ENTREPRENEURSHIP AND INNOVATION

COMMENTS BY THORSTEN BECK

CASS
BUSINESS SCHOOL
CITY, UNIVERSITY OF LONDON
EST 1894

TWO EXCELLENT PAPERS

- Albert/Caggese: Cyclical Fluctuations, Financial Shocks, and the Entry of Fast-Growing Entrepreneurial Startups
- Gupta/Hacamo: Early Career Choices of Superstar Entrepreneurs

- Short summary
- Some comments
- Putting papers into broader picture

ALBERT/CAGGESE

- Negative growth and financial sector shocks reduce entrepreneurship and more so for high-growth enterprises – composition of entry channel
- Combines theory and empirics, with a good link between both
- Adds more evidence on the importance of alleviating financing constraints for entrepreneurship, especially for high-growth enterprises

ALBERT/CAGGESE – SOME COMMENTS

- Theory – why are Type 2 enterprises not riskier (higher default probability)
- Gap between low and high entrepreneurs can also be explained by an alternative story – recession/crisis results in unemployment and higher self-employment (of the low-growth type).
- GDP growth as proxy for collateral constraints – can we do better than that?
- Paper focuses on financial distress – alternative approach: financial structure (availability of venture capital, market finance etc.)
- Econometric quibble: as variable of interest is on country-year level, shouldn't standard errors be clustered accordingly (Table 3)
- Implications for job market – interesting, but not general equilibrium, so this is again a composition effect rather than aggregate job loss

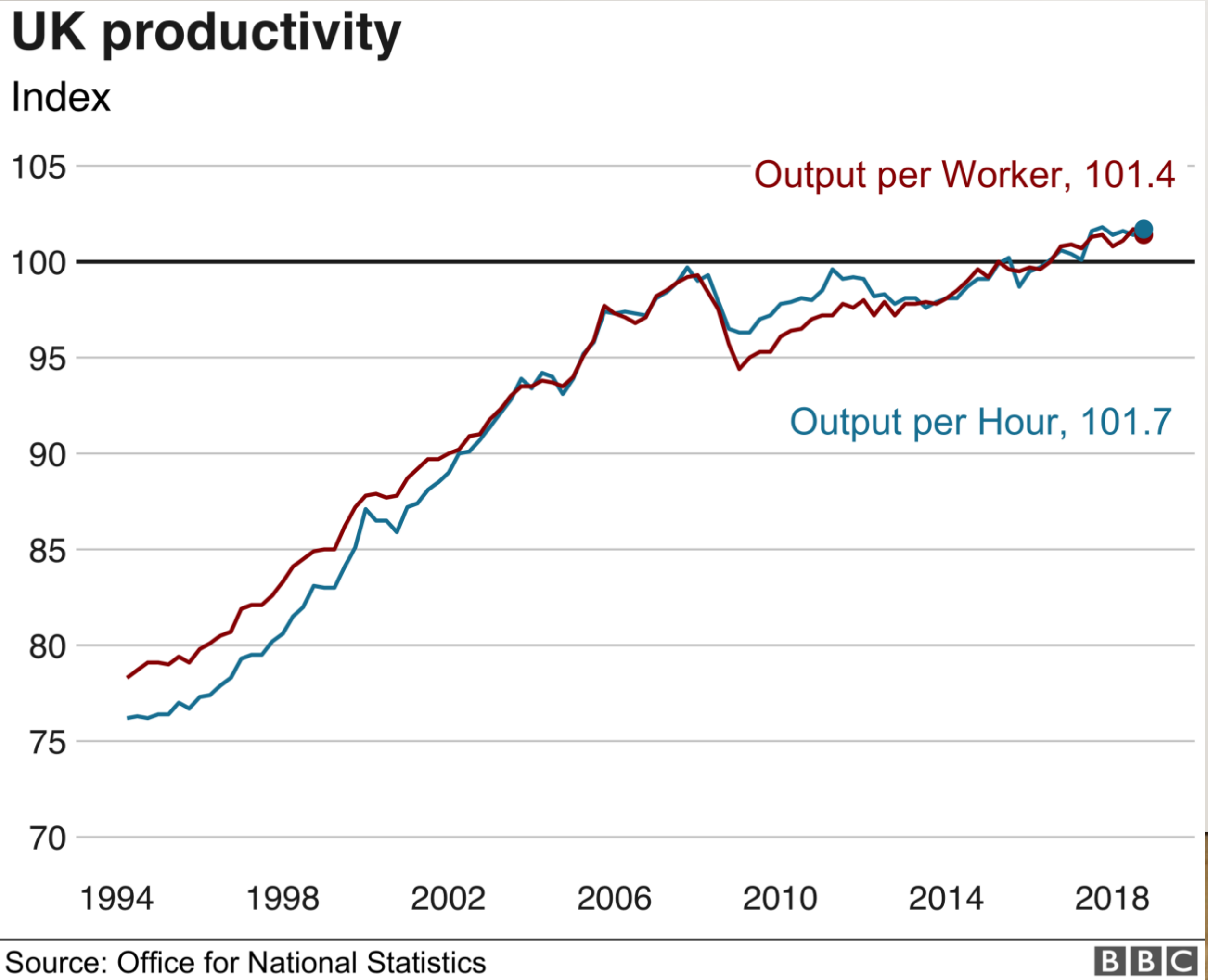
GUPTA/HAMACO

- Engineering graduates are more likely to work in financial sector if they start out in an MSA with a higher share (and thus higher growth) of financial sector employment or study in a state that deregulates interstate banking
- This results in relatively fewer start-ups founded by engineering graduates that go into finance, as well as less innovation and less VC funding by such start-ups
- Evidence for brain-drain from engineering to finance
- Great data, nice identification strategy and important policy message (too much finance can hurt)

GUPTA/HAMACO – SOME COMMENTS

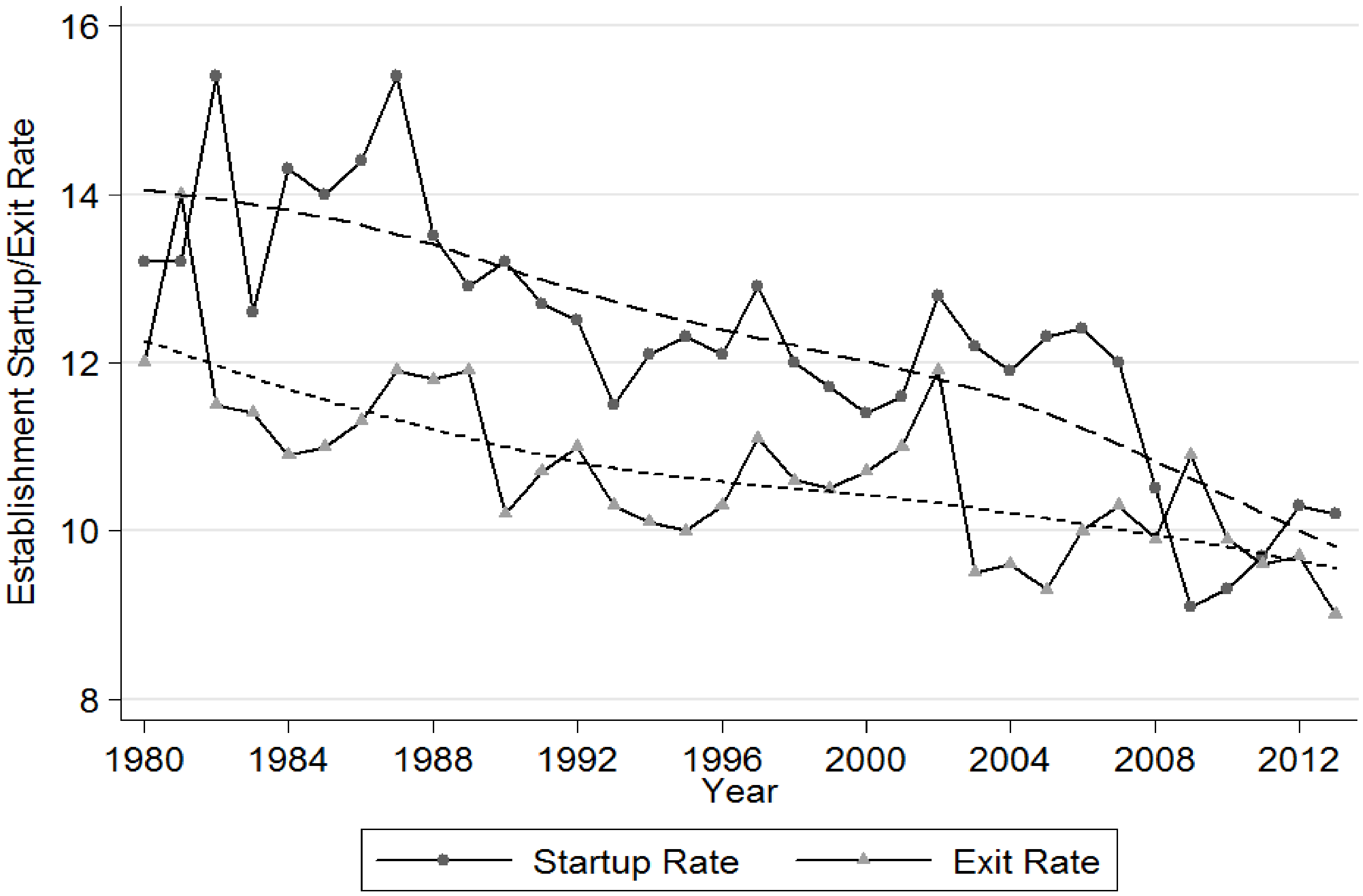
- Why 12 schools?
- When considering shifting from engineering into finance, why not interact with time since graduation? Also: differences in this probability over time?
- What are the real implications of your findings?

THE BIGGER PICTURE



- Financial crisis has contributed to lower productivity growth
- Albert/Caggese show that this might be due to financial distress

THE BIGGER PICTURE (2)



- Can the decline in entrepreneurship in the US be explained by the brain drain from manufacturing into finance?
- Gupta/Hamaco suggest that yes
- Certainly, it cannot be explained by federal regulation (Goldschlag and Tabarrok, 2018)

CONTRADICTIONS?

- Albert/Caggesse show how financing constraints impede high-growth firms to be established
- Gupta/Hamaco show how finance crowds out entrepreneurship
- How can we reconcile these two findings
- Non-linearity of finance?
- Intermediation vs. non-intermediation business?

THE BRIGHT AND DARK SIDES OF FINANCE

- Finance-growth relationship works through resource allocation and productivity growth
  - Entrepreneurship is thus an important channel, especially transformational entrepreneurs
  - Typically stronger in emerging markets, though there is evidence that it might work also in high-income countries (as, in Albert/Caggese)
- Finance-growth relationship does NOT work through the size of the financial system (e.g., employment in financial sector) and not necessarily through non-intermediation business
  - Tentative evidence in Beck, Degryse and Kneer (2014)
  - Evidence for brain drain (Kneer, 2013a,b), even when controlling for financial intermediation
  - Conclusion: financial sector can grow too big and can crowd out the real sector

ONE ATTEMPT AT RECONCILING RESULTS

- Gutpa/Hamaco: stronger effect of brain drain through securities business rather than credit business – does this capture non-intermediation business in the financial sector (e.g., trading)?
- Albert/Caggese: can we focus more on specific financing forms/intermediaries for start-ups?

- In summary: two exciting papers that show the ambiguity of the role of the financial sector in modern high-income countries

THANK YOU

THORSTEN BECK

TBECK@CITY.AC.UK

WWW.THORSTENBECK.COM

@TL_BECK_LONDON

CASS BUSINESS SCHOOL
CITY, UNIVERSITY OF LONDON
EST 1894