ENTREPRENEURSHIP AND COMPETITIVE ADVANTAGE: EXAMINING THE CASE OF *ILLYCAFFÈ*

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ABSTRACT

Academically, the dominant view in the entrepreneur field usually focuses on business venturing or, at best, on the large, intensive high technology firms. Particularly in agriculture-related cases, such as that of the coffee roasting industry, few cases in this literature emphasize the significance of the entrepreneurial role to provide a fine illustration of how entrepreneurs can exploit heterogeneous resources in order to capture the competitive advantage. Thus, it is necessary to address these unfilled gaps in this literature. Initially, this paper sophisticates the concept of entrepreneurship in the sense of Knight (1921) and then link this Knightian Entrepreneurship (Langlois 1992; Langlois and Foss 1999; Foss and Klein 2004; Ishikawa 2006; Foss and Ishikawa 2006) with dynamic transaction cost framework (Langlois 1992; Langlois and Foss 1999) within the context of the resource-base view pioneered by Barney (1986) and Rumelt (1984, 1987). Finally, the paper examines the significance of the role of entrepreneurship in the historical development of the coffee roasting company named *illycaffè* by taking our Knightian entrepreneur framework. Through this examination, we draw a number of implications applied not only to business venturing and technology intensive firms, but also to the other industrial sectors.

INTRODUCTION

Academically, the dominant view in the entrepreneur fields is usually focused on the business venturing, small business (e.g. Hofer and Sandberg 1987) or, at best, on the large, high technology intensive firms although Drucker emphasized that the significance of the role of entrepreneurs should be applied to the every part of our economic development (1985). Particularly, in the agriculture-related case such as one in the coffee roasting industry, almost none of us find the systematic study that emphasizes the significance of the role of entrepreneur and provides a fine illustration of how the entrepreneur can capture the competitive advantage. Indeed, notwithstanding there have been the huge contributions to extant entrepreneur literature (e.g. Schumpeter 1942; Kirzner 1973; Baumol 1968, 1990, 1993; Murray and MacMillan 1988; Ivan and Willard 1993), unfortunately the concept of the entrepreneurship seemingly having the general application validity is rarely used to analyze the industry such as the coffee roasting.

Coffee industry analyses often draw on traditional models of Industrial Organization focusing on price adjustment in oligopolic industries. The approach herein suggests that the very dynamics of the market would induce endogenous innovation strategies, usually developed in R&D centers of large firms (Cotterill 1999). In this sense, both the firm and its rivals play a game in which only the end outcome is known in advance, as though entrepreneurs shared a common knowledge.

Thus, by ignoring the role of the entrepreneur as the driving force in the development of capitalist economies, traditional neoclassical models show how a firm's adjustment occurs, but they say nothing about changes in an uncertain world or about a firms' heterogeneity. Thus, to disregard the entrepreneur's dimension is akin to telling a partial history about the behavior of the firm and the dynamic of the economies. It is, therefore, necessary to address this gap in the literature.

Basing on this agenda, this paper designs as follow. Firstly we sophisticate the concept of entrepreneurship in the sense of Knight (1921). Secondly, this Knightian Entrepreneurship is linked (Langlois 1992; Langlois and Foss 1999; Foss and Klein 2004; Ishikawa 2006; Foss and Ishikawa 2006) with dynamic transaction cost framework (Langlois 1992; Langlois and Foss 1999) in the context of the resource-base view pioneered by Barney (1986) and Rumelt (1984, 1987). Thirdly, we examine

the significance of the role of entrepreneurship in the historical development of the coffee roasting company named *illycaffè* by using the Knightian Entrepreneur framework. It is revealed that entrepreneurial judgment determined the first step to potential competitive advantage. The argument here implies our need to understand the analytical effectiveness of the concept of entrepreneurship to enhance it and narrow the focus to discussing the role of firms in the development of the capitalist economies.

Lastly, we can draw a number of implications applied to not only business setting and technology intensive firms but also for the other industrial sectors although our approach presented in this paper never intends directly to generalize its conclusion.

ENTREPRENEURSHIP, DYNAMIC TRANSACTION COST AND HETEROGENEOUS RESOURCE

What is Entrepreneurship?

The role of the entrepreneur in economic activity has long been ignored in orthodox economics although the concept of entrepreneur, originally rooted in Cantillon's work, has emerged since a couple of century ago (Elkjaer 1991). Orthodox economics is mainly focusing on the market competitive equilibrium. This framework sets generally called " price taker " and " perfect knowledge " assumptions; buyer and seller both having "perfect knowledge" in the market adjust his/her response to market prices perfectly and thereby, market equilibrium is instantaneously achieved. Thus, there is no room for time lags and the functional role of entrepreneurs.

Contrast to this orthodox approach, Austrian economists has long placed the entrepreneur's role centrally in their analysis. Generally, it is widely known that Schumpeter conceptualized the entrepreneur as 'innovator', one who carries out new combinations (Schumpeter 1912). He saw the entrepreneur within the Walrasian general-equilibrium system as an agent who is having exogenous force and breaks the static economic circular flow. He called this process 'creative destruction' (1942). While Schumpeter's argument, especially starting with the perfect equilibrium framework where there is inherently no logical role for the entrepreneur, was not clear

cut,[1] Kirzner (1973) are focusing on the entrepreneur as the important driver for the reality-based market where there is always supposed to be disequilibrium.

Indeed, the entrepreneur, in the Kirzner's framework, is interpreted as the arbitrageur who discovers the profit opportunity rooted in the discrepancy among present prices. The knowledge of where to discover this market data and how to open up the possibilities for profit opportunities is what he calls entrepreneurship as "alertness" although mere alertness is not sufficient for characterizing the role of entrepreneur.

Particularly Knight (1921) argues that entrepreneurship consists of judgmental decision making under conditions of uncertainty. Thus, the judgment primarily refers to the process of businessmen forming estimates of future events in situations in which the relevant probability distributions are themselves "uncertainty" (Foss and Ishikawa 2006). Especially it is crucially important that this uncertainty violates the role of the price system (perfect competition equilibrium) as theoretically meaningless with the entrepreneur taking up this role (Ibrahim and Vyakarnam 2003). This implies that entrepreneurship not only represents the judgment that cannot be assessed in terms of marginal product (as in the manner of mainstream economics), but also that the expected output, as judged by an entrepreneur to be produced, is not taken as a *given*. As opposed to Kirznearian entrepreneurship, Knightian entrepreneurship is interpreted as making judgments in relation to the uncertain event, such as defining a new market where no preceding market exists for the entrepreneurs to base their judgments on (Ishikawa 2006), rather than arbitraging the discrepancy among present price in existing market (Casson 2004). More generally, judgment is required "when no obviously correct model or decision rule is available or when relevant data is unreliable or incomplete" (Casson, 1993). Thus, Entrepreneurship should be seen to link to "commercial experimentation" (Hayek 1948; Demsetz 1988; Foss and Klein 2004, Ishikawa 2006; Foss and Ishikawa 2006).

Heterogeneous Expectation and Entrepreneur-specific Judgment

Following Shane (2000), individual entrepreneurs who appear to be in the same situation have different interpretations and, thereby make different judgments to

[1] Indeed, it is noted that the original Schumpeterian model he relied on makes no attempt to deduce how an entrepreneur can make innovations. As Baumol (1993) indicates, what Schumpeter did was to provide a generalized list such as five classes of innovation (Schumpeter 1912).

business opportunity. Indeed, it is believed that experience is the “raw material out of which all expectations are formed” (Lachmann 1956, p. 21), since each expectation is formed as a result of a cumulative process in which previous expectation is revised through the process of “trial and error” (p. 18). This sometimes leads to what Hayek (1945) called “the knowledge of the particular circumstances of time and place.” Thus, the different expectations that trigger entrepreneurial judgment are generally different from entrepreneur to entrepreneur.

Indeed, if entrepreneurs share exactly the same expectations, it is implied that there will be no profit existed, and thereby no change happens in this equilibrium setting because nothing unexpected happens (Hayek 1945). There is no strategic significance in a situation characterized by the absence of change, requiring no plan or no decision (Lewin and Phelan 2002).

Contrast to this situation, it is, therefore, apparent that the emergence of strategic opportunity must be due to the different expectations among the economic actors. It is these differences that determine the different qualities of judgment made by entrepreneurs. Strategic opportunity is, therefore, in the hands of the entrepreneur’s successful judgment. Ultimately it is clear that the real strategic opportunity emerges neither from outside the firm, nor does it even objectively exist, but rather it emerges from the entrepreneur’s “subjective expectation” (Hayek 1948; Ishikawa 2006; Foss and Ishikawa 2006). Under the Knightian uncertainty, entrepreneurial judgment is highly subjective in nature. The more heterogeneous the expectations, the more specific the entrepreneurial judgment becomes.

Dynamic Transaction Cost in Entrepreneurial Judgment and Heterogeneous Resource

In the previous section, it is clear that strategic opportunity emerges from inside the entrepreneur’s expectation. When the entrepreneur pioneers the strategic opportunity, it is inferred that the entrepreneur requires the exploitation of judgment because of its subjective character. Especially it is true when the market cannot provide the right input shaped by entrepreneur’s judgment at right point in time. More over, even if the entrepreneur tries to sell his/her judgment (heterogeneous knowledge) on the market, its significance cannot be sufficiently communicated through the market (Teece 1980, 1982). As Polanyi (1958) taught us, knowledge cannot be always formed or

transmitted in words. In fact, much knowledge, including especially the one shaped by entrepreneur's subjective judgment, may be specific and "tacit" (Hayek 1945; Nonaka 1994). Basing on bounded rationality (Simon 1945[1997]), it can be acquired only "through a time-consuming process of learning by doing" (Langlois and Foss 1999, p.207). This will cause to the extremely high level of what Langlois (1992) has categorized as "dynamic transaction cost[2]" in trying to achieve the market transaction; "the cost of persuading, negotiating, coordinating and teaching outside suppliers" (p.113). Putting different way, there is a specific category of cost that "close[s] the market for entrepreneurial judgment" (Foss, Foss, Klein, and Klein 2005, p. 9). The market cannot act as a substitute for judgment; that is, the market fails.

Thus, in order to gain the profit, entrepreneur has an incentive to exploit the judgment by the entrepreneur's own efforts. In fact, to the extend that the heterogeneity of the judgment is extremely high, the dynamic transaction cost in integrating the judgment into firm would be lower than relying on out side market. In other word, the exploitation of the entrepreneur's knowledge determines the degree of integration in the transaction and the boundary of the firm. This is because the application of the knowledge shaped by entrepreneur judgment, which cannot be easily known by others, would be relatively or efficiently more concentrated than using arms length transaction-based. The intra-firm transfer of entrepreneur's knowledge avoids the need for repeated negotiations, persuasions, coordination, and teaches (Williamson 1975; Teece 1980; Langlois 1992). It is important to notice that this essentially leads the firm specificity-assets, for judgmental decision-making is ultimately decision-making about the heterogeneous way of allocating resources (Foss and Klein 2004; Ishikawa 2006; Foss and Ishikawa 2006). Indeed, the heterogeneity in the resources would be typical because the resource combinations are actually developed in the particular firm through the firm-specific, path-dependent learning process (Dierickx and Cool 1989; Teece, Pisano, and Shuen 1997; Jacobides and Winter 2005).

[2] Originally, Coase (1937) pioneered the first theoretical insight into understanding the concept of transaction costs. He explains that firms exist because "there is a cost of using the price mechanism" (p. 390). The cost is generally called "transaction cost" (Williamson 1975). In a market economy, there are always certain transaction costs such as discovering appropriate prices, negotiating the term and enforcing the contract. Dynamic transaction cost is distinguished from mere transaction cost. While the former emphasizes "the cost of persuading, negotiating, coordinating and teaching" later emphasizes " a cost of using the price mechanism.

Heterogeneous Resource and Competitive advantage

Rumelt (1987) argued that entrepreneurial profit emerges from the difference between the *ex post* value and the *ex ante* cost of resource combination. Because if we hypothesize expectational equilibrium, that is, *ex ante* cost equals expected *ex post* value, then it will be soon clear that profit is zero (Barney 1986). Thus, we can conjecture that the profit is the result of entrepreneurial judgment in *ex ante* uncertainty. Similar to Rumelt' argument, Barney (1986) argued that suppose all the resources for firm level strategy in the ultimate sense must be purchased in the external factor market, there would emerge no economic profit from this market, while economic profit could possibly be gained if the entrepreneur could control heterogeneous resources that did not previously exist in the factor market.

Since entrepreneur-specific judgment is not a thing that is completely tradable on the market, the factor markets (or competitors) cannot easily evaluate the entrepreneur's expected value of resources (in other words, the discounted net present values as seen by the supply side of factor markets are likely to differ from the entrepreneur's appraisal) and even the factor markets may be rarely able to place a value on entrepreneurial judgment *per se* (Schumpeter 1912; Knight 1921; Kirzner 1973).

On the other side, the force to imitate this resource combination is weakened by the fact that knowledge shaping the resource combinations is not easily conveyed through the market. Firm level resources initiated by entrepreneur judgment are causally ambiguous (Lippman and Rumelt 1982; Rumelt 1984), are highly characterized by complexity and interconnectedness among the resources and, thereby, are inelastic in supply (Barney and Arikan 2001). As Resource based scholar taught us, the heterogeneous resource are associated with different efficiency (Barney and Peteraf 2003) and contributed to gain the superior profit; in other word, competitive advantage (Barney 1991). However, without the entrepreneurial judgment, firm cannot gain the competitive advantage.

EXAMINING THE CASE OF *ILLYCAFFÈ*[3]

An Analytical focus on this case

Following Knightian Entrepreneurship presented here, entrepreneur transforms his/her specific judgmental knowledge into heterogeneous resource as potential competitive advantage. This paper presents a discussion on the role of the entrepreneur in driving competitive advantage. Although many questions remain unanswered, such as how to formalize the concept of the entrepreneur at the operational level, still it should be useful to analyze the successful entrepreneur's behavior, here taking the case in *illycaffè.*

It is inferred that in this case, the competitive advantage is certainly associated with Dr Ernesto Illy's capacity to carry out actions that differentiate him from other entrepreneurs in the sector. This paper will focus two factors which explain the great success of *illycaffè* and which seem to be relevant in defining the singularity of successful entrepreneur's judgment: Dr Illy's specific knowledge of the inherent features of roast and grind coffee production and his novel judgment in direct sales to his customers.

illycaffè and Dr Ernesto Illy's strategy

illycaffè is inserted in the coffee roasting and grinding industry, which generally requires simple production technology and low set-up costs. Its production process encompasses roasting and grinding green coffee beans and packaging them to be later consumed filtered or espresso. Most companies in this sector are characterized with labor intensive, having a minimum capital investment. The gains of scale, mainly with packaging systems, make the sector highly concentrated. Thus both the easy access into the industry and the clustering process allow companies of different sizes to join the industry, which is thereby characterized as an oligopoly with the presence of a competitive fringe. Now the number of companies can range from 50 in Germany to around 400 in Japan and one thousand in Italy (Sutton 1991).

In 1933, Francesco Illy established *illycaffè*. It is headquartered in Trieste, Italy. Dr Ernesto Illy who is Francesco Illy's son inherited the company in 1956 and was its CEO until early 2000, when his son Andréa Illy took over the business. When Dr

[3] Interview conducted with Dr. Ernesto Illy on March 9 2006.

Ernesto Illy left, *illycaffé* had some 500 employees, a turnover of over € 200 million and operations in almost 70 countries (Neves, Saes, Resende 2003).

Understanding the characteristics determining the quality of the coffee (aroma, flavor and stability) started to be the main target of the company when Dr Ernesto Illy realized the full economic potential of a market opportunity in the production of exceptional quality coffee, one not yet anticipated, or not even imagined by other market competitors. Dr Ernesto Illy believed that, like wine or even water, coffee should not be perceived merely as a commodity, but rather, it should meet consumers' differentiated demands.

Positioning a single product in a high aggregated value market with a single brand meant high stakes for the company. For one reason, the green coffee input is highly unstable, depending on ideal climate conditions, adequate nutrition and careful handling of the crops. In other words, the quality of the product requires a close coordination with the sector at the upstream end of the company. And, for another reason, most coffee producers are from poor countries with precarious conditions for educations, production techniques and capital.

The production of espresso relies on the supply of raw material within a defined, stable standard. Coffee, as a commodity, can be purchased through dealers, but the ordinary classification makes the achievement of a desired quality standard very expensive. And this was Dr Ernesto Illy's major dilemma: how to resolve this is now his major strategy.

Heterogeneous Resources exploited by illycaffè: Electronic sorting of machine

A random but recurring event led Dr Ernesto Illy invest in the research and development of a machine capable to sort high quality green coffee beans.
From time to time, high quality coffee coming from his African produced a foul odor, a characteristic that consumers resented. To bring his strategy into fruition, Dr Ernesto Illy had to solve that puzzle at any cost. After years of investment in research, associated German scientists discovered that the problem arose because the eggs of an insect deposited on the ripe fruits produced a disease that provoked this negative effect. Though it was actually a rather hard problem to work out, those scientists eventually were able to find out that those fruits could be eliminated from the production process in the factory if a selection could be made using ultra violet rays,

since contamination produces a fluorescent stain in the coffee beans.

No such equipment was available at that time and developing it would take years of investigation and a huge amount of capital. In fact, the type of research lab required involved a large, highly uncertain investment. Even though Dr Ernesto Illy had confidence to grasp this new profit opportunity, this seemed totally an abnormal decision, comparing to others who considered this opportunity as mere irresponsibility. This led, similar to Knightian entrepreneur framework, Dr Ernesto Illy had to exploit the judgment by his own effort.

Indeed, He understood that the quality of the product should not be hampered by faulty inputs. In the Arabica species,[4] bean contamination was observed to produce an amplification of the quantity of volatile aromas that dissolve when coffee is processed through pressurization. Pressure increases the solubility of all the gases, which then concentrate those aromas. A huge amplification occurs: one grain contaminates 10 kilos of coffee.

That observation originated the decision to control quality based on science and not on human analyses.[5] Research thus involved an associated English company called Sortex, which developed a machine to select in *natura* beans using an ultra refined technique (near infrared spectrophotometer), thus causing the elimination of coffee beans contaminated by microorganisms that affect the quality of the beverage. The research team worked three years with spectrophotometric methods that allowed the product to be sound and free of all defects. To create a machine that selects 400 beans per second involves a new vision in business. In the words of Dr Illy, “that is like having a Stradivarius. Though it costs 2 million dollars, if not well played, it will only be enjoyed by cats”. And that means one has to learn how to use the instruments to reach high levels of utilization.

illycaffè was granted the patent of that machine and today all major ground and roast

[4] There are many coffee species and varieties. The most economically important species used in production are: Coffea Arabica generally called "Arabica" coffee, and C. Canephora, called "Robusta" coffee. The former is better known for its quality and superior price. The enterprise illycaffè use only the Arabica specie. It is mainly grown in Brazil, Colombia, Central America, Kenya and Tanzania. The latter is grown in a larger scale in Vietnam, Brazil, Ivory Coast, Angola, Uganda, India and several other countries in Africa, Asia and Oceania (Saes and Farina 1999).

[5] Traditionally, coffee classification is made by an expert that counts the quantity of faults seen in a sample of 300 grams of green coffee beans.

firms use this process to classify coffee beans. This strategy illustrates how the entrepreneur exploits his/her specific knowledge, which is in turn shaped by judgment. The innovations idealized by entrepreneurs require human or physical specific assets that are not readily available on the market. Thus the limits of the firm must be understood within the context of the passage of time. In the case in point, the capability required to accomplish the innovation strategies could not be found on the market, and hence the need to vertically integrate the electronic coffee bean sorter.[6]

In the development of *illycaffè*, this electronic sorting machine had long been placed on the illy's competitive advantage.

Dr Ernesto Illy's new way to manage green beans supply in Brazil

The same motivation– beverage quality– pushed Dr Ernesto Illy into a new way to ensure the supply of coffee according to his needs. The coffee supplier in Brazil is a strategically significant for *illycaffè* and, besides being the largest producer worldwide; it is also responsible for approximately 65% to 70% of the blend of *illycaffè*'s coffee.

The main reason accounting for this fact is that Brazil is one of the few countries using dry-processes in production. Such practice is essential to the composition of the espresso, since sun-dried coffee contains a higher content of sugar, which provides more aroma and body to the blend, and which comes from the migration of the sugars of the gum to the grain (Neves, Saes and Rezende, 2002).

Although *illycaffè*'s presence in Brazil is traced back to 1933, it was only in the 1990s when it started to increase operations with green beans. Before that period, the Brazilian market was regulated by the Brazilian Institute for Coffee (IBC), and the exportation of the produce was made by certified exporters who mixed coffees from different qualities and regions, thus making the achievement of the desired pattern too expensive. Out of 10 to 12 coffee samples received, only 1 used to be approved for purchase.

In the early 1990s, depressed coffee prices in the international market reflected in

[6] The research center actively pursued new methods of objective evaluation regarding the quality of the beverage. The analysis of the beverage is usually made through the sniffing and cup tasting techniques performed by experts. But *illycaffè* went further to create the "Aromalab" in 1998, which provided for the analytical identification of coffee chemical compounds, thus avoiding the subjectivity factor.

significant falls in the quality of the Brazilian coffee causing *illycaffè* to have to address supply difficulties. In 1989, out of the 36 samples examined by *illycaffè*, not a single one was approved.

By and large, the coffee trading practice in Brazil did not value product with superior quality. As a result, producers stopped making investments and an adverse selection occurred, with the prevalence of coffee with a large number of defects.

Supply hitch concerns fueled Dr Ernesto Illy's decision to conduct an *in loco* observation. While visiting coffee estates in Brazil, though he became quite surprised at the high quality of the coffee, he also felt frustrated with harvest and processing methods, as well as with the mixtures of beans, which all resulted in the low quality of the product.

Dr Ernesto Illy saw the opportunity to explore a new way to obtain the raw material in order to pursue his strategy of producing high quality espresso. But, how could he do it? He had a dilemma: How could he coordinate the Brazilian downstream supply chain (production, processing and trade)? What could he do to induce traders to modify the way the bought coffee beans? How could persuade growers to invest in high quality if the market did not provide the right signalization? The usual practice in the market was not to pay for quality. Indeed, traders' comparative advantage relied solely on buying the cheapest coffee bean. How would Dr Ernesto Illy show that all of the chain's agents could earn more if growers produced high quality?

Trusting his judgment, Dr Ernesto Illy endeavored to solve the difficult task of convincing all of the chain agents to accept his vision, mainly taking into account the path dependence in the process of acquiring the coffee beans.

Dr Ernesto Illy's solution came in the new way of managing suppliers in order to obtain high quality raw material: an annual quality contest," the Brazilian Award for Quality of the Espresso", in 1991. The event had been born out of his observation of the strategy of the Italian fashion designer Ermenegildo Zegna, whose difficulty finding quality cashmere had led him to launch a contest to financially motivate the communities offering the best fabric (L'espresso *illycaffè* 2006).

The annual Brazilian contest aims to identify the best gourmet coffees, which are purchased by the company after receiving a premium of 25% to 30% above the international prices of good quality coffee.

The contest was an innovative solution that allowed creating new way of managing suppliers. Whereas in the traditional classification system the whole bulk of information on raw material quality was completely lost, the annual quality contest enabled the company to identify the growers present in the transaction and offer the right incentives (Zylbersztajn 1996).

Now the *illycaffè* contest was a landmark in Brazilian coffee production; it trigged a dramatic change in the pattern of competition. Brazilian producers realized that their average-quality coffee could actually obtain premium prices on the international market so long as better harvest practices and new marketing strategies were adopted. The number of candidates interested in supplying to *illycaffè* becomes higher every year. Through a multiplying effect, other contests have appeared and regions that usually produced low-quality beans seek technology for their processes (Saes and Nakazone 2003). Dr Ernesto Illy's strategy to motivate growers to produce quality solved the problem of adverse selection.

Encouraged by the results of the contest, the Brazilian government announced policies to support its coffee growers and regional associations joined the quality marathon. *illycaffè* has established strong alliances with cooperatives, associations, government bodies, the coffee roasting industry, as well as with the scientific and academic communities dedicated to the study of coffee.

In both examples, the development of a machine to sort green coffee beans and based on a new way to manage the supply chain, provided above, the entrepreneurial judgment led to the firm's competitive advantage.

IMPLICATIONS AND DISCUSSIONS FROM *ILLYCAFFÈ*'S ENTREPRENEURSHIP

The Conceptual Effectiveness of Entrepreneurship

Through examining the rare case in the entrepreneur literature, our aim in this paper intends to argue the significance of entrepreneurship to not only business venturing and technology intensive firms but also for the other service sectors, rather than directly generalize the validity of Knightian entrepreneur framework. Whereas this paper focused only a single case, still fruitful implications to the real firm's behavior

such as business policymaking can be possibly gained.

The Significant of Entrepreneur-specific Judgment

In examining the case of *illycaffè*, it is clear that entrepreneurial judgment determined the first step on the road to potential competitive advantage. It is implied that the source of competitive advantage is derived from entrepreneur's judgment. Indeed, it was true that Dr Ernesto Illy's specific judgment seemed totally implausible at first, however this, as a result, allowed *illycaffè* to have the heterogonous resources basing the competitive advantage and it become the strong barrier to the competition. Strategically speaking, this means that the *ex ante* limits to competition are one of the most important dimensions in strategic activities. In other words, there is always logically first the superior judgment in forming the competitive advantage.

Despite our inability to know which judgments will bring competitive advantage, it nonetheless remains important to understand that the entrepreneur is the endogenous driver of the successful firm.

No panacea for successful Entrepreneurial Judgment, but no choice

Indeed, it is also noted that even in *ex ante* it is by no means sure which judgment will bring competitive advantage. Thus, this successful case is not implied that whatever decisions are made profit is automatically gained. Rather, the real problem is that any successful entrepreneur's judgment may be like 'needles in a haystack of mistakes' (Denrell, Fang and Winter 2003). There is no doubt that in a world of uncertainty some entrepreneurial judgments will fail while others will succeed, some even beyond expectations. However, unless entrepreneurial judgment is forged under circumstances of uncertainty *unknown* to others, the uniqueness of this judgment holds no special role. As we can learn from the case of Dr Ernesto Illy, it was true that Entrepreneur must sometimes judge when he believed that he farced the profit opportunities that no one really realized. Firm's innovation should be understood in this way.

Positive Influence of the Entrepreneur's initial knowledge

In order to understand the nature of the decision based on uncertainty, we must examine the entrepreneur's initial knowledge. Since different expectation is gained through learning and proceeding experience, superior knowledge forming judgment will increase entrepreneur's chance of success. As we have seen, when Dr Ernesto Illy

took over as *illycaffé'*s C.E.O., he already had a sound knowledge of the coffee market, consumers and his enterprise. This knowledge, fruit of his experience in the enterprise, was one of the factors that give him a better basis for judgment. This made him chose differently from others.

The Further development for Entrepreneurial literature

Not only in the practice, but also in the academic field, it is now clear that the fruitful insights into a firm's behavior can be gained by bringing entrepreneurial theory into a more central role. Although this article focuses particularly on the entrepreneur's judgment, it also showed that an important relation exists between the entrepreneur-specific judgment and the appropriate types of "governance structure" in the sense Williamson (1975). The entrepreneur-specific knowledge tends to increase the vertical integration since entrepreneurs do not find on the market the necessary capability to accomplish their innovation strategies.

illycaffè's experience indicated that alternative supply chain structures will depend on the cost of implementing them. This finding is implied that our approach presents a greater opportunity to bridge the entrepreneurship approach with theory of firm initiated by Neo Institutional economists. Therefore, it is hoped that this will stimulate a more comprehensive understanding of the strategic behavior of the firm.

SUMMARY AND CONCLUSION

This paper examined the real concept of entrepreneurship through the case study of *illycaffè*. It is clear that the competitive advantage of *illycaffè* is illustrated as a result of entrepreneurial judgment. Indeed, our approach presented in this paper intends only to possess some implications to business policy rather than directly generalize its conclusion.

The *illycaffè* case study reconfirmed our understanding of the importance of the entrepreneur concept showing that *illycaffè'*s source of competitive advantage derived from Dr Illy's judgment. His entrepreneur vision allowed *illycaffè* to base its competitive advantage on heterogonous resources not available in the market that became the strongest barrier to competition.

This paper revealed that judgment based on superior knowledge in critical areas

increases an entrepreneur’s chance of success. In essence, it was Dr Ernesto Illy’s sound knowledge of the coffee market, consumers and his enterprise that refined his ability to judge marketing strategies in a world of uncertainty. It is also showed an important relation exists between the entrepreneur-specific judgment and the appropriate types of “governance structure”. The entrepreneur-specific knowledge tends to increase the vertical integration when the firm cannot find on the market the necessary capability to accomplish its innovation strategies. Although further research is still necessary to address this specific issue, this finding is an opportunity to bridge the entrepreneurship approach with theory of firm that was initiated by Neo Institutional economists.

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