THE COMMON THREAD AMONGST ENTREPRENEUR, MANAGER AND CAPITALIST: A THEORETICAL APPROACH

Onakoya, Adegbemi Babatunde
Department of Economics College of Social and Management Sciences Tai Solarin University of Education, Ijebu Ode, Nigeria

Abosed, Adebiyi Julius
Department of Business Administration Faculty of Social and Management Sciences Olabisi Onabanjo University, Ago-Iwoye Nigeria


ABSTRACT

The continued sustainability of the firm rests on the troika of effective management of the present, imaginative vision for the future and adequate funding of opportunities. For the firm's robustness to become faster, more cost efficient and responsive to current markets, the requirement for regular assessment of the vision, willingness to adjust or change strategies, products and markets must be complimented by effective corporate governance. This paper highlights the role of entrepreneurs, managers and capitalists in value creation. It concludes that the common attribute of capitalists, managers and entrepreneurs is the entrepreneurial spirit which propels each and all of them to work for the future, often in uncertain terrain.

Key Words: Entrepreneurship, Capitalist-owner, Management and Firm performance

Introduction

The need for value creation underlies the theory of the firm. The creation of value is achieved through the combination of the various factors of production coordinated by the entrepreneur. This is viewed as a key aspect of an economic system. During dynamic economic crisis which are also historically times of industrial renewal, less efficient firms fail while more efficient ones emerge and expand. The third in the Rostow (1960) stages of economic growth theory requires the active participation of the entrepreneur. The leading sector of this third stage is akin to the
cotton textiles of Britain and New England where the possibilities of innovation or of exploiting new or unexplored resources in the early days of the industrial revolution were manifesting (Jhingan, 2005). Schumpeter (1942) identifies entrepreneurship as being responsible for making things happen and bringing new products or services to the market (creative destruction). The variables of interest to this study - entrepreneurs, managers and capitalists (owners) are armed with different skills that are critical to the firm. (Busenitz & Barney (1997) highlight the manager's expertise in resource organization and the capitalist's ability to discern among alternatives in the choice of venture portfolio. The entrepreneur is said to be endowed with the intuitive capacity of defining contexts of the future through which new product and process opportunities are created. These disparate skills and orientation portend conflicting yet common trends in the formation and maintenance of firms in the avowed bid to return value (profit) to the various stakeholders (Abosede & Onakoya, 2013).

The link between uncertainty and the profit of the firm as provided by Knight (1921) involves the exercise of the judgment factor which he described as the process of establishing estimates of future events in situations in which the relevant probability distributions are themselves unknown. In essence, the judgment cannot be assessed in terms of its marginal product and cannot therefore be remunerated accordingly. Since the entrepreneur, manager and capitalist (owner) operate at different levels of risks and uncertainties; their rewards cannot be provided as paid salaries alone but rewarded in part from the residual value of the firm. Arising from this, this paper attempts to examine the theoretical and empirical literature with the aim of bringing forth the key roles and relevance of the manager, entrepreneur and capitalist in the value creation process of the firm. The rest of the study is presented as follows: Section Two reviews the theories and implications of the concepts. Section Three discusses similarities and differentiation amongst the functions and traits of the entrepreneur, the manager and the capitalist. Section Four concludes.

**Theories and Implications of Concepts**

**Entrepreneurship**

Several theories underline the understanding of the entrepreneurship concept. The risk theory by Hawley (1907) as cited by Knight (1964) posits that although good managers can create profits
through incremental innovation, they are not entrepreneurs unless they also assume the risk of ownership. Although the entrepreneur is in the leadership position in the composition of the firm, he is virtually absent from the received theory of the firm. (Baumol, 1968). The dynamic theory states that the function of the entrepreneur is to locate new ideas and put them into effect. This theory of profit which commences with the neoclassical economic theory puts profits forward as arising from the dynamic change from the static equilibrium state of perfect competition (Hayek, 1937). Schumpeter (1934, 1961) views entrepreneurs as being the source of disequilibrium through creative destruction. On the other hand, the Austrian School views the entrepreneur as bringing the market back into equilibrium. Indeed, Kirzner (1973) identifies an entrepreneur as a decision-maker whose entire role arises out of his alertness to hitherto unnoticed opportunities.

The entrepreneurial function as advocated by Shane and Venkataraman (2000) entails the discovery, assessment and exploitation of opportunities. These tasks involve the creation of new products, services and production processes in addition to novel management strategies, organizational forms and markets. These original inputs and output may hitherto, be previously not in existence. The entrepreneurial opportunities are created by creative agents with differing ideas on the relative value of resources. Alvarez and Busenitz (2001) posit in the theory of the entrepreneur that the heterogeneity of beliefs about the value of resources is the key prompter of entrepreneurial pursuit. Reynolds (2005) agrees that the entrepreneurial function is the discovery of opportunities which subsequent leads to the creation of new economic activity through the creation of a new organization.

In discussing entrepreneurial spirit, Miller (1983) emphasizes the need to accentuate exploration, search and innovation functions of the entrepreneur as opposed to the exploitation of business opportunities which is in the purview of managers. In the neoclassical growth theory, the entrepreneurial factor is the new explanatory variable hitherto omitted in production model as quite distinct from labour and capital. This factor is remunerated with profit or surplus value as consideration for the discovery and exploitation of opportunities. Entrepreneurial behaviour as explained by Miller (1983) combines the classic theories of Schumpeter’s (1942) innovative entrepreneur and the risk-taking entrepreneur as proposed by Knight (1921).
The entrepreneur with initiative and imagination creates new avenue for correctly anticipating market imperfections in addition to enhancing innovative capacity for the creation of new product/service offerings. This may be within or outside an existing organization. The entrepreneur’s central activity is that of business creation; which can be studied at an individual or at group level. In developing countries, Oladele, Akeke and Oladunjoye (2011) are of the belief that small and medium enterprises, created by entrepreneurs are the critical engines of economic growth.

The traits school of thought states that the function of the entrepreneur to locate new ideas and put them into effect is determined by the traits of the individual entrepreneurs. The theory evaluates the variables that explain the personality characteristics including the psychological profile and non-psychological variables (education, experience and social networks for instance). Other studies on social-environmental variables lay emphasis on the institutional legal framework (Eckhardt & Shane, 2003); the economic environment (McClelland, 1987); the spatial environment and the technological and financial institutions (Tushman & Anderson, 1986). In consideration of these traits, Kihlstrom & Laffont (1979) surmised that entrepreneurial activity as a human activity does not spontaneously occur. It has to be nurtured and conditioned by the human traits and the environment.

**Management**

Precise definition of management is not so simple because the term is used in a variety of ways. The contributors from economics, sociology, psychology, anthropology and other disciplines view management differently. The theory of management is the collection of ideas which set forth general rules on how to manage a business or organization. Management theory addresses how managers and supervisors relate to their organizations in the knowledge of its goals, the implementation of effective means to get the goals accomplished and how to motivate employees to perform to the highest standard. The economists treat management as 'a factor of production'. Henri Fayol (1841–1925) as cited in Dunod (1966) presents management as consisting of six functions: forecasting, planning, organizing, commanding, coordinating and controlling. Thus, management is seen as the manipulation of the human capital of an enterprise to contribute to the success of the enterprise.
Drucker (1985) states that the basic task of a manager consists of marketing and innovation. Drucker identifies marketing as a key essence for business success which together with innovation forms the two different branches of business administration knowledge which is central to strategic management. In effect, innovation is not consigned to the purview of the entrepreneur alone. Management is a continuous process which functionally consists of planning, organizing, directing and controlling the resources to ensure that resources are used to the best advantages of the organization in achieving the policy’s objectives. Management also aims at achieving predetermined objectives. A very important function of a manager is decision-making which is selecting the best among alternative courses in order to achieve maximum profit or surplus value. Directors and managers have the power and responsibility to make decisions in order to manage an enterprise when given the authority by the shareholders.

Management is also dynamic and therefore, not static. Over a period of time, new principles, concepts and techniques are developed and adopted by management. It is also a profession with focus on specializations such as marketing management, finance management, personnel management, industrial management, production management and quality management. (Dover, & Dierk, 2009). All these functions are required for the smooth running of a large organization although may be combined in varied forms in small and medium enterprises.

The manager is involved with incremental innovation which ranges from cost-reduced versions of existing products to add-ons or enhancements for an existing production process. These derivative projects are usually minor, requiring fewer development resources than the other categories. Breakthrough projects (or radical innovation) at the other end of the development spectrum involve significant changes to existing products and processes. They therefore often incorporate revolutionary new technologies or materials, usually requiring revolutionary manufacturing and management processes. The involvement of the capitalist - owner is often required to actualise this type of innovation (Garvin & Levesque, 2006 as discussed in the next section.

**Capitalist (Owner)**

Also referred to as the residual owner, the capitalist is often ignored in the neoclassical theory of the firm. The theory of profit maximization from the perspective of the manager - a hired agent
has responsibility for running the firm. The new institutional economics which extends the subject by focusing on the social and legal norms and rules that underlie economic activity beyond earlier institutional economics and neoclassical economics addresses the relevance of the owner (Rutherford, 2001). The capitalist who is the ultimate decision maker as the primary supplier of the capital that funds the plant controls how much authority to delegate to operational managers. Therefore, in order to understand the theory of firm, it is important to focus on the actions and plans of the suppliers of financial capital. Money capital is treated as a factor of production in the production-function model. The cost of capital is simply treated as another cost (albeit assumed to be exogenously determined) whilst the profit is retained by the capitalist. In view of this, Rothbard (1962) suggests that ownership can be a factor of production since the investor -capitalist is both the ultimate decision-maker and residual claimant.

In the traditional capitalist firm, ownership and control are fused. As the corporate form developed in the nineteenth century and firm began to issue stock to the public, the connection between ownership and control became problematic. The separation of ownership from control became necessary. Berle and Means [1932] (1968) highlight several consequences arising from this separation. Managers were less subject to the dictates of shareholders with respect to day to day management and policy formulation including dividends. The increased firm size, market share and profitability gave managers access to greater amounts of internally generated funds with consequential insulation from external stakeholder pressures.

The connection between ownership structure and firm performance remains ambiguous. The investigation by Karaca and Ekşi (2012) of this relationship of 50 companies, listed in manufacturing industry on the Istanbul Stock Exchange during the 2005-2008 reveals positive effect of ownership structure on profit before taxation. However, there was no observed impact on Tobin's q. This contrasts with the finding of inverse relationships between the diffuseness of shareholdings and firm performance by Berle and Means (1932). Demsetz (1983) argues that the ownership structure of a corporation is an endogenous outcome of decisions that reflect the influence of shareholders and of trading on the market for shares. The ownership structure whether concentrated or diffuse, ought to be influenced by the profit-maximizing interests of shareholders, such that, as a result, there should be no systematic relation between variations in ownership structure and variations in firm’s performance.
Douma, George and Kabir (2002) examine how ownership structure affects the performance of firms using firm level data in India by focusing on ownership diversity (nationality, foreign institutional and foreign corporate shareholders). The study finds positive effect of foreign ownership on firm performance. This is attributable to foreign corporations that have, on average, a larger shareholding and a higher degree of commitment and long-term involvement. BurkartGromb and Panunzi (1997) posit that the ownership structure of the firm is an instrument to resolve the trade-off problem between control and initiative. In the more dispersed ownership structure, shareholders with weaker intervention capacity make managers confident enough that they will not be dispossessed of the benefits of their initiative.

Entrepreneur, Manager and Capitalistic Comparison

The review of the literature suggests that managers, entrepreneurs and capitalists bring different skills and capabilities to their company roles. The manager focuses on current business complexity, the entrepreneur on opportunities and the capitalist on provision of funding required for on-going and new businesses. The two classifications of firms suggested by Fraja (1996) are the entrepreneurial firm, where the capitalist or entrepreneur is in exclusive control of its operations and the right to residual returns. The other type is the managerial firm, where the shareholders who have the right to residual returns of the company and hires the management.

![Fig.1: Sustainable Growth of the Firm: Role of the Entrepreneur, Manager and Capitalist](image-url)
The differentiation between the functions of entrepreneur, manager and capitalist is aptly captured in Table 1. The small scale entrepreneurial individual identifies and / or creates business opportunities for exploitation through either existing company or a new small / medium sized organization. The chief executive of large firms in his role as corporate entrepreneur is required to manage the resources of the firm and coordinate its activities. Beyond this, he must also play the role of entrepreneur by anticipating change and reinventing the firm. Where need be, he may need to create new enterprise (spin-offs) and develop company networks to take advantage of new opportunities.

**Table 1: Entrepreneur, Capitalist, Manager**

<table>
<thead>
<tr>
<th>Characteristics</th>
<th>Entrepreneur</th>
<th>Capitalist</th>
<th>Manager</th>
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<tbody>
<tr>
<td></td>
<td>Discovers and exploits Opportunities.</td>
<td>Provides funding for the firms resources in return for profit / surplus value.</td>
<td>Creates and maintains competitive advantage.</td>
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<td></td>
<td>A creator who initiates and motivates the process of change.</td>
<td>Can be active and controlling or passive shareholder.</td>
<td></td>
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<tr>
<td>Functional Approach</td>
<td>Sets mission and objectives and identifies resources to help realize vision them</td>
<td>Evaluates competing opportunities both rationally and intuitively.</td>
<td>Works on efficient and effective use of resources to reach goals and objectives.</td>
</tr>
<tr>
<td>Change Management</td>
<td>Key is initiating change.</td>
<td>Key is financing change.</td>
<td>Key is adapting to change.</td>
</tr>
<tr>
<td>Organizational Framework</td>
<td>Defines tasks and roles that create an organization framework.</td>
<td>Operates both existing and start-up organizations.</td>
<td>Operates within an existing framework.</td>
</tr>
<tr>
<td>Work Pattern</td>
<td>Work pattern implies imagination and creativity.</td>
<td>Work pattern implies imagination and creativity.</td>
<td>Work pattern is rational decision making.</td>
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<tr>
<td></td>
<td>Work centred on processes that take the resulting from a differentiated view of the Environment.</td>
<td></td>
<td>Work centred on the design of environment into account processes.</td>
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<td></td>
<td></td>
<td></td>
<td>Supervision of the Organizational processes.</td>
</tr>
<tr>
<td>Organizational Behaviour</td>
<td>Corporate leadership initiates new ways of behaviour that questions the status quo.</td>
<td>Assesses alternatives in the choice of venture portfolio</td>
<td>Creates trust to enhance Cooperation within the organization</td>
</tr>
<tr>
<td>Innovativeness</td>
<td>Identifies business opportunities for existing businesses and the creation of new enterprise</td>
<td>Demands new opportunities for investment</td>
<td>Maintains the status quo or at best, initiates incremental improvements</td>
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The constraint to the combined roles of efficiently managing the present while, at the same time, creating a climate that encourages future entrepreneurial vision according to Dover and Dierk (2009), is the need to meet stifling urgent challenges of daily responsibilities. Struggling companies find it hard to survive while entrepreneurial firms often grow too quickly to build effective management processes.

The primary function of the manager is to take charge of the process of combining resources and efficiently managing the firm’s resources. Another critical role of the manager is building a cohesive team in an atmosphere of trust that harmonizes the conflicting individual objectives into a system of cooperation. The manager should seek to achieve a greater degree of efficiency by reducing supervision and agency costs. Although beset with the aversion to risk taking, the owner assesses alternatives in the choice of venture assets. In order to achieve organic growth, the corporate manager is required to consider the key shareholders that take an active part in the firm, along with managers that share in making up the firm’s basic competences (Cuervo, Ribeiro and Roig, 2007).

Managers pursue objectives by making effective and efficient use of resources. They normally operate within frameworks previously defined by someone else. The organisations created by entrepreneurs, however, are really an extrapolation of their subjective worlds. What entrepreneurs do is closely linked to how they interpret what is happening in a particular sector of the environment. Entrepreneurial activities require a systemic framework that includes concepts (Peterson, 1981 and Drucker, 1985), although on a different level from management. Managerial activities also demand elements of intuition and imagination. However, the conceptual activities and skills of the two groups are different. The capitalist who is the provider of the firm’s funds, either in the form of a passive shareholder or as a majority or active shareholder assumes both the entrepreneurial and managerial functions especially in small and medium sized business entities.

An entrepreneur as suggested by Gartner, Bird and Starr (1992) is both a manager and a capitalist, with a willingness to accept risk, uncertainty and an eagerness to exploit change and profit from market niches. Piperopoulos (2011) however contends that entrepreneurs have a certain set of skills that is superior to that of a manager in terms of productivity and profitability. The typical entrepreneurial capabilities in his view include features such as investigating
opportunities, believing in innovation and strategic planning upon the latest developments on the market. Where managers are given some latitude to undertake innovative actions, they are more likely to show initiative to so do. This is the position of Aghion and Tirole (1997) who contend that with concentrated ownership, the monitoring of management is more which tends to curtail the manager’s initiative or incentive to innovate.

The capitalist, entrepreneurs and managers as postulated by Burns (2007), can also be distinguished by their character traits and the type of business they run. The entrepreneur is opportunistic, innovative, self-confident and acts proactively in taking risks. These explain the tendency for the manager to run growth-induced firms and pursue personal wealth. The owner-manager (capitalist) who is infused with uncertainty, measured risks and independence often runs a lifestyle firm that is based on trade or craft which, however, do not usually grow to any considerable size. The manager is involved in running and managing an entity that does not belong to him with the mission of building up the organisation. Burns (2007) however provided some exceptions to these generalisations. He submits that an owner-manager may nurture a growing business, while an entrepreneur could jointly manage a business and therefore not have complete control over the capital. The findings in an Israeli exploratory study by Malach-Pines et al (2002) reveal a number of entrepreneurial trait similarities as well as differences between the managers and the entrepreneurs. The question of why managers and entrepreneurs are who they are is answered within a psychoanalytic-existential framework. The framework focuses on the managers’ positive identification with their father and better relationship with both parents as compared to the entrepreneurs’ negative identification with father and greater identification with work. The entrepreneur however demonstrates a greater sense of significance in their work. Beyond the trait, Stewart et al (1999) acquiesce to the fact that the art of entrepreneurship can be learnt and that the skills set regarding the way entrepreneurs work on tasks and complete them including personal organization and interpersonal interaction are similar those of the manager.

Shailer (1994) considers the role of the capitalist and entrepreneur in the context of owner-managed firms. In answering the question of who serves the capitalist function, the conclusion is that while nearly all owner-managers are obliged to assume the role of capitalist, only a minority will act as entrepreneurs due to the pressure of running daily operations in small and medium enterprises. Busenitz and Barney (1997) explore differences between entrepreneurs and
managers in large organizations by examining differences in the decision-making processes used by entrepreneurs and managers. Building on non-rational decision-making models from behavioural decision theory, they find that entrepreneurs are more susceptible to the use of decision-making biases and heuristics unlike managers who deploy rational, logical approach. The publicly held business firms have performed better in harnessing the strengths of the manager, entrepreneur and the multitudes of its capitalist owners. As an awesome social invention itself, millions of individuals shareholders who have voluntarily entrusted their resources to managers on the basis of trust have suffered occasional losses arising from poor corporate governance. However, the growth in the use of the corporate form as well as the growth in market value of established firm suggests that overall; this form of corporatization is functioning despite the agency costs (Jensen & Meckling, 1976).

The dilemma confronting the capitalist with regards to the manager is the principal–agent problem which concerns the difficulties in motivating the agent to act in the best interests of the principal rather than in his own interests. The problem arises as a result of different interests and asymmetric information since the agent is usually in possession of more information obtained from his close proximity to the running of the firm. The principal cannot directly ensure that the agent is always acting in his (the principal's) best interests. Indeed, the principal may choose not to enter into a transaction at all, when that deal would have actually been in both parties' best interests resulting in a suboptimal outcome that lowers overall welfare (Bebchuk & Fried, 2004). The success of the firm is therefore dependent on the inter-twined functions of the manager, entrepreneur and the capitalist.

Conclusions

Managers, owners and entrepreneurs can be distinguished not only by their character traits but they are also more likely to lead an organization that is typical for their respective role. In order to be more competitive, modern organizations try to incorporate selected features of entrepreneurship into management and ownership and. Since the business process includes the identification, assessment of opportunities and conversion of such to value adding products / services, this study agrees with the position of Lee and Peterson (2000) who recommends that managers and owners should adopt entrepreneurial behaviour when developing their strategies in order for the firm to achieve its objectives.
The skill and traits of the three actors are to some extent similar yet different. The manager's expertise is focused on resource organisation; entrepreneur's know-how is on defining contexts and the strength of capitalist is identifying winning project(s). At the level of small and medium scale enterprises, the intertwined skills sets of the manager, entrepreneur and owner-managers are critical to the long term success and survival of the firm. At the corporate level for large companies, the role of the capitalist - ownership is usually diffused. Capitalist investment decisions depend upon entrepreneurs’ initiative to select investment projects ex-ante, and financiers’ incentive to control management and entrepreneurs’ ex-post. The point to emphasise is that the common attribute of all three actors is the entrepreneurial spirit which propels each and all of them work for the future in uncertain terrains.

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