IOSR Journal of Business and Management (IOSR-JBM)
e-ISSN: 2278-487X, p-ISSN: 2319-7668. Volume 17, Issue 10 .Ver. II (Oct. 2015), PP 51-54
www.iosrjournals.org

Effectuation Framework as an Alternative Paradigm to Opportunity Identification for Creation of New Venture Enterprise

Afolabi Y.A.
Department of Business Administration and Management, Osun State Polytechnic, Iree.

Abstract: *Opportunity identification represents a unique entrepreneurial behavior yet its processes and dynamics remain mysterious. In line with more recent process views of effectuation framework, this paper draws upon literature on effectuation theory, vis-a-vis opportunity identification. The paper delineates the domain of entrepreneurial action within the context of effectuation framework. It demonstrates the efficacy of effectuation as a framework that can be used to explain the behavior of entrepreneurs in the process of opportunities identifications. The methodology to be employed is the analytical research of existing literature about the role of effectuation as an alternative paradigm to opportunity identification for creation of new venture enterprise.*
Keywords: *Opportunity identification, Enterprise creation, Effectuation theory.*

I. Introduction

As the empirical investigation of entrepreneurship progresses, an increasing number of scholars are concluding that opportunity identification represents the most distinctive and fundamental entrepreneurial behavior (Gaglis, 1997; Kirzner, 1979; Stevenson and Jarilo, 1990; Ventakaraman, (1997). Other market actors - apart from entrepreneurs - do not have the responsibility to create innovative market opportunities although they do not have an obligation to consider such opportunities once they are available in the market place. (Gaglio and Katz, 2001). Consequently, understanding the opportunity identification process represents one of the core intellectual questions for the domain of entrepreneurship. (Gaglio and Katz, 2001). One of the most central discussions in entrepreneurship research is on entrepreneurial opportunities (Eckhart and Shame 2003; Vaguely and Julien, 2010). It is widely accepted that the entrepreneurial process is constituted by acts of opportunity discovery, creation, evaluation and exploitation (Shane and Ventakaraman, 2000). However, although literature argues that entrepreneurship is a process, which begins with the new opportunity (Shane and Ventakaraman, 2000), such literature discusses mainly the emergence of entrepreneurial opportunities in terms of the opposing views on the nature of opportunities. An awareness of activities of entrepreneurs is critical to understanding an entrepreneurial economy. In her ground breaking research, (Sarasvasthy, 2001, 2008) advanced our understanding of the entrepreneurial process by describing two distinct approaches to new venture creation: Causation and effectuation. While Causation is consistent with planned strategy approaches, including such activities as opportunity identification and business plan development, effectuation processes are consistent with emergent; iterative strategy that include a selection of alternatives based on loss affordability, flexibility and experimentation. (Sarasvasthy, 2008). Effectuation theory (Sarasvasthy, 1998) as will be elaborated in this paper, consists of a set of heuristic principles such as the affordable loss principles or the logic of control that apply specifically to the creations of new organizations and markets. In fact, the theory of effectuation, as elaborated later in the paper, points to an explanation as to why effectuation framework is an alternative paradigm to opportunity identification for new venture creation. In opportunity creation theories, entrepreneurs do not become aware of new business opportunities by recombining knowledge in ways, but they create previously absent knowledge for activity. Then, they receive market responses for these actions, learn from them and then act again. Therefore, this paper intends to show the relevance of effectuation framework to our environment that is lacking in institutional supports for entrepreneurial activities. This framework rests on the principles of achieving entrepreneurial plans based on one's means. Resources for achieving entrepreneurial plans are not externally determined but driving by one's own means.

II. Literature Review

Opportunity Theories

There are two perspectives on opportunity in entrepreneurship literature. The first states that opportunities are natural events previously existed in the world and then they are discovered and exploited by entrepreneurs. Proponents to this view include Kirzner (1973), Drucker (1985), Singh (2000), Singh (2001), Shane (2001), Kickuland Gundry (2000) and Krucger (2000). In contrast, the second view states that opportunities should be considered as thought in concepts that entrepreneurs are seeking to create risks in a world that basically depends on their mentality and actions for development.

In this view, opportunities are not discovered as creative and social processes. Proponents of this view include Corbett (2005), Ucbasaran (2003) and Macline (2000). Researchers have attempted to link these two conflicting views under broader theoretical frameworks. Some psychological issues on creativity suggest that both discovery and creation aspects are special cases from more general processes. Psychological models generally mention five steps in creativity: preparation, incubation, insight, evaluation and description.

Lumplcin, Hills and Scurader (2007) entrepreneurship is the process of creating and pursuing opportunities regardless of currently available resources. The fact is that, there is no special and unique process to correctly recognize opportunities and competitive advantage factors, but one should rely on the manger's insight of business environment; an insight which is the result of their true recognition an understanding of the environment and business rules. So one of should try effective ways to meet customers needs, truly interpreted the theory of effectuation brings another perspective to the table. It suggests we need to give up ideas such as the successful personality, or clearly superior characteristics of the successful firm or organization. The focus of this paper, would shift from "How to build a successful firm?" or How to become a successful entrepreneur?" to what types of ideas and opportunities should you pursue?" and "Given who you are, what you know, and whom you know, what types of economic and / or social artifacts can you, would you want to and should you create?" (Sarasvasthy, 2001).

Causation and Effectuation Process

Sarasvasthy (2001) states that "Causation processes take a particular effect as given and focus on selecting between means to create that effect." In new venture creation, entrepreneurs following a causation process clearly define the objectives they want to accomplish up front and systematically search (Fiet, 2002; Herron and Sapienza, 1992) for entrepreneurial opportunities within developed industries that meet those objectives. They evaluate and select opportunities that maximize expected returns (Drucker, 1998). Sarasvasthy (2001) opines that 'the underlying logic is, "To the extent we can predict the future, and we can control it."

The theoretical foundations for the causation process derive from the rational decision making perspectives of neo-classical micro-economics (Stingier, 1952). In a causation process an individual makes rational choices based on ail possible information relevant to his decision and an estimated expected utility for each option (Viale, 1992). Most of the existing entrepreneurship literature has theoretical foundations in the causation approach. For example, in the research on opportunity discovery Fiet (2002) opines that opportunity detection results from a rational search process in which alternatives are identified and analyzed. The alternative with the highest expected return is selected and implemented. Entrepreneurial opportunities are driven by exogenous forces, and the role of the entrepreneur is to examine the environment and existing projects in the market place, utilize a sequential seeing process and choose the project with the highest expected return (Casson and Wadeson, 2007). Thus, entrepreneurial rents accrue to individuals with superior search and implementation skills (Caplan, 1999).

The business plan and its popularity in entrepreneurship practice is another example of institutional conformity to the causation approach. Most textbooks on entrepreneurship are built around business planning models (Allen, 2003; Kuratico and Hodgetts, 2004; Scarborough and Zimmerer, 2003; Timmous and Spinelli; 2004). The development of a business plan is a rational activity that assists the owners of new firms (entrepreneurs) to earn larger profits through efficiency gains and increased sales (Honig and Karlsson, 2004).n although the empirical research regarding the effectiveness of business plans has been mixed (Honig and Karlsson, 2004; Liao and Gartner, 2006) the business plan with its step-by-step rational process is a primary deliverable in many university or polytechnics entrepreneurship programs.

Sarasvasthy (2001) states that effectiveness approaches "take a set of means as given and focus on selecting between possible effects that can be created with that set of means."

Creation, entrepreneurs following an effectuation approach might begin the new venture process with general aspirations to create a new venture, but as they make decisions and observe the results of those decisions, they utilize this new information to change course. Because the future is an unpredictable, entrepreneurs using an effectuation approach may try different approaches in the market place before setting on a business model.

Also, they are likely to put mechanisms in place that allows them to have some control over the outcome.

Sarasvasthy (2001), the underlying logic is, "To the extent we can control the future, we do not need to predict." The theoretical foundations of an effectuation approach lie in cognitive science, particularly the work which emphasizes entrepreneurial framing how entrepreneurs view inputs, make inferences perceive alternatives, and attend to constraints (Dew *et al*, 2009; Johnson and Lakoff, 2002). Sarasvasthy's (2001) theoretical conceptualization and the ensuing empirical work (Dew *et al*, 2009; Sarasvasthy and Kotha, 2001;

Sarasvasthy *et al*; 1998) have demonstrated that entrepreneurs following an effectual logic are less likely to try to predict the future and more likely to change their initial goals and visions for the new venture. Rather than predicting the future, they are more likely to work with means within their control and make adjustments as necessary (Dew *et al*, 2009) using effectual logic they frame the future as resulting from co-creation by intentional agents (networks of partnerships consisting of investors, partners, and customers) who are "structured together" (Dew *et al*, 2009). Goals emerge by developing potential courses of action that are based on the available means of who a person is, what they know, and whom they know. (Chandler *et al*, 2011).

Differences between Causation and Effectuation

Sarasvasthy (2001) outlines four principles that differentiate causation and effectuation approaches: (1) a focus on short-term experiments to identify business opportunities in an unpredictable future (effectuation) versus prediction of an uncertain future by defining the final objective up front (causation). (2) a focus on projects where the loss in a worst-case scenario is affordable (effectuation) versus maximization of expected returns (causation), (3) an emphasis on pre-commitments and strategic alliances to control an unpredictable future (effectuation) versus business planning and competitive analyses to predict an uncertain future (causation), and (4) exploitation of environmental contingencies by remaining flexible (effectuation) versus exploitation of pre-existing capabilities and resources (causation).

This work will contributes to the developing stream of empirical and analytical research that investigates entrepreneurial decision making under conditions of uncertainty (Will Bank *et al*, 2009; Dew *et al*, 2009).

Table 1:The Effectual Activities Could Be Compared With More Traditional Activities (Sarasvasthy, 2008).

Traditional activities	Effectual activities
Doing market research	Negotiating effectual commitments.
Bringing the right people on board	Working with self-selected stakeholders
Obtaining finances requisite for performance projections	Zero resources to market or investing what one can afford to lose
Betting on probabilities	Strategizing on conditioning assumptions
Avoiding failures	Managing and averaging failure
How to become the successful entrepreneur	How to do entrepreneurship well
Managing trade off	Designing synergies
Manipulating constraints	Reconstructing objective functions.

Principles Of Effectuation (Effectual Cycle) (Sarasvasthy, 2008).

- Bird in hand - means available, start with your means principle. The questions that I am? What? Whom I know? Answering the questions will activate action to describe competences, find knowledge and start creating contracts.
- Affordable risk - setting goals, focus on the downside risk. Answering the question what can I do? Defines and helps to understand courses of actions for developing business idea.
- Pilot-in-the plane - control versus predict. This principle is based on the idea that learning entrepreneurship through experiencing effectual cycle focuses only those activities which are in their own control.

III. Conclusion

Summarily, effectuation has been proposed as alternative paradigm for new venture creation processes used by entrepreneurs. These different processes which suggest that entrepreneurs and firms not only need to invest better ways to predict the future, they also need to develop devices that allow them to create opportunities as well as adapt to their environment (Dew and Sarasvasthy, 2001). An understanding that both causation and effectuation processes are legitimate ways to initiate and grow businesses provides entrepreneurs and potential entrepreneurs with a more comprehensive and well- developed set of skills that can be used to initiate viable ventures.

Effectuation is the very process which provides entrepreneurs with an opportunity to create, predict, market and organization where non existed. Effectual manager/entrepreneur need wonder whether a forecast is accurate, or whether the market was segmented correctly.

IV. Implications

- Additional research is needed to make sure that we have identified the most relevant sub-components of effectuation. Future research might examine whether there are other dimensions of effectuation that distinguish this process from causation processes.

- It is adduced that not only entrepreneurial opportunities identification are situations that enable new venture creation but also effectuation processes.
- Besides uncertainty, are there other antecedents to the choice between causation and effectuation processes? Previous research in entrepreneurship has shown that the entrepreneur's human capital (e.g. entrepreneurial experience, education) and cognition (e.g.; entrepreneurial alertness, entrepreneurial scripts, counter factual thinking. Cognitive style, heuristics) (Dew *et al*, 2009; Mitchell *et al*; 2007) may have an impact on the choice of process. Further research should explore the relationship between these determinants and causation and effectuation processes.
- Effectuation theory (Sarasvasthy, 1998), as elaborated in the paper, consists of heuristic principles such as the affordable loss principle or the logic of control that apply specifically to the creations of new venture. Future research should not negate the importance and validity of other factors that predict and explain effectuation process and opportunity identification.
- Should successful entrepreneurs be modal in their thinking, presenting predictive information to inventors while acting effectually during the operation of their firms? A given that a non-predictive approach is positively related to new venture success.

References

[1]. Allen, K. (2003): Launching New Ventures: An Entrepreneurial Approach. Houghton Miffin, Boston, MA.
[2]. Caplan, B. (1999): The Australian Search for Realistic Foundations. Southern Economics Journal 65(4), 823-828
[3]. Cassson, M, and Wadeson, N. (2007): The Discovery of Opportunities: Extending the Economic Theory of the Entrepreneur. Small Business Economics 28(4), 285-300
[4]. Chandler, G.N; DeTienne, D.R.; Mckelvie, A; and Mumford, T.V. (2011): Causation and Effectuation Processes: Validation Study. Journal of Business Venturing 25 (375-390)
[5]. Dew, N and Sarasvasthy, S.D (2001): Of Immortal Firms and Mortal Market: Dissolving the Innovator's Dilemma. Presented at the Second Annual Technology Entrepreneurship Research Conference. Robert H. Smith School of Business, University of Maryland.
[6]. Dew, N, Read, Sarasvasthy, S.D. and Wiltbank, R. (2009): Effectual Versus Predictive Logics in Entrepreneurial Decision-making: Differences between Experts and Movies. Journal of Business Venturing 24(4), 263-282
[7]. Drucker, P.F. (1985): The Discipline of Innovation. Harvard Business Review, 63, 67-72
[8]. Drucker, P.F. (1998): The Discipline of Innovation. Harvard Business Review 76(6), 149-157
[9]. Eckharat, J.T. and Share, S.A. (2003): Opportunities and Entrepreneurship. Journal of Management, 29 (3) 333-349.
[10]. Fiet, J.O. (2002): The Systematic Search for Entrepreneurial Discoveries Auorum Books, Westport, and cit.
[11]. Gaglio, C.M. and Katz, J.A. (2001): The Psychological Basis of Opportunity Identification: Entrepreneurial Alertness. Small Business Economics. Journal, Kluwer Academic Publishers Printed in Netherlands. Pp.95-111.
[12]. Heron, L. and Scapienza, H.J. (1992): The Entrepreneur and the Initiation of New Venture Launch activities Entrepreneurship Theory and Practice 17(1), 49-55
[13]. Honig, B and Karlsson, T. (2004): Institutional Forces and the Written Business Plan. Journal of Management 30(1), 29.
[14]. Johnson, M and Lakoff, C. (2002): Why Cognitive Linguistics requires embodied Realism. Cognitive Linguistics 13(3), 245-263.
[15]. Kickul, I.J and Gundry L.K. (2000): Pursuing Technological Innovation: The Role of Entrepreneurial Posture and Opportunity Recognition among Internet Firms.
[16]. Kirzner, I.M. (1973): Competition and Entrepreneurship. University of Chicago Press, Chicago, IL.
[17]. Krueger, N.F. (2000): The Cognitive Infrastructure of Opportunity Recognition. Entrepreneurship Theory and Practice, 24, 5-23.
[18]. Kuratko, D.F. and Hodgetts, R.M. (2004): Entrepreneurship: Theory, Process, and Practice. Thomson South-Western, Mason, OH.
[19]. Liao, J. and Gartner, W. (2006): The Effects of Pre-venture Plan Timing and Perceived Environmental Uncertainty on the Persistence of Emerging Firms. Small Business Economics 27(1), 23-40
[20]. Mitchell, R.K, Busenitz, L.W, Bird, B., Gaglio, C.M., McMulien, J.S., Morse, E.A, Smith, B., (2007). The Central Question in Entrepreneurial Cognition Research. Entrepreneurship Theory and Practice 31(1) 1-27.
[21]. Sarasvasthy .S. (2008): Effectuation: Elements of Entrepreneurial Expertise. Edward Elgar Publishing Limited, Cheltenham, U.K.
[22]. Sarasvasthy S. (2001): Causation and Effectuation: Toward a Theoretical Snuff from Economic Inevitability Academy of Management Review 26 (2) Pp.243-363.
[23]. Sarasvasthy, D.K, Simon, H.A and Lowe, L (1998): Perceiving and Managing Business Risk: Difference between Entrepreneurs and Behavior and Organization. 33(2), 207-225.
[24]. Sarasvasthy, S.D. and Kotha, S. (2001): Dealing with Knighting Uncertainty in the new Economy: The Real Networks Case. In: Butler, J.E. (Ed), Research on Management and Entrepreneurship. Greenwich, /AP Inc, 31-62.
[25]. Scarborough, N.M. and Zimmerer, T.W. (2003): Effective Small Business Management: An Entrepreneurial Approach. Prentice Hall, Upper Saddle River, N.J.
[26]. Shane .S. and Ventakaraman. S. (2000): The Promise of Entrepreneurship as a Field of Research. The Academy of Management Review, 25(1) Pp217-226.
[27]. Shane, S. (2003): A General Theory of Entrepreneurship: The Individual Opportunity Nexus Alder shot: Edward Elgar.
[28]. Singh, R.P. (2000): Entrepreneurial Opportunity Recognition through Social Networks, New York / London: Garland Publishing, Inc.
[29]. Singh, R.P. (2001): A Comment on Developing the Field of Entrepreneurship through the Study Opportunity Recognition and Exploitation, the Academy of Management Review, 26, 10-12.
[30]. Stringier, G.J. (1952): The Theory of Prices Macmillan, New York, NY.
[31]. Timmons, J.A. and Spinelli, S. (2004): New Venture Creation: Entrepreneurship for the 21st Century. McGraw Hill/Irwin, New York, NY.
[32]. Vaguely, I.P. and Julien, P. (2010): Are Opportunities Recognized or Constructed-? An Information Perspective on Entrepreneurial Opportunities Identification. Journal of Business Venturing, 25, Pp. 73-86.
[33]. Viale, R. (1992): Cognitive Constraints of Economic Rationality in: Simon, H (ed), Economics Bounded Rationality and Cognitive Revolution. Edward Elgar Publishing Limited, Brookfield, VT, 174-193.
[34]. Wiltbank, R; Read, S; Dew, N and Sarasvasthy, S.D. (2009): Prediction and Control under Uncertainty: Outcomes in Angel Investing, Journal of Business Venturing 24(2) 115-133.