

# THE INFLUENCE OF SOCIO-CULTURAL ENVIRONMENTS ON THE PERFORMANCE OF NASCENT ENTREPRENEURS: AN INSTRUMENTAL VARIABLE APPROACH

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## ABSTRACT

The importance of informal institutions and in particular culture for entrepreneurship is a subject of ongoing interest. Past research has mostly concentrated on cross-national comparisons, cultural values, and the direct effects of culture on entrepreneurial behavior, but in the main found inconsistent results. The present research adds a fresh perspective to this research stream by turning attention to community-level culture and cultural norms. We hypothesize indirect effects of cultural norms on venture emergence. Specifically that community-level cultural norms (performance-based culture and socially-supportive institutional norms) impact important supply-side variables (entrepreneurial self-efficacy and entrepreneurial motivation) which in turn influence nascent entrepreneurs' success in creating operational ventures (venture emergence). We test our predictions on a unique longitudinal data set (PSED II) tracking nascent entrepreneurs venture creation efforts over a 5 year time span and find evidence supporting them. Our research contributes to a more fine-grained understanding of how culture, in particular perceptions of community cultural norms, influences venture emergence. This research highlights the embeddedness of entrepreneurial behavior and its immediate antecedent beliefs in the local, community context.

## INTRODUCTION

Entrepreneurship is important for national economies as it contributes to job creation, productivity and economic growth (Parker, 2009; Van Praag and Versloot, 2007). Our understanding of individual factors enabling and hindering entrepreneurship has significantly increased. Less research addresses the embeddedness of entrepreneurial behavior in local or national institutions. Emerging cross-national research has yielded valuable insights into formal institutions influencing entrepreneurial behavior (e.g., Aidis, Estrin and Mickiewicz, 2010; Bowen and DeClercq, 2008; Levie and Autio, 2008; Van Stel, Storey and Thurik, 2007). By contrast, little research explores the role of informal institutions including culture. This is surprising as a number of disciplines consider informal institutions to be important forces shaping economic behavior such as entrepreneurship (e.g., Hayton, George and Zahra 2002; North, 2005; Stephan and Uhlaner 2010; Thornton, Ribeiro-Soriano and Urbano 2011; Uhlaner and Thurik 2007).

Our research provides a fresh perspective on the role that informal institutions play in entrepreneurship by highlighting the importance of the *community context*. Community has been

variously defined (Rattan and Welter, 2011). We adopt a common geographic definition of a community and define the community as a proximal spatial area that is smaller than a state or county. A community captures an area such as a small town, a village, a collection of small villages, or a greater neighborhood within a larger city (see for instance Kilkenny et al., 1999 for a similar definition). This concentration on a community perspective can usefully complement past research, which has focused on the national context (e.g., Stephan and Uhlaner, 2010). Compared to national culture, community-level cultural norms reflect a more proximal context within which entrepreneurial action takes place. Community culture is both influenced by national culture and also distinct from it. Such a perspective is in line with research highlighting within-nation, regional heterogeneity in culture, entrepreneurial attitudes and behavior (Davidsson, 1995; García-Cabrera and Garcia-Soto 2009; also Tung, 2008). It is also consistent with the broader view that sub-national units (e.g., regions, organizations) have distinctive cultures that are nested within broader national cultures (House, Hanges, Javidan, Dorfman and Gupta, 2004; Leung, Bhagat, Buchan, Erez and Gibson, 2005). The purpose of the present research is it to suggest that community-level cultural norms are a useful concept due to the predominantly local nature of entrepreneurial activity (e.g., Brixy, Sternberg and Stueber, 2012).

The present research contributes to our understanding of the *mechanisms* by which informal institutions – in particular the perception of socio-cultural norms – impact the business creation process. We argue that the impact of socio-cultural norms on entrepreneurial start-up success may be mostly indirect through supply-side variables. Drawing on the person-culture fit perspective (Tung, Walls and Frese, 2007), we suggest that culture may impact on important individual beliefs, which in turn determine whether nascent entrepreneurs succeed in creating operational ventures or whether they select out of the start-up process. We focus on culture's influence on two key individual beliefs: an entrepreneurs' motivation to work hard to create an operational venture (start-up motivation) and their confidence that they have the skills required to create an operational venture (entrepreneurial self-efficacy).

We propose that the perception of performance-based socio-cultural norms and of socially supportive institutions (state and local government, financiers and community groups) impact key individual beliefs and subsequently influence nascent entrepreneurs' success in creating operational businesses. (Hereafter we refer to the successful creation of an operational business as venture emergence.) It is likely that cultural norms in a community lead to endogenous matching such that those entrepreneurs who better fit into the cultural context are more likely to succeed. In particular, strongly motivated and highly self-efficacious entrepreneurs will thrive in performance-based socio-cultural environments. Additionally, a socially-supportive institutional environment enables nascent entrepreneurs to access important resources to create their business, which also has a positive motivating effect and strengthens nascent entrepreneurs' self-efficacy, such that they are more likely to succeed in their venture creation efforts.

Taken together this research makes several contributions. First it supplements the literature on the institutional embeddedness of the entrepreneurial process and particularly the literature on informal institutions (e.g. Thornton, Ribeiro-Soriano and Urbano 2011; Stephan and Uhlaner, 2010) by adding the focus on community-level cultural norms. Second, past research on culture and entrepreneurship has concentrated on establishing a direct effect of culture on the level of entrepreneurship (e.g., Hayton et al., 2002; Stephan and Uhlaner, 2010; Uhlaner and Thurik, 2007; Wennekers, Thurik, Van Stel, and Noorderhaven, 2007). Our research investigates whether the important effects of culture on venture emergence are indirect, mediated through their

impact on key individual beliefs (start-up motivation and entrepreneurial self-efficacy). Thus we clarify one mechanism through which culture influences venture emergence. In this way, our research also contributes to a better understanding of contextual antecedents of start-up motivation and entrepreneurial self-efficacy. Past research demonstrates important consequences of these beliefs for entrepreneurial outcomes (venture emergence, venture growth, venture success, e.g., Baum and Locke, 2004; Cassar and Friedman, 2009; Townsend, Busenitz, and Arthurs, 2010; Rauch and Frese, 2007), yet, few studies investigate their antecedents.

## **THEORY AND HYPOTHESES**

### **Performance-based Socio-cultural Norms**

Performance-based cultures are cultures which reward individual accomplishment (Stephan and Uhlaner, 2010). They reflect “the extent to which a community encourages and rewards innovation, high standards and performance improvement” (Javidan, 2004, p. 239). Entrepreneurship is an achievement- and performance-orientated activity (e.g. McClelland 1976; Rauch and Frese 2007), in which individuals expend effort in return for expected financial and non-financial rewards. Non-financial rewards include for instance the high levels of autonomy, job satisfaction and well-being that entrepreneurs enjoy (Stephan and Roesler 2010; van Praag and Versloot 2007). In line with the notion of person-culture-fit (Tung et al., 2007), entrepreneurship thus should thrive in socio-cultural environments which support performance-based behaviors including taking initiative, working to high standards, and achieving success through one’s own personal effort rather than through status or inheritance (McClelland 1976; Stephan and Uhlaner 2010; Weber 1930). We build on and refine this argument below.

Entrepreneurship is a legitimate behavior in performance-based cultural contexts as it is in line with wider societal expectations of taking one’s life in one’s own hands and working hard to achieve a goal. Entrepreneurs who particularly conform to these expectations, i.e. entrepreneurs who work hard and show the culturally approved “can do attitude” will find it easier, relatively speaking, to create an operational venture. Important stakeholders such as business partners, suppliers, financiers, customers and employees are more likely to regard these entrepreneurs as capable and legitimate as they closely conform to their cultural expectations about effective performance-based behavior. Conversely, entrepreneurs who are less aligned with cultural expectations around performance-orientation are more likely to withdraw from venture creation. These are entrepreneurs who are less determined to create a business, i.e. they are less willing or able to work very hard to create a business and also entrepreneurs who are more in doubt of their entrepreneurial abilities. These entrepreneurs will be less legitimate in the eyes of important stakeholders as they are misaligned with the cultural norm. Stakeholders will have less faith that these entrepreneurs will succeed to create successful businesses and consequently are less likely to support them. This in turn makes it yet more difficult for these entrepreneurs to create operational businesses and consequently they are more likely to give up their venture creation efforts.

In sum, we suggest that the expectation to demonstrate a hard working attitude combined with determined and confident high-performance behavior is stronger in performance-based cultures. Thus strongly motivated and highly self-efficacious entrepreneurs will thrive in these cultural contexts. They will be seen as legitimate by important stakeholders and consequently have relatively easier access to resources, both of which are crucial to succeed in creating

operational ventures. In other words, performance-based cultural norms in a community are likely lead to endogenous matching between the norms and corresponding compatible potential entrepreneurs. Highly motivated and self-efficacious entrepreneurs fit more closely, and comparably less strongly motivated and self-efficacious entrepreneurs fit less well with performance-based cultural norms. Thus,

*Hypothesis 1. The perception of performance-based cultural norms is positively associated with higher levels of H1a) start-up motivation and H1b) entrepreneurial self-efficacy in nascent entrepreneurs.*

### **Socially-supportive Institutional Environment**

As much as entrepreneurship is a performance-based behavior and success in the venture creation process is due to the efforts of the nascent entrepreneur, entrepreneurship is also a behavior contingent on social support through others (e.g. Stephan and Uhlaner 2010; Thornton et al. 2011). Nascent entrepreneurs are likely to lack the resources that are needed to complete all relevant and critical tasks to create a new business (Pfeffer and Salancik, 1978; Davidsson and Honig, 2003). The major challenge in creating an operational venture is to access sufficient resources, both tangible, such as finance and also intangible such as information and emotional support (e.g., Aldrich, Rosen and Woodward, 1987; Bruederl and Preisendoerfer 1998; Hitt et al., 2011). The importance of the various types of social support for the venture creation process are most frequently discussed with reference to social capital, or the “goodwill that is engendered by the fabric of social relations and that can be mobilized to facilitate action” (Adler and Kwon 2002, p. 17). According to Cope, Jack, and Rose (2007), the term social capital also applies to broader external networks such as actors in the community, who might help founders to coordinate the foundation process more effectively.

Thus an environment in which various community actors from local investors, through government, to community groups actively support business creation efforts is likely to enhance entrepreneurs’ access to resources and thus their chances of success. In turn, the display of support by various community actors gives the emerging venture added legitimacy with its various stakeholders thereby further enhancing its chances of success. Cross-national evidence supports such reasoning and finds cultures with stronger socially supportive norms to have higher subsequent rates of business creation (Stephan and Uhlaner 2010).

We suggest that the perceptions of community support from government, financiers and local groups will increase nascent entrepreneurs’ motivation to expend effort in the venture creation process, thus making its success more likely. The more nascent entrepreneurs perceive community support to be available, the more they will feel motivated to “keep going” and invest greater effort in the venture creation process rather than abandon it. Venture creation is typically a long, effortful process. Knowing that “one is not alone” and can tap into community support and resources if need be, is reassuring for the nascent entrepreneur and motivates them to forge ahead in their venture creation efforts. For instance, past research within work settings shows that the perception of the availability of social support impacts employees’ work motivation (Van Yperen and Hagedoorn 2003).

*Hypothesis 2a: The perception of socially-supportive institutional environments is positively associated with higher levels of start-up motivation in nascent entrepreneurs.*

Socially supportive institutional environments may also empower nascent entrepreneurs through building their entrepreneurial self-efficacy. Research in organizational behavior suggests that socially supportive cultural environments enhance individuals' self-efficacy beliefs (e.g. Choi and Chang 2009). In such environments individuals feel safe to experiment and try out various things without fear of failure, thus increasing their faith in their abilities to master challenges. Such behaviors are arguably also critical to venture creation efforts, where barriers are abound and entrepreneurs often need to engage in trial and error to find which course of action gets them further in their venture creation efforts (Sarasvathy 2001). Supportive environments which allow for such experimentation have a greater tolerance towards making mistakes and failures, which is crucial for learning and developing mastery beliefs (e.g., Edmondson, 1999, 2004; Stephan and Uhlaner, 2010; also Gelfand, Frese and Salmon, 2011).

*Hypothesis 2b: The perception of socially-supportive institutional environments is positively associated with higher levels of self-efficacy in nascent entrepreneurs.*

## METHODS

We use the Second Panel Study of Entrepreneurial Dynamics (PSED II) dataset. The PSED II is a representative survey of entrepreneurial activities in the United States that portrays individuals during their business creation process. Detailed descriptions of the methods and sampling used to generate PSED II and an overview on the data structure can be found in Reynolds and Curtin (2009).

Nascent entrepreneurs were first identified through telephone interviews with a population-representative probability sample of 31,845 individuals in late 2005 of which 1,214 individuals were classified as active nascent entrepreneurs. A follow-up interview of these nascent entrepreneurs was conducted in early 2006, and then followed by yearly interviews. The last follow-up interview was completed in January 2010. In other words the PSEDII provides longitudinal data on entrepreneurial activity over a time span of 5 years. Of all 1,214 nascent entrepreneurs sampled, 460 disbanded their venture and 228 perceived their venture as operational. Another 247 nascent entrepreneurs reported ongoing activities as per Wave E, but did not perceive their venture as operational. Lastly, 279 nascent entrepreneurs omitted at least one wave. These observations are excluded from the present analysis. Our final sample thus consists of 590 nascent entrepreneurs that either disbanded or successfully created their venture.

We estimate a standard probit model alongside an instrumental variable probit model to analyze the effect of socio-cultural environments on entrepreneurial self-efficacy and start-up motivation, and on the subsequent likelihood of venture emergence. As argued above, we suggest that socio-cultural environments affect venture emergence not directly but rather indirectly through impacting the supply side of entrepreneurship – in particular start-up motivation and entrepreneurial self-efficacy. In other words, motivation and self-efficacy are endogenously determined by socio-cultural environments. Start-up motivation and self-efficacy appear as causal variables in the estimation model for venture emergence but are, correlated with the error terms of such a model (Block, Hoogerheide, and Thurik, 2011). This correlation is due to omitted variables, such as perception of cultural norms as argued above. Given that individuals are likely to display behavior in accordance with social norms prevalent in their environment, we need to separate the indirect effect of social cultural norms from the subsequent

performance implications of the corresponding endogenous supply side variables. To accommodate this endogenous nature of self-efficacy and motivation, we employ an instrumental variable analysis where start-up motivation and entrepreneurial self-efficacy are instrumented by the perception of the community cultural norms.

## **DISCUSSION**

Drawing on a 5-year longitudinal study of nascent entrepreneurs and their venture creation efforts, we tested mechanisms by which informal institutions – in particular the perception of community-level socio-cultural norms – impact the business creation process. In line with our arguments we found that community-level cultural norms influence venture emergence indirectly through their impact on nascent entrepreneurs' start-up motivation and entrepreneurial self-efficacy beliefs, i.e. key supply-side variables. Performance-based and socially-supportive community cultural norms shape important individual beliefs, which in turn determine whether or not nascent entrepreneurs succeed in creating operational ventures. We found full support for our hypotheses that performance-based culture impacts entrepreneurial self-efficacy and start-up motivation. With regard to socially-supportive institutions, we found the hypothesized influence on start-up motivation but not on entrepreneurial self-efficacy.

Our study makes two important contributions to the relatively under researched field of cultural norms and entrepreneurship. First, our study contributes to research on culture by providing a fresh perspective of community-level as opposed to nation- or regional-level culture and the importance of these community-level cultural norms for venture emergence.

Second, it highlights culture's role as a "background" variable in that cultural influences on entrepreneurial behavior may best be considered as indirect effects impacting key supply-side variables, in our case important individual beliefs. In other words, we highlight the mechanism through which culture influences individual behavior. We show that entrepreneurial self-efficacy and start-up motivation are endogenously influenced by community-level culture. In doing so, our research provides a conceptual framework to bridge and integrate the literatures on culture on the one hand and individual-level determinants of entrepreneurship such as self-efficacy on the other hand. Here our study goes beyond past research that either equated culture with individual-level personality characteristics or proxies culture by the region or country in which the entrepreneur lives (e.g. Thomas and Mueller, 2000). It also advances beyond past research which used culture scores from existing data bases and merged these with country-level prevalence rates of entrepreneurship – neglecting for the most part individual-level antecedents (e.g. Stephan and Uhlaner 2010; Uhlaner and Thurik 2007; Wennekers et al. 2007).

Our research is the first to demonstrate these relationships for community-level culture and in a longitudinal study of venture emergence. It complements recent cross-national, cross-sectional research which finds similar associations on aggregate country-level scores of national culture and national aggregates of individual beliefs (Stephan and Uhlaner 2010). Taken together, our research highlights the embeddedness of entrepreneurial behavior and its immediate antecedent beliefs in the local, community context.

## **ENDNOTES**

1. Both authors contributed equally to this work, they alternate author order.

## **REFERENCES AVAILABLE FROM THE AUTHORS**