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Excerpt
More information

PART ONE

THE ENTREPRENEURIAL SOCIETY

What's Governance Got to Do with It?

1

Entrepreneurship Policy

What It Is and Where It Came from

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Entrepreneurship was in vogue in the 1990s. Best-selling books and feature-length movies documented the trials and tribulations of trendy start-up companies, complete with foosball tables and macaws-in-residence. Twenty-somethings worth billions on paper partied with Hollywood stars and were feted by Washington pols. After the dot-com bubble burst in 2000, turning a lot of that paper into confetti, the cultural fascination with entrepreneurship faded. The old brand names of corporate America, by and large, regained their places in the consciousness of consumers and investors. As 2001 closed, the autobiography of General Electric CEO Jack Welch topped business book buyers' Christmas lists; one can be confident that neither "foosball" nor "macaw" appears in the index of *Jack: Straight from the Gut*.

But appearances can be deceptive. The entrepreneurship fad rested on a foundation of fact. New companies have made significant contributions to economic growth in the past decade, both directly and by stimulating their more established competitors, as they indeed had in the decades before that. If the fad exaggerated these contributions, its fading should not obscure them entirely. Entrepreneurship is an economic phenomenon worthy of attention from those who worry about

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economic growth and particularly from those charged with sustaining that growth.

Such, in any case, is the premise of this volume. The contributors collectively assert that the level and quality of entrepreneurship make a difference in the economic vitality of communities, regions, industries, and the nation as a whole. We argue that policymakers may be able to enhance the economy by enhancing entrepreneurship, although we are hardly uniform in our assessment of how to go about trying. What matters most at this point is that the policy community not toss out the entrepreneurship baby with the dot-com bathwater. Entrepreneurship ought to be an explicit focus of policy design, choice, and implementation. Analysts can and should do a much better job of assisting policymakers in making it so.

The term "entrepreneurship policy" is intended to capture this concept.[1] The domain of entrepreneurship policy is large. It encompasses activities at several levels of government, from local to national (and perhaps beyond). It bears on low-technology economic activity as well as high-technology (although the latter is emphasized here). It includes governance capacities more familiar under other headings, ranging from regulatory policy to economic development partnerships to poverty alleviation, along with some capacities that are new.

A modest volume like this one cannot comprehensively survey the myriad facets of this sprawling domain. Nor, given the inchoate state of scholarship, does it make much sense to attempt to establish a consensus about what entrepreneurship policy ought to be. We aspire merely to crystallize the idea of entrepreneurship policy and to illustrate its significance. If a lively national conversation about the interaction between public policy and entrepreneurship ensues (and even if we receive some brickbats in the process), we will have accomplished our main objective.

We have good reason to believe that the ground for such a discussion remains fertile, the boom and bust of the 1990s notwithstanding. U.S. policymakers, particularly at the state and local levels, have been groping toward an explicit entrepreneurship policy for at least a couple of

[1] "Entrepreneurship policy" is a concept and a phrase whose time seems to have come. Although rarely used in the past, it has begun to achieve modest prominence, particularly in Europe. See Lundstrom and Stevenson (2001); European Commission (2003).

decades. Their experiments have typically been pragmatic, inspired by immediate needs and pressures and by one another's examples, rather than by a grand theoretical design. Scholars have come to the subject more recently (with the exception of a few pioneers, some of whom are contributors to this volume, who have been exploring this terrain for many years). A number of disciplines, each with its own distinctive history, style, and language, have now converged on it, and their interaction promises to add momentum to all.

In the rest of this introductory chapter, I sketch out the domain of entrepreneurship policy more fully, defining crucial terms and situating the contents of this volume in a variety of contexts, including the international comparative context. I also lay out one version of what might ultimately be called the "prehistory" of entrepreneurship policy in the United States. I conclude by mapping out the rest of the volume.

ENTREPRENEURSHIP: A NARROW DEFINITION

"Entrepreneur," "entrepreneurial," and the like have become highly desirable labels in recent years, so much so that the definition of entrepreneurship has blurred nearly beyond recognition. Public agencies are urged by advocates of reinventing government to become more entrepreneurial. The founders of nonprofit service delivery and advocacy groups call themselves "social entrepreneurs." "Intrapreneurs" challenge large corporations to adopt new ways of doing things.

None of these neologisms is relevant to "entrepreneurship policy" as the phrase is employed in this volume. As will be seen, we adopt a dangerously broad definition of "policy," but by "entrepreneurship" we mean (with the inevitable few exceptions) the processes of starting and continuing to expand new businesses. Our vision of these processes derives from Joseph A. Schumpeter, who conceived of the entrepreneurial venture as "the fundamental engine that sets and keeps the capitalist engine in motion" by creating new goods, inventing new methods of production, devising new business models, and opening new markets (Schumpeter 1942, 83). Entrepreneurship policy aims to foster a socially optimal level of such venturing. Usually (although this need not necessarily be the case), policymakers seek to raise the level of entrepreneurship; entrepreneurship policy thus bears not only on actual entrepreneurs but also on "nascent" entrepreneurs, who are seriously considering starting a firm (Reynolds et al. 2000).

Entrepreneurial ventures are not the same as small businesses, and entrepreneurship policy is therefore distinct from small business policy. Although many entrepreneurial ventures are small, they can be quite large in lines of business like airlines and telephony where the minimum efficient scale of operation is large. On the other hand, the well-established neighborhood restaurant or dry cleaner, although small, falls outside the definition. The distinguishing elements of entrepreneurship are novelty and dynamism. The phrase "continuing to expand" is essential to the definition, even though it creates serious difficulties for measurement and analysis.[2]

As Schumpeter suggests, technological innovation is a particularly important mechanism through which entrepreneurial ventures express their novelty and dynamism. Its importance stems in large part from the contribution that new technologies make to economic growth. Whether by saving capital, labor, or natural resources or by creating new capabilities, technological innovation expands the potential output of the economy, rather than simply shifting economic activity from one enterprise to another. Writing in 1940, Schumpeter predicted that the innovation process would be routinized in large, stable enterprises, but this prediction has not been fully realized. New entrants seem to be important catalysts of technological innovation, even when they prove to be business failures, as they often do (Scherer 1992; Utterback 1994). Older firms are forced to adapt under the pressure of innovative rivals, lest they be replaced. The current interactions between traditional retailers and electronic commerce start-ups and between large pharmaceutical firms and biotechnology start-ups illustrate some of the potential patterns.

Economic globalization heightens the importance of technology-based entrepreneurship for the contemporary United States, as David Audretsch points out in his chapter and elsewhere (Audretsch and

[2] Some researchers, following the lead of David Birch, address this difficulty by focusing on "gazelles," publicly traded companies that have grown at an annual average compound rate of 20 percent or more for the previous four years.

Thurik 2001). The country cannot and should not compete internationally on the basis of labor costs. Huge pools of low-cost labor in developing countries are becoming available for export production, and they are likely to continue to grow in the coming years. U.S. competitive advantage lies in the creation and rapid exploitation of new ideas, whether for products, services, or productivity improvements. The term "knowledge economy" in this volume's title signals this emphasis in the selection of contributions.

The knowledge economy, let me be clear, is only an emphasis and not an exclusive focus of this volume and of the field of entrepreneurship policy that we hope it will help to spawn. Entrepreneurship policy strategies that target lower-technology entrepreneurial ventures may well be appropriate for particular jurisdictions. Analyses using aggregate data on entrepreneurship may shed light particularly on such strategies and ventures, since they vastly outnumber their high-tech brethren. The definition of entrepreneurship offered here embraces all businesses that are new and dynamic, regardless of size or line of business, while excluding businesses that are neither new nor dynamic as well as all nonbusiness organizations.

PUBLIC POLICY AND GOVERNANCE WITHIN THE CONTEXT FOR ENTREPRENEURSHIP

The determinants of entrepreneurship, entrepreneurial success, and the impacts of entrepreneurship on society are the subjects of a growing body of research, primarily in the disciplines of economics, geography, management, psychology, and sociology.[3] Early work in the field concentrated on the qualities of entrepreneurs as individuals and the business strategies that they employed. Recent work has sought to integrate this understanding of the "supply" of entrepreneurs and entrepreneurial strategies with an analysis of the "demand" for entrepreneurial ventures or, more broadly, the "opportunity structure" or "context" for entrepreneurship (Aldrich and Wiedenmayer 1993; Thornton 1999).

[3] My own field of political science is notably absent from this area of social science research.

The context for entrepreneurship includes a wide range of economic, social, and cultural factors. General economic conditions and the availability of such resources as financial capital, intellectual property protection, and specialized skills are clearly important. So too are the density and intensity of competition within the nascent entrepreneur's chosen market. The legitimacy of the potential venture – whether it conforms to well-understood and well-accepted social and cultural norms – may influence its viability, success, and impact as well. The availability of specialized information may determine whether entrepreneurs are able to recognize and act on potential opportunities (Aldrich and Fiol 1994; Shane and Venkataraman 2000).[4]

Public policy and governance can shape virtually all the contextual determinants of the demand for entrepreneurship and, over a longer time scale, the supply of entrepreneurs as well. Public policy and governance, as these terms are employed in this volume, refer to intertwined but distinct processes. Public policy means the intentional use of the powers of government to effect a societal outcome, like a change in the number of entrepreneurial ventures. Governance refers to conscious collective action that extends beyond government, deploying, for instance, the capacities of businesses, community groups, and academic institutions to bring about such an outcome. Entrepreneurship policy often aims to catalyze better governance, for instance, by fostering networks of potential customers and service providers, the presence of which reduces the uncertainty facing nascent entrepreneurs.

Not all public policy that shapes the context for entrepreneurship and the supply of potential entrepreneurs is entrepreneurship policy, as we use the term here. Education policy, for instance, may influence the legitimacy of entrepreneurial ventures and the knowledge, skills, and networks possessed by individuals and social groups. Macroeconomic policy, to take another example, affects short-term capital availability and the conditions of international trade. All these policy outcomes contribute to the context for entrepreneurship. This volume, however, concentrates on policy that can have an impact within a period

[4] This paragraph illustrates, rather than exhausts, the list of contextual factors that may affect entrepreneurship.

of years on what the 2001 *Global Entrepreneurship Monitor* (*GEM*) labels "intermediate conditions" for entrepreneurship, rather than education policy and the like, which influence "background conditions" over a decade or more, or macroeconomic and associated policies that shape "short-term conditions" on a monthly basis (Reynolds et al. 2001).[5]

The reader should not draw the conclusion that areas of public policy and governance omitted from our definition of entrepreneurship policy are unimportant. Indeed, a growing body of research suggests that background conditions are especially important in explaining differences in levels of entrepreneurship and economic development across countries over long periods of time. Systems of property rights, for instance, which provide the fundamental legal underpinnings of markets, profoundly structure investment and risk-taking behavior. There are complex feedbacks between legal systems, cultures, institutional development, and economic change that warrant further attention from scholars and practitioners alike. U.S. institutions, viewed at this high level of abstraction, are quite supportive of entrepreneurship (Rosenberg and Birdzell 1986; North 1994).

Our limitation of the scope of entrepreneurship policy by reference to intermediate conditions is largely pragmatic. Since the contributions to this volume are confined to a single country, background conditions do not vary very much. More important, the time scale on which intermediate conditions can change allows policymakers the possibility of perceiving (and perhaps taking credit for) the consequences of their efforts. This definition also permits us to take for granted some well-established boundaries among policy domains, like education and macroeconomic policy, for which entrepreneurship is not generally a driving consideration. Without such boundaries, there is a danger that entrepreneurship policy will simply encompass all of public policy and thus lose its meaning. As *GEM* puts it, "the more careful the analysis, the more complex the entrepreneurial process appears to be"; the same could be said of the linkages between entrepreneurial and policy processes (Reynolds et al. 2001, 23).

[5] One of the inevitable exceptions to this statement that merits note is the discussion of entrepreneurial education programs in the chapter by Pages, Freedman, and Von Bargen.

ENTREPRENEURSHIP POLICY BY OTHER NAMES: A BRIEF HISTORICAL OUTLINE

Entrepreneurship policy and related processes of governance for our purposes, then, are not unlimited in scope, but they nonetheless encompass quite a bit. They are carried out at the local, regional, state, and national levels within the United States. The specific capacities of government and its partners in governance that are deployed to foster entrepreneurship vary as substantially as the communities and economic activities they seek to influence. Some of these capacities are quite old, whereas others have risen afresh in just the past few years. We hope to knit these diverse threads together conceptually to form the fabric of entrepreneurship policy.

The Federal Level

Perhaps the most obvious place to begin a survey of what we hope our new rubric will embrace is the Sherman Antitrust Act, which was passed by the U.S. Congress in 1890. It is this legislation more than any other single entrepreneurship policy measure that distinguishes the United States from other industrial countries historically. The Sherman Act was the culmination of years of popular agitation sparked by the perception that large firms were becoming dominant in the economy. It restricted the behavior of these firms in part to preserve opportunities for entrepreneurship, although it is important to acknowledge other motives behind the antitrust movement, including protectionism (with respect to existing small town businesses) and moral outrage (at the power wielded by the captains of industry). Over more than a century of development of antitrust law and policy, the entrepreneurship motivation has endured, and the analysis of barriers to entry and how they are maintained remain at its center (Hart 2001a).

Federal regulatory policy also intersects significantly with entrepreneurship. Economic regulation, such as that imposed on the energy, communications, transportation, and financial sectors, was initially oriented toward stability, reliability, and coordination, virtues thought to inhere in monopolistic or oligopolistic industrial structures. Regulatory policy as it was implemented through most of the twentieth century thus discouraged entrepreneurship. On the other hand, the architects of "deregulation" over the past quarter century (which might, as Viktor Mayer-Schönberger describes in his chapter, more appropriately be labeled "regulatory restructuring") have sometimes explicitly sought to expand entrepreneurial opportunities in regulated sectors. Eli Noam's chapter on entrepreneurship in telecommunications describes one particularly vivid chapter in this story.

The constraints imposed on established firms by antitrust and regulatory policy have been paralleled by a set of federal policies intended, at least by some accounts, to support entrepreneurial ventures. The intellectual property rights regime, for instance, has been tightened steadily since the 1970s, so that rights-holders have become more likely to win protection and to prevail in court. New sorts of products and processes, ranging from life forms to business methods, have become patentable, and software and other new digital forms of expression can be copyrighted. Universities and other recipients of federal research and development (R&D) funding have been encouraged to seek intellectual property protection for findings made with federal support and permitted to offer exclusive licenses to exploit them. These protections have provided the asset base for many recent entrepreneurial ventures.

Financial incentives for entrepreneurship have also been forthcoming from federal policymakers. Modest direct subsidies for entrepreneurial ventures have been made available through, for instance, the government-wide Small Business Innovation Research (SBIR) program and the Commerce Department's Advanced Technology Program. More significant are preferential procurement programs that have channeled money from federal projects to small businesses and to businesses owned by women, minorities, and other groups historically underrepresented in the entrepreneurial community (although not all the recipients necessarily meet our definition of an entrepreneurial venture). Federal loan guarantee programs encourage private lenders to do business with such firms as well. Changes in the U.S. tax code, such as fluctuations in the treatment of capital gains, have affected the availability of equity financing for entrepreneurial ventures. Federal rules governing investment also have such effects on occasion; a 1979 rule change that permitted pension funds to place a small portion of their assets in high-risk investments, for example, contributed significantly to the expansion of the venture capital industry, which in turn has fueled entrepreneurship.