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# ***Working for an entrepreneur: Heaven or Hell?***

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## **Abstract:**

Recruiting employees to an entrepreneurial venture is a challenging task. From the employee's perspective, accepting a position in an entrepreneurial venture potentially implies considerable uncertainty. This paper provide a literature review and identifies research gaps related to labor mobility of employees into and out of entrepreneurial firms. Who works for an entrepreneur? What are the conditions under which the employees of entrepreneurial firms work? Additionally, labor mobility after an employee works for an entrepreneurial firm is discussed. In conclusion the quality of the jobs generated by entrepreneurial firms may be questionable (and still relatively unexplored in empirical research), but they are nevertheless important from a labor dynamics perspective. Better understanding about motives to work for an entrepreneur, issues related to job security beyond survival rates, and job quality may contribute to ease the recruitment problems that many entrepreneurial firms struggle with. Furthermore, the relevance and potential pros and cons of working for an entrepreneurial firm in future career paths (entrepreneur or employee) needs to be carefully addressed in future research.

JEL codes: L26; J21; J62

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## 1. Introduction

*“You’re either one of those people who will change the world or you’re insane, and as a result you’ve decided you want to work for an entrepreneur.”*

Steimle, Josh (2013)

Entrepreneurial<sup>1</sup> firms, and specifically high growth firms, are found to be important for long-term employment growth (e.g., van Praag and Versloot, 2007; Block et al., 2018). From the perspective of the entrepreneur, recruiting employees to an expanding venture is a challenging task. Many entrepreneurs, particularly in the seed stage, experience difficulties recruiting personnel (see e.g., Aldrich and Ruef 2006; Behrends 2007; Williamson et al. 2002; Greer, et al. 2016). According to The Swedish Confederation of Employers (2016), approximately 1/4 of Swedish businesses perceive difficulties recruiting qualified employees as an obstacle to growth. Furthermore, recruitment problems for entrepreneurial firms may lead to skill mismatches, which may be detrimental to the venture when it is in its initial vulnerable stage.

From an employee’s perspective, according to previous research, working for an entrepreneur potentially implies great uncertainty, low wages and benefits, and a high probability that the firm will not survive. Hence, it is often argued that entrepreneurial ventures offer low quality jobs (see e.g., Shane 2009; Parker 2004; Coad et al. 2017; Block et al. 2018). Hence, many employees would probably think carefully before leaving an existing job to work for an entrepreneur.

Entrepreneurship research has largely focused on the decision to become an entrepreneur and on the entrepreneurial decision-making process; such research has produced knowledge about when, where and by whom entrepreneurial opportunities are discovered, evaluated and exploited (see e.g., Shane and Venkataraman 2000). Less attention has been paid to the decision processes of employees who decide to become employed by an entrepreneurial venture

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<sup>1</sup> Entrepreneurship is a multidimensional concept that is not unanimously defined in the literature. The operationalization of entrepreneurship differs across the studies reviewed in this paper. However, in this paper the term entrepreneurial firms/ventures is used, which usually refers to firms that are newly created and less than 5 years old (Block et al. 2018).

(Nyström 2018; Adrjan 2018). Hence, our knowledge about the process of recruiting employees to entrepreneurial ventures remains limited (Greer, et al. 2016). Recent research has stressed the potential for future entrepreneurship research focusing on entrepreneurship as a career choice (Burton et al. 2016). By also focusing on the labor market transitions before and after working for an entrepreneur, this paper contributes to developing a career perspective on the choice to work for an entrepreneur. Furthermore, there is a lack of research regarding the quality of jobs generated by entrepreneurial firms (Block, et al. 2018; Kim 2018) and a better understanding of the nature and quality of the jobs generated by entrepreneurial firms should be of great interest to policy-makers who aim to stimulate job creation by promoting entrepreneurship.

This paper provides a literature review, identifies some research gaps, and discusses avenues for further research regarding our knowledge of employment in entrepreneurial ventures. The review covers three perspectives related to the labor market mobility to and from entrepreneurial firms: who works for an entrepreneurial venture (section 2), working for an entrepreneur (i.e., the conditions at an entrepreneurial firm) (section 3) and labor mobility after working for an entrepreneur (section 4). The discussion of who works for an entrepreneurial venture includes a discussion of the matching process; that is, the process of finding the right employees from both the employer and employee perspectives as well as a discussion of who decides to work for a new firm. The section on the working conditions at an entrepreneurial firm includes a discussion of the quality of the jobs created by entrepreneurial firms such as wages, job security and job satisfaction. Finally, the section on labor mobility after working for an entrepreneur includes a discussion of subsequent career paths, such as deciding to become an entrepreneur or employment with other firms.

## **2. Who works for an entrepreneurial venture?**

### **2.1 Finding the perfect match—recruitment for entrepreneurial ventures**

Before any hiring decision can be made,<sup>2</sup> a matching process must occur; both the employee and employer must feel that the outcome is satisfactory for both pecuniary and nonpecuniary returns associated with the employment. A hiring decision by the employer as well as the decision to accept a job offer includes the problem of asymmetric information between the employer and the employee. The employer does not have full information about the skills and abilities of the employee and the employee does not know the skills and abilities of the entrepreneur and the prevalent working conditions at his or her future workplace. In disentangling this matching process including asymmetric information, we need to consider the perspectives of both the employer and the employee.

#### ***Finding the perfect match—the employer perspective***

During the recruitment process, entrepreneurial ventures are potentially at a disadvantage because they cannot rely on their name, reputation or market share to attract employees (Aldrich 1999). Firms with a strong reputation attract more applicants, and with a higher quantity of applicants, the probability of a better match increases and the firm can select higher-quality employees (Turban & Cable, 2003). In addition, career advancement prospects may be limited at entrepreneurial firms due to, for example, the high mortality rate of such firms in their early stages. In addition, many entrepreneurial firms are unable to provide additional benefits, such as social benefits or training, which makes them less attractive to applicants (Tumasjan et al. 2011). Finally, many entrepreneurial firms lack well-defined job descriptions, which may make them seem less legitimate to potential employees (Williamson 2000).

An important aspect of the matching process between the employer and potential employees is the fact that the recruitment processes of entrepreneurial firms tend to differ from the processes of large and well-established firms. First, many entrepreneurial firms face financial constraints in their early stages of development (see, e.g., Parker, 2009), which have implications both on the wages they can pay and the amount they can spend on recruitment processes. Furthermore, they often lack the institutional resources necessary for formal recruitment processes such as

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<sup>2</sup> It should be acknowledged that many entrepreneurial ventures do not want to hire any employees or grow at all. Naturally, the likelihood of recruiting a first employee increases if the start-up is opportunity-based (Coad et al. 2017). For the remainder of the paper, entrepreneurial firms with growth ambitions are assumed.

specialized knowledge in HR. Regarding the recruitment processes of entrepreneurial firms, it should be noted that there is a lack of literature specifically focusing on entrepreneurial ventures (Greer et al. 2016). Most of the previous research focuses on small firms versus large firms. For small firms, it is argued that adopting informal recruitment practices based on social networks are common (Aldrich 1999; Barber et al. 1999; Aldrich & Ruef 2006; and Barrett & Mayson 2008). It is also often argued that “soft” qualifications such as the potential employee’s personality are more important to small firms, while “hard” qualifications such as academic credentials and work experience are more important to large firms (see e.g., Barber et al. 1999; Bartram et al. 1995; Pritchard & Fidler 1993; Cardon & Stevens 2004).

Similar to the recruitment process in small firms, recruitment based on social networks is one way for an entrepreneur to reduce the problem with information asymmetry in the recruitment process. Regarding the “soft” qualifications that entrepreneurs seek among their new employees, Kristof-Brown et al. (2005) claim that entrepreneurs are interested in recruiting entrepreneurial-minded employees because such individuals are well suited to the employment offerings of a new venture. However, it should be noted that recruitment practices change over the developmental stages of an entrepreneurial firm. Leung et al. (2006) find that during the transition from the start-up phase to the growth phase, entrepreneurial firms shift their recruitment efforts from personal social networks to business networks to achieve diversity and different competencies among employees.

### ***Finding the perfect match—the employee perspective***

For a potential employee to accept a job at an entrepreneurial venture, there must be a satisfactory match of many dimensions. To an individual, a job may have a variety of meanings and values (Kalleberg, 1977) and these work values and characteristics help to explain occupational choices and job satisfaction. In Kalleberg’s framework (1977), work characteristics can be both intrinsic and extrinsic. The intrinsic dimension refers to the work task, i.e., if the work task is interesting, it allows for development and the worker can see the results of his or her work. Extrinsic work characteristics refer to the financial dimension (e.g., wages and fringe benefits), the convenience dimension (e.g., convenient travel to work and physical surroundings), relationships and coworkers (e.g., friendly and helpful coworkers that take an interest in you), career (e.g., chances of promotion and promotions that are handled fairly), and resource adequacy (e.g., the employee has adequate resources to perform the job).

Which job characteristics do potential employees consider important when choosing among potential employers according to empirical research? Terjesen et al. (2007) find that undergraduates perceive organizational attributes such as investment in training and development, opportunities for long-term career progression, and a dynamic and forward-looking approach as more important than a high starting salary. Similar attributes are considered attractive by Swedish students entering the labor market. A creative, dynamic and friendly work environment as well as challenging work tasks and managers who support employees' future development are important attributes of a future workplace. These attributes are considered more important than a competitive basic salary (Universum 2014). However, it should be acknowledged that in the case of employment with newly established firms, it may be particularly difficult to predict long-term opportunities due to their low survival chances. However, if the newly created firm does survive, there may be good opportunities for long-term learning as well as the possibility of earning a higher income in the future. Hence, employment with a new firm may provide an opportunity for great future achievement and high income, although such employment comes with high risk.

Given the vast interest in entrepreneurs as innovators and job creators, surprisingly little research has been done regarding the extent that entrepreneurial firms differ from incumbent firms with respect to the characteristics of human capital and, in particular, the employees' motives to join the venture (Cohen & Sauermann, 2007). In a study of U.S. R&D employees, Sauermann (2017) finds that employees who join entrepreneurial firms place less importance on salary and job security and more importance on independence and responsibility compared to employees in established firms. These differences in motives among employees partly help to explain the higher innovative performance in entrepreneurial firms. Focusing on recruitment for entrepreneurial firms, based on a study of German students and recent graduates, Tumasjan et al. (2011) find that the attributes of team climate, responsibility and empowerment, and flexibility of the working schedule are the top three attributes for prospective applicants for jobs in new firms.

The attractiveness of working for a new firm naturally depends on the available alternatives. When accepting a job with an entrepreneur, one may either be outside the labor market (for example, unemployed or a recent graduate) or already employed but considering a change to a new job. In the latter case, the job change may be voluntary or involuntary. A voluntary job change may, for instance, be made to pursue new opportunities. The change may provide

pecuniary benefits, for example, higher wages. However, it should be stressed that nonpecuniary benefits are also important drivers of voluntary job changes. For example, changes in household composition may stimulate employees to change to a more family-friendly employer with, for example, a more flexible work environment (Kronenberg & Carree 2012). Other important nonpecuniary reasons for changing jobs are job satisfaction and job security (Carless & Arnup 2011; Clark 2001). Involuntary job changes occur due to layoffs or firm closures. It should be noted that being at a higher risk of a layoff is not random. Workers with low unobservable human capital tend to place themselves in smaller or more unstable firms (Winter-Ebmer 2001; Winter-Ebmer 1995), which has implications for who decides to accept employment with an entrepreneurial firm and the amount they get paid (more on this issue in section 3).

## **2.2 Who works for an entrepreneur? Empirical evidence**

Given the difficulties of attracting employees to entrepreneurial firms, it is often assumed that individuals who are willing to take the risk of accepting employment with an entrepreneurial firm lack other alternatives or are in some way marginalized in the labor market; for example, they may be unemployed or have difficulties holding a steady job (Bhide 2000). Lately, individual-level employer-employee matched datasets covering large populations have become available in several countries. This makes it possible to study the individual characteristics associated with employment in entrepreneurial firms in a more detailed and systematic way. Nyström (2011) uses employer-employee matched data from Sweden and finds that the share of recently graduated employees, immigrants and people entering the labor market is higher in entrepreneurial firms. Hence, entrepreneurial firms might play a more important role for individuals with a weaker position in the labor market. Additionally, using employer-employee matched data from Sweden but focusing on people who change jobs, Nyström and Zhetibaeva Elvung (2015) support the hypothesis that the selection of individuals into entrepreneurial firms is not random. Immigrants and individuals who make an involuntary job change (defined as induced by a firm closure) are more likely to become employed in entrepreneurial firms, while individuals with secondary or tertiary education are less likely to be employed by an entrepreneurial firm (Nyström & Zhetibaeva Elvung 2015). Using Danish employer-employee matched data, Coad et al. (2017) find that people who are hired by entrepreneurial ventures are more likely to be less educated, previously unemployed or employed with a lower income before they are hired by a solo entrepreneur. Ouimet and

Zarutskie (2014) provide evidence that entrepreneurial firms disproportionately hire young employees. Hence, in conclusion, there is convincing evidence that the selection of employees into entrepreneurial firms in the labor market is not random; these firms have a tendency to employ those whose individual characteristics are often associated with a weaker position in the labor market.

What are the motivations for joining an entrepreneurial venture? This is a research area that clearly requires further exploration. As previously mentioned, entrepreneurs may be interested in recruiting entrepreneurial-minded employees. Moser et al. (2017) explore which dimensions of new ventures entrepreneurial-minded individuals find attractive. Following De Jong et al. (2015), they measure entrepreneurial-minded employees by their innovativeness as well as their proactive and risk-taking behavior. Their empirical findings show that for entrepreneurial-minded employees measured by innovativeness, ideological attributes (e.g., the strategic vision of the new venture) and founder legitimacy are important for firm attractiveness. Transactional attributes (such as remuneration) are less important. However, the authors found no relationship between the other two measurements of entrepreneurial behavior (proactive and risk-taking behavior) and employer attractiveness.

### **3. Working conditions at an entrepreneurial firm**

#### **3.1 Job security and labor turnover**

An important aspect to consider when accepting a job in an entrepreneurial firm is the firm's chances of survival. It is well known from empirical research that the survival rate of new firms is low. According to the facts presented in a review of the literature, Geroski (1995) concludes that approximately 60% of firms exit within five years and nearly 80% exit within ten years. According to the OECD (2017), nearly one-half of newly created firms do not survive their first three years, and survival rates are, on average, lower among employer firms than nonemployer firms. Hence, there is a great risk that an employee of an entrepreneurial firm will be searching for new employment after a very short time. Based on German data, Schnabel et al. (2011) conclude that established firms offer higher job stability than entrepreneurial firms. What type of contracts do entrepreneurial firms offer? De Matos and Parent (2016) find that entrepreneurial firms in Portugal to a greater extent offer fixed-term contracts and less job security.

The previous section discussed the recruitment and matching problems associated with employment in new firms. The perceived mismatch may be on both the employer and employee sides. If the consequence of these matching problems is lower quality in matching, we can expect labor turnover to be higher in new firms compared to incumbent firms. Additionally, it can be hypothesized that the skill mismatch of employees in entrepreneurial ventures contributes to those ventures' lower survival rates. Hence, in future research, it would be interesting to study whether employee turnover is higher in entrepreneurial firms than established firms; it would also be interesting to examine employee turnover in firms that do survive, i.e., whether the termination of the work contract originates from a mismatch and to what extent skill mismatches influence the performance of entrepreneurial ventures.

### **3.2 Wages and pecuniary returns**

In a well-cited paper, Shane (2009) argues that jobs created by entrepreneurial firms are worse than jobs in incumbent companies in terms of, for example, pay and fringe benefits. Shane (2009) refers to a review paper by Wagner (1997), who reviews empirical studies of job quality and firm size and does not specifically focus on firm age. In fact, it has primarily been the firm size-wage relationship and not the firm age-wage relationship that has been the focus of most of the early research in this field. In his literature review, Wagner (1997) concludes that in small firms, wages are lower, fringe benefits are lower, job security is lower and opportunities for skill enhancement are worse than in large firms. The hypothesis that smaller firms pay lower wages is confirmed by Troske (1999), Bayard and Troske (1999) and Waddoups (2007). In these studies, the link between firm size and wages is studied empirically, controlling for a number of individual characteristics (for example, age, educational attainment, and tenure), firm characteristics (for example, industry and occupation), and labor market conditions (for example, industry and region). However, the observable characteristics do not fully account for the wage premium paid by larger firms (see e.g., Brown and Medoff 1989; Troske 1999; Millimet, 2005).

What are the potential explanations for why large employers pay higher wages? According to Troske (1999), large employers hire better workers because both large employers and their employees are more likely to invest in firm-specific human capital. Furthermore, Gerlach and Hübler (1998) find that larger firms attract more qualified workers. Hence, the composition of employment regarding the quality of workers differs across large and small firms. Individuals

with greater abilities and skills tend to disproportionately select employment in larger and, on average, older firms; this selection contributes to explaining wage differentials between large and small firms.

Contributing to this discussion, Brown and Medoff (1989) note that because younger firms tend to be smaller, it is relevant to ask whether small firms are also entrepreneurial firms and to what extent the wage premium of larger firms is, in fact, a relationship between firm age and wages. Hence, investigating the firm age-wage relationship, a frequently cited study by Brixy et al. (2007) found a wage penalty of 8 percent for employment in entrepreneurial firms. Brown and Medoff (2003) find that the relationship between firm age and wages is not monotonic because wages fall and then rise with years in business. Heyman (2007) uses a matched employer-employee dataset from Sweden. The results indicate that the inclusion of firm age does not affect the impact of firm size on wages. In summary, a firm's age does not fully account for wage differentials across individuals and firms.

As we have seen in the previous section, the selection of employees to entrepreneurial firms is not random, and this finding should have implications for wage levels. Several recent studies have tried to address this nonrandom selection of employees into entrepreneurial firms. Focusing on labor market entrants, Nyström and Zhetibaeva Elvung (2014) study whether there is a wage penalty for employment in entrepreneurial firms. Using employer-employee matched data from Sweden and propensity score matching to address that selection of employees into entrepreneurial firms is not random, they find that a wage penalty for employment in entrepreneurial firms does exist and the penalty is, on average, 2.9 percent. Using Danish data, Burton et al. (2018) find, contrary to previous research, that after controlling for individual characteristics, younger firms pay more. A recent paper by Adrjan (2018) using an employer-employee matched dataset from Great Britain also finds that young firms pay a small (1-2 percent) wage premium to new hires. For the group of employees at venture-capital-backed startups, Kim (2018) found that these employees earn 10 percent higher wages than their counterparts in established firms, but that this wage gap disappears if individual fixed effects are considered.

It should be emphasized that there is substantial heterogeneity among entrepreneurial firms regarding the wages they pay. Some entrepreneurial firms that survive and become highly productive firms pay higher wages compared to similar employment by firms that

subsequently have low productivity or do not survive (Adrjan 2018). Looking more closely at employees who change jobs, Nyström and Zhetibaeva Elvung (2015) find that individuals who change to a job in an entrepreneurial firm are more likely to lower their wages; 40 percent of employees who change to a job in an entrepreneurial firm lower their wages, while the corresponding figure for those who change to a job in an incumbent firm is 31 percent. Furthermore, Dorner et al. (2017) study academic spin-offs and find that these firms in general do not pay any wage premium, but a spin-off that commercializes new scientific results or methods pays a wage premium for their employees with a university background. In conclusion, these more recent studies on the wage gap between incumbent and entrepreneurial firms show that addressing individual heterogeneity and selection into entrepreneurial firms seems to generate lower wage penalties or even wage premiums. In fact, also supported by the recent literature review by Block et al. (2018), the previous conventional wisdom that entrepreneurial firms pay less must be reconsidered. A plausible explanation for these new findings is that the more recent empirical work has used detailed matched employer-employee data and have been able to control for selection and heterogeneity across individuals and firms to a larger extent.

What about the long-term wage development of employees working in entrepreneurial firms? If an employee expects an entrepreneurial firm to provide a career path and/or less financial constraints as the firm matures, the employee may tolerate a lower wage during the first years and hopefully enjoy a steeper earnings trajectory later. There is very little research to date on this matter. Two exceptions are very recent papers by Adrjan (2018) and Sorenson et al. (2018). Using matched employer-employee data from Great Britain, Adrjan (2018) investigates the lifecycle earnings of employees in young firms and finds that subsequent wage growth is better at mature firms. This finding is valid for individuals who remain in their jobs and when they change jobs. Using Danish registry data, Sorenson et al. (2018) find that employees who join small (i.e., among the first 50 employees) and entrepreneurial firms (i.e., less than 4 years old) on average earn 25 percent less over the subsequent ten-year period compared to employees in large firms that had been operating more than four years. However, approximately half of the wage differential stemmed from the sorting of younger and less qualified employees into employment in entrepreneurial firms. Nevertheless, a wage penalty of approximately 10-15 percent remained over the subsequent decade and there was no evidence of earnings disparities improving over time; rather, earnings disparities between incumbent and entrepreneurial firms grew over time. According to Sorenson et al. (2018), these patterns emerge from two factors: liability of newness, suggesting that since entrepreneurial firms have a higher probability of

exit this creates spells of unemployment that are costly for their former employees, and path dependence in career moves, which suggests that once an employee joins an entrepreneurial firm he or she moves to other entrepreneurial firms that also pay less.

### **3.3 Work hours, job satisfaction and stress**

As mentioned above, most previous empirical research that may be relevant to the discussion of the working conditions in entrepreneurial firms is primarily based on small businesses or is focused on the entrepreneurs themselves. Regarding entrepreneurs, empirical research shows that male entrepreneurs work longer hours on average, and in particular, the entrepreneurs who are employers work longer hours. On the other hand, entrepreneurs tend to benefit from higher job satisfaction (see the literature review in Parker, 2009). It is also interesting to note that recent empirical evidence matching prescription records with entrepreneurial data shows that entrepreneurship is associated with increased stress for both entrepreneurs and their spouses. However, entrepreneurs are less likely to use antidepressants (Dahl, et al. 2010).

For small firms, rather than explicitly focusing on entrepreneurial firms, there is a somewhat inconclusive empirical finding based on UK and U.S. studies in which Atkinson and Storey (1994) argue that there is weak evidence of higher job satisfaction of employees in small firms, while Rowden (2004) refers to studies in the U.S. showing that employees in small businesses report higher job satisfaction. What are the working conditions that influence job satisfaction in small firms? Davis (2004) discuss some advantages and disadvantages related to job satisfaction based on previous research. A disadvantage is that when organizational problems occur in small firms, they are less likely to be approached scientifically and in a timely manner. However, working for a small firm comes with frequent interpersonal contact with other employees, customers and managers and often involves a high degree of complexity and challenge, which may be rewarding if an employee prefers these types of job characteristics. Finally, according to Parker (2004), employees in small firms receive lower levels of training, work longer hours and face a greater risk of major injury at work.

However, to the best of my knowledge, it is not known whether these poor working conditions for entrepreneurs or employees in small firms pertain to workers in entrepreneurial firms. The lack of knowledge regarding these issues related to the quality of the jobs created by entrepreneurs is further illustrated by the absence of such studies in the recent literature review

by Block et al. (2018), which does not include any studies of stress or work hours.<sup>3</sup> What could be expected in terms of working conditions? If work tasks are not clearly defined in entrepreneurial firms, it is reasonable to expect that work hours would be longer for the employees of those firms (given that the employee are on a contract that allows paid or unpaid overtime). Financial constraints and a potential lack of priority for employee training in the initial stages are plausible reasons we should expect lower levels of training in entrepreneurial firms. However, it should be noted that the need for training may be less prevalent in entrepreneurial firms since knowledge and skills necessary for performing the work tasks are unlikely to become obsolete in the short-term (such as the lifetime of an entrepreneurial firm). Regarding stress, it is possible that the employees are also affected by the insecurity that many firms face in their initial stages; however, perhaps the challenging tasks result in greater job satisfaction. These are important and interesting questions for future research to explore.

#### **4. Subsequent to working for an entrepreneurial firm**

##### **4.1. Career choices including entrepreneurship**

In the entrepreneurship literature, it has been suggested that employees of small firms are more likely to become entrepreneurs themselves (Hyttinen & Maliranta 2008). This proposal is known as the “small firm effect”. What explains this small firm effect? Elfenbein et al. (2010) argue that employment in small firms has several features similar to those of being an entrepreneur. Hence, individuals who like working conditions that offer independence and less bureaucracy tend to select employment in small firms. Furthermore, employees who are less risk-averse select employment in small firms. In addition, the lower wages of small firms imply that employees are more likely to transition to entrepreneurship to increase their income. Finally, employment in small firms helps employees develop knowledge and skills relevant to entrepreneurship because they are required to perform many different tasks within the small firm. This entrepreneurial learning may stimulate an individual to become an entrepreneur. Similar arguments are also valid for employees in new firms, i.e., arguments related to the nonrandom selection, learning and opportunity identification that occur after an employee

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<sup>3</sup> In their section on work content and types, Block et al. (2018) refer to two studies that primarily concern the skill levels of the jobs created and to what extent the jobs in entrepreneurial firms contribute to the growth in average wages.

works for an entrepreneurial firm. However, related to the discussion of self-selection of individuals with a preference for entrepreneurial work values into entrepreneurial firms, it can be argued that if there is a good fit between entrepreneurial work values and characteristics, these individuals may receive sufficient job satisfaction in this dimension at their current job and do not need to become entrepreneurs themselves. Based on this argument, it can be argued that the “new firm effect” should primarily be driven by the learning effect and result in opportunity-based entrepreneurship. The selection effect would then be valid to explain the situation in which a higher share of employees begin their own venture after their previous employer closes. To what extent the “new firm effect” empirically exists is less investigated (compared to the small firm effect) in the literature; exceptions are Wagner (2004), Sørensen (2007) and Zhetibaeva Elvung (2016a).

Based on German microdata, Wagner (2004) finds that work experience in both small and young firms increases the probability that an employee will subsequently become an entrepreneur. Using employee-employer data covering the whole Danish population, Sørensen (2007) shows that employees in less bureaucratic firms, as measured by size and age, have a higher probability of becoming entrepreneurs. Sørensen (2007) argues that this effect is not due to these firms attracting a more entrepreneurial type of individual, but rather that the work environment itself creates entrepreneurs, hence supporting the learning effect. Another interesting finding is that the probability of becoming an entrepreneur increases if the employee joined the employer during the formative years of the business (i.e., when it was less than three years old). Using Swedish individual-level matched employee-employer data, Zhetibaeva Elvung (2016a) finds that employees of entrepreneurial firms are more likely to transition to entrepreneurship, which supports the “new firm effect”. In particular, individuals with the lowest and highest levels of ability are more likely to enter entrepreneurship. Interestingly, in a recent meta-analysis of the literature on individual and firm characteristics related to entrepreneurial spawning, Garrett et al. (2017) do not find support for the small firm effect, while the hypothesis that firm age is negatively related to entrepreneurial spawning is supported.

Under which circumstances do former employees decide to become entrepreneurs? Here, the spin-out literature may offer some guidance. For instance, employees who experience frustration with parental inertia or perceive the existence of underexploited opportunities are more likely to transfer to spin-outs (Agarwal et al. 2004; Klepper & Thompson, 2010).

However, it should be noted that this literature does not explicitly discuss the extent to which the age of the parent firm influences the probability of becoming an entrepreneur. Another reason why employees at new ventures may become entrepreneurs is that they have gained entrepreneurial knowledge and inspiration from their former coworkers. Nanda and Sørensen (2010) find that individuals are more likely to become entrepreneurs if their former coworkers have previously been entrepreneurs. Furthermore, Nanda and Sørensen (2010) find that peer influences are substitutes for other sources of entrepreneurial influence because the effects of peer influences on entrepreneurship are strongest for individuals with less exposure to entrepreneurship in other aspects of their lives.

Sorgner and Fritsch (2018) study the extent to which an occupation-specific environment influences the choice to become an entrepreneur. Based on German microlevel data, they find that future entrepreneurs opt for different types of occupations when they enter the labor market as paid employees. In addition, when future entrepreneurs enter the labor market, they are more likely to choose occupations that require a relatively high variety of skills. Furthermore, Sorgner and Fritsch (2018) find that people working in occupations characterized by relatively high unemployment risks, high earnings risks, and high self-employment rates have a high probability of moving into self-employment. Sørensen and Sharkey (2014) study how organizational opportunity structures influence the transition to entrepreneurship, i.e., how the shape of the hierarchy in an organization affects the decision to become an entrepreneur. Based on Danish microlevel data, they find that employees who work in organizations with lower wage ceilings and greater internal wage inequality are more likely to transition to entrepreneurship.

In transitioning to entrepreneurship from the public sector, Özcan and Reichstein (2009) argue for both context and tenure effects. The context effect assumes that employees who are dissatisfied with the intrinsic job characteristics and bureaucracy in the public sector are more likely to leave employment in the public sector in favor of an entrepreneurial career. The tenure effect implies that if an employee stays for some time with an organization, the organization shapes the individual's ability to pursue entrepreneurial activities. Individuals adopt and develop attitudes consistent with the organization's expectations and role. Applying this framework to employees working for an entrepreneurial firm implies that these employees over time would adapt to the entrepreneurial organizational culture and hence may increase their probability of becoming entrepreneurs. The available literature discussed in this section partly

addresses the reasons and motives for former employees to become entrepreneurs. However, an avenue for further research would be to attempt to further disentangle the interplay between selection and learning mechanisms behind the “new firm effect”, in particular in a context that considers if the ventures created are opportunity- or necessity-based.

This section has addressed a transition to entrepreneurship after an employee has worked for an entrepreneur. Less is known about alternative career paths for former employees of entrepreneurial firms. In the labor market, part-time jobs, temporary contracts and low-wage jobs are discussed as potential “stepping stones” toward “better” jobs in terms of wages or permanence (Sicherman & Galor, 1990). Given that entrepreneurial firms hire individuals who have weaker positions in the labor market, can employment in a new firm act as a stepping stone toward permanent employment? According to Zhetibaeva Elvung (2016b), this may be the case for individuals with nonemployment status prior to their employment in new firms. Additionally, the stepping stone effect is more pronounced for younger individuals.

#### **4.2 Performance in subsequent career choices**

When a former employee launches a venture, does the prior experience of working for an entrepreneur have implications for the performance of the venture that he or she creates? Again, the spin-out literature provides us some insights. Previous research on spin-outs argues that a parent of high quality in terms of, for example, larger stocks of capabilities, spawns more and better spinoffs than a low-quality parent (e.g., Agarwal et al., 2004; Klepper & Sleeper, 2005). However, the role of the parent in relation to the performance of the spin-out is challenged by Hunt and Lerner (2012), who find spin-off performance to be more heterogeneous; they find that founder-specific experience rather than parental lineage is the primary driver of spin-off performance heterogeneity. Again, it should be noted that these papers do not distinguish between experience working at an entrepreneurial firm or an experienced firm; instead, their empirical analysis may include the number of years of working experience and the diversity of occupational experience. On this topic, Åstebro and Yong (2016) find that entrepreneurs with experience working in many different occupations within the same industry have the best chance of being successful as entrepreneurs. Hence, there is more research to be done focusing on whether employees’ entrepreneurial learning at entrepreneurial firms has implications for the performance of their subsequent start-ups.

What about the performance in career paths other than entrepreneurship for previous employees of entrepreneurial firms? Unfortunately, questions related to the future career paths of employees in entrepreneurial firm remain relatively unexplored. For individuals who decide to exit entrepreneurship, it has recently been shown that there are positive rewards from entrepreneurship in subsequent paid employment (Luzzi & Sasson 2016; Lougui, & Broström, 2018). The positive reward for entrepreneurship experience is shown in particular for entrepreneurs hired in highly innovative sectors (Luzzi & Sasson 2016) and jobs requiring general and managerial skills rather than industry specific expertise (Lougui, & Broström, 2018). In this literature, is argued that entrepreneurs are multiskilled “jacks-of-all-trades” (Lazear, 2004) either by selection or by acquiring these skills through learning during their entrepreneurial experience. As discussed above, similar arguments can be proposed to individuals who decide to accept employment at an entrepreneurial firm. Interesting research questions to explore would be to study the earnings of former employees in subsequent employment using a methodology similar to Luzzi and Sassi (2016). In addition, it would be interesting to explore if former employees of entrepreneurial firms, for instance, take on managerial or innovative positions in other firms to a greater extent. What do their career paths look like if they decide to remain in the entrepreneurial venture (assuming that the firm survives)?

## **5. Conclusions and summary of identified research gaps**

The primary focus in the field of entrepreneurship research is the entrepreneur and the entrepreneurial process. However, the research field has now come to expand to also take interest in the individuals who work for the entrepreneur. These individuals and their working conditions are in focus in this paper. Based on the empirical evidence summarized in the paper, it is impossible to answer the question of whether working for an entrepreneur is heaven or hell. Nevertheless, advantages and disadvantages associated with working for an entrepreneur are discussed and some important research gaps identified. Three perspectives are covered: the individuals who work for an entrepreneurial venture (i.e., the labor mobility to entrepreneurial firms), the conditions of working for an entrepreneur, and career paths after working for an entrepreneur.

The empirical evidence show that entrepreneurial firms tend to hire employees with weaker positions in the labor market. Hence, it can be argued that the employees' motives may be necessity-driven in many cases. However, employees' motives to begin working for an entrepreneur constitute a research area that needs to be further explored. Furthermore, successful recruitment strategies for entrepreneurial ventures a promising avenue for future research. If entrepreneurs can adopt successful recruitment practices, their potential to create jobs is enhanced since many firms perceive difficulties in recruitment as an obstacle to growth.

Regarding the working conditions at entrepreneurial ventures, the literature review show that there is considerable research on the pecuniary aspects of working for an entrepreneur. However, in contrast to what has been argued previously, if focusing on entrepreneurial firms (and not small firms) and addressing the selection problem associated with employment in entrepreneurial firms as well as using comprehensive employer-employee matched data, recent research shows that the wage penalty for working in an entrepreneurial firm seems to be quite small or may be positive. Hence, the previous conventional wisdom of a wage penalty associated with employment in entrepreneurial firms may need to be reconsidered. Nevertheless, there is a clear scarcity of research regarding the long-term wage trajectories of employees in entrepreneurial firms. The current empirical evidence available regarding lifecycle earnings suggests better wage development at mature firms over entrepreneurial firms.

In addition to more comprehensive empirical research, we need a better understanding about which mechanisms may drive these results.

It is a well-known fact that employees face a high probability of needing to search for new employment again soon, as the survival rates of entrepreneurial firms are low. However, issues related to job security beyond survival rates are less explored in the literature. Are the employees of entrepreneurial firms more exposed to labor turnover due to skill-mismatch or as the needs of the firm change over its development stages? Furthermore, the dimensions of job quality of working for an entrepreneur that remain largely unexplored are issues related to work hours, job satisfaction and stress. If poor working conditions are the reasons for the perceived recruitment problems of entrepreneurial firms, this may be an important issue for policymakers to address and may have the potential to enhance the job creation power of entrepreneurial firms.

What is the subsequent value of working for an entrepreneur? Empirical evidence supports the new firm effect, suggesting that employees of entrepreneurial firms are more likely to become entrepreneurs. However, less is known about how former employees of entrepreneurial firms perform as entrepreneurs. Even less is known about the value of previously working for an entrepreneur if the employee changes to a job in another part of the labor market. Entrepreneurship research has lately come to move beyond focusing on the period of entrepreneurial activity and take interest into the relevance of entrepreneurial experience in future career paths. This literature is still emerging and widening the perspective to also include the employees of entrepreneurial firms has potential to provide important insights. This may include questions related to how the experience of working for an entrepreneurial firm influence firms future earnings, innovativeness and positions.

As a final note, it is important from a policy perspective to acknowledge that although the quality of the jobs generated by entrepreneurial firms may be questionable, these firms are important from a labor dynamics perspective. By being an important entry point for, in particular, employees with a weaker position in the labor market and a stepping stone toward more stable employment, these jobs play an important role in a dynamic labor market.



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