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## Entrepreneurship has emerged as the Economic Engine and Social Development throughout the World

**Abstract**

This paper consists of an introductory survey of two fundamental questions regarding the link between international entrepreneurship and economic growth. The first step in establishing the linkages requires the formulation of knowledge about the psychological make-up of entrepreneurs. The paper explains that Entrepreneurial activity breeds innovation, injects competitive pressures and develops opportunities in economies. It is the foundation in many respects for broader economic development. Entrepreneurship policies are equally important, as an engine of innovation, in developed countries as they are in developing or transition economies. The purpose of this paper is to explain why the model of the entrepreneurial economy maybe a better frame of reference than the model of the managed economy when explaining the role of entrepreneurship in the contemporary, developed economies. While borrowing constraints or other financial frictions affect entrepreneurship productivity and the distribution of income by restricting agents from profitable occupations that require capital, such as entrepreneurship, this paper is devoted to exploring issues aiming to increase national wealth and to improve international competitiveness of the national economy.

**Keywords:** Entrepreneurship, small firms, economic growth, economic development, policy

**1. Introduction**

International entrepreneurship involves a combination of innovative, proactive, and risk-seeking behaviors that crosses country borders, and is supposed to create value in organizations. International entrepreneurship uses technological and regulatory advances to improve the flow of information, transportation and resources across global borders. International entrepreneurship may involve the discovery, enactment, evaluation, and exploitation of opportunities- across country borders- in order to create goods and services. The strategic role of the entrepreneur as an agent of economic transformation in society is visible in employment and wealth generation, stimulation of indigenous entrepreneurship or promotion of entrepreneurial culture. In the recent development literature occupational choice is at the center of the development process (e.g. Banerjee and Newman (2000), and Galor, 1993). Able individuals who start poor are doomed to remain poor.

Entrepreneurs produce solutions that fly in the face of established knowledge, and they always challenge the status quo. They are risk-takers who pursue opportunities that others may fail to recognize or may even view as problems or threats. Whatever the definition of entrepreneurship, it is closely associated with change, creativity, knowledge,

innovation and flexibility-factors that are increasingly important sources of competitiveness in an increasingly globalized world economy. Thus, fostering entrepreneurship means promoting the competitiveness of businesses.

The paper advocated a shift in paradigm in re-thinking entrepreneurial failure in the developing countries. In these models, borrowing constraints or other financial frictions affect productivity and the distribution of income by restricting agents from profitable occupations that require capital, such as entrepreneurship. To understand the significance of entrepreneurship for national economies it is important to consider cross-border entrepreneurship or the involvement of SMEs and new ventures in the international economy. Cross-border activities, such as exports, are an important means through which small and new ventures are able to create value, to generate growth and to access new knowledge and technologies abroad (Yeoh, 2004). Governments support cross-border entrepreneurship and in particular exports with the aim to increase national wealth and to improve international competitiveness of the national economy (OECD, 1997). The missing links to successful entrepreneurship were identified to be entrepreneurial competencies, defined as the cluster of related knowledge, attitudes, and skills which an entrepreneur must acquire or possess to enable him produce outstanding performance and maximize profit in the business. These entrepreneurial

competencies were the critical success factors to entrepreneurship, and they deserve serious consideration in entrepreneurial discourse and not to be neglected.

Entrepreneurship, as measured by various indicators such as start-up activity rates or the increase in business ownership, plays an important role in national economies (Van Stel, 2006). Entrepreneurship is considered to be an important mechanism for national economic development e.g. through its contribution to the generation of employment and innovation (Acs and Audretsch, 2003; Baumol, 2002; Carree and Thurik, 2003; Wennekers and Thurik, 1999; Schumpeter, 1934). However, considerable differences exist between countries in the extent to which entrepreneurship is growth- or innovation oriented (Autio, 2007; Hessels, van Gelderen and Thurik, 2008a), and consequently in the extent to which entrepreneurship contributes positively to national economic development. Therefore, it is essential for scientists, policy makers and entrepreneurs, to gain insight into the factors that affect the emergence of entrepreneurship and into the economic outcomes of entrepreneurship. A substantial part of this paper is devoted to exploring such issues. One particular type of entrepreneurship that receives considerable attention in this paper is international entrepreneurship.

Knowledge has typically been measured in terms of R&D, human capital, and patented inventions. Many scholars have predicted that the emergence of knowledge as an important determinant of growth and competitiveness in global markets would render self-employment and small firms even more futile. Despite these forces, small and young firms have returned as the engine of economic and social development in highly developed economies. This return required a dramatic economic switch. Audretsch and Thurik (2001a, 2004) call this the switch from the managed economy to the entrepreneurial economy. The model of the managed economy is the political, social, and economic response to an economy dictated by the forces of large-scale production, reflecting the predominance of the production factors of capital and (mostly unskilled) labor as the sources of competitive advantage.

As additional studies were conducted and articles published, interest in the arena increased, and the field of international entrepreneurship broadened from its early studies of new venture internationalization theory. For example, insightful studies on national culture (McGrath & MacMillan 1992; Thomas & Mueller, 2000), alliances and cooperative strategies (Steensma, Marino, Weaver, & Dickson, 2000; Li and Atuahene-Gima, 2001), small and medium sized company internationalization (Lu & Beamish, 2001), venture financing (Roure, Keeley & Keller, 1992), and technological learning (Zahra, Ireland & Hitt, 2000) have all helped move the field forward. Reflective of the multi-disciplinary nature of both entrepreneurship and

international business, researchers have drawn upon theories and frameworks from international business, entrepreneurship, anthropology, economics, psychology, finance, marketing, and sociology. The entrepreneurs in turn exploit the available opportunities in the society or their environmental domain, to create or develop new products or services, thus adding value to society while equally maximizing benefits or profits. The impact of the activities of the entrepreneurs or small and medium enterprises (SME) on the socio-politico-economic life of emerging economy is quite obvious. It is clear that the domain of international entrepreneurship is rich in opportunity.

Because the field is broad, there are many interesting research questions to be explored, and many existing theories may be beneficially employed. Opportunities for both multidisciplinary and multi-country collaboration are clear.

Entrepreneurship has been an engine of sustained economic expansion in both developed and emerging economies (e.g., Baumol, 2002; Peng, 2001; Smallbone & Welter, 2001; Thornton, 1999). One critical success factor for entrepreneurial firms is gaining sufficient access to external sources of finance (Ahlstrom & Bruton, 2006; Le, Venkatesh, & Nguyen, 2006). This is particularly true in emerging economies because such resources are severely constrained. For example, capital markets, venture capital, and angel investors are typically at nascent stages of development. As such, bank loans tend to be the only significant formal sources of external funding for private small and medium-sized enterprises (SMEs) in emerging economies. Therefore, a key challenge for many entrepreneurs is to find a means of accessing bank loans efficiently.

### 1.1. What is international entrepreneurship?

The rules of entrepreneurship still apply in principle, but the medium has changed drastically. This is probably the best time in our history to pursue entrepreneurship. Entrepreneurs are defying the logic and business rationale to make things happen individually. Days are when you needed huge capital and veteran management teams to form companies and to wait for another several years to rake in the profit. International business scholars Wright and Ricks (1994) highlighted international entrepreneurship as a newly emerging research direction, and it became clear the arena included (1) comparisons of entrepreneurial behavior in multiple countries and cultures as well as (2) organization behavior that extends across national borders and is entrepreneurial. While these foci have remained over time, the definition of "international entrepreneurship" has moved from a very broad one, which avoided prematurely proscribing important nascent interests (Giamartino, McDougall, & Bird, 1993), to excluding nonprofit and

government organizations to be consistent with the commonly accepted definition of “international business” (McDougall & Oviatt, 1997). One trait that is common with both entrepreneurs is that each of them is leveraging on simple inexpensive tools that are readily available to most entrepreneurs. You might ask how these successful online ventures are relevant to the conceptual economy. Conceptual economy encourages entrepreneurs to use both left and right brains. Entrepreneurship generally doesn't depend on their technical and subject matter experts, but only focusing solely on their technical skills. Rather, they are conceptually leveraging on their technical skills as well as testing their creative skills to conceptualize, design, develop and market their ideas - in most cases on their own without any help.

However, to be consistent with the interests of entrepreneurship scholars in such issues as social entrepreneurship, that exclusion was eliminated: The definition of entrepreneurship, however, is a matter of continued debate. As a result, the meaning of entrepreneurship continues to evolve. The idea that entrepreneurship is a combination of innovative, proactive, and risk-seeking behavior finds its origins in strategic management literature (e.g., Covin & Slevin, 1989; Miller, 1983), but those are not the only entrepreneurial dimensions that scholars have identified. (Lumpkin, G. & Dess, G. (1996) highlighted a variety of “entrepreneurial orientation” dimensions and distinguished them from the definition of entrepreneurship itself, which they equated with new entry, or the act of launching a new venture.

Among the factors contributing to the success of the U.S. economy over the past decade—as reflected in the doubling of productivity growth compared to the preceding two decades—is the continued transformation of the U.S. economy toward a more entrepreneurial form of capitalism. In such a system, innovative new firms play an unusually central role in developing and commercializing the radical technologies that provide the underpinnings to whole new ways of doing things and enjoying life. In the last century, innovations which have changed the social and economic landscape in the United States and in much of the rest of the world, such as the automobile, airplane, air conditioner, the personal computer and its operating system, and, most recently, many of the leading Internet-based business models, all were commercialized by entrepreneurs (Ewing Marion, 2007). Despite these counteracting forces, entrepreneurship has emerged as the engine of economic and social development throughout the world. The role of entrepreneurship has changed dramatically, fundamentally shifting between what Audretsch and Thurik (2001) introduced as the model of the managed economy and that of the entrepreneurial economy. The purpose of this paper is to explain why the model of the entrepreneurial economy maybe a better frame of reference than the model of the

managed economy when explaining the role of entrepreneurship in the contemporary, developed economies.

## 1.2. The emergence of the entrepreneurial economy in developing countries

Schøtt, and Jensen, (2008) argue that developing countries are prone to implement policies that are based on experiences in developed countries which have not proven to transfer fittingly to developing economies, (2) are only partly implemented and are not internally consistent as a result of a lack of resources to do so, and (3) are more beneficial on paper than on actual activity. Following this perspective, the pairing between entrepreneurship policy and entrepreneurship activity is hypothesized to be lower for developing countries than for developed countries. Given the painstaking and careful documentation that large-scale production was driving out entrepreneurship, it was particularly startling and seemingly paradoxical when scholars first began to document that –what had seemed like – the inevitable demise of small business, began to reverse itself from the 1970s onwards. Loveman and Sengenberger (1991) and Acs and Audretsch (1993) carried out systematic international analyses examining the re-emergence of small business and entrepreneurship in North America and Europe. Two major findings emerged from these studies. First, the relative importance of small business varies largely across countries, and, secondly, in most European countries and North America the importance of small business increased since the mid-1970s. In the United States the average real GDP per firm increased by nearly two-thirds between 1947 and 1989 – from \$150,000 to \$245,000 – reflecting a trend towards larger enterprises.

## 2. Significant constraint on future entrepreneurs in developing countries

The most significant constraint on their future entrepreneurs growth is the difficulty finding and attracting “talent”—highly skilled, entrepreneurial workers. This also looms as one of the more important challenges facing the developing economy. Meeting this challenge will require major, entrepreneurially driven improvements throughout their educational system (K–12 through graduate school) that allow more choices for students and their families; improved schools from which to choose; accelerated learning opportunities; increased funding for college and graduate-level training; and research and development in engineering and the physical sciences. In addition, the nation could benefit from more enlightened immigration policies, designed to attract and retain highly skilled citizen workers and potential entrepreneurs to start and work for new businesses.

Innovative entrepreneurship cannot occur unless the innovation pipeline is full and incentives for

commercializing innovation are in place. The distinctions between growth-oriented entrepreneurs in developing and developed markets are rooted in the inefficiency of markets in many developing countries, but the response of entrepreneurs to these inefficiencies is often surprising and counterintuitive. The wealth and poverty of developing countries has been linked in modern times to the entrepreneurial nature of their economies. Where it has existed in plenty, entrepreneurship has played an important role in economic growth, innovation, and competitiveness and it may also play a role over time in poverty alleviation (Landes 1998). Yet, entrepreneurship in developing countries is arguably the least studied significant economic and social phenomenon in the world today. Over 400 million individuals in developing countries are owners or managers of new firms (Reynolds et al. 2004). Of these, over 200 million are found in China and India alone, compared with just 18 million entrepreneurs in the United States. Yet, in one of the best general books on the state of research on entrepreneurship, China is mentioned on two pages and India is not mentioned at all (Bhidé 2000). In particular, the cognitive bias of over-optimism has helped us to understand why entrepreneurs start businesses in the face of odds of firm survival (often less than 50%) that would argue otherwise. In relation to developing countries, the most rewarding future research effort in this area may be to analyze the “differences in ambiguity aversion, self-control, susceptibility to framing and so (that) play a crucial role in the formation and evolution of businesses” (Bhidé 2000). How these differences may vary across countries, and the underlying drivers of these differences, may help us to gain a better understanding of why some countries have more successful entrepreneurs than others.

### **2.1. Entrepreneurs in developing countries face a different set of circumstances**

Opportunities for entrepreneurs in developing countries are broader in scope than in developed markets, allowing firms to pursue a portfolio approach to strategy that can efficiently manage the higher levels of business and market risk. Entrepreneurs in developing countries face a different set of circumstances than their counterparts in developed economies. These differences are rooted in the underlying economies in which they operate. It is clear that the domain of international entrepreneurship is rich in opportunity. Because the field is broad, there are many interesting research questions to be explored, and many existing theories may be beneficially employed. Consequently, the opportunity for entrepreneurship in emerging markets is pervasive. While Western entrepreneurs operate at the fringes of the economy, emerging market entrepreneurs operate closer to the core – the needs and opportunities are more widespread. Entrepreneurs in emerging markets rely very heavily on informal sources of finance to start their businesses; these sources provided between 87% and 100%

of the outside capital raised by entrepreneurs (Bygrave 2003). Other sources of financing typically targeted by development finance institutions interested in improving access to finance in the emerging markets—bank lending and venture capital—play a very limited role at present in financing entrepreneurs, at least in the startup stage.

Inadequate access to capital and fragmented retail and distribution often require entrepreneurs to begin businesses downstream with direct access to the end customer. Starting downstream businesses reduces initial capital requirements as working capital is much reduced and permits access to customers and information flow that is frequently lacking. Access to such information is often overlooked as a key success factor. Lack of access to the end customer is a primary reason for the failure of South American businesses to move beyond commodity markets into higher value added activities (Fairbanks and Lindsay 1997). Having achieved success in retail and distribution, successful entrepreneurs often leverage the domain experience, information flow, and cash flow generated to vertically integrate and move into upstream businesses.

Research on the determinants of private savings in developing countries suggest that countries that have experienced economic instability are more likely to have higher rates of private saving, maintained as an insurance mechanism (Loayza, Schmidt-Hebbel, and Servén 2000). Crisis represents opportunities; at least as far as forming the pools of private capital necessary for startup finance is concerned. Moreover, while successful entrepreneurship is correlated with urbanization, urbanization also results in an increase in individual consumption and a concomitant decrease in private savings. Thus, successful entrepreneurs are likely to find ways to access the greater pools of private saving in the countryside in order to start their businesses. This highlights the possible importance of well-developed family networks that span both urban and rural areas. How such private rural savings are intermediated into urban entrepreneurship is not at present well understood and almost certainly will vary by country.

Scholars have categorized the institutions that shape entrepreneurial behavior into three main groups: I. property rights; II. contract enforcement; and III. entry costs and regulation. Djankov (2008) asserts that the most important effect of recent entry costs and regulation reforms in developing countries (as measured by the World Bank’s Doing Business initiative) has been increased movement of informal firms into the formal economy. Recent research by Malesky and Taussig (2008) using firm survey data from Vietnam, in turn, finds time spent in the informal economy before registering as companies is significantly lower when property rights are stronger, but finds no effect for



contracting institutions. We hypothesize that a less favorable regulatory environment means higher risks of doing business and therefore increases the importance of property rights in shaping entrepreneurial strategy. Improving regulatory conditions through measures such as the Enterprise Law should then lower investment risks and thereby diminish the pivotal role of property rights.

## 2.2 Entrepreneurship policy and activity in developing countries

While the increasing importance of entrepreneurship for economic growth has widely transferred into national as well as international political agendas, not all national governments have been equally successful in devising policies that have generated economic growth. Notably, developing countries have been significantly less able to stimulate national economic growth when compared to developed countries. Easterly (2001) reports, that whereas median per capita income growth in developing countries in 1960-1979 was 2.5 percent, it declined to 0.0 percent in 1980-1998 – a period that Easterly terms as “the lost decades”. By a lack of entrepreneurship policy to support entrepreneurial activity per se, but rather a consequence of the circumstance that the entrepreneurship policies in developing countries are less fit for the local economic and cultural contexts in which they are implemented (Meyer *et al.*, 1997), and that the coupling between policy and action is looser in developing countries than in developed countries (Drori, 2003).

From an institutional perspective, people engaged in policy-making are much more enactors of scripts from institutionalized worldwide models defining legitimate agendas for local action, than they are actors pursuing rational responses to internal and external contingencies (Meyer *et al.*, 1997). Yet, from a functional perspective, elements of worldwide models are often not internally consistent and are often poorly fitted to local practices. In addition, elements of world models are often adopted electively and diffused at various levels. In turn these inconsistencies form the basis for a loose coupling between purpose and structure, between intentions and results, and hence disconnect between policy and activity is likely to result (Meyer *et al.*, 1997). Yet, decoupling is more likely to exist under some circumstances. The availability of resources in a country not only affects the likelihood of a fit between scripts from the world models and the local practices of the country, but also affects the ability of the country to adopt such scripts for national policy, planning and activity. This means that more elaborate models exist to describe entrepreneurship in developed economies than in developing economies. Adopting entrepreneurship policy scripts from the world model toolbox may necessitate a substantial amount of resources available for the local

government in order to implement the necessary actions to support local entrepreneurship.

Given that less developed countries do not have such resources; it is likely that even if scientific recommendations are included in public policies, that implementation of the necessary activities will not happen accordingly. The theory is that developed countries have a tight relationship between entrepreneurship policy and activity, whereas for developing countries there will be a loose coupling between entrepreneurship policy and entrepreneurship activity. Yet, the conceptualization of tight versus loose pairing extends beyond that of interdependence between system elements. As noted by Weick (1976) loose coupling describes a situation in which elements are responsive to one another yet retain much separateness and identity. This conceptualization of loose coupling allows system elements to, on the one hand, act rationally on the technical level, while on the other, being faced with indeterminateness on the institutional level being exposed to outside forces (Orton and Weick, 1990).

## 2.3 The framework policy promote entrepreneurial enterprises in USA

Economist Joseph Schumpeter described that not every business owner is an entrepreneur – far from it. Consequently, he described as a true entrepreneur somebody who breaks through existing conventions by devising a new product, a new production process, a new business model, or by entering a new, untapped market. If entrepreneurs play such an important role, we would like to have more of them and enable them to be successful. This inevitably leads to the question of what (if anything) can be done to help and foster entrepreneurship, especially through public policies. But our admiration of innovative entrepreneurs, especially in high tech, is not only naïve infatuation. It is linked to the evolution of USA economy. We are transitioning from an industrial economy, based on labor and capital intense mass-production of goods, to a knowledge economy, in which information and knowledge are becoming co-equal in importance to capital and labor. In such an economy, the person who can take a radically new idea and bring it successfully to market is of central importance.

Our purpose here is to concentrate on the policy framework that can best promote the development and growth of these entrepreneurial enterprises—in short to sustain and deepen the transition away from the *managerial capitalism* of the 1950s and 1960s (when citizens and policymakers looked to large established firms to carry the economy) to the *entrepreneurial capitalism* of the last several decades and which we are currently witnessing today (where much driving force behind the economy’s growth is being provided by rapidly growing new firms). This is not to

ignore the importance of the many millions of smaller businesses whose owners intend for them to remain small or to grow only modestly. These firms also greatly contribute to US economy, while sustaining the lives of their proprietors and their families. But the relatively small fraction of all entrepreneurs who bring to market new or innovative products or services or means of producing or delivering them deserve society's special attention because these innovations deliver benefits widely throughout the economy, raising its productivity and the standard of living. Concerning the path of development, Lall (2001) says that the appropriate strategy for any country depends not only on its objective economic situation but also on its government policies and national views regarding the appropriate role of the state.

In the West, the resulting industrialization and economic development were based on the establishment of individual property rights that encouraged the growth of private capital. Competition and individual enterprise thrive in this environment because individuals pursue their self-interest of survival and wealth accumulation. The instinct to survive under competitive pressures yields innovation and productivity increases, which eventually lead to both increased profits for business and lower prices to consumers. However, the rise and spread of capitalism led a number of thinkers to examine the consequences of the market-based approach to development. Socialists argued that capitalism (or private ownership of capital) can lead to greater inequalities of income and wealth, while developmental economists argued that private decisions may not always lead to socially desirable outcomes (particularly in the case of market imperfections). Indeed, many policymakers at the time saw market failures as quite common and therefore assumed that only appropriate government interventions could guide an economy to a path of sustained economic development (Krueger, 1993).

The most prevalent and compelling views of entrepreneurship focus on the perception of new economic opportunities and the subsequent introduction of new ideas in the market. As Audretsch (1995) argues, entrepreneurship is about change, just as entrepreneurs are agents of change; entrepreneurship is thus about the process of change. "Entrepreneurs are agents of change and growth in a market economy and they can act to accelerate the generation, dissemination and application of innovative idea. Entrepreneurs not only seek out and identify potentially profitable economic opportunities but are also willing to take risks to see if their hunches are right" (OECD, 1998, p. 11).

## Results and Findings

Entrepreneurial activity has a direct impact on society by providing increased consumer choice; more appropriate,

affordable and even indispensable services; and further employment opportunities both directly and indirectly through suppliers. Entrepreneurial activity breeds innovation, injects competitive pressures and develops opportunities in economies. It is the foundation in many respects for broader economic development. The key role of entrepreneurship is now increasingly recognized by international policy makers as perhaps the key element in national development strategies. Entrepreneurship policies are equally important, as an engine of innovation, in developed countries as they are in developing or transition economies.

In many countries, in particular developing countries but also in developed countries, the regulatory environment with which entrepreneurs find themselves faced can be both oppressive and emasculating. Employers' organizations have a key role to play in publicizing the benefits of formalizing economic activities. Entrepreneurs are often faced with an array of barriers and obstacles - such as business registration or access to workable systems of contract enforcement. In the more short to medium term employers' organizations can urge governments to develop incentives to innovate, through intellectual property rights and, perhaps most importantly, capitalizing on existing technology developments. Even if countries are not inventors of technology they can still be beneficiaries through the importation of technology - this is a well traveled and proven path for many countries.

Governments must genuinely aim to create the space for entrepreneurship to flourish and for a culture of innovation to take hold. A good investment climate (such as good social and physical infrastructure; environment conducive to enterprise development; good governance structures, rule of law, property rights, etc) makes it easier for firms to enter and exit markets in a process that contributes to higher productivity and faster growth.

## Conclusion

The key role of entrepreneurship is now increasingly recognized by international policy makers as perhaps the key element in national development strategies. Entrepreneurship policies are equally important, as an engine of innovation, in developed countries as they are in developing or transition economies. We further used the Human Development Index as an indicator of a country's stage of development. We therefore advocate for a *Schumpeterian approach to policymaking* in order to facilitate entrepreneurial activities: policy frameworks should not be seen as regulatory backdrops that are designed to provide stability, but as dynamic tools to create and bring about opportunities that entrepreneurs can seize and exploit.

Policy makers, particularly in developing countries, have limited resources that must be used strategically and efficiently. Organizations that leverage their expertise and resources, pursue policies systematically and have strategies to achieve initiatives that lie within their competencies and capacities are likely to have the most success in advocating policies to foster entrepreneurship. Of course, as all entrepreneurial activity, they also entail risks. But devising successful policies for entrepreneurship is not an impenetrable black box. A preliminary analysis yields three rules-of-thumb policymakers should heed in designing Schumpeterian policies that can be summarized as act, experiment, and risk.

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**Acknowledgements:** Author would like to thank the editor and anonymous referees for their comments and insight in improving the draft copy of this article. Author further would like to declare that this manuscript is **Original** and has not previously been published, and that it is not currently on offer to another publisher; and transfer copy rights to the publisher of this journal after the paper is accepted.

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