

THE SEARCH FOR OPPORTUNITIES BY SMALL BUSINESS OWNERS

Laurence G. Weinzimmer
Fred L. Fry
Bradley University

Paul C. Nystrom
University of Wisconsin-Milwaukee

ABSTRACT

This paper identifies specific factors that cause some small business owners to search for new opportunities while other owners choose to remain with the status quo. Using concepts drawn from the literatures in decision making, entrepreneurship, organization theory, and strategy, we develop a model of factors that stimulate opportunity identification. Determinants include characteristics of the industry environment, intentions and personalities of small business owners, and strategic planning activities. The model is then applied to two actual small businesses in order to illustrate its potential usefulness. Implications for small business managers, consultants, and business researchers are discussed.

INTRODUCTION

Small business owners are, by definition, opportunists. They are more tolerant of risk and ambiguity than non-entrepreneurs and more adaptive than managers of larger firms (Schere, 1982). Small business owners differ among themselves, however, in their propensity for opportunity identification -- the search of the competitive environment for unmet needs which can be exploited by a firm. Therefore, some small business owners have a very proactive, aggressive strategic orientation while other small business owners have a very reactive, passive strategic orientation.

In the entrepreneurship literature, the study of opportunity identification has generally been restricted to start-up situations. In particular, studies of entrepreneurial traits, backgrounds and intentions have been directed at differentiating between those individuals who start new ventures and those who choose not to start new ventures. The majority of research examining existing firms has been limited to the study of intrapreneurship or the rejuvenation of large and stagnant firms, with the exception of Naffziger, Hornsby, and Kuratko (1994). However, no integrative research exists that examines factors influencing the search for new opportunities which may allow existing small businesses to grow.

Opportunistic decisions are critical to growth-oriented small businesses for at least two reasons. First, the types of strategies available to most small firms are limited. Porter (1980) identified three major strategies available to organizations: cost leadership, differentiation, and

focus. Smaller firms, however, seldom have the resources necessary to achieve the economies of scale needed to succeed as cost leaders, and limited resources prevent most small firms from succeeding in product differentiation. However, small firms are agile and can position themselves to adapt quickly to focus on selected target markets or niches since organizational structures of small businesses are generally simple (few divisions), flexible (few layers), and channels of communication are open (Olson, 1986). Therefore, small firms have the advantage that they can seize an opportunity before the "window" closes.

The second reason to study opportunity search is that small business owners are relatively less risk averse and more receptive to ambiguity than are managers of large firms (Schere, 1982). In their classic work, Cyert and March (1963) suggested that managers tend to react to problems and avoid uncertainty rather than seek risky opportunities. Small business owners, however, tend to be moderate risk takers (Olson, 1986). Additionally, Schere (1982) has shown that small business owners have significantly greater capacity to tolerate ambiguity than do managers in large organizations. Given that opportunities have been defined as a special case where decision making is risky and ambiguous (Simon, 1977) and given that small firms are flexible and can adapt to change, opportunistic decision making should be of great interest to those small businesses that desire growth and change. Therefore, this paper develops an integrative model of opportunistic decision making for small business owners. In particular, the focus of the model is on those factors which can stimulate the search for new opportunities. The model is comprised of three parts -- dynamics of the industry environment, characteristics of the small business owner, and strategic planning activities.

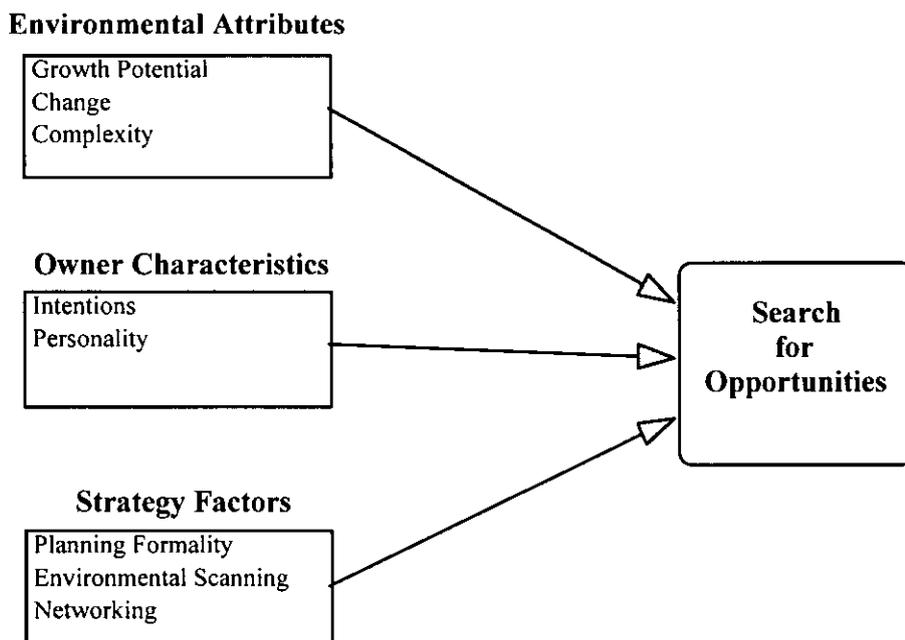
A MODEL OF THE OPPORTUNITY SEARCH DECISION

Three areas of research have occupied much of the entrepreneurship and small business literature in recent years. The first area examines the environment as an important factor in predicting small business behavior. The second area investigates personal characteristics and entrepreneurial intentions of those individuals who start ventures. The third area considers planning activities, including planning processes, business plans, organizational structure and venture strategies. This paper examines all three of these areas in trying to identify factors that lead to opportunity identification. The integrative model of opportunistic decision making developed in this paper can be seen in Figure 1.

To perform an investigation of specific variables, this paper used factors found in the entrepreneurship, strategy and organization theory literatures. While the variables used in this paper are not intended to represent all possible predictors of the intensity of opportunity search activities, based on an exhaustive review of the literature from 1986-1995¹, these variables represent commonly studied factors used to examine aggressive versus passive strategic orientations.

¹ The journals reviewed include *Academy of Management Journal*, *Administrative Science Quarterly*, *Entrepreneurship Theory and Practice*, *Journal of Business Venturing*, *Journal of Management*, *Journal of Small Business Management*, *Journal of Small Business Strategy*, *Organization Science* and *Strategic Management Journal*.

Figure 1
Integrative Model of Opportunity Identification



ENVIRONMENTAL FACTORS

The first set of factors to consider when evaluating the degree to which searches for opportunities are actively performed by small business owners is the external environment in which a firm exists. The industry environment can play an important role in determining the need for a small business to identify opportunities. Using industry growth potential, degree of environmental change, and industry complexity, a framework can be developed to determine the relevance of different environments on the opportunity-search processes of small businesses.

Industry Growth Potential

An environment with low growth potential contains minimal resources, constraining or thwarting organizational growth, while an environment with high growth potential is characterized by ample resources, facilitating considerable growth (Tushman, 1977).

When an environment is characterized by low growth potential, resource scarcity increases the risk to organizations that remain in that environment because resource scarcity

will cause competition to intensify (Dess & Beard, 1984; Porter, 1980). As resources become more scarce, increased intensity in competition leads to a zero-sum game, which means that the only way for a firm to realize growth is to take market share away from competitors (Castrogiovanni, 1991). Growth for individual firms becomes more difficult because firms must compete with each other for resources needed to sustain growth (Porter, 1980). As resources become depleted, opportunities for growth are seldom readily available and waiting to be exploited. Instead of having the luxury of acting on existing opportunities, small business owners must create opportunities by identifying new niches in a current industry, or search for opportunities outside of their original industry.

Conversely, when an industry has considerable growth potential, organizations within the industry can all experience growth without competing as intensively for market share or raw materials. Stated differently, when growth potential is high, firms may experience success simply by being members of that industry (Eisenhardt & Schoonhoven, 1990). Therefore, small business owners can act on existing opportunities, making it unnecessary to consider opportunities outside of their original industry. For example, during the mid-1980s, many small firms entered the video-rental business. Given the tremendous growth potential at that time, it was not necessary for video-rental firms to seek out new opportunities outside of their industry in order to survive and prosper. By the 1990s, however, growth in video-rental stores other than Blockbuster and other major chains had stopped almost completely. Small business owners in the video-rental industry were forced to consider niches or to consider totally different industries.

Degree of Industry Change

The concept of industry change has also been recognized in organization theory studies as an important dimension of an organization's environment. Environmental change creates a state of disequilibrium which, in turn, creates market opportunities for firms within that industry (Dean, Meyer, & DeCastro, 1993). Tushman and Anderson (1986) showed that environmental change usually takes place incrementally, sometimes punctuated by unexpected radical shifts. These environmental changes can be classified as either competence-enhancing or competence-destroying change because they either enhance or destroy existing organizations in a given environment.

Competence-enhancing changes are improvements in a product or process that build on existing know-how within an industry. These developments substitute for older technologies but do not render obsolete the skills required to master the old technologies. Examples of competence-enhancing improvements would be upgrades in existing computer software and the development of Intel's 286, 386, 486 and Pentium microprocessors. Since competence-enhancing changes build on existing technologies, they create growth opportunities for incumbent firms to modify existing products or services, therefore creating an increase in opportunities for firms in the industry.

Conversely, competence-destroying changes are characterized by an innovation so extreme that the new technology fundamentally alters the set of relevant competencies within an industry. Examples of competence-destroying changes are: steam vs. diesel locomotive, the

slide rule vs. calculator, and the typewriter vs. the computer. Since competence-destroying changes replace existing technologies, many small firms that already have sunk costs in an industry cannot afford to incorporate a radical change. Some firms search for new opportunities, other firms are replaced by new entrants. Therefore, both competence-enhancing and competence-destroying changes may increase the need for opportunity identification. Stated differently, environmental change creates both threats and potential opportunities.

For example, many small typewriter repairs shops during the 1970s and early 1980s noticed that the need for their service was declining. Some firms sought out new opportunities, such as computer-repair, in order to survive. An example of this is More Computers, a computer superstore located just outside Philadelphia. Elliot Baretz purchased Valens Business Machines which had begun as a typewriter repair shop in the 1970s and had evolved into a computer repair store. Baretz renamed the business Valens Information Systems, and used it as a springboard for a customer friendly computer superstore. Unlike Baretz, many small business owners are not proactive in opportunity identification, so when a need arises to search out new opportunities because of a shrinking market, it may be too late -- the small business doesn't have the resources to pursue new opportunities.

Industry Complexity

In contrast to industry change, which examines the change of environmental factors over time, complexity is a static measure, which examines the differences or uniqueness of environmental factors in an industry (Dess & Beard, 1984). The number and uniqueness of external elements in the environment in which the small firm exists will determine the level of complexity. In a complex environment there are a large number of diverse elements affecting the firm; in a simple environment few environmental elements impact the firm (Segev, 1989). In a highly complex environment, pursuit of new opportunities may be limited because scanning a diverse environment could be too costly for small firms. Conversely, in a simple environment, characterized by similar elements, environmental scanning for a small business becomes much more plausible.

Key Considerations for Environmental Factors

1. Small business managers should consider industry growth potential when assessing the need to proactively identify opportunities. When growth potential is high, firms can act on existing opportunities, so focus should be placed on maximizing performance in that industry. However, as growth potential begins to decrease, opportunity identification intensity may have to shift outside of the original industry. If a small business owner in a declining industry waits too long to identify new opportunities, firm survival may become threatened.

2. Change creates both opportunities and threats. As an industry environment experiences change, a small business manager should examine if the change improves on existing conditions or replaces existing conditions. Both scenarios create opportunities, so change should trigger an increase in opportunity identification intensity.

3. Industries characterized by high complexity will make it difficult for small business managers to effectively identify opportunities. The more complex the environment, the more difficult and costly opportunity identification will be. This suggests that although environmental factors may, by themselves, increase or decrease the existence of opportunities, seldom do they account for all the difference in the intensity of search for opportunities.

SMALL BUSINESS OWNER FACTORS

The prevailing area of research in entrepreneurship focuses on the intentions and characteristics of individuals who start new ventures. Little research has been done on the differences between start-up small business owners and post-launch small business owners regarding either their characteristics or their intentions. We do not know, for example, whether the risk-taking propensity of small business owners either increases or decreases once the venture begins. Nor do we know whether their entrepreneurial intentions, broadly defined, continue on or slowly atrophy if the venture is a low growth or stagnant business. The following section discusses what is known about the traits and intentions of small business owners.

Intentions of Small Business Owners

An important area of small business research has focused on intentions of small business owners. Until recently, this stream of research had not been discussed in the small business context. Bird (1988) discussed entrepreneurial intentions as a guide to small business owners' goal setting, communication, commitment and organization. This area of research acts to direct attention to questions about how small business owners create, sustain, and transform organizations. Opportunity identification can be identified as an important criteria in a small business owner's intention because opportunity exploitation can lead to organizational growth. This is an important consideration because empirical evidence suggests that the ambitions and skills of a small business owner will determine the size and growth potential of the venture (Carland, Hoy, Boulton & Carland, 1984; Hambrick & Cozier, 1985). Entrepreneurial intentions are self-limiting factors. That is, those owners who do not intend to grow will not, regardless of growth opportunities in the environment.

Characteristics of Small Business Owners

Herron and Sapienza (1992) offer credence that the traditionally held beliefs about start-up entrepreneurs are, in fact, operable for existing small business owners. Their basic model suggests that the skill levels, values, and personality, as well as the context (environment) affect the "type and level of aspirations" and the "type and level of dissatisfaction" that the potential small business owner possesses. This level of dissatisfaction, in turn, affects the information-search process (e.g., opportunity identification).

We accept and appreciate the concerns of those who contend that it is difficult to prove unequivocally that small business owners: (1) are more achievement oriented; (2) are less risk averse; (3) have a higher internal locus of control; and (4) have greater tolerance for ambiguity than managers or the general public (cf., Brockhaus, 1982; Sexton & Bowman, 1986).

However, we also recognize that the vast majority of studies do support at least these four constructs. We posit that the characteristics and intentions normally accepted for start-up entrepreneurs do, in fact, hold for owners of existing businesses as influences in the owners' propensity to engage in opportunity identification activities. Over a fairly broad range, increases in any of those four factors may increase propensity to grow the business.

Key Considerations for Small Business Owner Factors

1. The degree to which opportunity identification is pursued by a small business may be directly attributed to the strength of the small business owner's intention towards growth. If a small business manager intends to achieve growth, proactive attempts to identify new opportunities may stimulate growth.

2. The intensity of opportunity identification may be influenced by a small business owner's personality attributes, such as propensity to accept risk, level of need for achievement, degree of internal locus of control, and tolerance for ambiguity. While a small business owner is unlikely to change his or her personality, an understanding of personality attributes may influence selection of other members of the management team. Also an understanding of how personality attributes influence opportunity identification may assist a small business owner by providing a rationale for why (or why not) a small business actively pursues new opportunities.

3. Interactions may exist between personal characteristics and intentions, since characteristics of a small business owner may moderate intentions toward growth. For example, since opportunities have been defined as a special case where decision making is risky and ambiguous, there may be a positive relationship between risk averseness and the intentions towards growth and a positive relationship between tolerance for ambiguity and intentions towards growth.

STRATEGIC PLANNING FACTORS

Initially, researchers concluded that small firms did not use the strategic planning processes based on normative models used by larger organizations (Robinson, 1982). Small businesses, however, are not simply small versions of big businesses. Therefore, by reframing these basic normative models to the small business context, researchers have shown empirically that small businesses actually do engage in strategic planning (Rice, 1983). Additionally, the planning process of an organization may influence the degree to which environmental scanning mechanisms are used by top management. Previous studies suggest that strategic planning and environmental scanning positively impact organizational growth (cf., Miller & Toulouse, 1986; Sandberg, 1986). Therefore, characteristics of the strategic planning process and implementation of environmental scanning mechanisms are considered as important factors in predicting the degree to which small businesses are involved in the search for new opportunities.

Planning Formality

The strategic planning process of an organization influences the degree to which proactive searches for opportunities are performed by top management (Miles & Snow, 1978). An important characteristic of the strategic planning process that may influence opportunity identification is planning formality. Planning formality can be defined as the extent to which written procedures and schedules guide the planning process (Dutton & Duncan, 1987). It may be argued that if this process is formalized, opportunity search will become more routinized and systematic. As the opportunity identification process becomes more sophisticated, the search for new opportunities should become more effective.

Environmental Scanning

Environmental scanning can be defined as the gathering of pertinent information and the introduction of results to the organizational decision-making process (Lenz & Engledow, 1986). It is a technique used to keep the organization aware of the nature of the environment in which it exists (Fahey, King, & Narayanan, 1981). The more cognizant the firm is of its external environment, the better the chance that it will recognize opportunities.

Pearce, Chapman, and David (1982) developed a taxonomy of environmental scanning techniques available to a small business owner. Two sets of information sources are identified: internal sources and external sources. Internal sources of information that can help to identify distinctive competencies and opportunities for small businesses can take one of several forms. The first is production and marketing information. In attempting to identify opportunities, a small business owner can question sales staff, technical representatives, suppliers, and customers. This is a very inexpensive technique and can help the small firm identify opportunities. Additionally, predicting sales and profits and assessing production, financial and resource capacity may be important internal sources.

In addition to internal environmental scanning, several external scanning methods are available. The first external source is the use of publications. General business periodicals, trade journals, government publications, industry studies (e.g., Standard and Poor's Industry Survey), and local industry data (e.g., Chamber of Commerce reports, Economic Development Counsel data, and Microcosim) are all potentially important sources of information. Pearce et al. (1982) label the use of publications as the cornerstone of any environmental scanning system.

Another external source of information available to the small business is consultants. Given the limited resources of small businesses, non-profit consultants would be most beneficial in helping the small firm to identify opportunities. Specifically, institutions such as universities, and government organizations (e.g., Small Business Development Centers) can be of benefit to a small business in trying to identify opportunities.

The final source of information discussed in the taxonomy is the use of trade shows and conventions. Here opportunistic decision makers can gain exposure to new technological advances in an industry, and also learn from others in the industry.

In addition to environmental scanning, one other source of information may help the small business in pursuing the identification of opportunities. Strategic networking or establishing relationships with important individuals in the industry in which a small business operates can lead to opportunity identification. More important, this may increase the possibility that the small firm becomes a recipient of an accidental opportunity. The use of bankers, accountants, lawyers, and professionals can act as advisors in helping the small firm to become proactive. Empirical research has shown, however, that the use of networking by small businesses is extremely underutilized Smeltzer, Fann and Nikolaisen (1988). In trying to increase the use of external expertise in internal opportunity identification, small firms generally establish an outside board of directors Robinson (1982).

Key Considerations for Strategy Factors

1. Formalized planning processes encourage routine or systematic analyses for the existence of potential opportunities.
2. Opportunities may exist inside the organization, as well as in the industry environment. Therefore, opportunity identification should consider both internal and external environmental scanning sources to ensure full coverage of information sources.
3. The process of actively networking within one's own industry may expose small business owners to sources of information otherwise not used to identify opportunities.

AN APPLICATION OF THE MODEL

In order to illustrate the potential usefulness of the model, we now apply it to two actual businesses located in a Midwestern city. Both companies are restaurants. We have disguised their names for this paper. The first company, which we will call Aggressive Pizza has aggressively pursued several opportunities, resulting in significant growth. The second company, which we will call Contented Pizza, has never attempted to identify or pursue opportunities, resulting in no or little growth.

Environmental Factors

Aggressive Pizza's owner recently located the first of his pizza stores in a growing suburban community near a mid-sized city. It was the first pizza restaurant to be located in the community. It was a franchise of an upscale pizza chain which featured higher priced pizzas and a wide variety of other foods for both dine-in, carry-out, and delivery. Contented Pizza is an older restaurant/bar which has existed in the same location for decades. It serves a large clientele of regulars, but its owner has never expanded beyond the existing building. The type of pizza that Contented sells is decidedly traditional, and this type of pizza has seen little growth in recent years. It is also located in an area of the city which is not growing. Its occasional customers do come from a reasonably wide area, but the regulars are likely to travel no more than two miles to the restaurant. It is clear that Contented Pizza's environment is one of little growth while Aggressive Pizza's customer demographics and its products are in a much higher growth stature. Therefore, Aggressive Pizza can simply pursue existing

opportunities in its current market, while Contented Pizza would have to create its own opportunities by considering additional product offerings or new geographic markets. Even though environmental factors may increase or decrease the existence of opportunities, by themselves, they cannot account for all the differences in the intensity of the search for opportunities.

Owner Factors

Aggressive Pizza's owner is a recent graduate of a Midwestern private university where he majored in management with an emphasis on entrepreneurship. After studying a new franchise of pizza restaurants headquartered less than three hours away, he decided that it was right for him. His growth intentions are illustrated by the fact that he was given the choice of buying a single franchise or paying a premium to become a master franchiser which would require him to open ten units within five years in his defined territory. Thus, both his stated intentions and his low level of risk averseness pointed clearly toward growth.

Contented Pizza's owner, by contrast, was nearing retirement. He had operated the restaurant in the same location for decades. It was known almost as much as a local bar as it was for its pizza. The owner never had intentions of growth beyond that business since it provided him and his family a comfortable living. Both owners started their ventures so they could be their own boss (need for autonomy). Both had an internal locus of control. But Aggressive's owner had a far higher need for achievement. Further, since the franchise, itself, was relatively new, Aggressive's owner was far less risk averse than the typical small business owner. He saw himself as taking a chance on a new concept which, if successful, could pay quite high rewards including involvement in the franchise itself in addition to his individual franchises.

Strategic Planning Factors

In the area of strategic planning, Contented Pizza's owner did little strategic planning. Indeed, little was needed. Since little growth was desired, the area was neither growing nor becoming blighted, the restaurant was stable, and it brought in an adequate level of income, there was little need nor desire to spend considerable time in the planning process. Aggressive Pizza's owner, on the other hand, spent considerable time in planning and scanning. After he opened his first restaurant, he immediately contacted a local university for help in site selection for a second location and development of a strategic plan. He met frequently with the franchise owners at company headquarters to keep in touch with changes in the industry and within their franchise. In order to obtain financing, he prepared a business plan to take to his local bank. Thus, his strategic planning was both in depth and formal, exposing him to potential opportunities that he may have otherwise never perceived.

In summary, Aggressive Pizza was in a high-growth environment, and the owner had strong intentions toward growth, was willing to accept risks and tolerate ambiguity, and was actively involved in strategic planning. Consequently, the owner was consistently searching for new opportunities. Conversely, Contented Pizza was in a low-growth environment, the owner had no intentions for growth, was not willing to expose the business to risks, and did not

actively plan. Therefore there was a complete absence of any opportunity searches. The two examples selected were clearly extremes regarding the search for opportunities. Yet, they serve to illustrate how the model can be applied to differentiate between opportunity search-oriented owners and more complacent business owners.

CONCLUSIONS AND IMPLICATIONS

Opportunity search is important to small business owners because the degree of search intensity is a fundamental element to the growth of a business. The model we presented used concepts from the decision making, entrepreneurship, organizational theory, and strategy literatures to attempt to provide new insights into opportunistic decision-making behaviors of small businesses. This paper suggested that small business owner characteristics and intentions are self-limiting factors that reflect the desirability of growth from an owner's perspective. Strategic-planning characteristics are primarily under the control of the small business owner because the owner sets the tone for the business. Therefore, a small business owner can influence the opportunity identification process. External factors, however, are beyond the control of the small business owner, although the small business owner can react to environmental factors at any time to take advantage of perceived environmental opportunities.

Implications For Owners and Consultants

The model we presented here suggests that two of the three factors influencing search for opportunities are under the control of the small business owner. The owner's characteristics and intentions affect opportunity search directly and also interact with the strategic planning activities. The third factor -- the environment -- is not under the control of the owner, but it does impact the propensity to search because of either the potential to act on existing opportunities when in a growth environment, or the need to search for new opportunities elsewhere when in a stable or declining environment.

Owners should consider the importance that opportunity search has for their businesses. The considerations developed in this paper may provide owners with new insights into environmental, managerial and organizational factors that may motivate them to increase opportunity search intensity. For example, if a small business owner is interested in pursuing new opportunities, formalized planning and scanning mechanisms should be implemented in order to provide decision makers with necessary information.

Small business owners should also be willing to accept risk and be tolerant of uncertainty. They should be aware that certain environmental conditions, such as high growth potential, competence-enhancing change, and low complexity, may create new opportunities. Similarly, environmental scarcity may create a need to force opportunity searches outside of the original industry. Moreover, small business owners can review the key considerations identified at the end of each section of determinants to see how specific factors may impact their opportunity search.

Consultants working with owners can address all three issues. Consider the case of Contented Pizza. Suppose the owner contacts a consultant to discuss why sales are stagnant. The consultant can suggest any of the following:

1. No change will occur unless the owner clearly decides that change is good.
2. Change will require a shift away from risk averseness.
3. Since Contented Pizza is in an older part of the city, growth is not likely to occur. In order to create opportunities, Contented's owner will have to diversify into other areas of the city or into other cities.
4. Identification of opportunities will require significant strategic planning. The consultant can suggest specific techniques or offer to train Contented's owner in strategic-planning processes.
5. The consultant can bring information about opportunities to the attention of the owner which might include articles on new types of pizza or contacts with developers of a new shopping center.

Research Implications

This paper contends that to understand better why some small business owners are involved in opportunity search and others are not, researchers must know what factors have contributed to this aggressive or non-aggressive strategic orientation. The integrative model developed in this paper has attempted to provide needed insight by discussing the effects of factors supported by the entrepreneurship, organizational theory and strategy literatures.

In addition to examining the main effects from the proposed model, future research opportunities also lie in the interactions between factors. For example, do risk averse owners react more favorably to a highly dynamic and complex environment or will they be even more hesitant to look for opportunities since they may not fully understand the impact of competition within that environment? Is planning formality more important in a dynamic environment since it provides more information or detrimental because it is more time consuming and costly? Since strategic planning and diversification require at least some willingness to accept risk, can the level of risk averseness be changed in small business owners? These and other interactions may provide new research opportunities for both conceptual and empirical investigation.

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