

How Cognitive Biases Affect Opportunity Cost and Value In The Pursuit of an Entrepreneurial Opportunity?

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Introduction

What makes an Entrepreneur pursue an opportunity when others do not? Research has looked at the personalities of Entrepreneurs and found no clear-cut differences between entrepreneurs and the standard population. (Shaver & Scott, 1991) However, differences between entrepreneurs and the general population have been found in relation to several cognitive factors, namely overconfidence (Busenitz & Barney, 1997) the illusion of control, and the belief in the law of small numbers. (Simon, Houghton, & Aquino, 2000)

These cognitive biases affect how the entrepreneur values opportunities and perceives risk. (Palich & Bagby, 1995) This does not infer that entrepreneurs do not evaluate opportunities based on opportunity cost and the perception of the risk involved; it merely means that entrepreneurs evaluate opportunities and risk using different perspectives than that of the typical business manager. So assuming that entrepreneurs see opportunities and perceive risk differently than the typical business manager, they will base their go/no go decision to pursue an opportunity using their interpretation of the opportunity cost and their perception of the risk.

This paper details the cognitive biases that are generally attributed to entrepreneurs, defines opportunity cost, opportunity value, and risk perception, and then shows how the areas are related with respect to the decision by an entrepreneur to pursue

an opportunity. In so doing, this research will add to entrepreneurship theory in relation to the entrepreneurs' decision to pursue an opportunity. It will aid entrepreneurial education programs by making them aware of the need to make budding entrepreneurs cognoscente of both their biases, and how the concept of opportunity cost and risk perception are impacted by these biases. Finally, practicing entrepreneurs will be made aware that they too have biases, which may affect their perceptions of opportunity cost and risk perception. Knowledge of cognitive biases, and their affect on the perceptions of opportunity cost and risk could enable entrepreneurs to reach greater success.