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Entrepreneurship and Economic Development: Theory, Evidence and Policy

Wim Naudé¹

Abstract

This paper provides an overview of the state of the art of the intersection of development and entrepreneurship. Given the neglect of entrepreneurship by development scholars it deals with (i) recent theoretical insights from the intersection of entrepreneurship and development studies; (ii) the empirical evidence on that relationship between entrepreneurship and development; and (iii) fresh insights for entrepreneurship policy for development that emerges from recent advanced in this area, including female entrepreneurship in developing countries.

Key words: Entrepreneurship, development, small business, private sector development

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1. Introduction

Adam Smith, founding father of modern economics ‘detested business men’ (Lewis, 1988: 35). Development scholars and development economists in particular have, if not detesting business men or entrepreneurs, (benignly) neglected them. Following Leff (1979:51) many development scholars took the position that ‘entrepreneurship is no longer a problem’ or a ‘relevant constraint on the pace of development’ in developing countries. Entrepreneurship scholars on other hand have been more concerned with the *who*, *why* and *how* of entrepreneurship rather than with the impact of entrepreneurship on development or developing countries (Shane, 1997; Bruton et al. 2008); a situation described as a ‘scholarly disconnect’ (Audretsch et al., 2007: 1-2).

Why does this matter? First, it is widely believed that entrepreneurship is beneficial for economic growth and development (Audretsch et al., 2006). Second, entrepreneurship has been remarkably resurgent over the past three decades in countries that achieved substantial poverty reduction – e.g. in China (Mohapatra et al., 2007). Third, donors and international development agencies have been turning to entrepreneurship to improve the effectiveness and sustainability of aid (Pronk, 2003; Hubbard and Duggan, 2009).

However, the theoretical and empirical cases for understanding the role of entrepreneurship are not yet solid. Evidence on whether entrepreneurship matters for economic growth is not straightforward; how entrepreneurship has been promoted and how it contributed to development in countries like China and the East Asian Tigers is still a matter of contention; and whether and why private sector development initiatives may be effective is not well understood (Bruhn and Zia, 2011; Karlan and Valdivia; 2010; Oosterbeek et al. 2010; Klinger and Schündeln; 2010).

Closer scrutiny of the relationship between entrepreneurship and economic development is therefore needed. In order to stimulate the development-entrepreneurship discourse it may be necessary to first attempt to formalize or reconcile the role of entrepreneurship in the “grand ideas” of development economics, and to consider how this resonates with available evidence, and what this means for policy (Naudé, 2010).

There are at least three “grand” ideas in development economics. The first is that development requires a structural transformation of what, how and where production and consumption takes place: from low-value added, low productivity and mainly rural (and agricultural) based activities to more productive, higher value added activities in services and manufacturing located largely in cities. The second idea is that development is a multi-dimensional concept that requires more than just the eradication of income poverty. The third is the idea that market failures are prevalent and that the state has an important coordinating and regulatory role to play in development.

All of these grand ideas are currently at the forefront of thought in development, and much of what development scholars are occupying themselves with either directly or indirectly resort under the umbrellas of these ideas.

Accordingly this paper provides an overview of the state of the art in terms of development and entrepreneurship. It is concerned with the theoretical insights from the intersection of entrepreneurship and development studies (section 2); with the empirical evidence on that relationship between entrepreneurship and development (section 3); and on the fresh insights for entrepreneurship policy for development that emerges from recent advanced in this area (section 4).

2. Theoretical Perspectives on Entrepreneurship in Development

2.1 Concept, Definitions and Relevance for Development

Entrepreneurship definitions can be categorized into *behavioral* and *occupational* definitions (Naudé, 2010). Recently Gries and Naudé (2011) proposed a *synthesis* definition.

- Behavioural definitions

Schumpeter (1950; 1961) famously defined the entrepreneur as the coordinator of production and agent of change ('creative destruction'). As such the entrepreneur is an innovator, rather than a manager or financier. Scholars who share this view of entrepreneurship do not consider entrepreneurship to be very important in earlier stages of economic development – they seen the contribution of entrepreneurship to be much more important at later stages of development, where economic growth is driven by knowledge and competition that pushes out the production possibility frontier. At earlier stages of development growth is not as such driven by entrepreneurship but by factor accumulation (Porter et al. 2002; Ács and Naudé, 2012).

Other behavioural definitions allow for a more substantial role for entrepreneurship in developing countries. Kirzner (1973) and Schultz's (1975) views of the entrepreneur as someone who facilitates adjustment to change by spotting opportunities for profitable arbitrage (and 'disequilibrium' situations in the market) has found resonance amongst scholars who emphasize the opportunity-grabbing-for-profit nature of entrepreneurship (e.g. Shane and Ventakaram, 2000) and who considers market disequilibria to be common in developing country circumstances.

Behavioural definitions also include definitions that stress the risk-taking dimension of entrepreneurship. Kanbur (1979:773) described the entrepreneur as one who 'manages the production function' by paying workers wages (which are more certain than profits) and shouldering the risks and uncertainties of production. Such definitions are seen as very relevant for developing country contexts characterized by high risk and uncertainty. The predominance of small firms in developing countries – the bulk of entrepreneurship studies in developing

countries are concerned with small and medium enterprises (SMEs) (Ayyagari et al. 2011) - has been postulated to be a symptom of economy-wide uncertainty, where the probability of success is small (Wiggins, 1995).

From these views policy implications follow – for instance that government policy for promoting entrepreneurship should reduce uncertainty / transaction costs. Policy though, is only a proximate cause for risk and uncertainty and in recent years development scholars have recognized ‘institutions’ (the “rules of the game”) as the ultimate determinant of development. Institutions affect not only the supply but perhaps even more importantly the allocation of entrepreneurship. According to Baumol (1990:895) entrepreneurial ability can be allocated towards productive, unproductive, or even destructive activities. He defines entrepreneurs as ‘persons who are ingenious and creative in finding ways that add to their own wealth, power, and prestige’ (Ibid, 1990:987). Underdevelopment may not be due to an insufficient supply of entrepreneurs, but due to institutional weaknesses that result in a ‘lack of profit opportunities tied to activities that yield economic growth’ (Coyne and Leeson, 2004:236).

- Occupational definitions

In economic theory entrepreneurship has been modeled as an occupational choice between self-employment and wage-employment (see Lucas, 1978; Evans and Jovanovic, 1989; and Murphy et al., 1991). Hence someone will become an entrepreneur if profits and the non-pecuniary benefits from self-employment exceed wage income plus additional benefits from being in wage employment. Entrepreneurship is thus often synonymous with self-employment. Because self-employment is often not by choice but by necessity, a distinction is often made in between necessity and opportunity entrepreneurs – as in for instance the Global Entrepreneurship Monitor (GEM – see Reynolds et al., 2005).

- A synthesis definition

Gries and Naudé (2011) proposed a synthesis definition; it combines behavioural and occupational views and relates entrepreneurship to the three big ideas in development economics as discussed in the introduction. They define entrepreneurship as “the resource, process and state of being through and in which individuals utilize positive opportunities in the market by creating and growing new business firms”. As a *resource*, entrepreneurship has the instrumental value that it is accorded in economics; as *process* it accords to the attention given in management studies on the start-up, growth and exit of firms and as *state-of-being* it recognizes that entrepreneurship is not limited to being instrumental, it is often valued in itself (as will be explained in greater detail in section 3).

Gries and Naudé (2011) emphasize the process value of entrepreneurship and describe entrepreneurial opportunities in a broader sense than is usual in the entrepreneurship literature. For instance Shane and Venkataraman (2000) define an ‘opportunity’ as when goods can be sold at a profit. From a development perspective this is inadequate because it implies that utility from

entrepreneurship depends only on monetary gains. “Opportunities” should include situations when persons can create new firms that will further the kind of lives they desire.

Their use of the adjective “positive” in relation to opportunities reflects a subjective assessment that while entrepreneurial *ability* may be allocated to destructive activities (as in Baumol, 1990) it should not be defined as entrepreneurship if it detracts from either individual or societal welfare.

The following sub-sections will consider the contribution that entrepreneurship can make to illuminate the three “big ideas” in development economics.

2.2 Structural economic transformation and entrepreneurship

One of the seminal contributions to development economics has been dual economy models inspired by Lewis (1954) and utilized to explain the structural transformation of underdeveloped economies.

Gries and Naudé (2010) extended the Lewis model to explicitly incorporate the entrepreneur. They follow the Lewis-model distinction between a traditional and modern sector, and underpin this with micro-foundations (optimizing households, firms and labour market matching). They also distinguish between mature and start-up entrepreneurs, between large firms and small firms and between necessity and opportunity-driven entrepreneurship. In their model the transformation from a low-income, traditional economy to a modern economy involves significant changes to production methods, a process of change where entrepreneurs provide essential roles, including providing innovative intermediate inputs, permitting specialization and raising productivity and employment.

Their model builds on extends earlier work of Rada (2007), Peretto (1999) and Murphy et al (1991). In Rada (2007) entrepreneurs ‘trigger’ an investment in the modern sector once they have perceived profitable opportunities and facilitate the re-allocation of production factors from the traditional to the modern sector. Peretto (1999) provided a modified endogenous growth model that implied long-run structural transformation depends on the degree to which an economy can make a transition from a growth path driven by capital accumulation (‘the Solow economy’) to a growth path driven by knowledge accumulation (the ‘innovation-driven’ economy).

In structural change entrepreneurial ability has been accorded centre stage. Murphy et al (1991) provided a model that described firm size and the growth of the economy as a function of entrepreneurial ability. Nelson and Pack (1999) assigns a key role to the ‘effectiveness of entrepreneurial ability’ which they see as a vital determinant of the rate of assimilation of technology (1999:420) – as in Michelacci (2003) where entrepreneurial ability is vital for R&D. In Nelson and Pack (1999) a ‘rapid’ expansion of skilled labour can only be absorbed if

entrepreneurial ability is high, and that without entrepreneurial ability the returns to physical and human capital is low.

The process of structural change as facilitated by high ability entrepreneurs lead to firms adopting more complex production methods and producing more complex and specialized intermediate inputs. As a result the technological intensity of a country's economic structure increases (Ciccone and Matsuyama 1996). These structural changes have interesting implications for the development of entrepreneurship itself, so that entrepreneurship may be itself endogenous in the development process.

Ciccone and Matsuyama (1996) explains this in a model where they make a distinction between consumer goods and intermediate goods. If a particular economy produces a limited range of intermediate goods, they show that the final (consumer) goods sector will use 'primitive' production methods and will have little demand for sophisticated, new inputs. This will lead to lower incentives for potential entrepreneurs to start-up new firms. The economy can get stuck in such an underdevelopment trap with primitive production in its (small) modern sector. They also point out that there might, in such an 'underdevelopment trap' be a case for assistance to new start-ups since these can provide both pecuniary and technological externalities if they start producing new intermediate goods—which will induce final good producers to demand more of these (in turn improving the incentives for other entrepreneurs to start-up firms due to greater demand and the example provided in the application new technology). In this model, start-ups face positive start-up costs that include R&D activities in bringing a new good to the market.

That entrepreneurs create a positive externality through bringing new goods to the market and in the process showcase new technology has been extended by Hausmann and Rodrik (2003) who point out that entrepreneurs provide not only these technological externalities in bringing new goods to market, but pecuniary externalities by providing information on the profitability of new activities. Entrepreneurs fulfill a 'cost-discovery' function in making sunk costs in a new activity which *ex ante* may or may not be profitable, but which will provide information *ex post* on such profitability to other entrepreneurs - information that often lacks in developing countries (Hausmann and Rodrik 2003).

Finally, an aspect of duality that is particularly pertinent to the debate on entrepreneurship in development is that between the formal and informal sector (Maloney 2004). De Paula and Scheinkman (2007) find that informal firms are often a form of 'evasive' entrepreneurship in order to evade taxes or regulations, or to engage in illegal trade. They also find that they are less efficient, less able to obtain finance, and more likely to be dominated by entrepreneurs of low ability. Thus the informal sector is much like the traditional/ subsistence sector in typical dual economy models, and growth may be enhanced by encouraging entrepreneurs of high ability to 'migrate' to the formal sector.

2.3 *Multi-dimensional development and entrepreneurship*

The entrepreneurship literature generally takes a restricted view of development. Most empirical studies on the relationship between entrepreneurship and development have similarly been limited to GDP, productivity and employment growth as proxies for development – and not multi-dimensional development (Ács et al., 2008a, 2008b; van Praag and Versloot, 2007).

Gries and Naudé (2011) proposed a framework wherein entrepreneurship can contribute to multi-dimensional well-being by contributing towards not only what people are or has, but what they can achieve through their capabilities. This notion of human development -or human flourishing - has been pioneered by Sen (1990; 1995; 2000), Nussbaum (2000) and others and is known as the Capabilities Approach (CA).

Gries and Naudé (2011) argue that the CA can inform both theoretical thinking on and measurement of entrepreneurship. From a CA view entrepreneurship is a human *functioning*² that can be valued as an end, and not just as a means to other ends. It can enrich human capabilities if people's complementary capabilities are expanded so that they can choose *not* to be entrepreneurs. An important implication from this approach is that the demand for entrepreneurs is not a derived demand as in the instrumentalist view (as e.g. in Casson et al., 2006).

Naudé, et al. (2012a;b) provide provisional empirical evidence supportive of the CA view of entrepreneurship proposed by Gries and Naudé (2011). Using individual level data from the Global Entrepreneurship Monitor (GEM) they find evidence of an inverse U-shape relationship between (opportunity) entrepreneurship and national happiness. This suggests opportunity-motivated entrepreneurship may contribute to a nation's happiness, but only up to a point. Not everybody should become entrepreneurs, and the happiness of a nation cannot be –indefinitely increased by increasing the numbers of (opportunity) entrepreneurs.

Although the literature on whether entrepreneurship matters for multidimensional development is scant, there has been more research on the subjective wellbeing (or or job satisfaction) of entrepreneurs (mostly measured as the self-employed). The evidence so far (more research is needed) suggests that entrepreneurs experience higher levels of job satisfaction than employees (Anderssen, 2008; Benz and Frey, 2008; Blanchflower, 2004; Lange, 2012; Parker and Ajayi-Obe, 2003). They have also been found to be healthier, less prone to negative feelings and depression, and to experience flow, than employees (Bradley and Roberts, 2004; Ceja, 2009; Graham et al., 2004; Patzelt and Shepherd, 2011) and to experience, in line with the CA, 'procedural utility' (Block and Koellinger, 2009).

2.4 *Market failures, the state and entrepreneurship*

² The term *functionings* is central in the capabilities approach, and refers to 'valuable activities and states that make up people's well-being' (Alkire, 2005:1) and includes 'working, resting, being literate, being healthy, being part of a community, being respected' (Robeyns, 2003:6).

The third “grand idea” in development economics concerns market and state failures. In the aftermath of World War II, when development economics was founded the belief was that market failures were important to understand underdevelopment. During the 1980s however the government was seen as similarly subject to failure, and that such state failure could be worse than market failure. Hence, under a set of principles for market-oriented reform described as the ‘Washington Consensus’, many economists and international development agencies started to promote a reduction of the role of the state and the liberalization of markets. The implicit assumption was that the supply of entrepreneurship would be forthcoming once the constraints imposed by state interference were loosened. After the global financial crises of 2008 and 2009 wherein market liberalization and ‘Washington Consensus’ type policies were found to be complicit, the regulatory role of the state has been revived.

One role of the state that has received more attention is in industrial policy (Szirmai et al., 2012). Here, old models of import-protection and state-owned enterprises have made place for policies that rely more on the private sector and entrepreneurship, but with government still playing an important role to address market failures in the entrepreneurial start-up and growth process. For example some have argued that entrepreneurial entry may be sub-optimal due to the externalities generated by such entry – see e.g. the discussion of Hausmann and Rodrik (2003) in section 2.1 that may justify ‘self-discovery’ through supporting innovation by SMEs and new firm start-ups, e.g., by reducing regulations and requirements and/or providing subsidized credit.

In contrast to such support others have argued for taxing (regulating) entrepreneurship because it may cast negative externalities. De Meza and Webb (1987; 1999) make the case that credit market imperfections may lead to ‘overinvestment’ when banks cannot accurately judge entrepreneurial ability. Because banks cannot observe any entrepreneur’s ability *ex ante*, interest rates on start-up capital will reflect average entrepreneurial ability. If the proportion of entrepreneurs of low ability increases, it will result in higher borrowing costs, which impose a negative externality on entrepreneurs of high ability, who will consequently borrow and invest less (Ghatak et al. 2007). The entry of entrepreneurs with low ability might also hinder development because such entrepreneurs may have less productive workers, who will earn reduced wages as a result, and in turn reduce the opportunity costs of self-employment, thereby causing the entry of even more low-ability entrepreneurs (Ghatak et al. 2007:2).

There is thus a clear case of the state to play a role in addressing the market failures that plague also entrepreneurial start-up and innovation activities; moreover this role will be different across different stages (Ács and Naudé, 2012) – although more research is clarify this, in particular given the fact that many countries exhibit various stages simultaneously in different sectors, and that countries can today leapfrog development.

Furthermore, the *how* of state support for entrepreneurship is essential – and this brings us to issues of entrepreneurship policy. For instance, private sector development (PSD) policies have tended to shy away from targeting entrepreneurs in specific sectors or industries for fear of

distorting markets, and for fear of government failure – in particular the potential for such selective support to encourage rent-seeking and corruption. The design of entrepreneurship policies are therefore a delicate art, and one that is increasingly in need of rigorous evidence. In the next section I turn to what we can learn from the empirical evidence on the relationship between entrepreneurship and development.

3. Empirical Evidence

3.1 Macro-level Relationship

The three most important global/macro databases on entrepreneurial activity in countries all take a occupational/formal-firm view of entrepreneurship: the International Labour Organization (ILO) measures self-employment, the Global Entrepreneurship Monitor (GEM) measures start-up rates of new firms, and the World Bank measures the registration of new firms. They are also concerned with formal as opposed to informal firms (for a discussion of these databases see Desai, 2010).

Studies using these databases have uncovered two sets of results. First, that there is a lack of clear empirical evidence of whether entrepreneurship drives economic growth (or productivity or employment) – studies find a mixed bag of results – and second, there seems to be an U-shaped relationship between entrepreneurship and a country's level of economic development (as measured by GDP per capita).

The U-shaped relationship implies a higher rate of entrepreneurial activity in low-income countries than in middle income countries (Carree et al., 2007; Wennekers et al., 2005). This result may reflect that entrepreneurs in developing countries are less innovative and tend to be proportionately more 'necessity' motivated (Ács et al., 2008a; Gollin, 2008). Higher levels of GDP may therefore be associated with more 'innovative' forms of entrepreneurship. Another implication is that rather than causality running from entrepreneurship to development, the causality may (also) run from development to entrepreneurship.

3.2 Micro-Level Relationship

Most micro-level studies of entrepreneurship has focused on the why and how of entrepreneurship, and not its impact on development. Nevertheless from a number of studies – for instance on the productivity, innovativeness, growth and female entrepreneurs – much can be learned on whether and how entrepreneurship matter for development. One lesson is that the finding on the macro-level that it is innovative entrepreneurship (by implication entrepreneurial ability) that matter most for development seems to be supported by micro-level evidence.

Van Praag and Versloot (2007; 2008) consider the literature on the impact of entrepreneurship (according to various definitions) on employment, innovation and productivity growth. They find

that (i) entrepreneurs do not spend more on R&D than their counterparts, although the quality and efficiency of their innovation is higher; that (ii) their contribution to productivity growth is low; that (iii) the majority of entrepreneurs would earn higher incomes as wage employees, and (iv) that entrepreneurs create more jobs relative to non-entrepreneurs but that the quality of jobs they create is lower. Hence not all entrepreneurs drive development and not all entrepreneurs are innovative (Shane, 2009; Stam and Wennberg, 2009).

As these findings refer to the impact of the average entrepreneur it perhaps suggest that focusing on the average entrepreneur may not be the best policy stance – it may be better for and policy to focus on the small subset of entrepreneurs – innovative entrepreneurs - that do make a difference. Studies tend to find that innovative firms, particularly in high tech sectors, have on average higher levels of productivity, tend to do enjoy higher employment growth, and cause positive spillovers for other firms (Coad and Rao, 2008; Hall et al., 2009; Freel, 2000; Koski and Pajarinen, 2010; Rochina-Barrachina et al., 2010; Stam and Wennberg; 2009). A study from an emerging economy, Brazil, with the focus on a panel of manufacturing firms over the period 1996-2002 and that uses propensity score matching techniques finds that firms who engaged in technological innovation experienced a 10.8 to 12.5 percent higher growth in employment, a 18.1 to 21.7 percent higher growth in net revenue, a 10.8 to 11.9 percent higher growth in labour productivity and a 19.9 percent higher growth in market share (Kannebley et al., 2010).

Micro-level evidence on entrepreneurship and development has in recent years started to give attention to female entrepreneurs in developing countries – important given the key role of women in development and the still widespread discrimination against women. In an overview of female entrepreneurship in development, Minniti and Naudé (2010) remarks that ‘evidence to date suggests that a variety of reasons contribute to explaining observed differences in entrepreneurial behaviour across gender and that such differences have significant implications at the macro-economic level’. Some of these differences with a broader societal impact include that women entrepreneurs’ businesses tend to be smaller and to provide less employment growth than those owned by men³ (Coleman 2007, DuRietz and Henrekson 2000); that women’s businesses tend to be less profitable than those of men (Robb and Wolken 2002) and generate lower sales turnover than men, even in same industry comparisons (Chaganti and Parasuraman 1996).

These differences in entrepreneurial propensity and performance between men and women reflect disadvantages and discrimination in education and the labour market. Labour market discrimination against women has been argued to lead to a self-selection of the most highly talented women into labour markets. As a result, less talented women will opt for self-employment, a characteristic reflected in their enterprises’ lower survival and growth rates (see

³ For instance women’s firms tend to grow slower in both sales and employment (Nichter and Goldmark, 2009; Amine and Straub, 2009) even if one controls for sectors. Women are also found to have on average lower growth expectations (Justo and DeTienne, 2008).

e.g. Rosti and Chelli, 2005). Furthermore, as a result of perceived underinvestment in their human capital, many women may not have sufficient confidence in their ability to start a firm (Langowitz and Minniti 2007). Yueh (2009) discuss the case of women entrepreneurs in China and supports the idea that lack of self-confidence is a significant constraint hindering women entrepreneurial entry in developing countries.

As a result they also lack access to credit and face higher start-up costs. Horrell and Krishnan (2007), for example, report that female-headed households often lack either assets or incomes, or both, and that this constrains their ability to diversify their economic activities. In this regard a large number of studies have found that access to micro-credit has improved women's decision-making autonomy (Amin et al., 1998) and general household welfare and consumption (Kevane and Wydick, 2001).

In conclusion, although much has been learned about the obstacles faced by female entrepreneurs, much less is known about how the level of aggregate activity influences women's decisions about entrepreneurship and even less about how the latter contribute to development (Minniti and Naudé, 2010). The lack of a systematic approach and data has prevented, so far, the formulation of a comprehensive and robust theory of female entrepreneurship and development. As Minniti and Naudé (2010) stress 'no "women only" theory is necessary. However, a solid understanding of how the distinctive characteristics of female entrepreneurship are accounted by existing models of growth would be very desirable for both science and policy'.

4. Policy Considerations for Enhancing the Developmental Impact of Entrepreneurship

A proper discussion of the policy implications inherent in the theoretical and empirical overviews in the previous sections would necessitate a separate chapter. The remainder of this chapter can only outline some of the most pertinent issues. Given the "grand ideas" in development economics with which I started this chapter, I will conclude by arguing that the main policy considerations for enhancing the developmental impact of entrepreneurship should be on (i) improving the quality and allocation of entrepreneurial ability and (ii) reducing the need for necessity entrepreneurship – i.e. make entrepreneurship a valued human functioning.

Improving the quality of entrepreneurial ability means not only improving the skills and education of entrepreneurs (their 'human capital') but moreover focusing on the innovative abilities of entrepreneurs. Indeed from the discussion in sections 2 and 3 of this chapter the implication is that it is innovative entrepreneurship that is most desirable for growth. Innovation policy should therefore a vital component of entrepreneurship promotion in developing countries (as it also remains the case in advanced economies).

Stimulation of innovation has not been paramount in most development agencies or donor's private sector development (PSD) programmes, nor in national entrepreneurship support

programmes. The only innovation relevant aspects of such support programmes have been their concern to improve the general business environment (a prerequisite for innovation) and to argue for patent protection - and to a lesser extent basic research (Lindahl, 2005). As such policies tend to be more concerned with improving static and allocative efficiency and not dynamic efficiency, although the latter is more important from a job creation and growth point of view (Evenett, 2005).

Taking aim at improving dynamic market efficiency through raising innovation, and aiming to limit necessity entrepreneurship, may have implications for policy that runs counter to many current entrepreneurship policies. For instance many aim to improve static and allocation efficiencies in markets through increasing competition (competition policy). However, this misses the fact that with underdeveloped financial markets in developing countries, raising competition might not improve dynamic efficiency, because in the absence of financial markets firms can only finance innovation through profits. If too much competition erodes their profits, it will also erode their innovative activities. And reducing the need for necessity entrepreneurship may imply policies to encourage job-creation and provide social security, policies not popularly associated with an entrepreneurial economy.

Promoting innovative entrepreneurship (and to an extent also labour market and social security policies) in developing countries runs into further difficulties in that there is a broad lack of sufficient impact evaluations⁴ with which to judge what works and what does not (Lerner (2009). Lopez-Acevedo and Tinajero (2010:2) mention that most existing evaluations entrepreneurship policies typically do not consider biases due to unobserved firm heterogeneity or self-selection, tend to be qualitative rather than quantitative, and cannot keep track with continual changes in programmes over time. Many ‘impact’ studies also do not attempt to attribute impacts or outcomes to interventions (White, 2009). Lack of reliable SME-data makes evaluation and cross-country comparisons of programmes difficult (Ardic et al., 2011). There is thus a need for much more rigorous empirical evidence as to what works and why, with respect to entrepreneurship policies and general, and even more so with respect to the impact of innovation policies (Braunerhjelm, 2010; McKenzie, 2011).

5. Concluding Remarks

This paper has shown is that a reconsideration of entrepreneurship’s role in development leads to three novel realizations. One, consideration of entrepreneurship in development provides fresh perspectives on three of the “grand” ideas in development economics; Two, entrepreneurship influences development outcomes positively as well as negatively; and three, entrepreneurship is in turn significantly determined by the dynamics of development.

⁴ Impact evaluation (or attribution analysis) is ‘a with versus without analysis: what happened with the programme (a factual record) compared to what would have happened in the absence of the programme (which requires a counterfactual, either implicit or explicit’ (White, 2011:3).

Entrepreneurship is therefore a valid and important subject of study for development scholars, and development is a worthwhile subject of study for entrepreneurship and management scholars. The growing availability of more and better data from emerging and developing economies, the increasing adoption of rigorous evaluation methods in policy assessments, and likelihood of closer collaboration across disciplines, all bode well for the intersection of development and entrepreneurship.

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