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## 38. Growth

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New-venture growth has been and continues to be a critically important area of inquiry for entrepreneurship research (Nason and Wiklund, 2018). Entrepreneurship scholars have invested substantial efforts in the growth phenomenon and the related theoretical and methodological foundations, such as defining various modes of growth that new ventures may pursue (McKelvie and Wiklund, 2010), understanding the consequences of researchers' measurement choices (Shepherd and Wiklund, 2009) or exploring the relevance of viewing growth as a development process consisting of a number of stages (Levie and Lichtenstein, 2010). Despite this progress, scholars have noted that theoretical development on new-venture growth has been notably slower than some other areas within the literature (cf. DeSantola and Gulati, 2017; Gilbert et al., 2006).

Growth is a dynamic process – a change in size from one moment to another – that shapes the new venture as the process unfolds (Levie and Lichtenstein, 2010). Streams of research concerning new-venture growth generally fall under three major conceptual approaches (cf. McKelvie and Wiklund, 2010) including: the antecedents of growth (that is, growth is the dependent variable, typically being explained by a set of independent variables in regression analysis); the consequences of growth (that is, studies that examine how organizations change as a consequence of becoming larger); and how firms grow, which examines how the growth process unfolds over time.

In this chapter, we explore these streams and then turn our attention to complexities of high-growth firms. While rare, these firms are very impactful. We conclude by highlighting several avenues related to new-venture growth that warrant future study.

### ANTECEDENTS OF GROWTH

In research, growth is often used as a proxy for overall firm performance among new ventures and forms an important part of the new venture performance and wider strategy literatures (cf. Shepherd et al., 2019). This stream of research seeks to explain variance in growth rates across firms. The factors contributing to explaining variation in growth across firms differ across multiple levels of analysis, including attributes of individual entrepreneurs, entrepreneurial teams, the firm, stakeholders and the institutional (for example, country, industry) context in which the firm operates.

#### **The Entrepreneur**

Owing to the relatively young age and small size of new ventures, the entrepreneur wields significant influence over the strategy and the performance of the firm (Miller, 1983). Ample evidence suggests that the characteristics of entrepreneurs influence whether and how their firms grow. Early research extensively examined the relationship between the

entrepreneur's human capital (for example, education and previous experience) and firm growth (Cooper et al., 1994; see also Gilbert et al., 2006 for a review), though meta-analysis suggests that this relationship, while positive, is relatively weak (Unger et al., 2011). Entrepreneurs' personal social networks have also been linked to the growth of their ventures (Ostgaard and Birley, 1996). Although building social networks requires large investment of the entrepreneur, the consensus of numerous studies is that this investment will pay off in most cases, with the strongest positive effects of network diversity (Stam et al., 2014).

Whereas the human and social capital of the entrepreneur are important, the entrepreneur's attitudes towards growth and their motivation to expand the business are equally salient (Baum and Locke, 2004). Ample empirical evidence challenges the notion that all entrepreneurs are growth orientated. Entrepreneurs start their businesses for multiple reasons, which have consequence for their willingness to expand. For example, those that primarily seek independence may not want to grow (Douglas, 2013). Also, preferences for small-scale and intimate work relationships as well as the possibility of working with favorite work tasks, rather than becoming an administrator, often keeps growth motivation down (Wiklund et al., 2003). Psychological income can be sufficient reason to continue operating a poorly performing firm (Gimeno et al., 1997).

Entrepreneurs' attitudes towards growth are shaped by the anticipated consequences of growth (Wiklund et al., 2003). Growth brings changes, sometimes disruptive, to the nature of the work and the firm. As firms grow, the nature of the entrepreneur's role within the firm changes, and often he or she becomes less involved in the day-to-day operations and more focused on higher-level firm issues (Mathias and Williams, 2018). If the firm adds new employees, professionalization of inner-firm processes and human resources also becomes increasingly important to the firm (Flamholtz and Randle, 2012). Growth often precedes profit, thus requiring an influx of external capital in the form of debt or equity, which in turn requires further growth to either fulfill debt obligations or appreciate the market value of the firm. As the founder's stake in the firm becomes diluted, so does his or her decision-making independence from outside influence. In light of these outcomes of growth, some entrepreneurs proceed with caution when considering growth strategies. For example, employee well-being and the entrepreneur's independence from stakeholders were among the most salient issues of concern among entrepreneurs in Wiklund et al.'s (2003) sample.

From the personal psychology viewpoint, researchers have also examined entrepreneurs' personality traits in the growth process (for example, Baum and Locke 2004; Lee and Tsang 2001). Meta-analysis by Rauch and Frese (2007) suggests that traits such as need for achievement, generalized self-efficacy, innovativeness and stress tolerance are crucial for new venture success, including firm growth. Focusing more broadly on the Big-5 personality traits, Zhao et al.'s (2010) meta-analysis finds the positive link between conscientiousness, openness to experience, emotional stability and firm growth. Recent works have started to look at negative personality traits though, such as the dark triad (narcissism, psychopathy and Machiavellianism) (Hmieleski and Lerner 2016). Narcissistic entrepreneurs have a higher propensity to pursue novel opportunities (Navis and Ozbek, 2016), while also having an easier time making difficult decisions, such as changing strategic course or making personnel changes, in uncertain entrepreneurial environments (Smith et al., 2018). Accordingly, narcissistic entrepreneurs hold a performance advantage in

uncertain environments. Similarly, while traits related to the entrepreneur's mental health, such as attributes linked to attention deficit hyperactivity disorder (ADHD), for example impulsivity, may have potential downsides (Lerner et al., 2019), they also have potential upsides for firm growth (Yu et al., 2019).

### **The Firm**

The findings in Yu et al. (2019) suggest that the entrepreneurial orientation (EO; Miller, 1983) of the firm mediates the relationship between entrepreneurs' ADHD and firm growth, highlighting that firm-level strategy influences growth. Entrepreneurial orientation has been one of the most examined firm strategic orientations in entrepreneurship literature, and numerous studies, including meta-analysis, highlight its positive role for firm growth (for example, Rauch et al., 2009). Further corroborating EO's influence on new-venture growth, more recent studies such as McKelvie et al. (2017) show that particular firm-level innovative activities, such as new product introduction and sales generated from new products, mediate the relationship between an entrepreneur's growth aspirations and achieved firm growth. In addition to EO, early research has also examined generic strategies, such as differentiation and cost-leadership, but with mixed results (for example, Baum et al., 2001; Chandler and Hanks, 1994; Siegel et al., 1993).

Firm strategy does not exist in a vacuum but is influenced and complemented by firm resources. Firms can be viewed as a collection of bundles of idiosyncratic resources. Hence, studies have adopted the resource-based view (for example, Mahoney and Pandian, 1992; Penrose, 1959) to examine how different types of resources can be linked to firm growth. Among the types of resources examined, previous literature has focused on, for example, financial, human and legitimacy-related resources (for example, Cooper et al., 1991; Wiklund and Shepherd, 2003b; Zimmerman and Zeitz, 2002). Instead of focusing on the types of resources, emerging research has started to investigate the versatility of the resources a new venture controls. Nason and Wiklund's (2018) meta-analysis found that versatile resources are superior to non-versatile resources in that they can be deployed or recombined to create growth. For example, high-quality leaders can be deployed to new projects to elude managerial capacity constraints – a common problem that stunts future growth (for example, Kor, 2003).

Collectively, researchers examining firm-level strategies and resources have adopted and called for an interactionist perspective, that is, firm growth depends on the complementarity between the strategy and the resource occupied by the firm. Particular strategies are to be better implemented when there is resource support; and firm growth is to be achieved when there is a fit between strategy and resource (Chandler and Hanks, 1994). For example, Wiklund and Shepherd (2003a) suggest and find that EO and firm growth is moderated by the firm's financial capital. Similarly, Chandler and Hanks (1994) find that the positive influence of quality differentiation strategy depends on resources in support of it.

### **External Stakeholders**

External stakeholders (Parmar et al., 2010) also influence the new venture's growth. Early-stage investors are often dependent on a high-value exit (for example, initial public

offering or buyout) from a few a select few of the firms in their portfolios (Huang and Pearce, 2015). Thus, entrepreneur's must tell a story that is congruent with this end goal in mind (Lounsbury and Glynn 2001). Further, professional investors such as venture capitalists are unmoved by displays of passion, and instead are moved by the preparedness of the founder(s) (Chen et al., 2009). Accordingly, professional investors are often heavily involved in their investments, amplifying the legitimacy of the firm with future customers and other investors (Ko and McKelvie, 2018), which in turn enables further growth.

In addition, stakeholders beyond shareholders have the potential to influence firm growth. One recent example can be found in benefit corporations. The benefit corporation (b-corp) is an external certification that's purpose is to highlight how the certified firm creates value with non-own stakeholders, such as their community, employees and the natural environment (Kim et al., 2016). An exploratory study found that maintaining b-corp status, which can be a foundational value of the firm that seeks certification (cf. Gehman and Grimes, 2017), inhibited the firm's growth (Parker et al., 2019). Some firms, such as Etsy, abandoned their b-corp certification as they approached their initial public offering. However, research on mission drift highlights the risks firms face as they abandon their core principles (Grimes et al., 2019).

### **Institutions**

The legal, political and market institutions surrounding the new venture influence growth. Firms operating in countries with high levels of corruption generally have lower growth rates (for example, Fisman and Svensson 2007). Despite the positive attributes micro-finance has on entrepreneurship in developing countries (Anglin et al., 2020), these firms struggle to grow owing to the instability of their governments (Ahlin et al., 2011), which often complicates the purpose of the firm (Moss et al., 2019). We noted previously the link between growth aspirations and growth (Douglas, 2013; McKelvie et al., 2017). In turn, country-level institutional factors influence growth aspirations. Corruption inhibits, and strong property protection and functional governments enhance growth aspirations (Estrin et al., 2013).

Firm growth is of interest to policymakers, as it can be a vehicle to reshape regions, create jobs and spur innovation (Shane, 2009). Public policy can be used to buffer new venture against resource scarcity, bridge new venture with necessary external stakeholders (Amezcuca et al., 2013) and/or boost organizational capacities for growth (Autio and Rannikko, 2016). Recent empirical research has set out to provide some implications for policies (for example, see Wright et al., 2015 for a review). Autio and Rannikko (2016) provide one of the most direct and robust tests. By examining Finnish high-technology new ventures, they find that 'policy initiatives that are selective, impose milestones and focus on capacity boosting are able to accelerate new firm growth' (Autio and Rannikko, 2016: 44).

## **HOW FIRMS GROW**

Whereas many have examined the determinants of growth, many fewer have opened the 'black box' of the growth process; that is, how the inputs are transferred to the outputs.

Growth is a continuous process resulting in changes within the firm (Penrose, 1959); thus, examining how a firm grows and the processual dynamics of growth are essential for our understanding of new-venture growth (cf. McKelvie and Wiklund, 2010).

To a large extent, early works in this vein built on stages of development or life-cycle metaphors (for example, Greiner, 1989; Kazanjian, 1988; Lewis and Churchill, 1983). That is, firms are viewed similar to living organisms that go through predictable stages of development. For example, Grenier (1972) argued that firms experience evolutionary (stability and growth) phases followed by revolutionary phases (disruptive changes) of development. These models have great intuitive appeal, but have been heavily criticized based on their lack of empirical validity (firms do not develop in accordance with these models) and because of their deterministic nature (for instance, Levie and Lichtenstein, 2010).

For example, avoiding determinism, McKelvie and Wiklund (2010) instead suggest that new ventures can choose to expand using various modes of growth. Firms choosing organic growth mainly create their own internal resources, while firms adopting acquisitive growth take over already existing resources from other firms. Collaborations, such as strategic alliances, constitute another option where firms co-utilize resources needed for growth.

While new ventures can be creative in developing resources (Baker and Nelson, 2005), they generally face resource constraints and lack internal capital to fuel their own growth in the way a larger firm might (Penrose, 1960; Baker and Nelson, 2005). This creates incentives to look externally for resources (Drover et al., 2017). However, the utilization of external resources often leaves new ventures in a difficult predicament because they have to balance the tradeoff between resources access and resource control. For example, in seeking external financing, founding teams often cede some level of control to their investors (Drover et al., 2014), and the greater the stake the in the firm, the more potential for conflicts on growth strategy (Khanin and Turel, 2015). Moreover, reliance on external resources can also deprive the firm of developing the necessary internal capabilities. For example, Nason et al. (2019) turned the spotlight on research and development (R&D). In their study, they found an inverted-U shape relationship between new-venture growth and leveraging R&D external to the new venture. However, this strategy eventually leads to power asymmetries with partners as the new venture's dependence on external R&D increases, which will then inhibit growth.

Through acquisitions, new ventures can expand their opportunity set. There are limits to how fast a firm can grow organically solely by generating its own resources internally, as predicted by Penrose's theory (Lockett et al., 2011). However, by relying on acquisitions, firms can expand their opportunity set (McKelvie and Wiklund, 2010). One recent example is Uber's acquisitions of firms specializing in artificial intelligence, which they have used to expand their driverless car capabilities.<sup>1</sup>

A key challenge to sustaining a high growth rate is the Penrose effect. Firms are limited by their ability to expand their managerial capacity to handle the expanding business, that is, access to competent managers is crucial to achieve growth. However, it takes time for individuals to acclimate to managerial responsibilities. Existing managers cannot endlessly expand their scope of responsibilities as the firm expands, and additional managers are needed to handle the expansion. However, regardless of a manager's previous experiences, he or she needs to gain an understanding of the idiosyncrasies of his or her new position. External hires need to be socialized into the firm. Employees newly promoted need to

learn new skills to be effective in their elevated role. As Penrose (1959: 46) states, a firm is not merely a collection of managers, but a collection of managers who have experience working together. The development of cohesion as a team takes time to unfold and, as it does, it places increased pressure on the experienced incumbent employees. The Penrose effect and the very elegant associated theoretical arguments were proposed in 1950s, but seem equally relevant today, although empirical examinations still remain sparse.

## THE CONSEQUENCES OF GROWTH

Growth can have both positive and negative consequences for the life of the entrepreneur, the employees and the firm itself. Running a highly successful new venture can be rewarding (Laguna and Razmus, 2019), but also highly stressful (Cardon and Patel, 2015) for the entrepreneur. Thus, the health and well-being of the entrepreneur is an important consequence of firm growth. Growth is not only a key mechanism to reduce the probability of firm failure, but also positively influences an entrepreneur's persistence (Stephan, 2018). Hence, growth can bring psychological well-being while failure is emotionally taxing for entrepreneurs (Shepherd et al., 2009). However, stress and burnout experienced by entrepreneurs may be particularly extensive during periods of rapid growth, especially when there are not enough experienced employees to share the responsibility (see Stephan, 2018 for a review), which will be inevitable during rapid growth (cf. the Penrose effect).

Growth is subject to the limits of managerial capacity, which takes time to develop internally (Penrose, 1959). Thus, one key outcome of growth is the limitations of firm growth in future periods (Lockett et al., 2011). As firm's increase their scope through the introduction of new products or expand into new markets, there are adjustment costs that must be absorbed by the firm, which have a negative impact on growth in future periods (Hutzschenreuter and Horstkotte, 2013).

Another key outcome of growth is the professionalization of the new venture (Flamholtz and Randle, 2012), which inevitably changes the firm's culture. As the firm evolves, the firm's founder(s) have little choice but to delegate tasks to their expanding leadership team (Mathias and Williams, 2018). Generally, founder(s) recruit to fill specific gaps in knowledge. While they try to fill the new roles with people that they think will be a good fit (Forbes et al. 2006), filling roles in this manner is challenging to maintain (Wry et al., 2011).

## RAPID GROWTH: A DOUBLE-EDGED SWORD

Mainly thanks to the observation that a small number of rapidly growing ventures contribute more to new job creation than the large number of more mundanely growing firms, policymakers (in particular) and scholars (to some extent) have become interested in understanding high-growth firms (HGFs). High-growth firms have been defined as firms that exhibit more than 20 percent annual growth over three consecutive years and have at least 10 employees at the start of the observation period (Eurostat-OECD, 2007). While HGFs constitute a small number of new ventures (Shepherd and Wiklund, 2009), they

have an outsize impact on the economy, leading some to suggest focusing more attention on HGFs instead of entrepreneurship in general (for example, Shane, 2009). These firms are largely responsible for the process of creative destruction as described by Schumpeter (1934), and many of them have completely redefined industries (for example, Uber for transportation, Square for point of sale and Airbnb for accommodation). As such, HGFs are of interest to scholars and policymakers alike (Coad et al., 2014).

To the firm and the entrepreneur, rapid growth may allow firms the ability to enter new markets quickly, capitalizing on their first mover advantage (Kuratko et al., 2020). High-growth firms may also be vehicles for rapid wealth creation. Countries with high levels of economic freedom (for example, property rights and low corruption) tend to produce a disproportionate number of billionaires who generate their wealth as entrepreneurs leading HGFs (Sanandaji and Leeson, 2013). High growth may also provide resources back to the entrepreneur's investors who can then reinvest into the next generation of new ventures. To workers, HGFs generate new job opportunities (Haltiwanger et al., 2013). As firms scale up, the quality of the jobs tends to improve to achieve parity with established firms (Burton et al., 2018). High-growth firms offer existing employees new career opportunities because expansion creates new positions (Bennett and Levinthal, 2017).

However, rapid expansion comes with challenges. Penrose's (1959) theory of firm growth highlights that growth has a tipping point where a firm faces managerial capacity constraints. Incumbent employees become overworked as new employees learn the internals of the firm. Developing and socializing new team members inevitably takes time and resources away from incumbent employees (Rutherford et al., 2003), and the effect is exacerbated when a majority of the firm's employees are new, as is the case when a firm's workforce doubles or triples in size in a single period. A key internal challenge for a firm facing managerial capacity constraints is the degradation of their company's culture (DeSantola and Gulati, 2017), often requiring the replacement of the founder and executive team (for example, Uber, WeWork).

While new venture survival rates increase with growth (Phillips and Kirchhoff, 1989), the effect diminishes when new ventures grow too quickly (Coad et al., 2020; Pe'er et al., 2016). Research also finds that HFGs are unlikely to sustain their extraordinary growth rate for very long (Daunfeldt and Halvarsson, 2015). Firms that grow too quickly without building the necessary capabilities have an increased likelihood of poor performance when entering markets. High-growth firms also tend to be dependent on external capital as they often run long-term losses for market expansion (Kenney and Zysman, 2019). If the firm fails to find a profitable avenue, investors may deescalate their commitment to the venture, ultimately letting it fail (Dimov and De Clercq, 2006).

## LOOKING FORWARD

Despite the progress within the new-venture growth literature, many questions have yet to be answered, leaving fertile ground for future research. First, as noted by many scholars (DeSantola and Gulati, 2017; Gilbert et al., 2006; Wiklund, 1998), the dynamics of growth are best studied longitudinally. Growth is function of time, and the effects of new-venture growth may also take time to unfold inside the firm. Thus, multi-year studies are necessary, with careful consideration for measurement, methods (Shepherd

and Wiklund, 2009) and growth mode (McKelvie and Wiklund, 2010). Second, given the problems scholars have in generating a set of independent variables that reliably predict growth across time and across samples, it may be appropriate to roll things back. A more fundamental issue is if there are factors that are necessary for growth to occur. That is, it could be fruitful to differentiate between necessary and sufficient (or other) conditions for growth, as a baseline. Are there things that firms must fulfill in order to grow, that they simply cannot be without? Researchers interested in this can readily adopt the new methodology termed necessary condition analysis (NCA; Dul, 2016), which has already been effectively used in examining nascent gestation activities (Arenius et al., 2017).

Third, as noted in previous research (for example, McKelvie and Wiklund, 2010), not all growth is the same. Scholars need to differentiate between, and clearly articulate, what mode of growth their research examines. The study by Lockett et al. (2011) provides a good example of the implications of studying growth mode, where they clearly demarcated organic and acquisitive growth, leading to new theoretical insights in how the growth mode influenced future growth. Next, growth can generate enormous amounts of wealth for entrepreneurs (Sanandaji and Leeson, 2013) and investors (Drover et al., 2017). The question remains as to whether new-venture growth is a key contributor to wealth inequality (for example, Carney and Nason, 2018) or if growth increases the standard of living for many stakeholders (for example, Packard and Bylund, 2018). Thus, who benefits from growth remains an open question. At a time when the concept of growth is being questioned for sustainability and other reasons, it seems that taking a wider view, and asking if and how new-venture growth influences various stakeholders, would be prudent. For example, future research could gauge the relationship between growth and environmental sustainability. Tension between commercial and socially orientated motives are inevitable (Moss et al., 2011; Stevens et al., 2015). A recent study by Parker et al. (2019) found challenges associated with retaining b-corp status and achieving firm growth simultaneously. Future studies should push this further, testing whether sales and employment growth have consequences for a firm's sustainability initiatives, and how these firms are perceived by their stakeholders (for example, employees and customers) if their actions become incongruent with the virtues they claim to uphold (Grimes et al., 2019).

Finally, whereas most previous research assumes that new-venture growth is a positive outcome, a more critical view also taking into account the dark side of growth, such as potentially negative effects on the entrepreneurial workforce and other stakeholders, can generate deeper insights. An example is Theranos, whose founder defrauded customers and investors, and bullied employees in a process of very aggressive growth. Although the company achieved extraordinary growth, it can hardly be considered positive. As the fraud was detected, investors lost millions of dollars and a number of employees lost their jobs. While the firm's culture will inevitably change during periods of rapid growth (cf. DeSantola and Gulati, 2017), the processes that trigger the toxicity leading to fraud and other bad behaviors remains underexplored.

## NOTE

1. [https://www.crunchbase.com/organization/uber/acquisitions/acquisitions\\_list](https://www.crunchbase.com/organization/uber/acquisitions/acquisitions_list), (accessed 28 February 2020).



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