Mastery vs. Profit as Motivation for the Entrepreneur

How Crony Policies Shape Business

G. P. Manish and
Daniel Sutter

August 2015

MERCATUS WORKING PAPER

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G. P. Manish and Daniel Sutter. “Mastery vs. Profit as Motivation for the Entrepreneur: How Crony Policies Shape Business.” Mercatus Working Paper, Mercatus Center at George Mason University, Arlington, VA, August 2015.

Abstract

Desire for mastery is an important human motive distinct from the profit motive. In business, mastery involves a product or service, and validation occurs through comparison with other entrepreneurs’ products. Consumers’ choices validate entrepreneurs’ performance. We term an entrepreneur’s intrinsic desire to produce a good product mastery seeking, and contrast mastery seeking with profit seeking. Success often coincides with profit, but the two motives are different and can diverge. We explore mastery seeking’s implications for the economics and politics of government privileges and favors for business. Crony polices can disrupt the consumer choice process and the validation of performance. Crony policies may increase profit but reduce realized performance for entrepreneurs, reducing the labor supply of entrepreneurs motivated by competition. A nation’s level of cronyism could affect the types of individuals who become entrepreneurs, with a high level of government intervention pushing success seekers to pursue mastery in other endeavors, with adverse implications for innovation and growth in the economy.

JEL codes: D72, M00, D01

Keywords: entrepreneurs, rent-seeking, mastery, government favors for business, cronyism, intrinsic motives, profit seeking

Author Affiliation and Contact Information

G. P. Manish
Assistant Professor of Economics
Manuel H. Johnson Center for Political Economy at Troy University
gmanish@troy.edu

Daniel Sutter
Professor of Economics
Manuel H. Johnson Center for Political Economy at Troy University
dsutter@troy.edu

Acknowledgments

Prepared for the Mercatus Center’s Project for the Study of American Capitalism. We thank Tyler Cowen and two reviewers for comments on an earlier draft of this paper.

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1. Introduction

Introspection, the evidence of daily life, and a significant volume of academic research from different fields demonstrate that many people exhibit a drive to excel. Psychologists label this drive mastery or competence, and we observe it in the efforts of master craftspersons, authors, athletes, musicians, and others who strive for excellence.

Profit maximization does not adequately explain mastery as a motive for entrepreneurs or business leaders. Profit is an extrinsic goal, while mastery is an intrinsic desire. A desire to write books for a profit or to write great books illustrates this contrast. We term the intrinsic desire to produce a valued good or service in business "mastery seeking" and contrast it with profit seeking.

Mastery offers some divergent perspectives and predictions for business and economics. Of the many interesting contrasts, we explore here the implications of mastery seeking for government assistance and favors for business, or what has been called rent-seeking or cronyism. Our analysis draws on the need for interpersonal validation of performance or comparison with the efforts of other performers. In business, the choices of sovereign consumers in the market validate performance. Consequently, although profit and mastery or performance will often coincide, the potential exists for government restrictions on competition to increase profits for entrepreneurs but reduce realized performance.

This perhaps innocuous observation holds significant implications for an assessment of cronyism. For instance, public choice theory explains the establishment and persistence of crony favors based on concentrated benefits and dispersed costs. Yet such policies, by disrupting the process of validating performance in the market, could make a mastery-seeking entrepreneur worse off, so some businesses may oppose such policies. If the pool of potential entrepreneurs includes some primarily profit seekers and other primarily mastery seekers, crony policies could affect the composition of entrepreneurs and business leaders as a group. The potential for a cronyism tipping point exists within an industry or the economy. At low levels of government intervention, markets validate performance and both profit and mastery seekers pursue business; entrepreneurs interested in validated performance will not demand choice-disrupting favors from government. If an industry becomes too rife with cronyism, market outcomes fail to validate performance, and mastery-seeking entrepreneurs exit, leaving profit seekers willing to pursue additional favors from government. If mastery seekers are "better" entrepreneurs on average, the exit of mastery seekers could be another means by which cronyism reduces growth.

We proceed in this paper as follows. Section 2 elaborates on our performance or mastery motive distinction and discusses its relationship to psychologists' work on intrinsic motivation, mastery, and competence. Section 3 provides a more formal treatment of mastery seeking, adding validated performance as an argument in an entrepreneur's utility function and drawing out some contrasts with traditional profit seeking. Section 4 offers evidence for the existence of such an intrinsic motive, drawing on academic research and the words and deeds of entrepreneurs. Sections 5 and 6 examine the interaction between the motives of entrepreneurs and government policies normally seen as aiding business, like purchase mandates and subsidies. By divorcing purchases from consumer judgment, such policies can disrupt market validation of entrepreneur performance. The final section offers concluding thoughts and directions for future research.

2. Defining Mastery Seeking

Economics and psychology have long extolled the role of incentives in shaping human behavior. Incentives, including profit, represent extrinsic motivation, which exists when "an activity is done in order to attain some separable outcome" (Ryan and Deci 2000, 60). A profit-maximizing firm does not necessarily care about making widgets, or the best widgets possible, except as a means to make profits.

Psychologists have recognized the importance of intrinsic motivation, or "the doing of an activity for its inherent satisfactions rather than for some separable consequence" (Ryan and Deci 2000, 56). Intrinsic motives arise from inside a person, such as the challenge of solving puzzles or activities people find enjoyable for their own sake. Laboratory experiments have documented the existence and importance of intrinsic motivation by controlling for possible external motives, or by comparing the performance of participants offered extrinsic rewards or not. For example, participants in experiments involving the cognitive performance test known as the candle problem[1] who were paid a bonus took significantly longer to solve the problem than participants not offered incentives (Glucksberg 1962). The intrinsic drive of curiosity outperforms external rewards as a means of motivating behavior, especially in the long run (Lepper, Greene, and Nisbett 1973). A comparison of the commissioned and noncommissioned works by professional artists judged the commissioned works to be less creative but of comparable technical quality (Amabile, Phillips, and Collins 1993). Among scientists and engineers working in industry, those motivated by intellectual challenge produced significantly

[1] In the candle problem, participants are given a candle, a book of matches, and a box of thumbtacks and asked how to fix the candle on a corkboard wall and light it so that the wax from the candle will not drip onto a table below.
[2] Kirzner (1973) argues that the essential element of entrepreneurship is alertness to new profit opportunities. Some entrepreneurs may thus define success in terms of the discovery of opportunities that elude other market participants.

more patents than those motivated by external rewards (Sauerman and Cohen 2008). This last result is particularly telling given the potential for sorting by motive across different categories of jobs; the scientists most motivated by intrinsic concerns could well have gravitated to academic or foundation-funded positions, with scientists in industry likely to be more extrinsically motivated. One particular issue investigated extensively in the psychological literature is the potential for extrinsic motives to reduce intrinsic motives (Deci, Koestner, and Ryan 1999). As Deci (1971, 105) puts the matter, "If a boy who enjoys mowing lawns begins to receive payment for the task, what will happen to his intrinsic motivation for performing the activity?"

Economists have recently acknowledged some limits of incentives, and particularly monetary incentives, in both life and business contexts (Cowen 2007). Gneezy and Rustichini (2000), for example, found that parents in Israel were more likely to pick their children up late when a daycare instituted a charge for late pickup, contrary to the expected incentive effect. Other economists, notably Robert Frank (1985), pioneered the extension of economics to consider nonmonetary factors like fairness and a desire to do the right thing. Bruno Frey (1997) offers one of the most comprehensive treatments in economics of intrinsic motives, and he also researches the phenomenon of external motives crowding out internal motives. Economists have also explored the potential for the self-employed to value autonomy (see section 4). But mastery and its application in business as a motive to succeed in competition remains relatively unexplored.

Many motives fall within the intrinsic category. We focus on a specific motive in the business realm: the desire to produce a good product or service. Both introspection and the evidence of everyday life demonstrate that a passion for excellence and desire to prove oneself in competition are important human motives. Psychologists term this mastery or competence. Our success motive translates the desire for mastery into business contexts. Entrepreneurs care about producing good widgets, not just about profiting from widgets. Our success motive assumes that entrepreneurs value the evaluation of their products or services as good in some sense.[2]

Intrinsic motivation "exists in the nexus between a person and a task" (Ryan and Deci 2000, 56) and thus can never be realized totally internally. Although mastery is an internal reward, the enjoyable activities themselves will be socially constructed. Edward Deci's early experiments used Soma puzzles (1971) that participants found intrinsically interesting though others had invented them. This has two implications for our analysis. First, individuals can have an interest in mastering a business that is constantly changing or may only recently have emerged. And second, the specific manifestation of the entrepreneurial master may only take shape when someone enters the business world or a given an industry, and the manifestation could change if the entrepreneur changes area of work. We do not mean to imply that a mastery-motivated tech entrepreneur must have wanted to excel in this field since childhood.

Competence is an important component of intrinsic motivations, with enjoyment closely tied to excelling at the task (Deci 1975). In laboratory experiments, verbal feedback on performance has been found to be closely associated with intrinsic motivation (Vallerand and Reid 1984). Although positive feedback in a laboratory experiment can be randomly assigned and consequently not necessarily valid, we believe that in the case of entrepreneurs, competence must have an existential basis and cannot be entirely imagined. Consequently, competence or performance requires external validation. As Robert Nozick puts it,

> A man living in an isolated mountain village can sink 15 jump shots with a basketball out of 150 tries. Everyone else in the village can sink only 1 jump shot out of 150 tries. He thinks (as do the others) that he's very good at it. One day, along comes Jerry West. . . . There is no standard of doing something well, independent of how it is or can be done by others (1974, 240–1).

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[2] Kirzner (1973) argues that the essential element of entrepreneurship is alertness to new profit opportunities. Some entrepreneurs may thus define success in terms of the discovery of opportunities that elude other market participants.

Consumer purchases provide external validation of a "good" product or service, and this is an important component of our notion of mastery. Purchases may not be the only way validation can occur; for instance, product reviews could also provide external validation. Yet reviews can be readily falsified, so genuine validation must require some element of truthfulness. Purchases are less likely to involve falsification, yet can also be based on poor information or confusion. Repeated purchases provide perhaps the clearest instance of external validation of performance.

We will abstract from a number of details in the generation of mastery, including: Does the purchase of a second unit by the same consumer provide additional validation? Does a greater willingness to pay for a product provide more competence or superior performance? Do the choices of all consumers count equally? Another potentially relevant question is whether purchases of a product that is "the best for the money" signal performance, or whether mastery must involve supplying only the highest quality products. Although we are not ruling out mastery from mass markets, mastery is plausibly more prevalent in the high-quality segments of markets.

3. Mastery, Money, and Entrepreneurial Decisions

Now that we have introduced the mastery motive, we now illustrate how performance complements money in an entrepreneur's effort supply decision. This formalization may help to resolve remaining unclear elements of the previous section's discussion. The utility function of a mastery-motivated entrepreneur can be written $U(x, v, l)$, where x is money, and v is validated performance, and l is labor effort allocated to entrepreneurship. The function $x = f(l)$ with $f' > 0$ describes the monetary earnings from entrepreneurship while the function $v = g(l)$ with $g' > 0$

describes performance. Money and performance increase utility while labor effort is costly, so $U_x > 0$, $U_y > 0$, and $U_l < 0$ (subscripts represent partial derivatives with respect to that argument).

The following first-order condition implicitly describes the labor supply decision of a pure profit-seeking entrepreneur, meaning one for whom v is not really an argument of U:

$$U_x \times f' = -U_l, \tag{1}$$

while the first-order condition for an entrepreneur who also values performance will be:

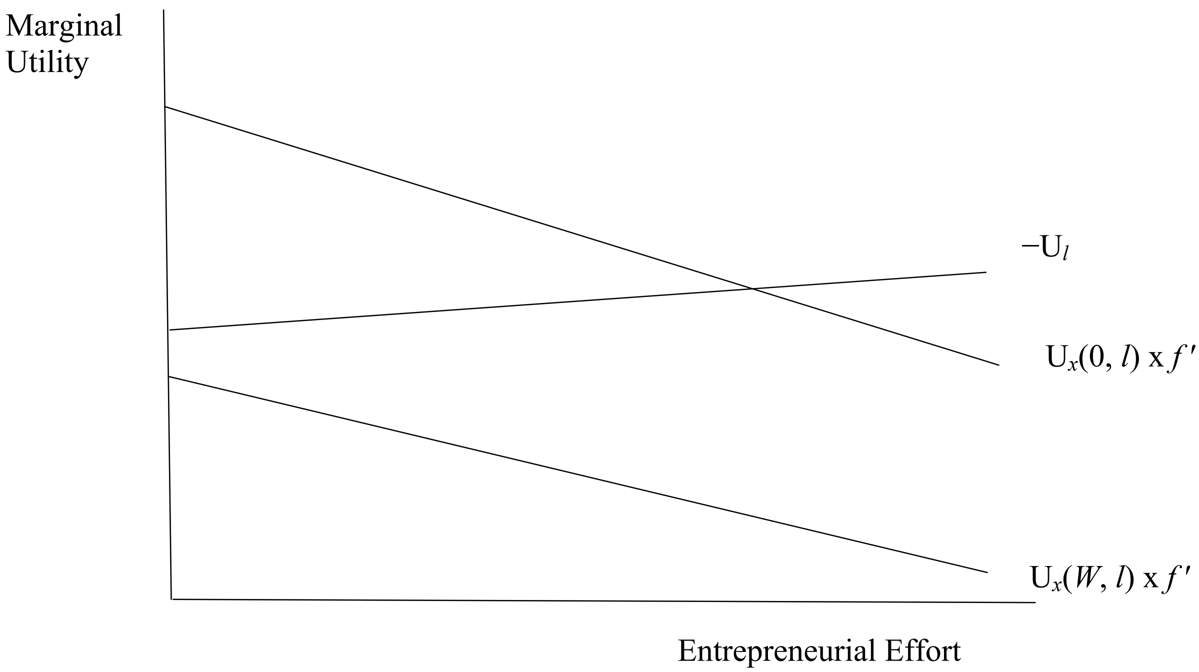
$$U_x \times f' + U_y \times g' = -U_l. \tag{2}$$

Mastery seeking tends to increase the labor effort supplied, and reduces the monetary compensation needed to supply a given level of effort.

The function g(l) incorporates the details of the validation of performance mentioned in section 2. Our focus here is on consumer choice process and success, which holds for a wide range of functional forms for $g(\cdot)$. The details of exactly how performance creates utility (e.g., does absolute or relative performance matter?) may generate interesting results, but are not the focus of this paper.

Mastery seeking can explain an otherwise puzzling aspect of entrepreneurial behavior, namely the tendency of many superrich entrepreneurs to continue to run businesses and start new ventures (see section 4 for examples). To keep our model simple, we interpret the planning horizon to be the remainder of the entrepreneur's life, with the value of a bequest already built into the money argument of the utility function. Let W be accumulated wealth at the start of the planning period. If we assume that marginal utility of income goes to zero as $x \to \infty$ and the marginal disutility of effort is bounded away from zero (effort always involves nontrivial disutility), for W large enough the corner solution $l = 0$ becomes optimal. Figure 1 illustrates the standard effect of the accumulation of wealth on work effort: the marginal utility of money eventually falls to the point where $U_x(W, 0) < U_l(W, 0)$. A sufficiently successful pure profit seeker eventually becomes satiated and retires. This need not be true for the entrepreneur who also cares about mastery as in (2), because even if satiation in money occurs, the marginal utility of performance does not vanish and could motivate continued work.[3]

Figure 1. Wealth Accumulation and Monetary Satiation



Mastery seeking also provides a new perspective on the effect that taxes on income or profits have on labor supply. A tax rate of τ leaves the entrepreneur with an objective function $U[(1-\tau) \times f(l), v(l), l]$, and the resulting first-order condition describing the supply of entrepreneurial effort is:

$$(1-\tau) \times U_x \times f' + U_v \times g' = -U_l. \tag{3}$$

[3] We assume a stock of accumulated wealth depreciates less rapidly than a stock of accumulated success or performance. Entrepreneurs value performance today, not past performance and not profit from the current period.

The tax only reduces the monetary return from entrepreneurship, not the performance component. Inclusion of mastery diminishes the reduction in quantity of entrepreneurship to a tax on money income. By contrast, consider a policy reducing the performance utility from entrepreneurship, but not the monetary return. To parallel the case of an income tax, assume this policy change results in a proportional reduction in performance of σ. The entrepreneur's utility function is now $U[f(l), (1-\sigma) \times g(l), l]$ and the first-order condition is:

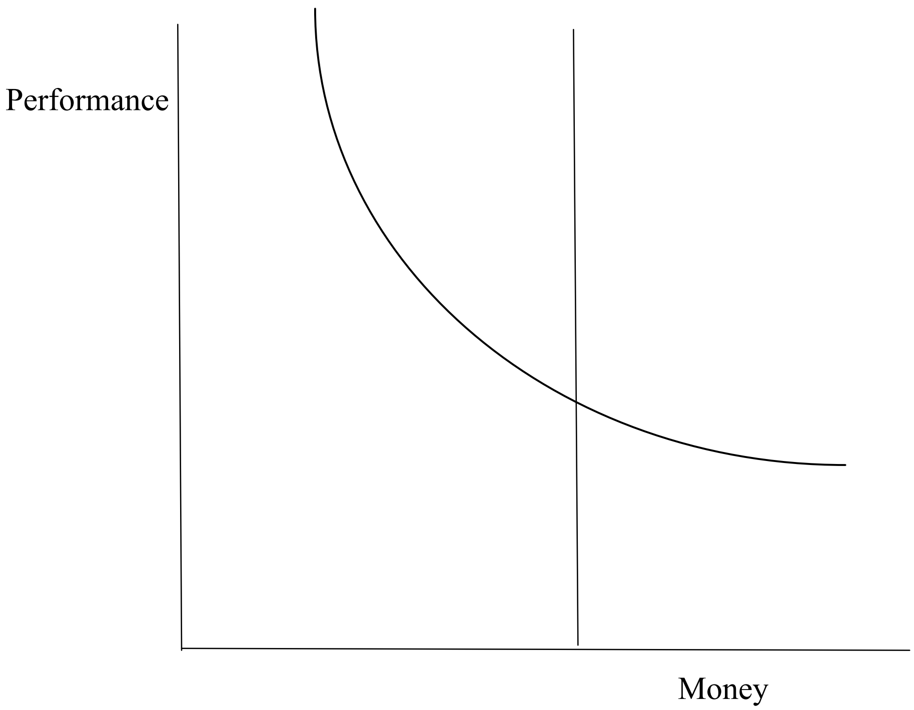
$$U_x \times f' + (1-\sigma) \times U_v \times g' = -U_l. \tag{4}$$

The quantity of entrepreneurship falls even though the monetary return is unaffected. Broadening entrepreneurial motives to include mastery will dampen the impacts of some government policies on entrepreneurship but could unexpectedly strengthen the response to others.

To be clear, we do not claim that all entrepreneurs or managers value mastery. Some may be pure profit seekers, while others may approach pure mastery seekers. Motive heterogeneity among entrepreneurs will drive much of our subsequent discussion. Importantly though, exclusion of the performance motive results in misspecification of the utility function of entrepreneurs as a group.

If we abstract from the effort supply decision and take the institutional environment ($f(\cdot)$ and $g(\cdot)$) as given, indifference curves can further contrast mastery seeking with pure profit seeking. Figure 2 illustrates this, with money on the horizontal axis and performance on the vertical. A pure profit-seeking entrepreneur has vertical indifference curves, whereas the entrepreneur who also cares about mastery might have traditional convex indifference curves. A "pure" mastery seeker (not shown) would have horizontal indifference curves.

Figure 2. Mastery Seeking vs. Profit Seeking



Note: Depicted are the participation constraint indifference curves of a pure profit seeker (vertical) and an entrepreneur who values both success and profit (convex).

The set of entrepreneurs is not fixed; instead, people must decide to start or manage businesses, or pursue other endeavors in life. If the reservation level of utility is U^0, the economy must afford $\mathrm{U}(x, v, l) \geq U^0$ for a given individual to pursue business entrepreneurship. If we interpret the indifference curves of the pure profit-seeking and mastery-seeking entrepreneurs in figure 2 as the U^0 participation constraint for each, it immediately follows that mastery seekers may become entrepreneurs under conditions for which the pure profit seeker would not, and vice versa. Selection into the set of active entrepreneurs may be the more significant economic effect than a change in the level of effort by an entrepreneur.

Mastery seeking will often be difficult to distinguish from profit seeking. Indeed, if sale of multiple units and the price paid affect the validation of performance, mastery may be isomorphic to profit.[4] The close coincidence of profit and mastery may help explain why economists have ignored mastery. Yet profit and mastery are not theoretically or observationally equivalent.

The existence of mastery-seeking entrepreneurs or investors does not imply that mastery will be a goal of all or even some businesses. Businesses engage numerous participants who must agree on common goals. Profit is a means to many different ends, and hence a common goal many might agree on.

The intrinsic success motive may be more relevant for individuals involved in a firm's operations. Outside investors will likely be more interested in profit than the nonpecuniary benefits from producing the best widget, since a business's performance provides less validation of the efforts of investors not involved in day-to-day management. (However, patrons sometimes seem to share in the success of the artists or athletes they support.)

Demsetz and Lehn (1985) argue that agreement on nonprofit goals is more likely to occur when ownership is concentrated. The evidence of autonomy as a motive for the self-employed (see section 4) is consistent with this observation. We expect that companies with more narrowly concentrated ownership—sole proprietorships, partnerships, and privately held companies—will be more likely to exhibit mastery as a goal. Several factors could impact the relative importance of mastery as a goal for a firm over time. For instance, a firm is more likely to be motivated by profit after an initial public offering of stock than before.

[4] If value creation, or the sum of consumer and producer surplus, is the form of validation, success seeking will coincide with efficiency.

4. Evidence of Mastery Seeking Among Entrepreneurs

We now turn to evidence in support of intrinsic motives, specifically mastery seeking, in business and among entrepreneurs. We rely on academic research, literature, and the words and deeds of entrepreneurs.

Intrinsic motives have been recognized as important for entrepreneurs (Shane, Locke, and Collins 2012). Hamilton (2000) finds strong evidence of internal motives in the returns to self-employment (often used as a measure of entrepreneurship in empirical research) in the US. After controlling for other characteristics, Hamilton finds that the self-employed start with lower earnings and experience lower earnings growth relative to paid employment. Moskowitz and Vissing-Jorgensen (2002) find that entrepreneurs invest a large share of their personal portfolios in their own businesses without a higher expected return, resulting in an undiversified investment portfolio that should be less preferable than a more diversified portfolio. Heavily investing in one's own business provides further evidence of an intrinsic motivation. Benz (2009) recently concluded, "Entrepreneurship cannot possibly be understood as a quest for profit alone. Rather, a more accurate description of entrepreneurship is that of a non-profit-seeking activity." Autonomy, or a desire to be one's own boss, has most often been associated with entrepreneurship, and performance can clearly be differentiated from autonomy.

Many business leaders and entrepreneurs argue that profit is not their primary goal. For example, John Mackey, founder and longtime CEO of Whole Foods, sees businesses as having a purpose apart from earning profits. Mackey observes,

> Business has the potential to have a higher purpose that may include making money, but is not restricted to it. . . . And if you think about it, all of the other professions in our society are motivated by a purpose, beyond a narrow interpretation of purpose as restricted to maximizing profits. . . . Every profession has a purpose beyond maximizing profits and so does business. Whole Foods is a grocer, so we're selling high-quality

> natural organic foods for people and helping them to live healthier and longer lives (Palmer 2011, 17–18).

Business leaders and entrepreneurs have made many similar statements. Whether such statements truly reveal a mastery motive (or other motive besides profit) is ambiguous, because a focus on quality, customer service, or values could all be proximate means to achieve profit.

Yet entrepreneurs do offer statements more directly consistent with performance, mastery, success, or excellence as motives independent from profit. Financial information services entrepreneur Michael Bloomberg observes, "Work was, is, and always will be a very big part of my life. I love it. Even today, after toiling for thirty years, I wake up looking forward to practicing my profession, creating something, competing against the best . . . receiving psychic compensation that money can't buy" (1999, 4). Tom Monaghan, founder of Domino's Pizza, observed, "To me, the real substance of life and work is the constant battle to excel . . . I am determined to win, to outstrip our company's best performance and beat the competition" (Krass 1999, 108). Ted Turner, who created the first 24-hour cable news network, remarked, "America is about competition and rising above that competition. That's the basis of what makes our . . . economy and our society tick" (Stossel 1999, 5:06). Steel industry pioneer Charles Schwab attributed his success to "appeal to the American spirit of conquest in my men, the spirit of doing things better than anyone has ever done them before" (Folsom 1996, 63). Cornelius Vanderbilt reveals such a competition motive as well in his remark, "If I could not run a steamship alongside of another man and do it as well as he for twenty percent less than it cost him I would leave the ship" (Folsom 1996, 5).

One of the most significant pieces of evidence of success seeking is that many entrepreneurs continue to work hard at growing and running a business even after making millions or billions of dollars. Instances of entrepreneurs working long after accumulating significant wealth are difficult to reconcile with a purely profit-seeking motive. For example, serial entrepreneur and billionaire Richard Branson has founded over 200 companies, while entertainment executive Barry Diller started the Home Shopping Network after receiving a $140 million payout when he left the Fox television network in 1992, which he had helped found. Entrepreneurs acknowledge something more than profit motivates them. Michael Bloomberg received $10 million when bought out as a partner of Salomon Brothers in 1981 before starting Bloomberg LP. After leaving Salomon, Bloomberg (1999, 3) noted, "Resources weren't a problem. I didn't have to worry about feeding my family." When asked about continuing to work 15-hour days after making millions building Cypress Semiconductors, T. J. Rodgers acknowledged that money was not the driving force: "The fact is, I can take what I have, and I'd never have to work another day in my life. As a matter of fact, I'd never have to spend another day in the same city for the rest of my life" (Stossel 1999, 27:52). In his profile for the 2013 *Forbes* 400 richest Americans, the richest American, Bill Gates, was described as planning to work more "with product managers at Microsoft as rivals like Google and Apple continue to outshine the company in the market." A fortune in excess of $70 billion has not satiated Mr. Gates' desire to see Microsoft products perform well in market competition with rivals.

Relative performance, or a desire to be richer than others, could produce behavior very similar to our success-seeking motive. Ted Turner offered this insight on how *Forbes*'s list of the richest Americans spurs his efforts: "You're on this list, you see, and you want to move up the list. You want to be number one" (Stossel 1999, 2:58). This statement could reflect envy or relative wealth as a motive, but we believe it describes the harnessing of a competitive drive. After all, when Mr. Turner decided to pursue yachting, he skippered the winning yacht in the America's Cup race. Succeeding in competition is a manifestation of the intrinsic mastery motive.

5. The Political Economy of Cronyism, Rent-Seeking, and Mastery Seeking

5.1. The Forms, Costs, and Inevitability of Cronyism

The market economy is the set of economic relations that emerge through voluntary cooperation based on a system of property rights. Government's role is to enforce property rights, adjudicate disputes as needed, and participate in markets only as a purchaser of inputs needed to produce the public goods supporting the market order (e.g., courts, police, national defense). In a competitive market, the existence of multiple sellers vying with one other for each dollar consumers spend ensures that the price of the product, in the long run, tends to settle at the equilibrium level. At this equilibrium, each producer manufactures and sells the optimal amount of the product and breaks even, in the process earning no more than the prevailing rate of interest. While this tendency toward equilibrium exists in every competitive industry, the variability of the real world ensures that it is never actually attained. The desire to earn greater profits and avoid further losses, which drives entrepreneurs to constantly revise their quantity produced, pushes markets toward equilibrium. The never-ending search for profit opportunities is the lifeblood of any competitive industry. This process aligns profit (an extrinsic motivation) with socially beneficial, value-creating activity, and it ensures optimal production of goods at a competitive price.

When the conditions of competitive markets do not hold, particularly if new challengers cannot easily enter, firms can make profits over time. Government possesses an array of means to restrict and limit competition, preserving otherwise temporary profits. Intrusion by government in the market is known as cronyism, or a system in which "the government rigs the market for the benefit of government officials' cronies" (Henderson 2012, 5). All variants of government intervention in the economy typically exhibit some elements of cronyism or favoritism (Holcombe and Castillo 2013); for instance, Communist party officials and their friends received numerous economic privileges (*blat*) not available to others under central planning in the Soviet Union (Smith 1976).

Government intervention can take a number of forms. Mitchell (2012) offers the following taxonomy of the forms of assistance government can offer to businesses: monopoly privileges which legally prevent competitors from entering a market; regulatory privileges, including price controls; direct subsidies from the government, allowing resources to be acquired through coercion as opposed to voluntary exchange; loan guarantees, which both cover losses and allow borrowing at lower interest rates; tax privileges, or avoidance of taxes imposed on other business; bailouts in the event of losses and the guarantee of such bailouts if needed; tariffs and quotas on imports to protect against foreign competitors; and noncompetitive bids on government contracts, allowing favored firms to earn rents on services provided to government. Stigler (1988[1971]) emphasizes that a company can use the powers of government to raise rival businesses' costs and restrict the availability of substitutes for the business's products. We take the prevalence of such crony policies as established.

Market interventions impose a number of significant costs on society. By stifling the forces of competition, market participants suffer a loss in welfare due to the fewer exchanges that result from the restriction in output and the rise in price. But as Tullock (1967) demonstrated, the welfare losses generated by government interventions do not end there. The prospect of higher profits induces firms to expend resources lobbying those in power to bestow these privileges on them. This process of rent-seeking entails lobbying, and the resources devoted to this endeavor, unlike the resources devoted to seeking profits in a market economy, do not produce anything of value. Instead, they are completely wasted, like the resources used to produce a bridge that leads to nowhere.[5]

The ability of businesses to profit through political activities will adversely affect the outputs of entrepreneurship in two ways. First, when profits must be earned through voluntary exchange, entrepreneurs will be alert to new opportunities to better serve consumers (Kirzner 1973), but as attention is directed to rent-seeking, attention to serving consumers will wane (Mitchell 2012). The devotion of a significant chunk of entrepreneurial energy to rent-seeking slows the rate of growth of an economy over the long run. A reduction in the number of entrepreneurs participating in value-creating activities will reduce innovation and technological progress, reducing the rate of growth. Thus, greater government intervention into economic activity and the resulting effort to obtain artificial profits from these interventions reduce the rate of improvement in living standards and the economic well-being of society.

Second, Baumol (1990) observes the potential for new discoveries to be directed toward socially unproductive but privately profitable activities. Unproductive entrepreneurs do not just seek to obtain a known set of regulatory privileges from the government. They also engage in the discovery of new ways of artificially inflating their profits, which they then lobby politicians and regulators to bestow on them.[6] Government policies also affect which entrepreneurs succeed and which fail and are driven from the market. In the market, satisfaction of consumer preferences ultimately determines business survival, but in a sufficiently interventionist economy, government assistance helps some firms survive despite failing to create value, and an inability to escape regulatory or tax burdens can crush firms even if they satisfy consumer preferences.

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[5] In addition to the aforementioned article by Tullock, the classic articles on rent-seeking are Kruger (1974) and Posner (1975). For reviews of the vast literature on this topic see Tollison (1982) and Congleton et al. (2008).
[6] For more on productive and unproductive entrepreneurship see Boettke and Coyne (2003, 2009).

Ability to secure favor from politicians becomes perhaps the most important criterion for the survival for entrepreneurs (Henderson 2012).

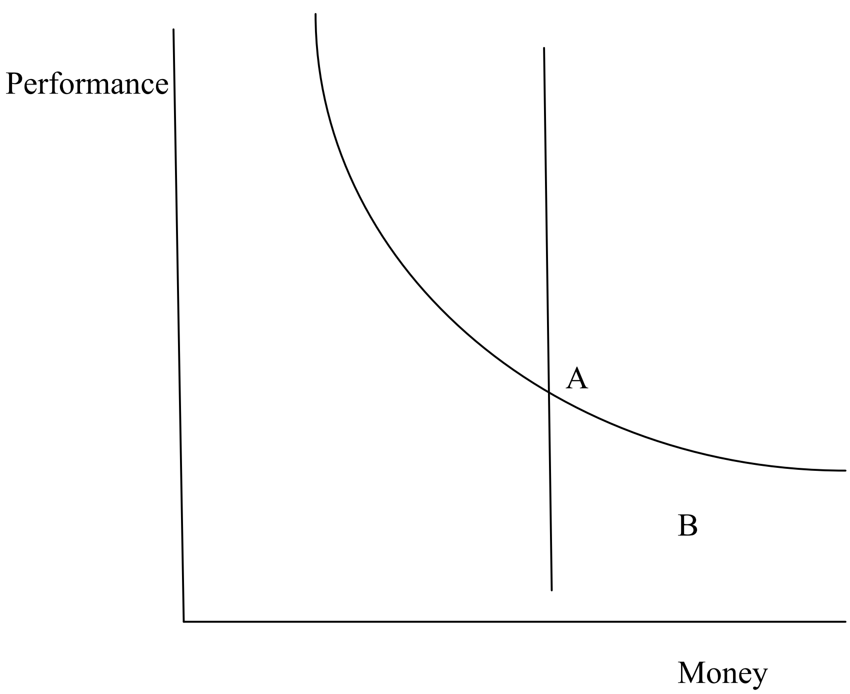
Public choice theory's law of concentrated benefits and diffuse costs also provides an explanation for the establishment and persistence of crony policies. Favors to business destroy more value in the economy than they transfer to favored businesses, but the favored businesses receive significant benefits while the cost to each consumer is small. Favored businesses reward their patrons in government with votes, campaign contributions, and perks, while most consumers are unaware of higher prices for certain goods or services and unlikely to vote against a representative for any specific rent-seeking action. The initial proposal for government restrictions can come either from businesses or politicians, who may act entrepreneurially to offer assistance to businesses in anticipation of reciprocation of the favor. Politicians can also cloak favors behind public interest rationales, garnering some citizen support (Yandle 1983). A balancing of the political benefits and costs by elected representatives systematically favors crony policies.

5.2. Adding Mastery-Seeking Entrepreneurs to the Model

The existence of mastery-seeking entrepreneurs alters this narrative. Many crony policies will disrupt the consumer choice process. As a specific example, consider the regulatory cartelization of an industry, with individual firms awarded exclusive control over specific routes or geographical areas. Such a system will generate substantial costs, as detailed above. Only consumer choice of a firm's product in the face of competition validates performance. Consumer "choice" from the only legal supplier indicates at most market demand and an unwillingness to use unauthorized suppliers. Crony policies in this circumstance may increase profit of the firm with exclusive control but will fail to validate performance.

Pure profit seekers benefit from the crony policy, but mastery seekers may not, as figure 3 illustrates using an indifference curve diagram. Here point A represents the money and performance combination offered by an unregulated market, while B represents the outcomes under a crony policy, with the mastery-seeking entrepreneur worse off with the crony policy. Hence mastery-seeking entrepreneurs and business leaders would oppose consumer choice–restricting policies embraced by profit seekers. Political demand for crony policies will be lower if entrepreneurs care about performance and mastery. Alternatively, crony capitalists are more likely to be profit seekers than mastery seekers.

Figure 3. Government Favors and Mastery Seekers



Most crony policies will yield such a tradeoff between profit and performance, but the reduction in validated performance may vary.[7] A system of localized monopolies would likely generate the least validated performance. By contrast, consider a price advantage in the market created by subsidies, tax credits, or discriminatory taxes. A price advantage increases sales, and the extra sales due to the price advantage will not validate the quality of the product or performance and should produce negligible mastery. Yet some consumers would likely purchase the product even without the subsidy. A small subsidy only modestly infringes on consumer choice and should not completely degrade validated performance. It would be difficult to determine how many or which consumers purchase only because of the subsidy.[8]

The potential existence of entrepreneurs and firms who value mastery raises issues for the concentrated benefits and diffuse costs explanation of crony policies. The existence of cronyism in economies today proves by example that the strength of the mastery motive among entrepreneurs and business leaders is not sufficient to eliminate all gains to politicians from brokering tariffs, loan guarantees, and the like. Yet George Stigler's (1988[1971], 212) proposition, "every industry or occupation that has enough political power to utilize the state will seek to control entry," implies that favoritism should be limited only perhaps by collective action problems among business (Olson 1965). Gordon Tullock (1989) argues that the return on political lobbying for business appears sufficiently high that the relevant puzzle becomes why

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[7] Conversely, consumer purchase over a subsidized rival could generate even more feeling of mastery for an entrepreneur. Private school entrepreneurs might be particularly likely to experience such supernormal mastery.

[8] Self-deception on the part of entrepreneurs could potentially sustain the validation of performance even with the introduction of policy-based nudges, incentives, or mandates. A parallel would be the question of whether a dictator who forces citizens to cheer at his parades can convince himself that the cheering crowds affirm his greatness, and thus gain utility from this approbation. Many dictators have coerced cheering crowds for their public appearances, suggesting perhaps a substantial capacity for self-deception. If self-deception is possible, different crony policies would still appear to differ in the mental evasion required for self-deception. Consider the contrast between a production subsidy and a legal monopoly. An entrepreneur would merely have to deceive himself about the elasticity of demand for his product in the former case to experience validated performance, while the monopolist would need to forget the purchasers' lack of other options.

businesses ever build factories instead of lobbying, or why all markets aren't highly controlled. The existence of entrepreneurs who value validated performance and mastery and who want their products or services judged by the market could provide a partial resolution to Tullock's puzzle.

6. Mastery and Cronyism: Additional Implications

In this section, we consider additional implications for the political economy of cronyism when some potential entrepreneurs are mastery seekers and others pure profit seekers. Specifically, we consider the potential for tipping points and multiple equilibria, plus an alternative channel through which cronyism could reduce economic growth.

6.1. Tipping Points and Cronyism

Mastery seekers, unlike pure profit seekers, care that profits result from outcompeting other sellers rather than from lobbying government. The level of government intervention in markets can affect the supply of entrepreneurial effort, as illustrated in section 3. The reduction in validated performance produced by a given amount of entrepreneurial effort can function similarly to a tax on profits. Crony policies that neither reduce business profits nor the marginal profitability of effort could still reduce the quantity of effort supplied by entrepreneurs, which would pose a puzzle if mastery were not recognized as an entrepreneurial goal.

Crony policies will also affect which types of potential entrepreneurs enter business. The presence of government regulations and privileges can deter mastery-seeking entrepreneurs from entering and drive incumbent mastery seekers out of the market. The potential exists for bandwagon effects, multiple equilibria, and tipping points, providing additional perspective on the dynamics of cronyism. Consider an economy approaching the ideal of a perfect market, with very few interventionist policies in place. Consumer sales validate performance, yielding both a normal profit and mastery, and a large proportion of entrepreneurs value mastery. The net political benefits to elected representatives of restrictions on competition will be low, and possibly even negative, as figure 3 shows.

Suppose that government intervention is established in the economy, perhaps as a residual of government expansion during wartime. As the validation of performance by markets dwindles, mastery seekers will exit and the proportion of profit-seeking entrepreneurs rises. Profit seekers benefit from crony policies, and so the business demand for additional restrictions rises. A vicious cycle is set into motion: government privileges drive out mastery seekers and deter others from starting new businesses, leaving only pure profit seekers behind. This, in turn, increases business lobbying for government intervention even more. Olson (1982) attributes the accumulation of rent-seeking in a society to the progressive organization of interest groups, who then lobby for their own special privileges. A change in the mix of entrepreneurs can augment Olson's dynamic.

The exit of mastery-seeking entrepreneurs will enhance the negative effects of cronyism on economic growth described in section 5.1. Mastery seekers desire validated performance, which arises by actually satisfying the preferences of consumers. Their alertness will focus on appraising and understanding the preferences of consumers and finding ways to reallocate resources to better satisfy these preferences. Profit seekers will pursue either value-creating or rent-enhancing innovations based on the extrinsic rewards. As the level of cronyism rises, profit seekers stop sharpening their skills of reading market conditions and serving consumers, and instead hone their ability to lobby the powerful. The exit of mastery seekers would be part of the decline in entrepreneurship attributed to rent-seeking.

The potential of an equilibrium with extensive government intervention and all profit-seeking entrepreneurs also affects prospects for the deregulation or liberalization of markets. Mastery-seeking entrepreneurs can serve as a force for disrupting political equilibrium in a regulated industry, since they may view validated performance as a substitute for guaranteed crony profit. The passenger ship industry in early America illustrates this: Cornelius Vanderbilt, from whom we offered a quote in section 4 consistent with the mastery motive, made his early fortune by entering existing markets and outcompeting politically favored incumbent businesses (Folsom 1996, 1-15). If mastery seekers exit business altogether, this important source for political change disappears. And after formal deregulation, success in attracting mastery-seeking entrepreneurs into previously government-dominated industries may be critically important in improving the performance (in terms of consumer preference satisfaction) of a deregulated market.

6.2. Cronyism, Mastery, and Growth

The proportion of profit seekers and mastery seekers among entrepreneurs can affect economic growth through another channel. Suppose that in addition to hard work, success in business is also a function of an entrepreneur's ability or skill, whether it be superior alertness, ability to formulate and execute a plan to exploit a profit opportunity, or other margins. The talent of the best entrepreneurs may be developed and not innate, but those pursuing success or closely related goals seem likely to have developed more talent. Presumably, a distribution of such ability will exist across the set of entrepreneurs. If mastery-seeking entrepreneurs are on average more able than profit seekers, and if cronyism reduces the proportion of mastery seekers in the pool of entrepreneurs, then average quality will also fall, further slowing economic discovery and growth.

The theory of a difference in the average ability levels of mastery and profit seekers may seem provocative, but evidence from outstanding performers supports a conjecture that mastery seekers will be better entrepreneurs than profit seekers. Intrinsically motivated individuals are more likely to master their chosen endeavors, be they sports, music, art, or entrepreneurship and business. The differential performance, and underlying skill level, emerges through extended and particularly deliberate practice (Colvin 2008, Gladwell 2008), which often discourages all except individuals with a passion for the endeavor. As Daniel Pink (2009, 77) puts it, "the most successful people, the evidence shows, often aren't directly pursuing conventional measures of success. They're working hard and persisting through difficulties because of their internal desire to control their lives, learn about their world, and accomplish something that endures." For example, artists whose interviews as students revealed a high intrinsic motivation for studying art produced works during their careers judged as superior to the works of students who expressed extrinsic motivations. The National Institutes of Health (NIH) and the Howard Hughes Medical Institute (Hughes Institute) both fund medical research, with NIH selecting scientists for awards based on ability to deliver defined results on time, while the Hughes Institute values long-term success and is more tolerant of failure. NIH-funded scientists were arguably more attuned to extrinsic rewards than the Hughes Institute–funded scientists, but the latter produced high impact research papers at a much higher rate than NIH-funded researchers.[9]

We have not offered a workable way to categorize entrepreneurs as profit or mastery seekers, and therefore we cannot offer any direct evidence regarding the joint distribution of talent and motivation. Yet even if the distribution of talent is uniform, pure profit-seeking entrepreneurs will be more likely to retire after significant financial success. Talented—and consequentially, eventually wealthy—entrepreneurs who continue to work will likely value

[9] These two studies are discussed in Pink (2009, 43–4).

validated performance and business success for its own sake. Because talented entrepreneurs will have greater success, satiation and early retirement will shorten the effective quality of entrepreneurs motivated only by profit.[10] Mastery counters the retirement effect on the quality of entrepreneurs. The more cronyism creates an environment where only profit seekers become entrepreneurs, the more fully the early retirement effect will be felt.

7. Conclusions and Suggestions for Future Extensions

We have argued that some entrepreneurs are motivated by more than just the desire to maximize profits. Entrepreneurs who have a drive to outcompete other entrepreneurs and produce the best product, in the process achieving external validation via the satisfaction of consumer preferences, will care not just about earning money but the conditions under which this money is earned. We have touched on just a few of the implications of this entrepreneurial motive.

One extension of our work would consider the potential for pervasive rent-seeking to alter the very definition of mastery. Consider a parallel to sports. Many athletes value winning competitions without cheating against other top athletes. Yet whether certain types of equipment, training and supplements constitute cheating is socially determined and changes over time. Cronyism could affect what comes to be viewed as mastery, or perhaps more importantly cheating, in business. Do the economic development incentives offered by state and local governments constitute special favors, or normal business practice? The standards and practices of mastery seekers desiring validated performance may change over time.

[10] Let the probability that an entrepreneur is highly talented be α and suppose that entrepreneurs have a two-period career, except that highly talented profit-seeking entrepreneurs retire after only one period. The highly talented entrepreneur is then replaced with a draw from the talent urn. If all entrepreneurs are profit seekers, the equilibrium proportion of highly talented entrepreneurs at any point in time will be $\alpha/(2-\alpha)$.

Economists of all ideological stripes agree on the power of incentives. Many attribute the success of economic freedom and market institutions to aligning incentives with wealth-creating activities. Yet intrinsic motivations are arguably just as important as external incentives, and in some circumstances can be undermined by extrinsic motivations (Deci, Koestner, and Ryan 1999). Some observers go further and criticize rewards generally. Daniel Pink (2009, 9) observes that organizations "continue to pursue practices such as short-term incentive plans and pay-for-performance schemes in the face of mounting evidence that such measures don't work and often do harm." Alfie Kohn (1999, 4) maintains that the doctrine of rewards' "assumptions are misleading and the practices it generates are both intrinsically objectionable and counterproductive."

Our discussion provides a possible reconciliation of such views from psychology with the overwhelming evidence that market institutions lead to prosperity and human flourishing. The extrinsic motivations of markets (profits) do not prevent people from gaining utility from intrinsic (or other nonmonetary) sources. Economic freedom may not lead to a tension between extrinsic and intrinsic motives. Rather, economic freedom affords people the freedom to pursue careers they love or careers that are most profitable. And the mastery motive is tied to consumer choice, with success providing intrinsically motivated persons the resources needed to continue their efforts. Even the market test could have meaning with respect to extrinsic and intrinsic motives. Economists often highlight the evolutionary or selection effects resulting from firms having to meet a market test, with firms unable to generate value for consumers losing control over resources. Yet this process does not deny that the participating entrepreneurs value the validation provided from successfully meeting the ongoing market challenge.

Humans exhibit a wide range of motivations. Businesspeople could be motivated by intrinsic goals other than mastery. For example, some people seem to particularly enjoy politicking, the process of exchanging promises, making deals, and trying to persuade others to assist them in a cause or task. While many people with such talents gravitate toward politics, some may also consider careers in business and entrepreneurship. We have explored the implication of mastery-seeking entrepreneurs, but expanding the universe of entrepreneurial motives could include intrinsically motivated political or dealmaking types. Although the term "political entrepreneur" typically refers to focusing entrepreneurial efforts on politicians instead of consumers, the intrinsically motivated dealmaker could also enter business. Such political entrepreneurs would seem to be the opposite of mastery seekers; born politicians would likely gravitate toward politics when the impersonal forces of the market govern businesses, but would become attractive as managers for firms as negotiating with politicians becomes more important.

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