contract if the quality is not maintained (Brickley & Dark, 1987). Consequently, strategies of efficiency and cost control are preferred while long term growth is accomplished through geographic expansion. In contrast, Participants in ETA have full decision rights including the freedom to implement any changes they believe will enhance the future prospects of the business without oversight from an outside entity. They have the freedom to pursue a variety of strategies including introducing new products or services, entering new markets or reconfiguring the value chain. In summary, ETA, LBOs, and franchising all involve the purchase of assets but are dissimilar in their purpose, governance, strategy and time horizon. The key difference is that ETA has the freedom and mandate to pursue transformational changes to grow the business over a longer term time horizon.

In the entrepreneurship literature, ETA represents an alternative path to business ownership because many of the challenges facing potential entrepreneurs in de novo opportunities are absent in ETA opportunities. Potential entrepreneurs must first have an idea for a business, develop a business model, and conduct activities to reduce uncertainty and mitigate risk. Start-up entrepreneurs increase their chances of success by remaining flexible and adapting as they reduce the uncertainty surrounding their opportunity. In contrast, an ETA entrepreneur's early success depends on their ability to forecast the future performance of the business and negotiate acquisition terms with current ownership. Once a decision to exploit an opportunity has been made, start-up entrepreneurs identify and seek to acquire the necessary financial, social, and human capital needed to support the new venture. Activities are focused on growing the business and developing legitimacy (Aldrich & Ruef, 2006). ETA entrepreneurs, on the other hand, become managers of established businesses that own a specific stock of human, social, and financial capital as well as a certain level of legitimacy. Activities for ETA entrepreneurs, post-acquisition, are focused on implementing their vision for the business and executing the strategy they believe will lead to success. In short, start-up entrepreneurs make decisions under uncertainty to create a new organization; ETA entrepreneurs are change agents that strive to overcome organization inertia to execute transformational strategies.

Entrepreneurial Processes in ETA

Entrepreneurs have the opportunity to create value in an ETA transaction through three distinct processes. First, they may create value as a Kirznerian entrepreneur through arbitrage by acquiring an undervalued company and selling it in the future at a profit. Second, they may create value as a resource organizer both by assembling the resources (such as debt and equity financing) needed to acquire the business and also by structuring the transaction. Finally, they may create value as a Schumpeterian entrepreneur by enacting their vision for the business through recombination. Here, revitalization occurs when the new owner engages in creative destruction as they enact their vision on the acquired organization. Each of these three processes, or mechanisms, shape the entrepreneur's perspective of ETA and thus their likelihood of engagement in an ETA transaction.

Arbitrage in ETA:

The concept of "entrepreneur as arbitrageur" has its roots in the Austrian tradition of economics. As opposed to the steady equilibrium world of neoclassical economics, the Kirznerian entrepreneur operates in a dynamic market where prices fluctuate in response to constantly changing supply and demand. Shortages, surpluses, and misallocated resources create opportunities for entrepreneurs to buy when prices are too low and sell when prices are high, thus moving the market in the equilibrating direction (Kirzner, 1997). Individuals can create an organization to buy undervalued assets at a low price with the intent to resell them in the future at a higher price as shown by many wealth management organizations. Alternatively, the individual can view the firm itself as an undervalued asset that can increase in value under the direction of the entrepreneur. The act of searching for a company to purchase with the intent to sell in the future for a profit is an act of arbitrage. As a result of incomplete information, ETA entrepreneurs

believe they are more aware of the market value of the target business than others, including the owners (Kirzner, 1973). Put differently, ETA involves the purchase of a set of tangible and intangible assets that, as a whole, are undervalued from the entrepreneur's point of view. The entrepreneur expects, in the context of uncertainty, that the value of the bundle of assets will appreciate in value over time. Purchasing an undervalued business with the expectation of reselling it in the future for a profit is the first step in value creation in an ETA opportunity.

Organization of Resources in ETA:

After an arbitrage opportunity has been discovered by the entrepreneur, acquiring the business requires the entrepreneur to act as an organizer of resources (Herbert & Link, 1989). The ETA entrepreneur acquires and organizes capital from institutions and investors by raising debt and equity financing to acquire the target firm. The entrepreneur believes, and convinces debtors and investors, the purchase of the business is a more efficient use of capital than alternatives given its comparable risk profile. Variation exists within the potential future capital structures of the acquisition. A more levered structure increases the risk of the acquisition and the associated cost of capital but multiplies the equity holder's return on investment. To efficiently organize resources, the entrepreneur must take into account the risks associated with the acquisition. Due to information asymmetry, the entrepreneur knows more about the quality of the acquisition and their abilities to successfully manage the business in the future than the resource providers. Therefore, debtor and investors will require terms that reduce their risk such as collateralization of assets or flexible investment instruments. Through negotiation, the entrepreneur can create value by structuring the transaction in a way that positions them for the best chance of success.

Recombination in ETA:

Post-acquisition, the entrepreneur renews the business through transformational change. In contrast to the Kirznerian entrepreneur, the Schumpeterian entrepreneur recombines resources in new ways to create new opportunities which lead to market disequilibrium. The entrepreneur enacts his or her new vision in a process of creative destruction by introducing new products/services, entering new geographical markets, using new raw materials, implementing new methods of production and/or organizing in new ways (Schumpeter, 1934). Value is created as the innovations introduced by the entrepreneur revitalize dormant assets and direct company vision and strategy to new opportunities.

Hypothesis Development

Given the unique nature of ETA opportunities, it follows that potential entrepreneurs might also have specific characteristics that influence how they evaluate ETA opportunities.⁴ The accumulated experience a potential entrepreneur possesses may influence the decision to proceed with an ETA opportunity in several ways. First, prior experience provides a foundation of knowledge from which to search for and evaluate opportunities. Entrepreneurial alertness, or the ability to notice overlooked opportunities (Kirzner, 1979), is an attribute that builds on prior knowledge (Ardichvili, Cardozo & Ray, 2003) and is developed over time (Baron & Ensley, 2006). More experienced potential entrepreneurs have had more time to build a stock of prior knowledge that can help them recognize opportunities that others do not see and accurately evaluate an opportunity's chances of success. This prior knowledge could include relevant industry trends or available technology that could be deployed in a new or acquired business.

Next, potential entrepreneurs with more experience are more likely to acquire financial capital (Bates, 1997; Mason & Harrison, 1996). The majority of entrepreneurs finance their venture with their savings (Aldrich & Ruef, 2006) and more experienced individuals have had more time to save the funds necessary to get their venture off the ground. More experienced potential entrepreneurs are also better positioned to raise external funding because they have had more time to develop the breadth of their overall network and strength of their network ties. Potential entrepreneurs with more developed social networks are more likely to share social ties with prospective investors and entrepreneurs who share social ties with investors are more likely to receive investment (Burton, Sorenson & Beckman, 2002; Shane & Cable, 2002; Shane & Stuart, 2002).

In addition to the effect experience has on social network development, industry and management experience also signal to potential investors that the individual has the ability to successfully exploit an opportunity (Casson, 1982). More experienced potential entrepreneurs have had more time to acquire knowledge and skills that provide the foundation for their entrepreneurial logic and management acumen. This experience sends a positive signal to potential investors that the individual can successfully navigate uncertainty and effectively manage the venture from inception to exit and therefore is more worthy of investment (Feeney, Haines & Riding, 1999).⁵

⁴ Individuals pursuing an ETA opportunity will often start a shell company to facilitate search activities, equity financing, and capital gain (loss) distribution (Grousebeck, 2010). In contrast to traditional start-up entrepreneurship, these shell companies do not aim to create future goods or services.

⁵ Extant research has shown that an inverted-U relationship exists between age and the likelihood of starting a business (Shane, 2003). However, these findings are based on studies of general populations while we are sampling individuals who have

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In an ETA context, more experience should increase the potential entrepreneur's ability to negotiate favorable acquisition terms with current ownership, sell retained employees on their vision for the company and motivate them to support the new direction of the business, and implement strategies that can lead to sustainable competitive advantage. Therefore,

Hypothesis 1: Potential entrepreneurs with more experience will be more likely to favorably evaluate an ETA opportunity.

In addition to work experience tenure, experience type also plays a role in entrepreneurial decision making (Hsieh, 2016; Dobrev & Barnett, 2005). Characteristics of previous employers, such as age, size, and reputation, have been shown to affect rates of entrepreneurial entry (Buenstorf & Klepper, 2009; Gompers, Lerner & Scharfstein, 2005; Stuart, Ding & Stuart, 2006). The hierarchical nature of large and established organizations promotes efficiency and control which limits opportunities to make decisions under uncertainty (Burns & Stalker, 1961). Individuals with work experience in hierarchical organizations are less likely to take entrepreneurial action for several reasons. First, hierarchies have rigidly defined roles and emphasize rules and routines in a way that can lead employees to focus on strict adherence to regulations which induces timidity and conservatism (Merton, 1968). Other studies have found that individuals who work in hierarchical organizations have less intellectual flexibility and greater social conformity than those who work in non-hierarchical organizations (Kohn & Schooler, 1982). Hierarchy's effect on employee attitudes and cognitive frames may increase timidity, conservatism, rigidity, and conformity which stands in stark contrast to attributes typically found in entrepreneurship such as boldness, risk-taking, flexibility, and going against social norms (Sorensen, 2007).

Second, hierarchies may hamper or prevent employees from developing skills that might be helpful in entrepreneurial settings. Employees in hierarchical organizations are more likely to be responsible for a narrow set of tasks while missing out on opportunities to develop a broader skillset that might be useful in entrepreneurial contexts. Lazear (2005), argued that entrepreneurs should be jacks of all trades, or have some knowledge of a large number of business areas to successfully bring together many different resources to create a firm. Entrepreneurs need to be able to come up with the initial product or service and create a plan to bring the product or service to market. They also need to be able to build their management team, outsource responsibilities to capable service providers, or perform the responsibilities themselves. Successful completion of these tasks requires a varied set of skills that are unlikely to be developed in hierarchical settings.

Finally, employment in hierarchies is often seen as preferable to smaller, less formalized organizations (Parker, 2006). Larger organizations provide more stability and career progression potential than smaller organizations where slack resources might be insufficient to weather a period of poor performance or where career advancement might be tied to the subjectivity of personal relationships. For many, the opportunity cost of leaving stable employment with career advancement to enter entrepreneurship is just too high.

Hypothesis 2: Potential entrepreneurs with hierarchical work experience will be less likely to favorably evaluate an ETA opportunity.

Individuals are motivated to enter entrepreneurship for a variety of reasons (Carsrud & Brannback, 2011; Yitshaki & Kropp, 2016; Farmer, Yao & Kung-Mcintyre). Early entrepreneurship theory identifies financial rewards as the primary motivation behind entrepreneurship (Knight, 1921; Cantillon, 1931; Schumpeter 1934) and more recent conceptual and empirical work has built on this premise (Benzing, Chu & Kara, 2009; Naffziger, Hornsby & Kuratko, 1994). However, other empirical studies have found that financial motivations are often less important than non-pecuniary motivations (Amit, MacCrimmon, Zietsma & Oesch, 2001; Block, Millán, Román & Zhou, 2015; Woo, Cooper & Dunkelberg, 1991). For example, in a study comparing 51 entrepreneurs and 28 technology industry managers, Amit et al. (2000) found that innovation, independence, vision, and challenge were significantly more salient motivations for entrepreneurial entry than wealth accumulation. While financial motivations might not be the primary reason to enter entrepreneurship, individuals understand the need to make enough money to support themselves and therefore must take into account the financial prospects of a potential opportunity.

In addition to wealth accumulation, other sources of non-economic and intrinsic motivations influence entrepreneurial entry. The desire for personal development and performing meaningful work can be accomplished through creating or managing a business that has a purpose that aligns with the entrepreneur (Edelman, Brush, Manolova & Greene, 2010; Jayawarna, Rouse & Kitching, 2011). The goal of finding meaningful work and making a positive contribution in the world has led to a surge in social entrepreneurship. B-corporations, an organizational structure that requires firms to meet social and environmental standards, have increased from their inception in 2015 to over 2500 certified B-corporations in more than 50 countries (bcorporations.net, 2019). Miller, Grimes,

previously indicated an interest in entrepreneurship. This restricted sample of aspiring entrepreneurs does not include older individuals who would be found on the downward-sloping portion of the inverted-U curve.

McMullen & Vogus, (2012) theorize that prosocial motivations lead to integrative thinking, prosocial judgement, and commitment to alleviating other's suffering which drives subsequent social entrepreneurship. Another benefit to entrepreneurship is the independence and autonomy that comes from firm ownership (Renko, Shrader & Simon, 2012; Reynolds & Curtin, 2008). The ability to decide when and where to work gives control over work-life balance which can lead to a higher quality of life (Kofodimos, 1993). Research has also shown that recognition and social status as an entrepreneur are motivations for some potential entrepreneurs to exploit an opportunity (Akehurst, Simarro & Mas-Tur, 2012; Edelman et al., 2010).

The motivations behind entrepreneurial entry are multifaceted and depend on the individual and the opportunity. Aside from potential financial rewards, aspiring entrepreneurs are often implicitly motivated by the prospect of having power (Carsrud & Brannback, 2011; Kets de Vries, 1985). The implicit power motive is the capacity to derive pleasure from having physical, mental or emotional impact on others. (Veroff & Veroff, 1972; Winter, 1973; Schultheiss, Wirth, Torges, Pang, Villacorta & Welsh, 2005). Recall our model of ETA involves three activities: arbitrage, reorganization and recombination. Each of these can fulfill an implicit need for power.

The act of buying and negotiating a purchase of a business can be an emotional decision because the identity of the business seller often becomes intertwined with the identity of the firm (Dehlen, Zellweger, Kammerlander & Halter, 2014; Berrone, Cruz, Gomez-Mejia & Larraza-Kintana, 2010). Getting the 'deal done' can itself become an emotional high for the purchaser. Research has shown that entrepreneurs display the greatest tolerance of risk, even in small gambles, as well as the strongest self-efficacy, internal locus of control, and need for achievement (Kerr, Kerr & Dalton, 2019).

In ETA, the entrepreneur has the responsibility and authority to hire new employees, fire existing employees and make changes to the organizational structure of the business. These changes can physically impact employees by changing the location they do their work or terminating their employment in the company. Organizational changes can also impact employees mentally if the scope of their responsibilities is changed or expanded. Each of these changes can help to fulfil the implicit needs for control and power for individuals who are driven by such considerations (Tiedens & Linton, 2001).

Finally, after the business has been acquired, the entrepreneur may also change the strategic direction of the organization through new resource combination and innovations. Researchers have shown that the ability to be innovative and creative can fulfil the implicit need for control and power (Larson, 1989).

In summary, ETA affords entrepreneurs who have implicit motivations for power and opportunity to make an impact within the organization and influence others physically, mentally, and emotionally.

Hypothesis 3: Potential entrepreneurs who have implicit motivations of power will be more likely to favorably evaluate an ETA opportunity.

Methodology

Data & Sample

To test our hypotheses, we use survey and LinkedIn data from 558 potential entrepreneurs from 2015 to 2018. LinkedIn profiles in management research have been used to study entrepreneurship in developing economies (Avnimelech, Zelekha & Sharabi, 2014), business model evolution (Snihur & Zott, 2020) and diffusion of practices (Dokko & Gaba, 2012). LinkedIn provides job and education history for each individual in our study.

The potential entrepreneurs in our sample are MBA students. These individuals voluntarily enrolled in an Introduction to Entrepreneurship class, an elective course offered in their MBA curriculum, and the majority of individuals expressed interest in participating in entrepreneurship in some capacity in the future. These potential entrepreneurs come from a variety of backgrounds, work experiences, and undergraduate majors.

We used a survey instrument to capture each individual's evaluation of a particular ETA opportunity, as well as the rationale behind their decision. This is described in more detail below.

Research Design

Research on ETA has been hampered by data access and identification. Despite the significant number of ETA deals completed each year, most details surrounding the transactions remain private. Additionally, it is very difficult to identify ex ante entrepreneurial intent in business acquisitions. Not all acquisitions are entrepreneurial in nature and growth is not necessarily an indicator of entrepreneurship (Davidsson, Delmar & Wiklund, 2006). Many acquisitions are completed to secure patents or human capital or as a competitive response to a perceived threat.

Our research design addresses some of these concerns. Our sample consists of potential entrepreneurs who all evaluate the same hypothetical ETA opportunity. Consistent with past research on decision making (Dearborn & Simon, 1958; Houghton & Goldberg, 2000; Simon, Houghton & Aquino, 2000), we use student responses to surveys based on several case studies to test our hypotheses. The surveys captured students' decisions to proceed or not proceed with a hypothetical ETA opportunity provided by a case study and the rationale behind their decisions. Our approach to use a classroom setting to study entrepreneurial decision making is consistent with Schwenk's (1995) assertion that classroom settings may be especially beneficial in examining cognitive processes. Other researchers

have used similar methods to study risk taking (Sitkin & Weingart, 1995), and propensity to start a business (Simon et al., 2000). This research design eliminates alternative explanations that could be attributed to heterogeneity of opportunity and creates a risk set of potential entrepreneurs, a challenge to research on entrepreneurial entry (Kim, Aldrich & Keister, 2006).

We use the Harvard Business School Publishing Case “Jim Southern” (5-389-073) as the setting for this study. This case features Jim Southern as the protagonist, a recent MBA graduate, and his experience as the first search fund entrepreneur. Search funds are a subset of ETA where potential entrepreneurs raise capital to search for and acquire undermanaged businesses that have the potential to increase in value through an infusion of capital and entrepreneurial strategic intent (Grousebeck, 2010). The case begins with Jim’s search for investors who are interested in helping him acquire and a low-tech company which he will subsequently manage. Following his search, Jim negotiates a purchase with the owner of a printing company while raising both debt and equity financing. Once the financing is secured, Jim must decide whether to continue with the purchase despite a last-minute ultimatum from the seller to personally guarantee a set of accounts payable or abandon the printing company and begin a new search. Jim acts as an arbitrageur by searching for an undervalued company to acquire. As an organizer of resources, Jim secures debt and equity financing to purchase the company. Finally, Jim plans to enact changes within the company to improve profitability should he decide to proceed with the acquisition. We ask each student to respond to two questions: “ (1) As Jim Southern, would you proceed with the acquisition? [Yes/No] and (2) Why or why not? Please provide an explanation for your decision.” The responses to the survey questions provide insight into the mindset of each individual on how they evaluate ETA opportunities and are the basis for the model. Responses to question (2) ranged from several very short sentences to long paragraphs.

Variables

Dependent Variable:

The dependent variable is the decision to proceed with an entrepreneurship through acquisition (ETA) opportunity, which is a binary variable that is coded as 1 for students who indicated in the survey that they would proceed with the entrepreneurship through acquisition deal, and is coded as 0 otherwise.

Independent Variables:

Data for the independent variables were collected from individual LinkedIn profiles, class rosters, and case surveys. From LinkedIn, we measure years of *Experience* as the time between the year the survey was taken and the date of the individual’s undergraduate degree.

We also identify veteran status from LinkedIn as employment in the military at some point in the individual’s career to measure *Hierarchy* (Visser, 2008; Stothard, Talbot, Drobnjak & Fischer, 2013). Previous research has used firm size as a proxy for hierarchy (Wagner, 2004; Eriksson & Kuhn, 2006; Dobrev & Barnett, 2005; Sorensen, 2007). However, many large companies opt for a flat organizational structure that minimizes hierarchy with the goal to increase innovation and cross-functional collaboration. Given the strict hierarchical structure found within military organizations, we measure *Hierarchy* as a binary variable that represents any previous military experience.

To measure *Power Motivation* we use computer-aided text analysis (CATA) to examine student responses to surveys on the two pre-cases noted above. Traditional methods of measuring implicit motivations use semantic coding of imaginative stories that require significant contribution from subjects and highly trained coders (Schultheiss & Pang, 2007). CATA provides a more efficient and reliable alternative to implicit motivation measurement by eliminating the human element (Neuendorf, 2002). Using CATA to measure implicit motivation, Schultheiss (2013) found that both traditional and CATA methods capture the implicit motives for power, achievement, and affiliation for both US and German University students and did not overlap with measures of self-attributed motivational needs thus demonstrating discriminant validity from self-reported motivations.

Like the Jim Southern case, the two pre-cases (“R&R”, HBSP case number 9-386-019 and “Paul Olsen”, HBSP case number 9-392-011) were also focused opportunity evaluation. For each case, students were asked whether they would proceed or not proceed with the opportunity and were asked to explain their rationale behind their decision. We analyzed the rationale offered for the responses to each question for each week independently using the Linguistic Inquiry Word Count (LIWC) dictionary (Pennebaker, Boyd, Jordan & Blackburn, 2015) and then found the average from the two previous cases. Taking the average from the previous two cases provides a more robust estimate of the individual’s true implicit motivations and reduces any response bias idiosyncratic to a single case. Implicit motivations of power was determined using the LIWC “Power” dictionary. The “Power” dictionary is a sub-category of the “Drives” dictionary and consists of 518 words associated with power such as superior and bully. The drives category within LIWC was assembled to measure needs and motivation (Pennebaker et al., 2015). Other “Drive” categories include affiliation, achievement, reward, and risk. One advantage of using LIWC as opposed to other CATA programs is that it produces results as a percentage of overall content which normalizes answers and eliminates variance that could result from the overall length of an individual response (Wolfe &

Shepherd, 2015). LIWC has been used to study entrepreneurial orientation (Moss, Neubaum & Meyskens, 2015; Wolfe & Shepherd, 2015b), customer service (Olekalns & Smith, 2006), and negotiations (Olekalns & Smith, 2009).

The use of CATA to measure constructs can also introduce measurement error including random response error, transient error, and specific factor error (McKenny, Aguinis, Short & Anglin, 2016). Random response error occurs when fluctuations in a participant's cognition influence the data provided (Schmidt & Hunter, 1999). This fluctuation can influence the words used by the author and could lower the reliability of the construct being measured. We address concerns of random response error in our CATA analysis by taking the average value of student responses to the two pre-cases in which they evaluated hypothetical entrepreneurial opportunities. Taking the average value of student responses also addresses transient error, which reflects the temporal factors that could influence a respondent reported values. By measuring implicit motivations of power at two different points in time and taking the average, temporal factors that might have influenced the respondent are mitigated. Finally, we address concerns of specific factor error, or content errors or bias in dictionary word lists, by using a predefined dictionary created and validated by external researchers.

Control variables:

From class rosters, we identify the individual's *Gender* and *Cohort*. We identify cohort as the month and year in which the student took the course. Because world events and instruction differed among cohorts during the three years of data collection, we control for cohort effects. We also control for the effect of classroom learning by measuring each student's prior decisions to proceed or not proceed with the previous two hypothetical case opportunities. We coded the student's decision as 1 if they decided to proceed with the case opportunity and 0 if they chose not to proceed. The sum total result for these two pre-cases was then determined for each student, which formed the basis for the variable *Prior Decisions*. For example, if a student voted to proceed with both hypothetical opportunities in the pre-cases, then the value of her *Prior Decisions* would be equal to two. Finally, *Prior Entrepreneurship Experience* was found using LinkedIn profile data for each student. We began by tracking each student's employment history. Any student with a job in their work history that was titled founder/cofounder, owner, CEO, President, Principal, or Proprietor in their work experience. Data were coded as "pre-founder" if the student had entrepreneurship experience prior to enrollment in the class.

Model

The dependent variable *ETA* (the decision to proceed with an ETA opportunity) is binary so we use a logit model for the analysis. Likelihood ratio chi-square values are reported with the results of the logit models; these test the null hypothesis that no regression coefficients were significantly different from zero. The models were estimated using STATA.

Results

Table 1 presents the descriptive statistics and correlations for the study variables. Twenty-eight percent of the participants indicated they would proceed with the deal. Twenty-six percent and seventy-four percent of the sample is comprised of female students and male students, respectively. On average, the individuals in our sample have 11.4 years of work experience.

While the correlations in Table 1 do not raise any particular concerns of multicollinearity, we additionally ran a variation inflation factor analysis (VIF) for further reassurance. We found that all variables have a VIF score of less than 2. Consistent with previous research, a VIF score of less than 10 is indicative of inconsequential collinearity (Hair, Black, Babin & Anderson, 1998).

	Mean	SD	1	2	3	4	5	6	7
1. ETA	0.276	0.447	1.000						
2. Experience	11.464	5.432	0.0949*	1.000					
3. Hierarchy	0.308	0.462	-0.1430*	0.039	1.000				
4. Power Motive	3.582	2.824	0.1026*	(0.026)	0.021	1.000			
5. Gender	0.263	0.441	0.031	(0.065)	-0.2494*	(0.007)	1.000		
6. Prior Entrepreneurship Experience	0.059	0.236	0.066	0.1479*	(0.069)	0.052	(0.047)	1.000	
7. Prior Decisions	0.943	0.670	(0.079)	(0.020)	0.046	0.007	(0.070)	(0.058)	1.0

N=558 * p<0.05

Table 1: Summary Statistics & Correlation Matrix

Table 2 presents the logistic regression estimates of the effect that *Work Experience* and implicit motivation have on the likelihood of proceeding with an ETA opportunity. Model 1 includes the control variables. The results suggest that *Gender*, *Previous Entrepreneurship Experience* and *Cohort* do not impact the likelihood to proceed with an ETA opportunity in a statistically significant way. Model 2 tested the effect of *Work Experience* on *ETA*. The coefficient is positive and significant (p<.05), showing support for Hypothesis 1. Potential entrepreneurs with more experience

will be more likely to positively evaluate an ETA opportunity. Model 3 tested the effect of *Hierarchy* on the likelihood to positively evaluate an ETA opportunity. The coefficient is negative and significant ($p < .05$), showing support for Hypothesis 2. Potential entrepreneurs with hierarchical work experience will be less likely to favorably evaluate an ETA opportunity. Model 4 tested the effect that *Power Motivation* (the implicit motivation of status and recognition) has on the likelihood to favorably evaluate ETA opportunity. The coefficient is positive and significant ($p < .05$), showing support for Hypothesis 3. Potential entrepreneurs with implicit motivations of power will be more likely to favourably evaluate an ETA opportunity.

	Model 1	Model 2	Model 3	Model 4	Model 5
Experience		0.039*			0.043*
		-0.017			-0.018
Hierarchy			-0.752***		-0.793***
			-0.236		-0.238
Power Motive				0.067*	0.074*
				-0.034	-0.035
Gender	0.09	0.119	-0.089	0.108	-0.052
	-0.215	-0.216	-0.223	-0.216	-0.225
Prior Entrepreneurship	0.519	0.391	0.421	0.492	0.242
Experience	-0.378	-0.385	-0.384	-0.382	-0.395
Prior Decisions	-0.276	-0.273	-0.27	-0.282	-0.277
	-0.145	-0.145	-0.147	-0.145	-0.148
Cohort Fixed Effects	Included	Included	Included	Included	Included
N	558	558	558	558	558

Standard Errors in parentheses

* $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

Coefficients estimated using logistic regression

Table 2 Logit regressions examining the influence of individual factors on the likelihood entrepreneurs to favorably evaluate an ETA opportunity

Supplemental Analysis: Entrepreneur Gender and ETA Evaluation

In conjunction with our primary analysis, we wanted to examine the potential moderating effects that entrepreneur gender may have on the relationships between each of the independent variables and the likelihood of the entrepreneur's favorable evaluation of an ETA opportunity (Table 3). Past research has shown that gender influences individual decision making. (Powell & Ansic, 1997; Schubert, Brown & Gysler, 1999). Following the suggestion put forth by Hoetker (2007), we divided our sample into two groups and ran the analysis for each interaction. We then conducted a Chow test for each (Chow, 1960) to test if there were statistically significant differences between male entrepreneurs and female entrepreneurs. None of the Chow tests were statistically significant, suggesting that gender does not have a moderating effect on the relationships between the independent variables and the likelihood of proceeding with an ETA opportunity.

	Male	Female
Experience	0.0612***	-0.0024
	-0.0212	-0.0325
Hierarchy	-0.9165***	-0.5255
	-0.2545	-0.6239
Power Motive	0.1383***	0.0375
	-0.0455	-0.084
Prior Entrepreneurship Experience	-0.3311	2.8384*
	-0.4618	-1.1407
Prior	-0.3176	-0.0329
Decisions	-0.1772	-0.3095
Cohort Fixed Effects	Included	Included
N	411	147

Standard Errors in parentheses

* $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

Coefficients estimated using logistic regression

Table 3: Moderating effect of gender on the likelihood to favorably evaluate an ETA opportunity

Discussion

This study investigates how an entrepreneur's work experience and motivation may shape the entrepreneur's evaluation of ETA opportunities. Specifically, we evidence that the length of work experience, the type of work experience, and implicit power motivation each influence the likelihood that potential entrepreneurs will favorably evaluate an ETA opportunity. Potential entrepreneurs with more experience are more likely to favorably evaluate an ETA opportunity while those with experience working in hierarchical organizations are less likely to favorably evaluate and ETA opportunity. Potential entrepreneurs who have stronger implicit motivations of power are also more likely to favorably evaluate ETA opportunity.

We then pushed further to investigate how entrepreneur gender may moderate these relationships. While our results did not demonstrate statistical significance, we were still able to discern some interesting differences between female entrepreneurs and male entrepreneurs in the context of ETA. First, years of work experience and prior experience in a hierarchical organization are significant determinants of the likelihood of favorably evaluating ETA opportunity for

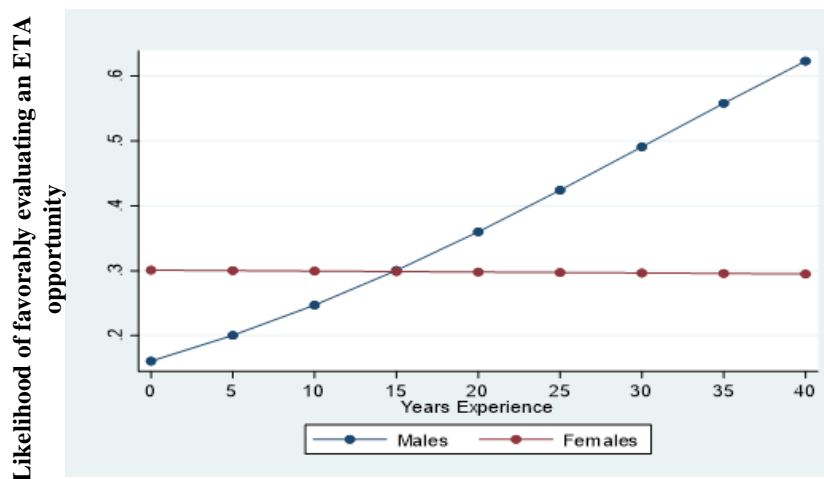


Figure 1: Differences in Experience Between Male and Female Entrepreneurs and the Likelihood of Favorably Evaluating an ETA Opportunity

males but not for females. Our finding that neither length nor type of work experience does not appear to influence women entrepreneurs' preference for ETA opportunities could be the result of the inherent challenges women face in management. The proverbial "glass ceiling" -- the practices, policies, and cultural factors that hinder advancement opportunities for women -- is a challenge many women face throughout their entire careers (Eagly, Eagly & Carli, 2007). Rather than considering the idea of acquiring an existing business, it is possible that some women prefer to continue fighting for promotion within their current organization.

In our sample, women with previous entrepreneurship experience are more likely to favorably evaluate an ETA opportunity but previous entrepreneurship experience for men does not impact the decision in a statistically significant way. Previous research on women in entrepreneurship finds that women are less likely to engage in entrepreneurship (Lerner, Brush & Hisrich, 1997; Robinson & Sexton, 1994), and encounter more challenges acquiring resources when they do decide to start a business (Harrison & Mason, 2007; Kanze, Huang & Conley, 2018). Women with previous entrepreneurship experience have overcome (as evidenced by the fact that they have previous entrepreneurship experience) at least some of the hurdles facing women entrepreneurs, which can lead to greater confidence in the likelihood of their success in an ETA opportunity.

From a practical perspective, these ETA insights have value for policymakers. There is increasing demand for capable entrepreneurs to take over existing businesses. Populations are aging in both the United States and Europe and many small businesses owners do not have children who want to take over the family business (Levesque & Minniti, 2011). Significant value is at risk if business owners are unable to find successors for their businesses including the loss of jobs, potential experience, and economic output. ETA provides a vehicle for succession and provides a way to preserve and renew the economic, intellectual, and cultural value contained in these aging businesses. Our results indicate that ETA may be a desirable avenue for women entrepreneurs; programs and support to encourage their engagement with ETA may prove particularly beneficial.

Limitations and Directions for Future Work

This study is the first, to our knowledge, that explores ETA and characteristics of how individuals perceive ETA opportunities. As previously mentioned, ETA is an understudied phenomenon and more research is needed to understand who engages in ETA, from both the entrepreneur and investor perspective. Continued exploration into

other drivers of ETA, such as the size, density, and structure of entrepreneur's network, could help shed light on how ETA opportunities are found and funded. Continued exploration of potential moderators that may affect the relationship between the antecedents of ETA and the decision to proceed with an ETA transaction are also potential avenues for future research. For example, researchers may examine how the entrepreneur's prior performance in both corporate and entrepreneurial roles may moderate the relationship.

Although the study's research design provided a useful platform from which to study opportunity evaluation, there are some drawbacks. First, the sample was drawn exclusively from entrepreneurship MBA students, which potentially limits generalizability. Future research is needed to understand if the findings from the study hold for non-MBA students. Non-MBA students have less work experience which could make taking over an existing business a daunting challenge. Their inexperience may also make it challenging to obtain debt and equity financing to purchase the business, thus discouraging non-MBA students from pursuing an ETA opportunity. Second, unobserved heterogeneity such as ability or effort could also be a factor in the determination of the results. It would be helpful to add additional controls such as age and previous entrepreneurial experience. Additionally, the robustness of the results of this study would be improved with a control group that did not have a predisposition to entrepreneurship. Finally, we used a hypothetical scenario to capture how potential entrepreneurs evaluated an ETA opportunity. To understand if the responses to proceed or not proceed really do indicate a proclivity to ETA, it would be helpful to follow the respondents over time to observe who actually engages in ETA in their future careers.

Conclusion

While most research on entrepreneurial opportunities highlights new ventures, we explore an important yet understudied opportunity context in ETA, or entrepreneurship through acquisition. Our findings suggest that both contextual and dispositional factors play important roles in entrepreneurs' evaluations of ETA opportunities. This research also supports earlier work on the negative effect that entrepreneurs' prior experiences with organizational hierarchy has on subsequent entrepreneurial engagement as well as the positive effect that entrepreneurs' work experiences has on entrepreneurial opportunity exploitation. These findings not only shed light on alternative modes of entrepreneurial entry, but also open the door for future research on other factors that might affect the entrepreneur's decision to proceed with an ETA opportunity.

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