17. The Impact of Entrepreneurship on Economic Growth

INTRODUCTION

The last two decades have witnessed a wealth of studies analyzing the determinants of entrepreneurship. While some of these studies are theoretical (e.g. Holmes and Schmitz, 1990), others are empirical (e.g. Evans and Leighton, 1990). The consequences of entrepreneurship, in terms of economic performance, have also generated an extensive literature. However, this literature has generally been restricted to two units of observations – that of the establishment or firm, and that of the region. Noticeably absent are studies linking the impact of entrepreneurship on performance for the unit of observation of the country. A large literature has emerged analyzing the impact of entrepreneurship on economic performance at the level of the firm or establishment. These studies typically measure economic performance in terms of firm growth and survival (Audretsch, 1995; Caves, 1998; Sutton, 1997).

The compelling stylized facts that have emerged from this literature are that entrepreneurial activity, measured in terms of firm size and age, is positively related to growth.1 New firms and (very) small firms grow systematically larger than large and established incumbents. These findings hold across modern Western economies and across time periods. The link between entrepreneurship and performance has also been extended beyond the unit of observation of the firm to include geographic regions. A small literature exists linking measures of entrepreneurial activity for regions to the economic performance of those regions (e.g. Audretsch and Fritsch, 2002; Acs and Armington, 2003).

However, when it comes to linking entrepreneurship to growth at the national level, there is a relative void despite recent efforts of the Global Entrepreneurship Monitor (GEM) research program (Reynolds et al., 2001). The purpose of this chapter is to provide a survey of what is known about the links between entrepreneurial activity and macro-economic growth. Despite

1See Audretsch, Klomp and Thurik (2002) for a recent survey of studies dealing with Gibrat's Law.
the numerous studies claiming a link of entrepreneurship to economic growth
the relative void may be attributable to a paucity of theoretical frameworks
linking entrepreneurship to growth, as well as severe constraints in measuring
entrepreneurship in a cross-national context. Furthermore, there is the reversed
causality of economic development influencing entrepreneurial activities. In
this chapter we provide five short overviews of the relevant literature and
complement them with some new material.

Explanations for economic growth have generally been restricted to the
realm of macro-economics (Romer, 1990). However, a different scholarly tradi-
tion linking growth to industrial organization dates back at least to Schumpeter
(1934). According to this tradition, performance, measured in terms of economic
growth, is shaped by the degree to which the industry structure utilizes scarce
resources most efficiently. This (most efficient) industrial structure does not
alter in case its underlying determinants are stable. However, as Chandler
(1990), Scherer and Ross (1990) and Dosi (1988) emphasize, a change in the
underlying determinants would be expected to result in a change in the industry
structure most conducive to growth. Certainly, Chandler (1990) and Scherer
and Ross (1990) identified a shift in industry structure towards increased
centralization and concentration throughout the first two-thirds of the previous
century as a result of changes in the underlying technology along with other
factors.

More recently, a series of studies has identified a change in the determinants
underlying the industry structure that has reversed this trend. The most salient
point of this change is that technological change, globalization, deregulation,
shifts in the labor supply, variety in demand, and the resulting higher levels of
uncertainty have rendered a shift in the industry structure away from greater
concentration and centralization towards less concentration and decentraliza-
tion. A series of empirical studies have uncovered two systematic findings
regarding the response of industry structure to changes in the underlying
derminants. The first is that the industry structure is generally shifting towards
an increased role for small firms. The second is that the extent and timing of
this shift is anything but identical across countries. Apparently, institutions
and policies in certain countries have facilitated a greater and more rapid
response to technological change and globalization, along with the other under-
lying factors, by shifting to a less centralized and more dispersed industry
structure than has been the case in other countries. The question of whether
countries that have shifted towards a greater role for entrepreneurship enjoy
stronger growth is of large importance to policy makers.

Entrepreneurship is “at the heart of national advantage” (Porter, 1990,
p. 125). Concerning the role of entrepreneurship in stimulating economic
growth, many links have been discussed. It is of eminent importance for carrying
out innovations and for enhancing rivalry. This directs our attention to two
related phenomena of the 1980s and 1990s: The resurgence of small business
and the revival of entrepreneurship. There is ample evidence that economic
activity moved away from large firms to small firms in the 1970s and 1980s.