



The Dual Nature of Failure in Entrepreneurship

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Abstract

It is well-known that 90% of startups fail (Forbes). Then, how do entrepreneurs respond when they face the many failures that they inevitably encounter? This article outlines the specific impact failure has on entrepreneurs and the factors that shape how people respond to failure. This research paper uses a literature review, case study analysis, and a comparison and contrast of different responses to failure by analyzing existing qualitative research. This paper's key findings reveal that entrepreneurial failure can lead to improved psychological resilience, social network and relationship building, and problem-solving capabilities. However, failure also causes substantial mental and emotional challenges. Businesses and entrepreneurs should use these insights to create an environment that accepts failures and views them as valuable learning opportunities rather than sources of discouragement, and to fully extract and learn from failure once they experience it.



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1. Introduction

It is well known that a majority of start-up businesses fail, with statistics showing that new ventures fail within the first few years of operating (Shepherd 2016). Many know of the statistic that 90% of startups fail (Forbes). As a result, companies and entrepreneurs are increasingly recognizing that failure is not only inevitable but sometimes even something to be celebrated, seen in cultures like Silicon Valley. This contrasts with past perspectives on failure, where entrepreneurs would try to avoid or hide it. This change in perspective is driven by changes in business culture and a more open approach to professional transparency. Nonetheless, entrepreneurs and businesses need to comprehend the dynamics and effects that failure has on entrepreneurial development, specifically, the entrepreneur's growth, skills, mindset, and future ventures. Additionally, the effects of failure on entrepreneurial development are complex, in that it is not always beneficial, and vary in how detrimental or beneficial it is to the entrepreneur due to factors such as individual characteristics, the context, and the nature of the failure, varying from case to case.

To better understand this complex dynamic, this paper aims to answer the question of how failure impacts entrepreneurs and the extent to which they utilize it. The central thesis of this paper is that while failure in entrepreneurship can lead to increased psychological resilience, valuable network and relationship building, and enhanced problem-solving capabilities, it also carries a significant psychological and emotional impact that must be carefully managed through appropriate support systems, learning frameworks, and cultural attitudes to maximize positive outcomes and minimize destructive consequences. This paper is important to comprehend the effects of failure further through reflection to utilize it in a way that benefits entrepreneurs rather than dejects them. Entrepreneurs should aim to understand the different results failure can have using the information from this paper, such that they can change their mindsets to extract the most valuable lessons from failure, especially since not all entrepreneurs can afford to learn from multiple failures.

2. Findings

Psychological and Personal Development

Research suggests that failure contributes significantly to entrepreneurs' psychological and personal development, building and developing character traits that aid their effectiveness in future entrepreneurial endeavors. Specifically, entrepreneurial failure is essential for building resilience and maintaining an optimistic entrepreneurial outlook. Studies have shown that entrepreneurs gain valuable insights from unsuccessful ventures through experiential learning, and their perspective on failure becomes more favorable as they accumulate experience with launching companies and experiencing business closures (Politis & Gabrielsson, 2009). According to Kolb's (1984) theory of experiential learning, experiential learning is the process by which an individual must go through concrete experience, reflective observation, abstract conceptualization, and active experimentation in order to learn from failure (Lattacher & Wdowiak, 2020). The psychological challenges entrepreneurs face when experiencing failure also create growth opportunities that may not emerge otherwise when entrepreneurs succeed

(Shepherd, 2003). For instance, entrepreneurs who successfully navigate failure develop enhanced emotional regulation capabilities, stress management skills, and the confidence that they can survive and recover from adversity (Hayward et. al, 2010). Conversely, entrepreneurs who encounter fewer failures may have fewer opportunities to develop these specific characteristics, which may impact their future endeavors.

One of the most important psychological benefits of failure is resilience and grit. Entrepreneurial resilience is defined as “the ability of entrepreneurs to anticipate potential threats, to cope effectively with unexpected events, and to adapt to changes to become stronger than before. This ability develops over time, depends on prior (positive and negative) experience, and is influenced by various individual as well as situational factors” (Duchek 434). This resilience helps diminish the anxiety around potential setbacks, improves the ability to extract lessons from experiences, and encourages the motivation to launch new ventures (Kaur 3). Entrepreneurial resilience is an important psychological characteristic that allows entrepreneurs to take appropriate risks in future ventures without being paralyzed by fear of failure.

Grit is defined as “a combination of perseverance through adversity and a focus on long-term goals over time”(Duckworth et al., 2007; Kwapisz et. al, 2022). Grit is particularly relevant, as the sustained passion and perseverance towards long-term goals despite setbacks provides entrepreneurs with the ability to continue, increasing their chances at success. Conversely, however, failure can also cause entrepreneurs to give up, and in many cases, it does not always build resilience. A complex interplay of internal and external factors, such as individual mindset, emotional regulation, social support, and past experiences, influences whether or not a person will be resilient or give up. Mindsets, such as an entrepreneurial mindset, or growth mindset can contribute significantly to the resilience of an entrepreneur.

Optimism and a growth mindset represent additional personality factors that significantly influence failure responses. Growth mindset, the belief that abilities and intelligence can be developed through effort and learning, enables entrepreneurs to view failure as feedback and development opportunities rather than proof of fixed limitations (Dweck 2006). Optimistic entrepreneurs are more likely to view failure as temporary and specific rather than permanent and pervasive, leading to faster recovery and maintained motivation. Traits like growth mindset optimism help entrepreneurs maintain hope and motivation even in the face of significant setbacks. Research by Dweck (2006) demonstrates that individuals with growth mindsets show superior performance following setbacks and are more likely to persist in the face of challenges. Reid and Ferguson (2011) found that among university students studying engineering, those who demonstrated a growth mindset showed higher comfort levels with uncertainty and better ability to recognize opportunities. Response to failure is dependent on the entrepreneur and how their personality traits and characteristics vary, leading to different reactions. However, this research also shows the importance of self-awareness regarding one’s mindset, allowing for change in response to failure, even if entrepreneurs are initially discouraged by it. As long as an entrepreneur can recognize their mindset and are open to change, they can become more resilient to failure and eventually learn from it. However, a growth mindset is not a necessary aspect for entrepreneurs to learn from their failures. Individuals without a growth mindset are still able to learn from failures and grow experience, although they may have a more negative and pessimistic reaction to failure, which may hinder progress.

Network and Relationship Building

Counterintuitively, entrepreneurial failure can build professional networks that prove beneficial for activities such as hiring senior leadership. For instance, entrepreneurs with more extensive founding experience, even if they had ventures that failed, are better positioned to receive investment funding and achieve more favorable company valuations when working with venture capital firms (Hsu 2004). Additionally, investor and stakeholder relationships can be strengthened through failure experiences when entrepreneurs handle the situation with transparency, accountability, and confidence (Hayward et. al 2010). This can look like clear communication with investors, taking responsibility for outcomes, and proactively outlining next steps for the business. Investors and stakeholders who observe how entrepreneurs manage failure often develop increased confidence in their character and leadership capabilities, potentially leading to future investment opportunities or business partnerships.

The opposite can happen as well, where entrepreneurs do not take accountability for their mistakes, and their investors lose faith in the entrepreneur, causing their companies to end up going bankrupt. This also plays a part in corporate social responsibility, as employees are likely to be less motivated and productive in a workplace that does not value integrity. One example of this is Netflix's Qwikster situation in 2011, where Netflix separated its DVD-by-mail service from its streaming service and renamed the DVD service "Qwikster", which increased costs for customers and required managing two different accounts. CEO Reed Hastings apologized for their decision to increase the price, but did not take any action to improve the situation, causing outrage from consumers to blow up and their stock prices ended up plummeting (Freeland 2013). This additionally shows that the acceptance of failure sometimes is not enough, and entrepreneurs must take responsibility for it, as opposed to just acknowledging it. Despite the rise of a culture where failure is generally accepted, entrepreneurs must still understand the detrimental nature of failure. This further emphasizes the importance of reflection on failure, as otherwise, it can lead to ineffective decision-making habits and result in recurring missteps (Taylor 2017). Reflection is also crucial as it allows for accurate attribution of causes, distinguishes between controllable and uncontrollable factors, and facilitates learning.

Innovation and Creative Problem Solving

Failure can also contribute to innovation and creative problem solving. Necessity driven innovation emerges when entrepreneurs must find creative solutions to overcome their experiences of failure. Limited resources, damaged reputations, or restricted access to traditional opportunities force entrepreneurs to develop innovative approaches that they might not have otherwise considered. As a result of this newfound innovation, entrepreneurs perceive themselves as "luckier" and can lead to breakthrough solutions that provide competitive advantages in future ventures (Taylor 2017). In a conversation with Tony Hsieh, CEO of Zappo, he explained that "people who self-described themselves as "lucky" picked up more hidden clues in a quiz [...]Why? We think it is because they approach the world with an open and optimistic mind that enables them to see unexpected opportunities more readily"(Taylor 2017). Additionally, this suggests that more failures and setbacks can improve luck and success, as increased attempts at ventures can create more opportunities, and therefore, lead to more

perceived luck. The case of James Dyson illustrates this phenomenon perfectly. Over five years, Dyson created 5,127 different prototypes before finally releasing his successful bagless vacuum cleaner, the Dyson Dual Cyclone Vacuum, in 1993. Additionally, after experiencing rejection from established vacuum manufacturers and facing significant financial pressure, Dyson was forced to develop innovative manufacturing and distribution approaches that ultimately became core competitive advantages for his company. Dyson later said that embracing failure was essential to life (Crosbie, 2025).

However, not every entrepreneur is able to experience what Dyson was able to. One reason could be the lack of capital. If an entrepreneur runs out of money after failing once, they may be prohibited from encountering various opportunities and developing innovative problem-solving. Additionally, the necessity for innovation can sometimes limit options instead of promoting creativity, as people may not be able to innovate with limited resources and opportunities.

Negatives: Psychological and Emotional Impact

The psychological and emotional consequences of entrepreneurial failure can be profound and long lasting, affecting entrepreneurs' mental health, self image, and overall well-being. These psychological impacts are often ignored in discussions of entrepreneurial failure but can be utilized in a way that leads to recovery and future success once understood. This can be demonstrated through Shepherd's (2016) self-determination theory. His self-determination theory explains "an individual's psychological well-being", where individuals need to have their three core psychological needs for competence, relatedness and autonomy. When entrepreneurial ventures satisfy these needs, they significantly enhance the entrepreneur's psychological well being, but it also generates more grief when these needs are disrupted by failure. As Figure 1 demonstrates, when an entrepreneurial venture fails to fulfill these three psychological needs for competence, autonomy, and relatedness, it can lead to a drop in psychological well-being and the motivation to persevere. Grief over entrepreneurial failure can lead to mental health issues and eventually discourage entrepreneurs from pursuing future ventures. Converting failure into future success and learning experiences require practical strategies that address the consequences of failure and the process of building new ventures or opportunities. When a project fails, and it undermines an individual's psychological needs, grief is generated and it reduces their drive to progress forward and commit effort into future projects (Shepherd and Cardon 2009). However, a business can solve this issue by gradually re-engaging the individual through other projects of equal or greater psychological value to what was lost (Shepherd et. al 2016). And so, the challenge businesses must face is to develop practical strategies which can overcome the emotional impact that failure can have to maintain employee motivation. Additionally, entrepreneurial failure can have a large impact on self-confidence, as individuals tend to incorporate these ventures' projections as part of their self-image. As a result, in the event that the venture fails, the entrepreneur's self-image can be damaged.



FIGURE 2.1: A self-determination model of grief over entrepreneurial failure

Figure 1: Self-determination model of grief over entrepreneurial failure

According to Doyle, Domino's CEO, companies and entrepreneurs face two primary obstacles that prevent greater transparency regarding entrepreneurial failure (Taylor 2017). He identifies the first obstacle as omission bias, the phenomenon where individuals with innovative ideas avoid implementation due to concerns that potential failure could negatively impact their career. The second obstacle involves overcoming loss aversion, part of the prospect theory, which is people's inclination to adopt defensive strategies focused on avoiding defeat rather than pursuing victory, since most individuals feel that losing is twice as psychologically painful as winning is pleasurable (Taylor 2017).

Prospect Theory

Prospect theory provides valuable insights into the psychological impact of entrepreneurial failure. According to prospect theory, humans value losses and gains disproportionately. People prefer to avoid a potential loss rather than risk a potential gain, as depicted in Figure 2. The X-axis shows outcomes of a certain situation, with the gains on the right and losses on the left. The Y-axis demonstrates subjective utility, or the satisfaction or benefit a person feels. In the figure is an S-shaped curve, which is steeper for losses than it is for gains, which demonstrates the loss aversion aspect of prospect theory. This steepness reflects that losing \$100 feels worse than gaining \$100 feels good. This loss aversion principle suggests that entrepreneurs experience failure more intensely than they experience equivalent successes, potentially explaining why some entrepreneurs struggle to recover psychologically from failure. The reference dependence aspect of prospect theory is particularly relevant to understanding entrepreneurs' psychological responses to failure. In the specific figure, the reference point is located at the origin of the graph. However, people evaluate outcomes relative to a reference point that could differ from that point. For instance, certain individuals may expect more gains, and consequently, gains and losses are measured at a higher point on the graph, which results in different utility outcomes depending on the circumstance. Consequently, entrepreneurs who have experienced initial success may find subsequent failures more psychologically devastating than entrepreneurs who have maintained more modest expectations.

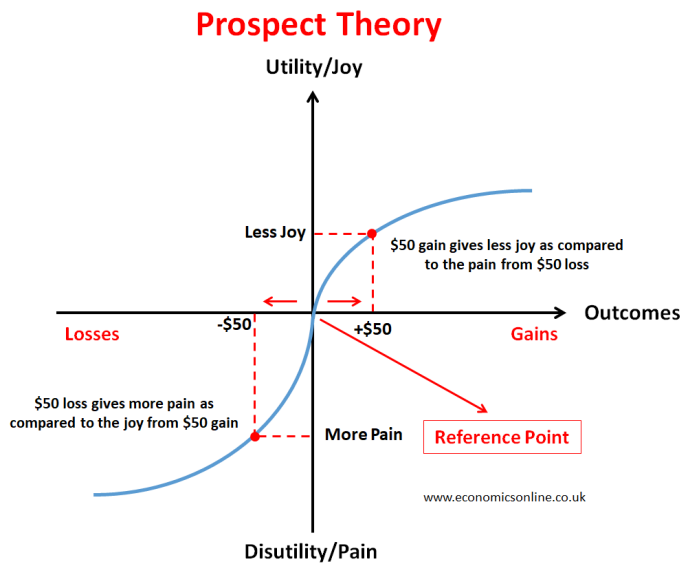


Figure 2.

Some entrepreneurs become excessively risk-averse following failure, avoiding opportunities that require reasonable risk-taking and limiting their potential for future success. This risk aversion may be reinforced because of prospect theory's loss aversion principle. Alternatively, some entrepreneurs develop unhealthy risk-seeking behaviors as they attempt to quickly recover losses or prove their capabilities, leading to poor decision-making and potential recurring failures. Thaler & Johnson (1990) demonstrated that individuals who have experienced losses often exhibit increased risk-seeking behavior in attempts to recover those losses, a phenomenon known as the "break-even effect."

3. Implementation of findings

Cultural Factors

Successful business leaders are increasingly urging their companies and colleagues to make more mistakes and embrace more failures, recognizing that failure experiences can drive innovation and competitive advantage. Companies like Netflix, Amazon, and Coca-Cola have made learning from failure a core component of their business culture, creating an environment that encourages experimentation and views failure as necessary for future success. Netflix CEO Reed Hastings once said, despite experiencing an abundance of new hit shows, that their "hit ratio is too high right now," and that they would "have to take more risk...to try more crazy things...we should have a higher cancel rate" of shows (Taylor 2017). In such an environment where failure is accepted, it encourages employees and entrepreneurs to continue to take risks and opportunities, as well as have further confidence in their actions. Morris (2023) has demonstrated that entrepreneurs' confidence in their own capabilities can allow for better recognition of opportunities (Tumasjan & Braun, 2012), stronger dedication and work intensity to goals (Trevelyan, 2011), work intensity, persistence (Cardon & Kirk, 2015), and innovation (Cumberland et. al, 2015). However, one must recognize that these successful business leaders are able to encourage such attitudes and mindsets because the company is successful, and as

a result, failures are typically not detrimental to the company. Contrastingly, entrepreneurs who recently just began their journey or companies without as much success as these companies may be impacted by failures more significantly, causing them to attempt and avoid failure as much as possible.

Additionally, cultural attitudes toward failure vary significantly across societies and communities, influencing both the social consequences of failure and entrepreneurs' psychological responses. For instance, cultures like those at Silicon Valley encourage and accept failure, to the point where it has been argued that a failed start-up can be seen as a badge of honor (Landier 2005). Contrastingly, cultures that view failure as shameful or evidence of personal inadequacy create more severe social consequences and psychological trauma following failure. Additionally, more often than not, Silicon Valley is a rare exception to how failure is treated, and most entrepreneurs that experience failure face significant disapproval from others (Shepherd 2016). The extent to which they receive stigmatization may vary, for instance, how failure is often treated with a high degree of stigma, shame, and disappointment in East Asia due to cultural concepts such as loss of face. Loss of face is defined as “a damaging social event in which one’s action is publicly given notice and negatively judged by others, resulting in a loss of moral or social standing” (Ho, Fu, & Ng, 2004). Additionally, Chua and Bedford (2016) found that fear of failure is especially prominent in Chinese societies compared to Western ones due to the emphasis of loss of face, which highlights the idea that entrepreneurs exposed to cultures such as those in East Asia could face worse social consequences as a result of failure, negatively influencing their psychological status.

Survivorship Bias

Many entrepreneurs should take survivorship bias into consideration, especially when researching and learning more about failure in other businesses and entrepreneurs. Survivorship bias is defined as “a logical error of concentrating on the people or things that made it past some selection process and overlooking those that did not”(Lockwood 2013). In this specific context, it is the tendency for people to focus on the successful entrepreneurs, and consequently, overlook those that have failed. This is particularly relevant, as a lot of research typically focuses on business culture who successfully integrate failure and encourage it rather than the opposite. It is quite difficult to find information and research that explain in detail these failed attempts at integrating failure due to survivorship bias, and consequently, not all perspectives and consequences can be covered, possibly leading to skewed perspectives on failure. As a result, cases of successful integration of failure into mindsets of entrepreneurs may not be fully representative of all scenarios, as there is a high possibility of entrepreneurs who exhibit the many personal characteristics where they would benefit from failure, yet still are not successful due to other outside factors. Consequently, entrepreneurs must take into consideration these implications, and consider that the benefits from accepting and learning from failure may not occur in every situation.

Discussion

The dual nature of failure in entrepreneurship needs a nuanced understanding. Success following failure is conditional, as it is influenced by the entrepreneur's mindset, support system,

access to resources, and cultural environment. In addition to a supportive environment and business culture that accepts failure, entrepreneurs must learn to reflect and think about their failures. Additionally, many entrepreneurs may not have the luxury to experience many failures due to issues such as lack of capital that bigger companies can afford, further emphasizing the need to deeply understand failure and the effects it has on entrepreneurs such that the entrepreneur can learn and gain more experience from failure.

Businesses should focus not only on teaching how to avoid failure but also how to extract value from it. Policymakers should work to reduce the psychological burden of failure and create policies that encourage risk-taking without punishing missteps too harshly. James Quincey, CEO of Coca-Cola, encourages a business culture where employees would “get beyond the fear of failure that had dogged the company since the “New Coke” fiasco of so many years ago”, stating that “If we’re not making mistakes, we’re not trying hard enough”(Taylor 2017). As previously stated, famous business cultures such as those at Silicon Valley are a rarity, and that majority of the time, failure is treated quite negatively and entrepreneurs and employees are both impacted by it. As a result, a lot of people get discouraged by failure, even if it is a necessary part to achieving success. The paper’s main message is that businesses should treat failure as a strategic resource that requires careful management and reflection rather than something to either avoid at all costs or celebrate unconditionally, leading to the need for entrepreneurs to deeply understand the consequences of failure. Success comes from building systems that harvest failure’s learning potential while protecting people from its destructive effects.

A common theme seen throughout successful entrepreneurs is that they learn to embrace the struggle of failure and derive satisfaction from overcoming challenges. Dyson, despite creating 5,127 different prototypes, stated that he actually enjoyed that process of misfiring and struggling, since it allowed him to gain wisdom. So much so, that he stated that ‘Life is about making things work, [and] if you’re not prepared to fail, you’re not prepared to learn. And unless people and organizations manage to keep learning as fast as the world is changing, they’ll never keep growing and evolving.’ Although each scenario where an entrepreneur faces failure is different, one can benefit from failure even without adequate resources or support systems if the individual can learn to enjoy the process of failure itself, and the possible learning benefits it provides.

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