

Comment on Justin van der Sluis and C. Mirjam van Praag: Is Economic returns to education for entrepreneurs: The development of a neglected child in the family of economics of education?

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Entrepreneurship as an academic field can be characterized as being phenomenon driven and multi-disciplinary. Consequently, theories and methods established in other disciplines such as economics, sociology and psychology are frequently applied in entrepreneurship research. In order to make advancements and gain legitimacy, it is important that this research utilizes the latest theoretical insights and methodological developments in these disciplines. In their article, van der Sluis and van Praag adhere to these principles by using novel methodological insights applying them to entrepreneurship.

Labor economists have since long established that it is difficult to directly estimate how education affects economic returns, since unobserved abilities are likely to affect both education and income so that those with greater abilities choose both longer educations and perform better at work, which gives them higher incomes. As a result, simply regressing income on education will lead to biased results. As van der Sluis and van Praag rightly note, these insights have not yet made their way into entrepreneurship research, thereby representing an area where entrepreneurship research has, so far, failed to keep up with methodological advancements made in the other disciplines. In their sophisticated and careful analyses of US and Dutch data, van der Sluis and van Praag show that because of the failure to acknowledge such relationships, previous research has underestimated the returns to education for the self-employed. In fact, they suggest that, if anything, the returns to education are higher among the self-employed than among the employed. Using similar logic and methodology, they then argue that capital constraints are, to some extent, dependent upon education, so that those with longer education find it easier to

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raise capital. Taking this into account, they suggest that this boosts the returns to education among the self-employed even further.

1. Methodological implications for entrepreneurship research

Before discussing the implications of these empirical findings, I wish to say a few words on the significance of the methodological advancements made in the article. In the past, there have been few high quality databases on entrepreneurial phenomena. Some databases developed for other purposes, such as the panel study of income dynamics in the US or the British household panel survey, lend themselves to addressing some entrepreneurship issues. More recently, however, we have seen an increase in high quality data bases specifically designed for addressing entrepreneurial phenomena. The most well-known is probably the panel study of entrepreneurial dynamics (PSED, see Gartner et al., 2004), which has applied similar methods in several countries for collecting panel data on entrepreneurial activities. As a result of this increase in high quality databases, there is a need for a larger number of entrepreneurship scholars to acquaint themselves with more sophisticated research methods than those used in the past. The work by van der Sluis and van Praag represents an effort in this direction that can be inspirational for several among us. It should be kept in mind, however, that methodological sophistication is not a purpose in itself. It should not come in the way of examining those issues that can have the greatest impact on empirical and theoretical advancement. There is sometimes a tendency for methodologically sophisticated research to care more about the application of the method than the relevance of the findings the methods can serve to uncover.

2. Interpretation of findings

As good research should, this study raises more questions than it answers. If we accept the finding that the returns to schooling are larger for the self-employed than for the employed, how do we interpret such a finding? Van der Sluis and van Praag suggest that it is easier for someone to maximize the productivity of his or her human capital being self-employed than being employed. In an existing organization, people are restricted in their actions by organizational structures and chains of commands. This, the authors argue, is not the case for the

self-employed who can better create a work situation that optimizes the returns to their human capital. I am not sure this is the most plausible explanation. The less educated that opt for employment are likely to have subordinate roles in an organization, allowing little freedom of action, whereas those with more education are more likely to take on managerial positions allowing greater discretion in the choice of work tasks. As self-employed, the differences in influencing work tasks are likely to be smaller rather than larger between more and less educated individuals. This would lead us to expect smaller returns to education for the self-employed than for the employed, rather than the larger returns presented in the article. Therefore, in the below, I offer three alternative explanations for the intriguing findings presented by van der Sluis and van Praag.

First, on the basis of the principal-agency framework, Douglas and Shepherd (2000) offer a straightforward model suggesting that, all else equal, high-ability individuals will gain more from turning to self-employment than low-ability individuals because of larger marginal returns to increased work effort in self-employment relative to employment. Second, depending on human capital, people vary in the performance thresholds at which they decide to leave their businesses (Gimeno et al., 1997). Highly educated individuals have more employment options. If self-employment does not provide the expected economic benefits, they may relatively easily find employment. For those with little education, this is not the case and they would be more likely to persist despite poor performance. Therefore, over time, the share of firms providing inadequate income is likely to be higher among the poorly educated than among the highly educated, because of more exits among the latter category. Third, in a recent study, Wiklund and Shepherd (2003) found that education had an impact on the extent to which firm behavior was under the volitional control of the entrepreneur. That is, those entrepreneurs who had longer educations were better able to implement the strategies that led to the fulfillment of their personal goals. Therefore, if maximizing economic returns were a personal goal, those with higher education should be better at achieving this goal. As these alternative explanations illustrate, there is still much more to learn about the returns to education in entrepreneurship. Hopefully, the study by van der Sluis and van Praag will spur such research.

3. Does switching to self-employment pay off for the highly educated?

A related and interesting question that is not addressed in the present study is how economic returns are affected by the entry into self-employment for people of different levels. In their policy implications the authors allude to highly educated earning more as self-employed than as employed, but this issue is not really addressed in the current article. While it appears that among the self-employed, those with longer education fair better, this does not mean that turning to self-employment would increase the economic returns for those who are highly educated. This is an important question, because it relates to whether people with substantial human capital choose employment or self-employment. A recent Swedish study focusing solely on the science and technology labor force (STLF), i.e., those with at least three years of university education in medicine, science or engineering, found that, on average, the businesses started by the STLF pay salaries far below what these individuals earn as employees (Delmar et al., 2003). This led the authors to conclude that starting an independent firm is a less attractive option for most members of the STLF. Given the low salaries paid, several of those starting businesses in fact do so because they are unable to find suitable employment opportunities despite their long educations. In other words, several of those starting businesses are likely to be pushed into it because they have few other options. While this may be a common situation for the labor force at large, it is surprising that it also applies to the STLF. Consequently, the opportunities exploited by those of the STLF starting their own businesses are probably not the most promising ones. It is difficult to know if this situation is unique for Sweden or if it also applies to other countries. Research into this area could have substantial policy implications and provides a natural extension to the work by van der Sluis and van Praag.

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