

GOODBYE

LENIN

HELLO

SCHUMPETER?

Comparative Economics of Entrepreneurship

Tomasz M. Mickiewicz

Social Sciences, SSEES, UCL

Inaugural Lecture, 27th January 2007

Introduction

Or: How I Learned to Stop Worrying and Love Economics



“That **refined common sense** we call “theory” and which provides us with the tools for approaching both facts and practical problems”

(Schumpeter, 1934, p.lxii)

“I have never tried to bring about a Schumpeter school. There is none and it ought not to exist. ... **Economics is not a philosophy but a science.** Hence there should be no schools in our field“

(Schumpeter, farewell address to students in Bonn)

Introduction: Why Entrepreneurship?

Entrepreneurship implies **change**. Positive effects follow from it.

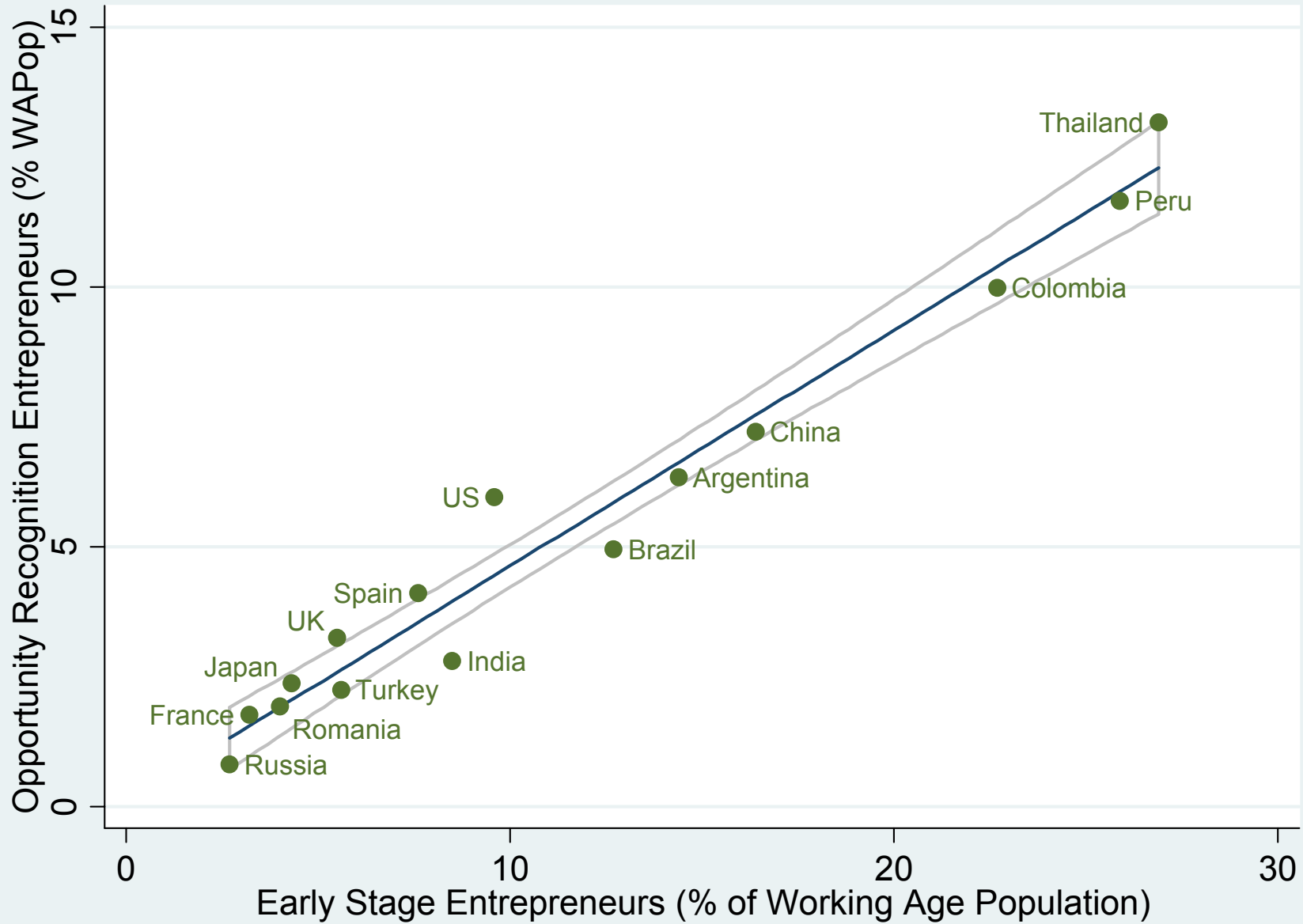
Related to **innovation**, **structural evolutions** and **growth**.

From the **economic** point of view: conditions not just for entrepreneurial entry, but for **fast growing, dynamic ventures** (eg. Intel, Apple, Microsoft, eBay, Google: 1 in 10,000 entrepreneurs, but one never knows in advance)

- Entrepreneurship also has **social effects**: it may create the most **effective way out of poverty** (De Soto; East Asia versus Latin America)
- And **political effects**: freedom of entry and dispersion of economic power support political freedom
- **Social, political & economic effects may be related** (**outsiders**, **insiders**; Acemoglu; Gerry & Mickiewicz; Buccellato & Mickiewicz)



and some countries have more entrepreneurs than others...



ENTREPRENEURIAL ENTRY



- Is it really not true to life or artificial to keep separate the phenomena incidental to **running a firm** and the phenomena incidental to **create a new one**?

(Schumpeter, 1934, p. Ixiii)

CHANGE IS BROUGHT ABOUT BY THOSE WHO ARE DIFFERENT

Hedonistically, therefore, the conduct which we usually observe in individuals of our type would be irrational.

(Schumpeter, 1934, p.92)

Motivation for entrepreneurial entry:

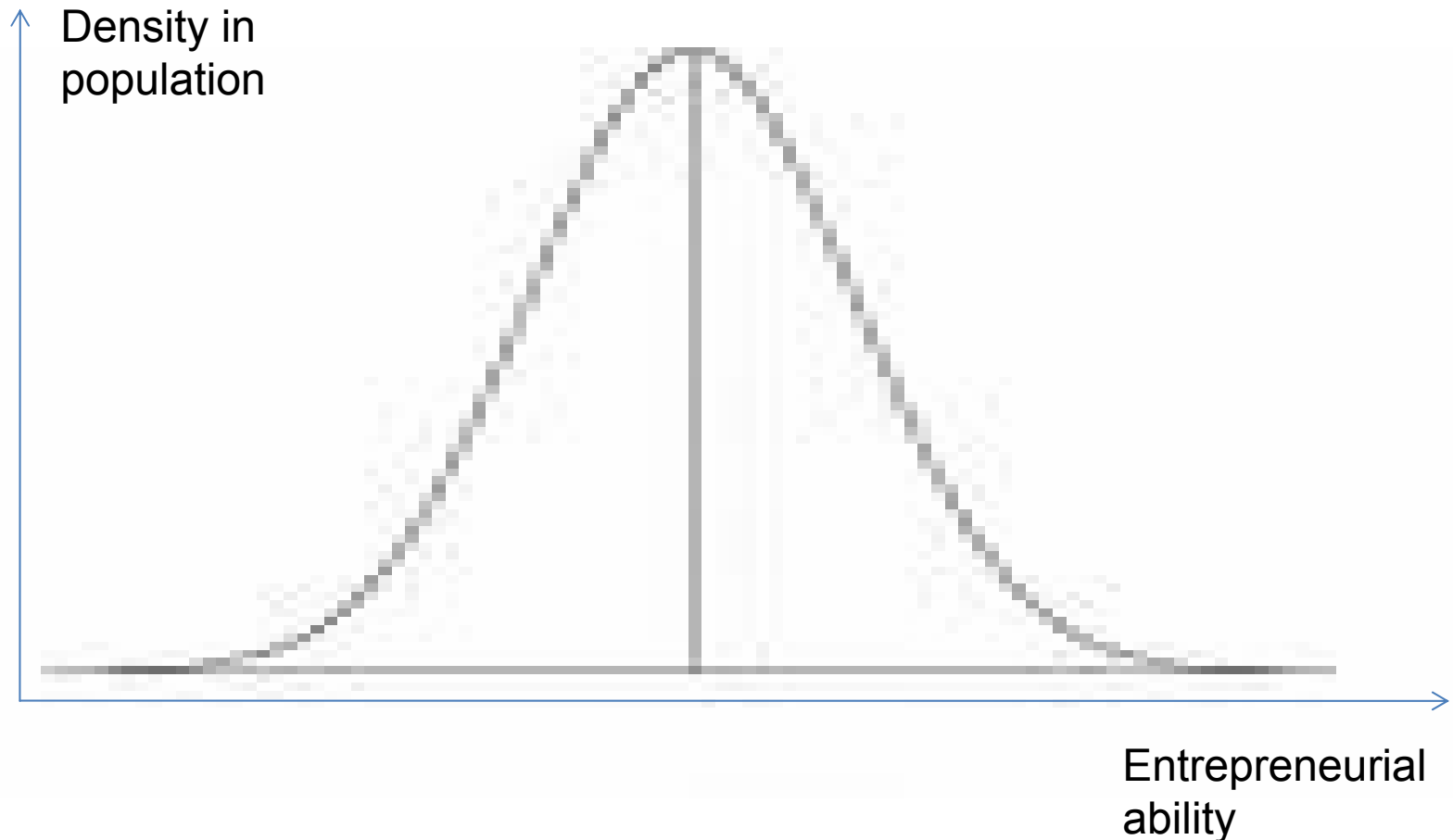
Social distinction ... [this motive] is specially strong for people who have no other chance of achieving social distinction (p.93)

The impulse to fight ... From this aspect, economic action becomes akin to sport (p.93) [yet the game may be seen as a power struggle; in contrast, for entrepreneurship, the rules of the game are important]

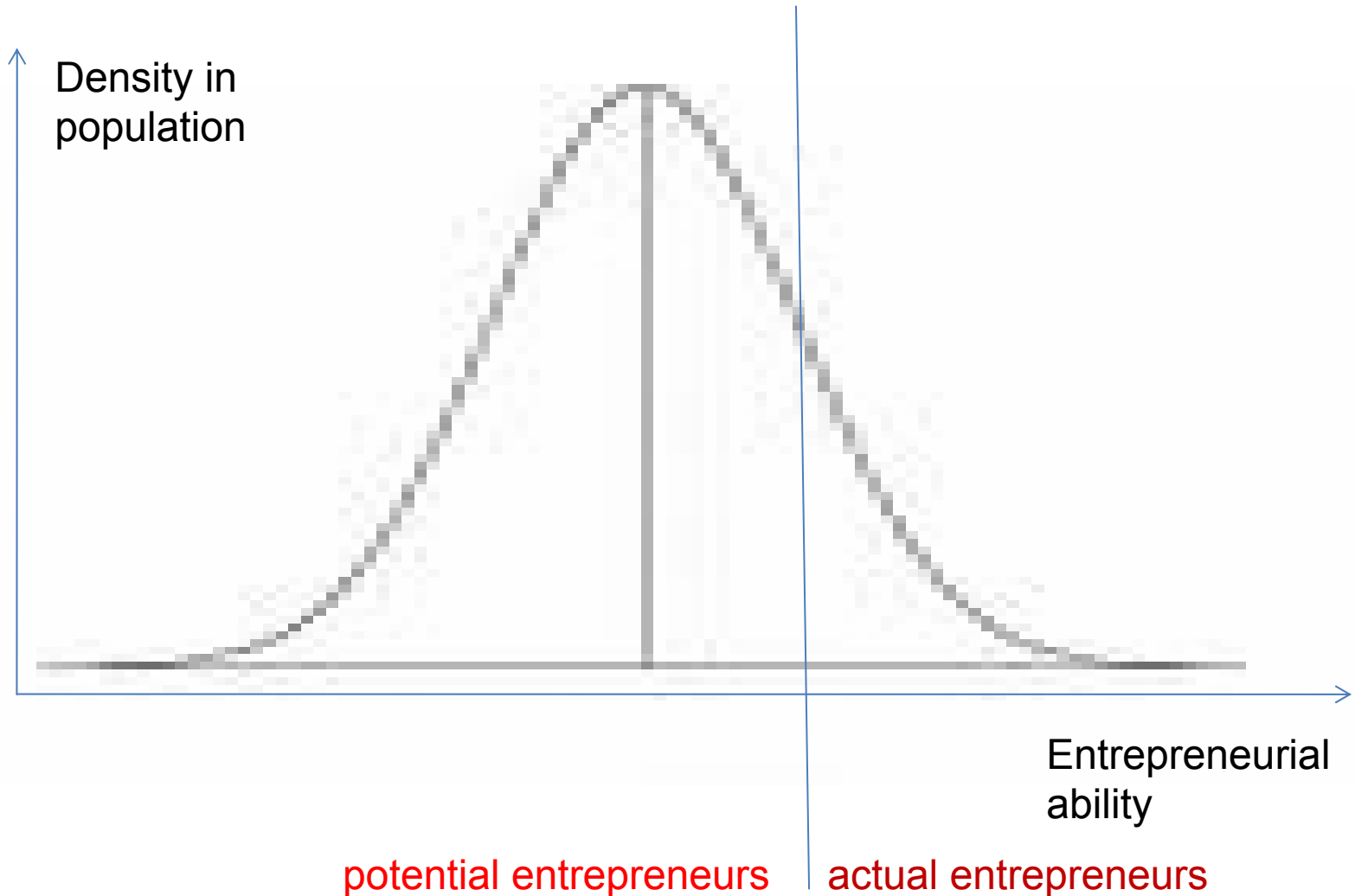
The joy of creating... This group of motives is the most distinctly anti-hedonistic of the three. (p.94)



...yet **”different”** does not imply
outside the field of economic analysis



Why potential does not always become actual?

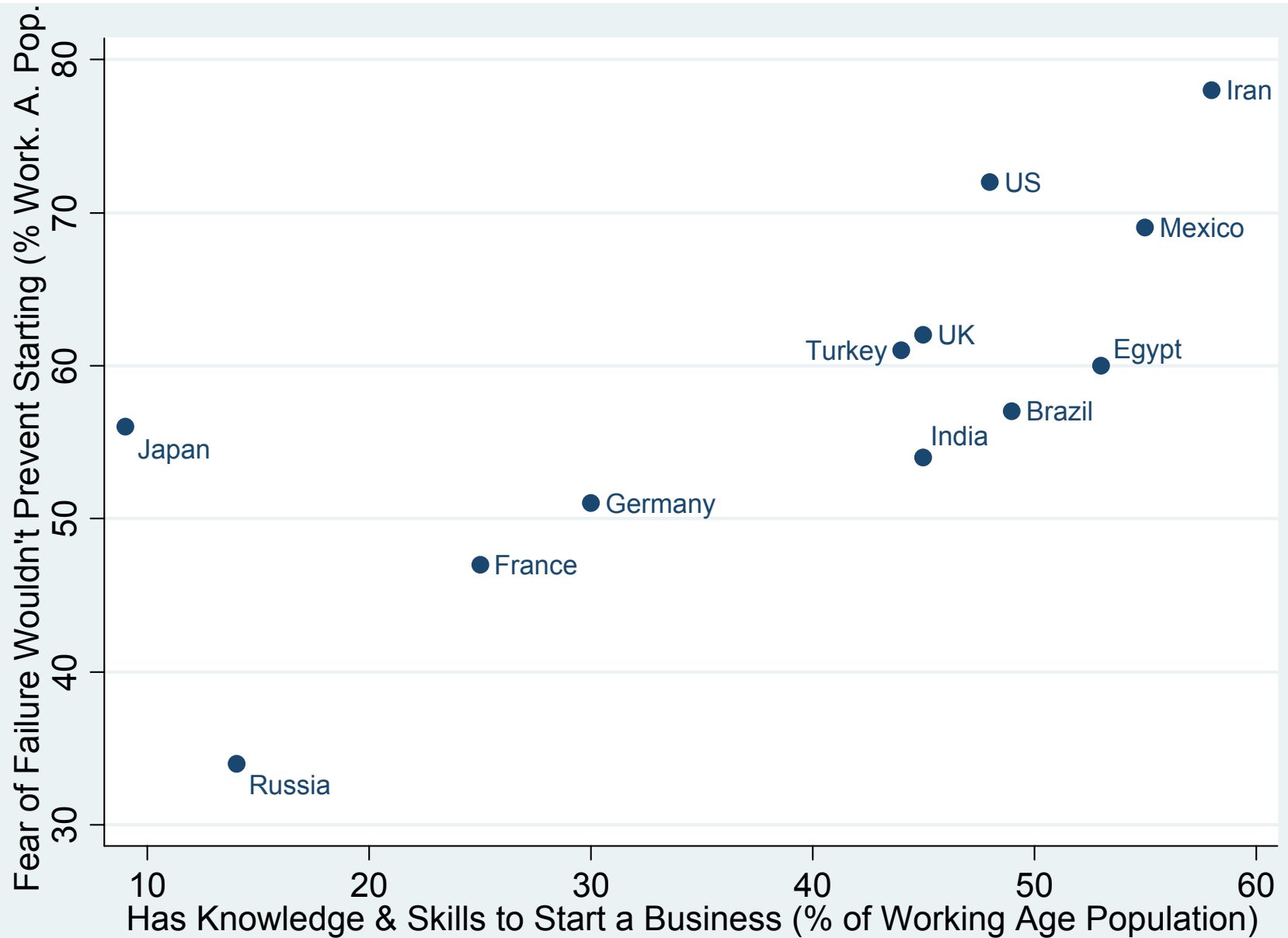


“every step outside the boundary of routine has difficulties”



- **Uncertainty**: Carrying out a new plan and acting according to a customary one are things as different as **making a road and walking along it**. ... (p.85)
- The very nature of **fixed habits of thinking, their energy-saving function**, is founded upon the fact that ... they yield their results automatically and are proof against criticism and even against contradiction by individual facts. But precisely because of this they become drag-chains when they have outlived their usefulness. (p.86)
- The **reaction of the social environment** against someone who wishes to do something new. ... This opposition is stronger in primitive stages of culture than in others, but is never absent. ... In economic matters this resistance manifests itself first of all in **the groups threatened by the innovation**, then in the **difficulty in finding the necessary cooperation**, finally in the **difficulty in winning over consumers**. (p.87)

... and attitudes differ across nations:



that leads us to **comparative economics**, which considers the **impact of variation in institutions** on attitudes and choices:

the institution of **private property** ... has an important **psychological dimension** that enhances our feelings of ... **internal control** ... and it thereby promotes **entrepreneurial alertness**" (Harper 2003, p. 74).

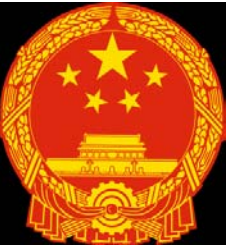
that in addition to standard **economics explanations**:

- "Command over means of production is necessary to the carrying out of new combinations" (Schumpeter, p.68)
- Risk of expropriation discourages entrepreneurship, as any other form of investment
- ...and valuable resources are sunk into protection



Economics
v.
Psychology

...yet to some extent **informal institutions** may substitute for **formal institutions**



- **China and Russia** are characterised by both **weak formal property rights** and by **financial repression**. Both factors should imply little use of external finance by entrepreneurs.
- However, **China** is one of the two countries (the other being Thailand) with the widest availability of informal finance (between 6-7% prevalence rate); and the value of informal capital in China has been estimated to vary between 2%-5% of GDP in the early 2000s.
- In contrast, availability of external informal finance in **Russia** is low (between 1-2% prevalence rate). A number of other **transition economies** are characterised by a low supply of informal finance. (Korosteleva and Mickiewicz, 2008)

Is Lenin no Longer with us?

Informal Institutions and Trust in Transition Economies

- “Tyrants conduct monologues above a million solitudes”
(Camus, 1951)



- “There are indeed truly individualistic societies with little capacity for association. In such a society, both families and voluntary associations are weak ... Russia and certain other former communist countries come to mind”
(Fukuyama, 1995)

However, trust does not solve everything...

- For high-powered entrepreneurship that generates growth and change formal institutions matter more:

complex forms of economic activity require complex contracts, and those in turn are conditional on formal rules

(Estrin, Korosteleva, Mickiewicz, 2009)



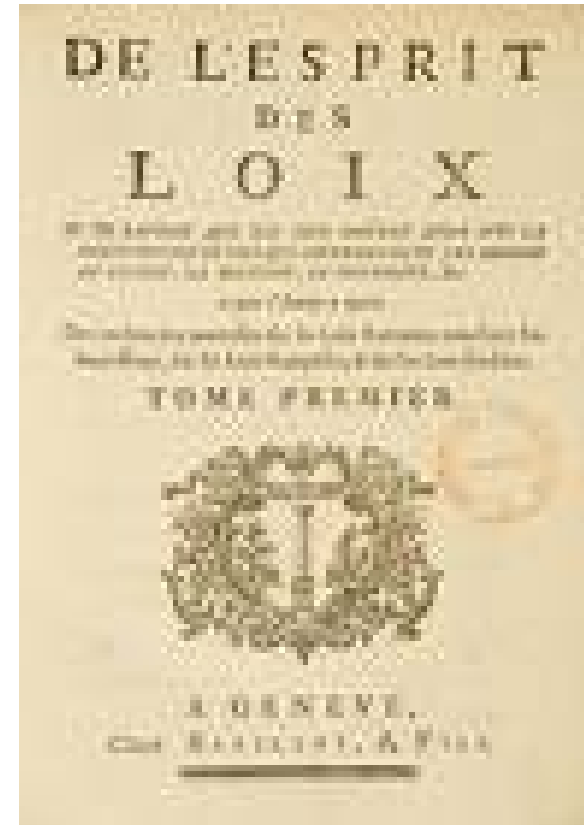
The formal institutions that matter
are 'higher order institutions':

Rule of law / protection of property rights

that consists of two key elements:

- constraints on the executive branch of the government
- protection of contracts:
independent and well-
functioning judicial system

*and the first element may be more
important than the second...*

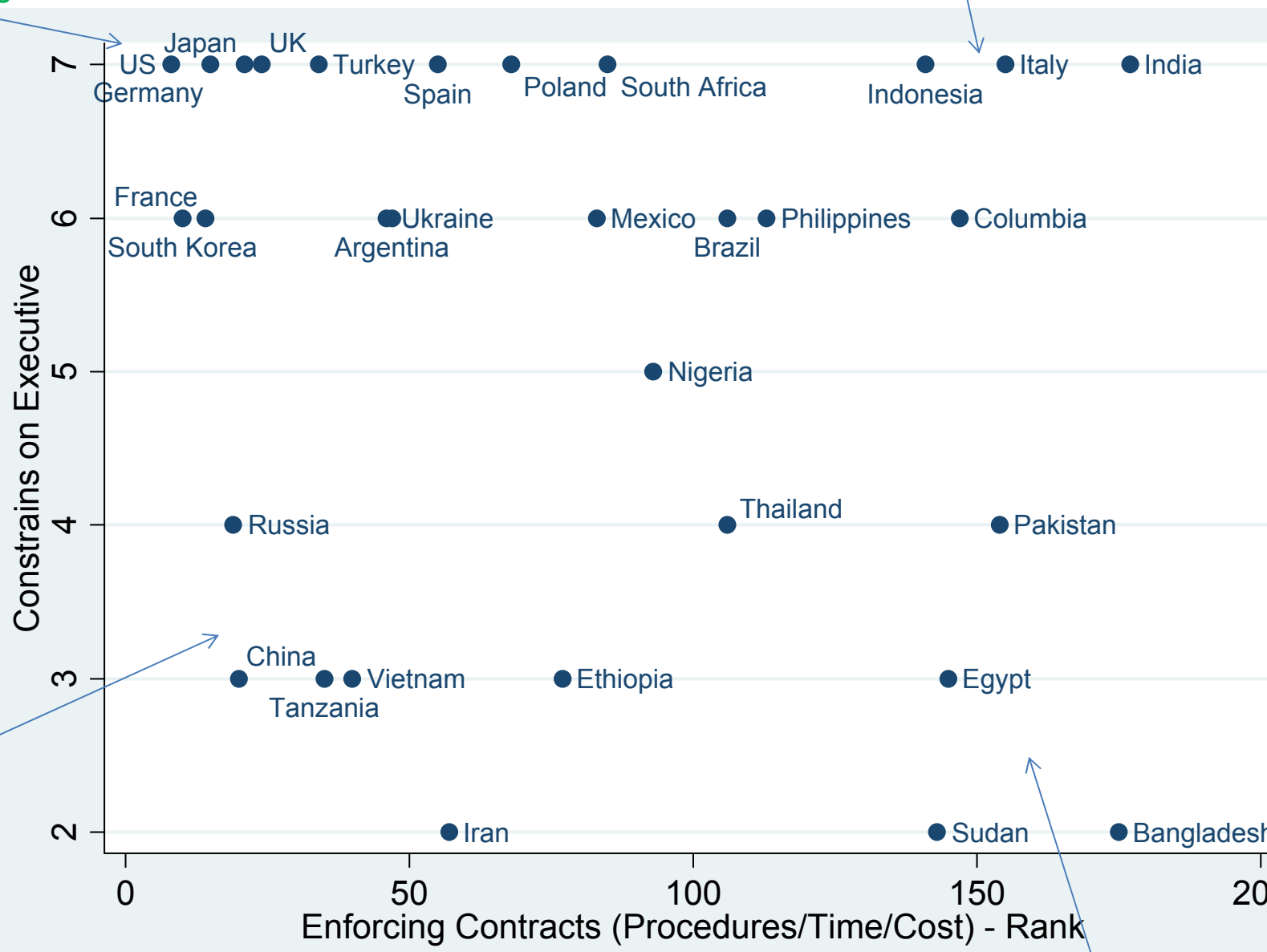


strong constraints on executive & efficient judiciary

strong constraints on executive & inefficient judiciary

weak constraints on executive & efficient judiciary

weak constraints on executive & inefficient judiciary



Source: Polity IV 2007; WB 2008

and finally, we may generalise the concept of entrepreneurship

- **Rule of law** is conducive not only to entrepreneurship but also to **institutional entrepreneurship**
- **Institutional entrepreneurship** (a change in institutions that goes beyond incremental adaptation) **is most effective when arrived at by encompassing consensus**, which implies **consistency with informal institutions** and therefore **effectiveness**. Such changes are more likely to last.
- The same rule applies to **systems with no rule of law**. However, in that case it is more difficult to base institutional entrepreneurship on broad consensus.



(Mickiewicz, 2009)