

Encourage that spark!

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Potential members of the BRW Young Rich list need a climate that allows for experimentation, even if not all the results are successful. By **Joshua Gans**

In the early 1990s, I was a postgraduate student at Stanford University in Silicon Valley. On those rare occasions when I had time to attend a neighbourhood barbecue, I invariably ran into some of the large numbers of electrical engineering and computer science students. Hearing that I was an economist, they would tell me enthusiastically of their plans to go straight from their studies into starting a business that could exploit the internet. My reaction was: "What, that email thing?"

Back then, the internet was moving out of government and the universities and into the commercial world but few people realised its potential. Even those of us who knew what the internet was saw it as a device for email - a primitive form of instant messaging.

I listened politely to their plans. One student I remember had some notion of using the internet to run auctions for ordinary folk. He thought that being an economist I might know something about that. It sounded interesting but I told him what I told many others: "If it is such a good idea, why hasn't anyone exploited it already?"

Then, in about 1994, some of these students put up a list of websites that were available on the local network. It was just a list with a few categories and subheadings. It looked pretty cool, but I couldn't see why those guys who lived a few doors down were spending their time compiling a list. Surely they had better things to do? Apparently not. A little later those same guys moved out of the campus accommodation, formed a company called Yahoo! and are now billionaires. Many of the people who attended those barbecues became millionaires at the very least.

Many of those appearing on the BRW Young Rich list remind me of these Stanford folk. They seized a new opportunity, didn't think much about why others were not there and forged ahead regardless. They took a gamble and won. The results are new businesses and retail brands, each of which has managed to make money nipping at the heels of larger corporations.

Of course, the BRW Young Rich also offers some cautionary tales. Sure, it is possible to become one - the difficult part is hanging on to the gains. Much of the wealth here is "book wealth" - yet to be crystallised. Looking at how people slide down and sometimes off the list each year shows that this book wealth can be fleeting: if you live by the sword of competitive opportunity, you can die as the blade swings back with a competitive response. Some of the Young Rich may not hold on to their wealth long enough for the Australian Taxation Office to get their hands on it.

But even these failures should be celebrated because even after the fallout, the influence of these entrepreneurs on the economy remains. Each has taken advantage of one of the hallmarks of our market-based economy: the freedom to conduct economic experiments. They bear much of the risk of failure but on the other hand they can keep the upside. According to the Stanford historian Nathan Rosenberg, this is how our economic system allows people to embark on various forms of experimentation, and it is the basis for continued economic dynamism and innovation. Professor Scott Stern, of the Kellogg Graduate School of Management at Northwestern University in Chicago (he won the Kauffman medal for entrepreneurship research in 2005), says that by not being part of established companies, entrepreneurs can undertake more extreme experiments. They are less constrained by the existing ways of doing things and can take a "whole-of-system" approach to new opportunities.

The challenge for Australia in dealing with these entrepreneurs is twofold. First, to create an environment in which a diverse set of economic experiments is possible and entrepreneurs can flourish. Second, to ensure that the results of those experiments - those that are a personal triumph or a personal failure for the budding entrepreneurs - make a lasting imprint on the Australian economy. That is, experimental learning is essential.

Many of the success stories of the BRW Young Rich come not from technological experiments - that is, pioneering advances in scientific knowledge - but from market experiments that take technologies and ideas from elsewhere and apply them in novel ways. The entrepreneurs try to make the market test work. And the task for the economy is to run multiple market tests. For example, in bringing mobile-phone technology to markets, experiments were required: in pricing (subscription versus cap plans); ease of use; additional content (such as television shows and live sport); and integrated technologies (cameras and noise-cancellation devices). In each of these areas, only a few entrepreneurs made money. But the benefits for the wider economy were huge because the diversity of experiments helped everyone to find the best way forward.

From market experiments such as these, the contribution remains mostly local. For Australia, the real promise of prosperity created by entrepreneurship is where the scientific knowledge can be exploited on a global scale. For instance, because of the absence of large pharmaceutical labs, Australia lacks some of the elements needed for experimental diversity in biotechnology. But start-up clusters of biotechnology are flourishing around some universities. These clusters provide a good basis for learning, but the ability to tap directly into the needs of the global market is lacking. The customers for biomedical research and medical devices are larger firms that can bring those products through regulatory hurdles to market. This is where distance takes effect. Clearly, there is an opportunity for entrepreneurs to devise ways of getting local research noticed.

But even if we can get the basics in place for a scientific-based set of economic experiments, do we have the entrepreneurs to advance them? Not much is known about what makes a person entrepreneurial. We know it requires some suspension of natural

scepticism. It also requires the confidence to believe that you might be the first with a particular idea. But most of all it needs a special go-it-alone quality.

Professor Scott Shane, of Case Western Reserve University in Cleveland, Ohio, and others have demonstrated that entrepreneurial drive may be genetic. They took an extensive sample of twins in the United Kingdom and compared their choices to become self-employed or not. Fraternal twins exhibited no greater tendency towards self-employment than their siblings, but for identical twins the tendency correlated strongly. That is, if one identical twin was self-employed, the chances were that the other would be as well.

If this line of research is valid, then our strategy should not necessarily be to encourage more entrepreneurs, but to ensure that the environment is such that when they emerge, they can easily conduct economic experiments. In the race to generate persistent innovation, surely providing a good platform - a secure and stable macroeconomic environment, low regulatory impediments for start-ups, a strong scientific basis and openness to the global economy - is the way to start. That was exactly the environment in Silicon Valley, but not everyone who lived there was aware of it.

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