Intervening for Entrepreneurship

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Abstract

Entrepreneurship is widely seen as the most sustainable vehicle for economic development. In countries such as China, India and Brazil, the entrepreneurial spirit has pulled millions of people out poverty. However, it can be argued, governments in these countries have supported and protected entrepreneurs against international competition, which has create an artificial bubble of prosperity and these short-term gains will be out weighted by the long-term damage. Nevertheless, in contrast to Austrian views on interventionism, entrepreneurship has flourish under semi-socialist regimes and socialist democracies. Indeed through the Austrian perspective, BRICS represent a bit of an enigma. All prescribe to diverse systems of governance, none advocate a free market economy, yet all have experienced exponential economic growth, well above traditional relatively free market economies. If we keep political and economic preferences to one side, the one constant here is entrepreneurship supported by government intervention. This paper reignites the Austrian and Keynesian debate on interventionism and how it might be used to develop a responsive policy framework.

INTRODUCTION

Although the role of entrepreneurship remains relatively unexplored, and at times oversimplified, it is widely recognized by many as the main engine for economic growth and prosperity (Shumpeter 1945; Minniti, et al,. 2006; Naudé, 2008; Harris, 2009). Despite this recognition, when viewed through different paradigms within economic science, opinions on how entrepreneurship should be fostered vary significantly. These inconsistencies are consequently reflected in different policy frameworks, that, although designed to encourage and support entrepreneurship, at times seem to be at the opposing ends of the scale (Rigby & Ramlogan, 2013). Furthermore, polices mainly tend to focus on the role of government and whether it should or should not intervene with tools such as taxation and subsidies (OFT, 2009; Hall & Sobel, 2006). At the generic level these views are fielded by two opposing notions in economic science, interventionism and non-interventionism. Competition and the price mechanism have historically performed an integral role in regulating the market (Hayek, 1945; Mises, 1949). However, arguably their influence has dwindled as corporations have accumulated excessive discretionary power. This development has certainly had a detrimental effect on how entrepreneurship has evolved and continues to evolve in developed and developing countries (De Jasay, 2010).

This paper seeks to assess these opposing views and argues the need for intervention, not just to protect but develop and nurture entrepreneurship. The existing policy frameworks rely on incentives and deterrents to direct entrepreneurship (Hall & Sobel, 2006). However, this paper attempts to go beyond current discussions on the type of intervention. In an era defined by big business, governments must adopt a dynamic policy framework that does not go out of date as markets evolve and reflects the needs of diverse entrepreneurial eco-systems (Bhat & Khan, 2014). Accordingly, this paper argues for an effective policy framework that at its core is guided by government, business and educational institutions to provide focused support for entrepreneurs. On the periphery this policy framework should be supported by the media, education and government incentives to influence and shape entrepreneurship in any particular entrepreneurial ecosystem.

Opposing paradigms of Interventionism damage

Arguably, governments can facilitate markets or impair them. Battles have been fought over this fine line for over a century. In a free market economy government's role would simply be limited to protect individuals and organizations from the threat of violence and harm (Mises, 1949). As Friedman (1964, p.2) once put it, for the reminder "government should simply butt out". For Austrian Economist this is as far as government should go, anything beyond this point starts to infringe on civil liberties and produce what Isaiah Berlin (1958) would call negative liberty. Worse still, as government adopts a bigger role it starts to disrupt and corrupt market data which is crucial for the effective running of markets (Hayek, 1945). Mises (1949) points to two possible systems, for example, the planned economy such as the ones found in Communism. There is no market for the means of production, all aspects of supply and demand are controlled and planned for centrally by the government. The second is a Capitalist, Free Market economy where supply and demand are left at the mercy of the market and the price mechanism. The third, a mix of the two systems is not possible, however, elements of both may exist parallel to each other. This essentially equates to the interventionist, mutated, form of eco-political system that exists in many economies today. In the Austrian view it is precisely the intervention from government, or indeed any third party not directly involved, that stops economic transactions reaching their natural ends and in doing so hampers the market and thus entrepreneurship (Hayak, 1945; Mises, 1949; Caldwell, 1997; Steele, 2001). Entrepreneurship gives human action purpose and direction to derive surplus value by innovating and exploiting opportunity (OCED, 2012; Mises, 1949; Stevenson, 1985). It is important to make a slight adjustment to this established understanding of entrepreneurship and add *new* to the equation. The new signifies an inherent fluid dynamism instead of the stagnant permanent structures corporations have come to represent. By exploiting new opportunities, creating new innovations or indeed finding new purpose, entrepreneurship can be seen as a regenerating and dynamic force, constantly improving and evolving. What Shumpeter (1942) would call creative destruction. A hampered market due to government intervention is seen as a threat to this evolution, because it is not just the market that is hampered, for what is the market but a collection of human actions. Therefore, in the Austrian view big government does not just hamper the market, it hampers human action and in doing so it denigrates what it is to be human.

These intervention usually comes in the form of subsidies (Hall & Sobel, 2006; Bhat & Khan, 2014). However, non-interventionist would argue, because of their subjective nature, costs and benefits cannot be accurately calculated by those not directly involved in the transaction (Hayak, 1945; Mises, 1949; Brownstein, 1980; Ravier, 2010). Therefore rather than supporting entrepreneurship these interventions strip the market of its key functions, such as price determination and resources allocation and in doing so deprive entrepreneurs of their senses. This gives rise to inefficient firms and increases the likelihood of market failure and economic chaos. If entrepreneurship is to flourish, certainly in the classical view, we need a market economy free from government interference so prices are not coerced and competition is fair (Rothbard, 1963). A meddlesome government disrupts the price mechanism which causes false messages to be transmitted to unsuspecting entrepreneurs, which in turn causes artificial market conditions that lead to inefficiencies and even market failure in the long-run (Hayek, 1945). The Austrian school does not argue for a minimal government on moral or political grounds, instead a free market is seen as the only logical and efficient system capable of delivering liberty and prosperity. Furthermore, with its power to coerce and compel, Mises (1949) saw the potential of government, essentially made up of acting individuals, to be corrupted and act in their own interest to produce policies that ensure self-preservation rather than make sound economic sense. Saving banks from certain failure in 2007 is a pertinent example of government intervention creating artificial conditions and propping up inefficient firms. In recent times the unintended consequences of well-intended government programs have been well documented (Easterly, et al., 1993; Buera, et al., 2012). Well-intended government programs may have a positive impact in the short run, however, these gains are outweighed by the long-term harm. For example, Buera, et al., (2012) highlights how credit subsidy programs have a positive short-term impact in establishing new firms. However, these firms are provided continued access even when they become inefficient, leading to negative long-term impact on the economy and on new entrepreneurs trying to access the market. This also distorts the role of competition which will be discussed in later sections (Buera, et al., 2012).

Reading the Austrian view is frustrating at times because for such a brilliant analysis of the market economy it almost entirely ignore the ability of the individual to accumulate discretionary power and use it to coerce market conditions and manipulate market outcome (De Jasay, 2010). Thus the danger does not only lie with big government but with any element in society that becomes too big. Huerta (1998) gives this point some more clarity. Like Mises (1949) he identifies homo politicus as homo economicus, but does not limit this to the political realm. Huerta (1998) argues that if everyone is free to do what they want, we will naturally try to out compete each other and in doing so use any means necessary to reach our ends. This Machiavellian streak stirs up the very notions a free market is meant to ward off, such as monopolies and serfdom (Huerta, 1998). Interventions designed to aid entrepreneurship may eventually lead to its demise whilst a non-interventionist approach may benefit those already in front and help them maintain their position of power. Thus the dilemma, to intervene or not to intervene. Interventionist would argue there is moral duty for government to intervene, ensure equality and protection from the negative elements of capitalism (Steele, 2001). The rise of the large, multinational corporation in modern times and its impact on entrepreneurs cannot be ignored (Backer & Sleuwaegen, 2003). Keynes (1942) famously said that capitalism needs to be saved from itself (cited in Steele, 2001). In the market today arguably entrepreneurs need to be saved from corporations. However, government subsidies alone are ineffective interventions. Entrepreneurship must be supported with intuitive policies that do not harm future entrepreneurs in favor of the current (Easterly et al., 1993; Buera et al. 2012).

Demise of Competition

When one thinks about survival of the fittest, in the economic sense, images of businesses locked in intense competition against other businesses come to mind. Efficient businesses survive and inefficient ones face the cull. And so in the classical sense competition acts as a natural regulator within the market. However, whilst this is true, competition serves an even higher purpose. Most business cease to exist not because of competition but because of their own inefficiencies. Hayak (1968) sees the real purpose of competition as a means of discovery. As firms and consumers try to outdo each other in order to obtain the most desirable goods and services they are forced to find new and more efficient means of achieving these ends. Competition facilitates the discovery process enabling entrepreneurs to discover new possibilities of serving consumer needs better. It not only preserves the market but helps it improve and evolve. It “forces” those who depend on the market not just to imitate the latest improvements but also to continuously innovate in a bid to achieve a competitive advantage (Hayak, 1968. p.19). Hayak's (1968) use of the word force is particularly poignant here and also helps delve deeper into the nature of homo economicus. It suggests, willingness to improve is not voluntary and that if competition was not there firms would continue as if they had always done. Without competition we might still be using beepers and not smart phones, without competition we might never have had cheap air travel. One can understand why established firms want to minimize competition, ultimately it adds to the cost whilst the only benefit it provides firms is the possibility of being better than the competition. Without competition firms would neither face this cost nor seek the benefit. Therefore it is also logical for firms to aim for a monopoly or forge alliances to create cartels at the very least (Rothbard, 1963).

Mises (1949) emphasizes the role monopoly prices play rather than just the existence of monopolies. Monopoly prices enable firms to enjoy greater control over supply and prices. Arguably many multinational corporations enjoy monopoly prices today. Government policies to create fairer competition have failed to achieve the desired outcomes. Deterrents also seem to be ineffective, for example, cases of price fixing by energy firms and interest rate fixing by major banks in the United States (US) and United Kingdom (UK) had insignificant consequences for the culprits (Macalister, 2012; Binham, 2014). On the other end of the barometer, competition policies can also lead to inefficient firms propped up and protected from the efficient firms (Buera et al. 2012). The later causes harm to the market because as government interferes and increases its grip on the economy the essential role of competition in regulating the market economy withers away (Read, 1958). According to Hayak (1968), inefficient firms are not only allowed to survive where they should have dissolved, but more importantly the process of discovering new and better ways to satisfy consumer needs gets compromised.

Austrian economist would do away with all government interference with competition, even to discourage monopolies. The premise being that in the long-run a monopoly only survives as long as the next innovation. However, this does not compensate for the short-term damage, nor does it take into account that homo-economicus is an acting woman and once a monopoly is created she will do everything to maintain it (Huerta, 1998). Hayak (1968) was writing at a time when markets and indeed capitalism was still developing and firms were fighting to reach a hiatus. Since then the economic landscape has changed, many large companies have become giant multinationals who have created defacto monopolies controlling all aspects of the supply chain and so the role competition once used to play is now insignificant. For the same reason the price mechanism is also obsolete. We see evidence of this in almost every global industry, be it Oil, Gas, or indeed money. The largest operators have colluded together to fix prices and the notion of competition has lost the meaning it once had. Hayak (1968. p.19) himself seems to point at this and recognizes that because competition forces firms to improve they "disinclined to compete". Well, why is it that firms are less inclined to compete? it is not because they have to improve, but because they have to pay to improve. So is it not a logical action for the rational economic agent to make alliances with other economic agents and come to an arrangement were they do not have to compete at the cost of each other’s profits but share the spoils of the market. Therefore, we cannot rely on competition to regulate markets, it certainly cannot be considered fair for new entrants into the market. Even the most efficient and innovative new entrants face unfair competition in established markets. Proponents of non-intervention are quick to point to Google and Facebook as prime examples of new entrants succeeding because they were efficient and innovative. Whilst this is true, another important factor for their success is the fact they were operating in relatively immature markets. Another new firm enjoying the same level of success is improbable. What’sApp being bought by Facebook in 2014 highlights this fact well.

Price Mechanism

For Austrian economists prices are the key component in a functioning market economy. They allow entrepreneurs and customers to calculate and compete for goods and resources in achieving their individual ends (Hayek, 1945; Mises, 1949; Steele, 2001). However, as Kirzener (1976) points out, the rise of public relations in the 20th century means prices are not the only mechanism to communicate market information. The power of marketing and the use of readily available qualitative information, to inform and persuade customers to buy and sellers to sell cannot be ignored. Thus, considering prices as the only factor in informing individual decision making is not enough in modern markets (Bikhchandani & Sharma, 2000). This undermines the Austrian analysis of the market economy, because in their view human actions is based on economic calculations, which in turn are based on prices. The mathematical nature of the price mechanism means individuals are able to make rational decision based on perfect knowledge. However, the advent of media and its uncanny ability to persuade individuals in making irrational decisions based on limited knowledge questions the characteristics of a market economy defined by the Austrian school of economics. The interplay of Human action ruled by individual ends, prices, resources, goods and competition no longer govern the market process, instead there are must be a recognition of other elements that affect this process. For example, government intervention is a reality, other factors include organizational size and internationalization (Hymer, 1972; Stiglitz, 1989). Furthermore, considering the power of self-interest and the irregularity of human action the market becomes an increasingly anti-competition entity (Krausz, 2004). Even Adam Smith acknowledged the tendency of totally free markets to develop anti-competitive monopolies (Bootle, 2011).

Proponents of pure laissez-faire economics would call for government to withdraw from the market altogether so that entrepreneurs can equally compete in a self-regulating free market (Hayek, 1945; Mises, 1949; Read, 1958). However, it is questionable whether a free market is possible or even desired. Our social evolution under a mutated economic system has led to certain sections of society accumulating excessive wealth and power which they may not have accumulated under a free market economy (Buchanan, 2000). We certainly do not have the luxury of starting from zero. Thus, opting for non-intervention would potentially enable these sections to monopolize industries, contradicting free market principles. Entrepreneurs have not been able to apply disruptive innovation as Schumpeter (1942) had predicted, instead as Kirzner (1971) points out perceived opportunities have not been fulfilled. Furthermore, whilst free market ideology is prevalent it is only applied when it suits the status quo. Since the 1970s leading world economies of the US and UK have tried to free key markets and the financial markets in particular (Carothers, 1991; Reisman, 1999). However, this has led of firms forming cartels to gain an unfair competitive advantage. The combination of ineffective regulation from government and anticompetitive behavior by firms has compromised the essential role of competition in regulating the market (Read, 1958). The situation we face today stinks of regulatory capture and resonates with Marx's notions, as a select section of society monopolizes the policy mechanism which in turn monopolizes the production mechanism (Carothers, 1991; Tirole & Laffont, 1991; Chomsky, 1996; Hopkins, 2007). There is romanticism with the free market in that it will deliver the most efficient outcomes best suited to the economy and society (Chomsky, 1996). This almost always ignores two uncomfortable facts. One, the market can be manipulated by those in power to deliver outcomes favorable to them. Second, even in a truly free market the most efficient outcomes are not always desirable in civil society. The ideological evolution of the human civilization has lead us to a point were corporations, and indeed democracy, is now synonymous with a dark, unfettered form of capitalism. Within this landscape entrepreneurs face a losing battle against corporations who enjoy monopoly prices and effectively control the market (Korten, 1995; Chomsky, 1996; Steele, 2001; Fukuyama, 2013).

A case for intervention

This paper is not a comprehensive comparison of Austrian and Keynesian schools, but, highlighting their opposing views on interventionism can help explain the diverse range of policies used by governments to support entrepreneurship. Whichever school one prescribes to, mainstream economists have their heads buried in text books, out of touch with reality (Buchanan, 2009). Each side is busy proving their religion is right whilst ignoring the humanity they were meant to save. For entrepreneurship to flourish, certainly in the classical view, we need a market economy free from government interference so prices are not coerced and competition is fair (Mises, 1949; Rothbard, 1963). However, interventions are a reality and although government efforts of trying to control elements of the economy have varied throughout the history of capitalism, the market has never been truly free (Friedman, 1964). So, it would be foolish to try and apply free market principles in polities that have never experienced a free market economy.

Furthermore, the demise of competition and the inability of the price mechanism to effectively regulate the market makes government intervention a necessity. It is true we cannot fully understand, thus, cannot fully control the market. Instead of good, interventions can potentially do harm because governments do not have the ability to see or even understand why, when, where and which type of interventions are needed (Mises, 1949; Caldwell, 1997). However, the argument, "if you can't fix it don't try", is also not acceptable and uncharacteristic of human action. We cannot accept and participate in a system we do not fully comprehend. A crucial aspect of human action is to understand, tame and manipulate all phenomenon useful to us and the entrepreneurial ecosystem is no different (Roathbard, 1963). It is clear we need interventions to save entrepreneurship from large corporations that enjoy monopoly prices and thus favorable competitive conditions. However, the type of intervention is equally important. For too long the interventionist paradigm has revolved around capital and we have generally seen government interventions for entrepreneurs in the form of tax breaks or subsidies (Holtz-Eakin, 2000; Li, 2002). These tends to be rigid, at times irrelevant and so useless to entrepreneurs. These interventions also do not discriminate against inefficient firms and thus create the free rider scenario for inefficient firms, distorting conditions within the entrepreneurial eco-system (Buera et al. 2012). As Buchanan (2009) suggests we should start by paying more attention to constitutional structures and the individual interactions and transactions that govern them.

Governments or their respective departments do not have the knowledge or expertise to provide suitable support for entrepreneurship in the long-run. Any policy framework to support entrepreneurship must be designed in partnership with public and private organizations. The resulting policy frame work must facilitate and combine the knowledge educational institutions have to offer with the expertise established firms can provide. Together this trinity of government, education and established firms can provide a robust and responsive policy framework that delivers focused support for entrepreneurs. The trinity framework is intended to provide a robust policy frame work that is intuitive, relevant and applicable to a range of entrepreneurial eco-systems. At the micro level this framework resembles the functions of an incubator, however, incubators do not combine different elements of government, education and private enterprises all at the same time. There certainly is no coherent strategy that deliberately combines these different elements within a policy framework (Groenewegen & Steen, 2007).

This paper seems to be turning into a proposal, however, that is not our intention. Instead our aim is to highlight the importance of public private partnerships in designing an effective policy frame that is responsive to the diverse needs of entrepreneurs and indeed entrepreneurship (Nelson, 2007; Grossman; 2008; OECD, 2012) . Furthermore, these partnerships can help ensure the support for entrepreneurs remains relevant and does not become a hindrance in the long-term. Entrepreneurship is fast becoming a public good and cannot be delivered through a policy framework alone. Any such framework must be supported by culture and promoted through effective entrepreneurship education. Popular media can also help promote the significance of entrepreneurship (European Commission, 2007).

CONCLUSION

The latest economic crises has highlighted inherent defects in an unchecked form of capitalism and free market ideology that has dominated political and economic thought since 1970s (Carothers, 1991; Boettke, 1997). In an era defined by scarcity, conflict and economic anarchy the debate between Keynes and Hayak is as important today as it was in the 1940s (Steele, 2001). This paper has attempted to highlight the key tenants of the Austrian reasoning for non-intervention, whilst providing a rationale for its insignificance in the 21st century. Non-intervention may work well as a theoretical frame work but in reality it will only favor those already ahead of the game. The sheer size and depth of corporations means they are able to enjoy monopoly prices and thus the role of competition is insignificant. Indeed in the age of big corporations, big government is a necessary evil to protect the integrity of the market and facilitate entrepreneurship. However, we must work with the world as it is, not as it should be, thus corporations must be part of the solution and not just the problem (Snyder, 2002). The importance of public private partnership to support entrepreneurship is clear. However, further investigation is needed to understand how a policy frame work combining the trinity of government, educational institutions and corporations can be used to provide effective protection and support for entrepreneurship. Whilst ensuring the policy framework itself remains relevant in a rapidly changing environment. Effective intervention that is intuitive to the changing needs of entrepreneurship is the only way real creative destruction can flourish and economies can develop. If entrepreneurship continues to be compromised, the forces of creative destruction will be hijacked by corporations, with economies and indeed countries at their mercy.

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