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Term of Strategic Entrepreneurship and Schumpeter's Creative Destruction Theory

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Abstract

The literature of strategic entrepreneurship is one of the few areas of strategic management writing in which Joseph Schumpeter has argued that entrepreneurs create innovations in the face of competition and thereby generate economic growth. The fundamental question in the field of strategic management is how firms achieve and sustain competitive advantage especially in the work of Schumpeter [1934, 1942] who argued that the main agents of economic growth are the entrepreneurs. The aim of this paper is to summarize and critically review the concept of the strategic entrepreneurship in the light of *economics history* by creating a better understanding of the intersection of the academic fields of entrepreneurship and strategic management.

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1. Introduction

One of the few areas of strategic management writing is the literature of strategic entrepreneurship in which Joseph Schumpeter has argued that entrepreneurs create innovations in the face of competition and thereby generate economic growth. The main question in the area of strategic management stream is how firms achieve and sustain competitive advantage especially in the work of Schumpeter [1934, 1942] who argued that the primary agents of economic growth are the entrepreneurs.

A country's wealth and economic dynamism depends upon the competitiveness of its own firms and also competitiveness of firms depends on the capabilities of its entrepreneurs and managers. Schumpeter gave economists

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food for thought with the concept of creative destruction during his career and until the 1950s. In his book *Capitalism, Socialism and Democracy* (Schumpeter 1942), Schumpeter made his famous prediction of the transition from competitive capitalism to trustified capitalism.

Vast number of opinions have been articulated about the role of the entrepreneur in a modern economy. Perhaps the best known is Joseph Schumpeter's view of the entrepreneur in the Theory of Economic Development.

Creative destruction (sometimes known as **Schumpeter's gale**) is a term in economics which has since the 1940s become most readily identified with the Austrian American economist Joseph Schumpeter. He derived it from the work of Karl Marx and popularized it as a theory of economic innovation and the business cycle. According to Schumpeter, creative destruction describes the "process of industrial mutation that incessantly revolutionizes the economic structure from within, incessantly destroying the old one, incessantly creating a new one".

Foundation of strategic management is Schumpeter's thinking (Lintunen, 2000). Schumpeter (1934) point that an entrepreneur, as an innovator, creates profit opportunities by devising a new product, a production process, or a marketing strategy. An entrepreneurial invention occurs, when an entrepreneur makes the conjecture that a set of resources is not being optionally utilised (Lahti, 2008)

Companies meet a lot of 'creative destruction' ideas during their explorative activities; however the real fortune for them is not the pure implementation of these ideas, but the successful running and construction of the existing and new fields at the same time (Szabo,2010).

The tie between entrepreneurship and strategic management is not new. The aim of this paper is to summarize and critically review the concept of the strategic entrepreneurship in the light of *economics history* by creating a better understanding of the intersection of the academic fields of entrepreneurship and strategic management.

The paper is organized as follows. In Section 2, we review historical approaches about entrepreneurship. In Section 3, we discuss strategic entrepreneurship in the concept of Schumpeter's view. In Section 4 includes conclusion.

2. Historical Approaches to Entrepreneurship: Evolution of the Literature

An entrepreneur action in society is probably as old as the institutions of exchange. Most economists would most likely agree with the opinion that; an entrepreneur is the most significant actor in economics. The word 'entrepreneur' is a French coinage. So, the story starts with contributions from early French writers (the earliest writer to recognize the role of entrepreneurship is Richard Cantillon) on entrepreneurship.

Richard Cantillon is credited with the discovery of economic theory and was the first to fully consider the critical role of entrepreneurship in the economy. He described entrepreneurship as pervasive and he casted the entrepreneur with a crucial role in the economy in the 18th century. He suggested that an entrepreneur is someone who has foresight and willingness to reduce risk and takes the action to make more profit.

Historical perspectives have played a role in the theoretical development of entrepreneurship since the very inception of the concept. J.B. Say, for instance, used the example of English textile industry over the earlier dominance of Belgian woolens and German cotton products to develop the theoretical distinction between "scientific" ability and "entrepreneurial" skill. The supply of entrepreneurship was critical in determining the wealth and growth of a nation's economy. He likewise used the example of the introduction of tea as a commodity in the seventeenth-century Dutch trade with China to extend Richard Cantillon's notion of entrepreneurship as risk-bearing by arguing for what he believed was a defining characteristic of entrepreneurship: running limited-risk experiments when introducing new commodities or entering into new markets (Wiklund et al.2002).

The English classical economists saw entrepreneurs as suppliers of financial capital in contrast to the French writers. Adam Smith himself seemed to have identified the entrepreneur as a prudent man who is frugal (i.e. he accumulates capital) and is an agent of slow but steady progress (Hebert and Link, 2009).

However, on the whole, classical and early neoclassical economic thought in the nineteenth and early twentieth centuries eschewed both the notion of entrepreneurship and the legitimacy of historical reasoning. Adam Smith and David Ricardo conceived of no distinctive role for entrepreneurship in even pulling together factors of production, as Say had. Even when the term “entrepreneurship” or “undertaker” was finally reintroduced into economic theory in the second half of the nineteenth century by J. S. Mill, F. A. Walker, A. Marshall and others, it tended to be conceived primarily as a *managerial* function rather than containing the dynamic and innovative connotations that the term’s use has today. Mill describes entrepreneurship as the “labour and skill required for superintendence” (Niosi, 2012)

With the neoclassical economics, A. Marshall analyzed the relations between the firms and markets. His main contribution was the internal and external economies of the firm. Marshall introduced into economic analysis the concept of representative firm that since Marshall’s contribution has been as the theoretical unit of analysis, instead of real one (Niosi, 2012)

Joseph Schumpeter began his now-famous 1947 article on “Creative Response in Economic History” with this idea: “Economic historians and economic theorists can make an interesting and socially valuable journey together, if they will” (Schumpeter, 1947). Though his article is most often cited for the distinction it developed between “adaptive” and “creative” responses in business, Schumpeter’s main purpose was to call for the extensive use of historical methods in the study of entrepreneurship. To Schumpeter, the very nature of entrepreneurship – the empirical difficulty of identifying it *ex ante*, the way it “shapes the whole course of subsequent events and their ‘long-run’ outcomes,” the great extent to which its character differed from place to place and over the course of time – suggested that a dynamic historical perspective was necessary in studying how it worked within capitalist economies (Jones and Wadhvani, 2006)

J. Schumpeter, in his book, *The Theory of Economic Development*, suggest that an entrepreneur, as innovator, creates profit opportunities by devising a new product, a new production process, or a new marketing strategy. Schumpeterian thinking is generally reduced to making innovation the key to competitiveness and the entrepreneur the destroyer of economic balance, these two factors constituting the principles of economic growth and development (Verstraete, 2002).

He insisted in *Capitalism, Socialism and Democracy*, creative destruction creates economic discontinuities. He suggests (1942) ;

- An entrepreneurial function is the act of will of the entrepreneur for the introduction of innovation in an economy,
- Entrepreneurial leadership is the source of creative energy for innovation
- Entrepreneurial profit is the temporary monopoly return on personal activity of the entrepreneur.

Schumpeter recognized that if his theory of entrepreneurship as the dynamic engine of capitalism was to have validity it needed to be studied as a historical fact. Social scientific investigation of entrepreneurship needed to focus not only on entrepreneurs and their firms but also on the *structure of and changes in the industries, markets, societies, economies, and political systems* in which they operated. In the Schumpeterian view, entrepreneurial behavior, made little sense without equal analytical attention to historical context in which it operated (Wiklund et al, 2002)

While Schumpeter’s (1942:84) notion of a “gale of creative destruction” has pointed the most attention in the research and practitioner literatures, it is the role profit plays in motivating innovation as a precursor to creative destruction that is the key to his theories. Historically, traditional theories of strategic management eschewed the Schumpeterian theory of disequilibrium as a base framework and chose instead the equilibrium-oriented approach of industrial organization. In so doing they placed emphasis on what Schumpeter (1947: 153) called the “adaptive response” of managers and on creating a sustained competitive advantage for a firm. Thus for decades sustained competitive advantage has been a dominant concept in strategic management research. Emerging from the structure-conduct-performance paradigm of industrial organization economics and popularized by the Harvard Business School and the work of Michael Porter (1985), sustained competitive advantage is the most influential mechanism for explaining the persistence of superior economic performance (Wiggins and Ruefli, 2005)

Schumpeter (1934, 1942) original objective was to describe the process of economic development in western economies. So he came to focus on major *revolutionary* technological and product market *shifts* (Schumpeterian shocks) and to dismiss, as relatively unimportant in the long run, price and other competitive actions of firms in a relatively stable industry. Revolutionary innovations in product, market or technology can only be anticipated imperfectly by firms. Revolutionary innovations will have *unexpected* favorable or unfavourable effects on a firm in a industry. Sometimes firms in an industry may survive a revolutionary innovation to become important actors in succeeding industry (Dagnino, 1995).

Schumpeter, saw economic development as consisting of a process where entrepreneurs dipped into a stream of technical opportunities ostensibly made for reasons independent of particular markets and brought those innovations to market. The successful innovator achieved a monopoly in a particular market through bringing to market something which was quite unique, only to have that monopoly successfully whittled away by the entry of imitators. The dynamic capabilities approach is a descendant of the Schumpeterian. However, it emphasizes organizational processes inside the firm more than Schumpeter ever did; and it is not just a positive theory of industrial change. It can also offer prescription because of its firm level orientation, and it looks inside firms to help explain market processes (Teece and Pisano, 1994).

Similar to some scholars, we believe that these two disciplines are often complementary. Meyer and Heppard (2000) yield that the entrepreneurship and strategic management disciplines are inseparable, making it difficult to understand one field's research findings without simultaneously studying the results reported in the other. Barney and Arikan (2001) argued that there is a close, although not fully specified relationship between theories of competitive advantage and theories of creativity and entrepreneurship.

3. Term of Strategic Entrepreneurship

The lack of a single definition is partly due to the differentiated traditions within the field of entrepreneurship research including: anthropology (de Montoya, 2000, Firth, 1967, Fraser, 1937), social science (Swedberg, 1993, Waldringer, Aldrich, & Ward, 1990, Weber, 1898/1990), economics (Casson, 2003, Kirzner, 1973, Schumpeter, 1934, Shane, 2003, von Hayek, 1948, von Mises, 1949/1996) and management (Drucker, 1985, 1999, Ghoshal & Bartlett, 1995) (aktaran Ahmad and Seymour, 2008). Conflicting definitions, even within the specific themes, such as economics, which is our key focus, are also due, in part, to the broad contextual focus of the studies, as demonstrated by the variety of entrepreneurship related indicators described above.

Although all of the different identities, entrepreneurs can be described as those persons (business owners) who seek to generate value, through the creation or expansion of economic activity, by identifying and exploiting new products, processes or markets. Besides this, entrepreneurial activity is the enterprising human action in pursuit of the generation of value, through the creation or expansion of economic activity, by identifying and exploiting new products, processes or markets. In addition, entrepreneurship is the phenomenon associated with entrepreneurial activity (HKU, 2010)

Schumpeter (1965) defined “entrepreneurs as individuals who exploit market opportunity through technical and/or organizational innovation”. For Frank H. Knight (2005) and Peter Drucker (1985) “entrepreneurship is about taking risk”.

Entrepreneurship was developing as an academic area of study when Karl Vesper founded an interest group within the Academy of Management's (AoM) *Business Policy and Strategy division* in 1974. In 1987, entrepreneurship finally became a separate division of the AoM (Meyer *et al.*, 2002). Now, entrepreneurship is acknowledged as one of the major determinant of the economy of every modern society. Besides this, this crucial term is considered as the instrument to cope with the new competitive landscape and its vast speed of changes (Kraus and Kauranen, 2009)

The entrepreneurial function includes the discovery, assessment and opportunities, in other words, new products, services or production processes; new firm strategies and organizational forms and new markets for new products (Shane and Venkataraman, 2000).

Entrepreneurship is “a process by which individuals –either on their own or within organizations– pursue opportunities” (Stevenson and Jarillo, 1990: 23). Entrepreneurs identify the commercial opportunities offered by innovations and transform these opportunities into new products that may improve the lives of all citizens and contribute to increased productivity throughout the economic life. Entrepreneurship is important for socioeconomic growth and development, providing new job opportunities and diverse goods and services to the population (Polowczyk, 2012)

The entrepreneurial opportunity is an unexpected and as yet unvalued economic opportunity. Entrepreneurial opportunities exist because different agents have differing ideas on the relative value of resources. The theory of the entrepreneur focuses on the heterogeneity of beliefs about the value of resources (Alvarez and Busenitz, 2001: 756).

Entrepreneurship or /and the entrepreneurial function can be characterized as the discovery of business opportunities and the following creation of new economic operation, often via the creation of a new and developing organizations (Cuervo et al., 2015)

Zahra & Dess (2001) specifically name strategic management as a most promising area to be integrated into entrepreneurship research. The positive outcomes of such an integration can be observed in real business life, where entrepreneurial enterprises are more inclined to engage in strategic management practices than more established enterprises which are by nature more conservative.

Entrepreneurship and strategic management are concerned with growth and wealth creation. Indeed growth and wealth creation are entrepreneurship’s defining objectives. In addition, entrepreneurship increasingly is viewed as a stimulus to wealth creation in emerging, developing, and developed economies as a result of the actions of individual firms (Ireland et al., 2003)

The behavioral perspective has created interests in the role of entrepreneurship in strategic management. Entrepreneurial behaviour is seen as behaviour that manages to combine innovation, risk-taking and proactiveness. In other saying, it combines the classic theories of Schumpeter’s innovative entrepreneur (1934, 1942), the risk-taking entrepreneur that occupies a position of uncertainty as proposed by Knight (1921), and the entrepreneur with initiative and imagination who creates new business opportunities (Ahmad and Seymour, 2008).

Strategic entrepreneurship is a newly recognized field that draws, not surprisingly, from the fields of strategic management and entrepreneurship. Strategic entrepreneurship (“SE”) is a newly recognized field that draws, not surprisingly, from the fields of strategic management and entrepreneurship. The field emerged officially with the 2001 special issue of the *Strategic Management Journal* on “strategic entrepreneurship”; the first dedicated periodical, the *Strategic Entrepreneurship Journal*, appeared in 2007. SE is built around two core ideas. (1) Strategy formulation and execution involves attributes that are fundamentally entrepreneurial, such as alertness, creativity, and judgment, and entrepreneurs try to create and capture value through resource acquisition and competitive positioning. (2) Opportunity-seeking and advantage-seeking—the former the central subject of the entrepreneurship field, the latter the central subject of the strategic management field—are processes that should be considered jointly (Klein et al., 2012)

Strategic entrepreneurship (SE) is an integration of entrepreneurial and strategic perspectives to design and implement entrepreneurial strategies that create wealth (Hitt et al., 2001).

Strategic Entrepreneurship which plays an important role in a highly turbulent environment, integrates strategic functions with the entrepreneurial actions. The goal of strategic entrepreneurship is to continuously create competitive advantages that lead to maximum wealth creation (Polowczyk, 2012). Entrepreneurship is described as a process of creative destruction by Schumpeter. Entrepreneurs have ‘carried out new combinations’, including the doing of new things or the doing of things that are already being done in a new way (Schumpeter 1934: 132)

Ireland et al. (2003) describe strategic entrepreneurs’ dimensions can be defined in four major sections. First, they define an entrepreneurial mindset and describe its key components—entrepreneurial opportunities, entrepreneurial alertness, real options, and an entrepreneurial framework. Second, writers examine entrepreneurial culture and entrepreneurial leadership as vital aspects of SE. In the third major section, writers discuss how managing

organizational resources strategically provides the foundation for the firm's opportunity-seeking and advantage-seeking behaviors. Grounded in resource-based theory, the strategic management of resources involves a comprehensive set of actions needed to recognize opportunities and to develop competitive advantages to successfully exploit them. Financial capital, human capital, and social capital are the most important resources involved with effective resource management. The fourth section is concerned with applying creativity and developing innovation, which are critical outcomes of an entrepreneurial mindset, an entrepreneurial culture and entrepreneurial leadership practices as well as the strategic management of the firm's resources. A model of SE as explained is presented in Figure 1.

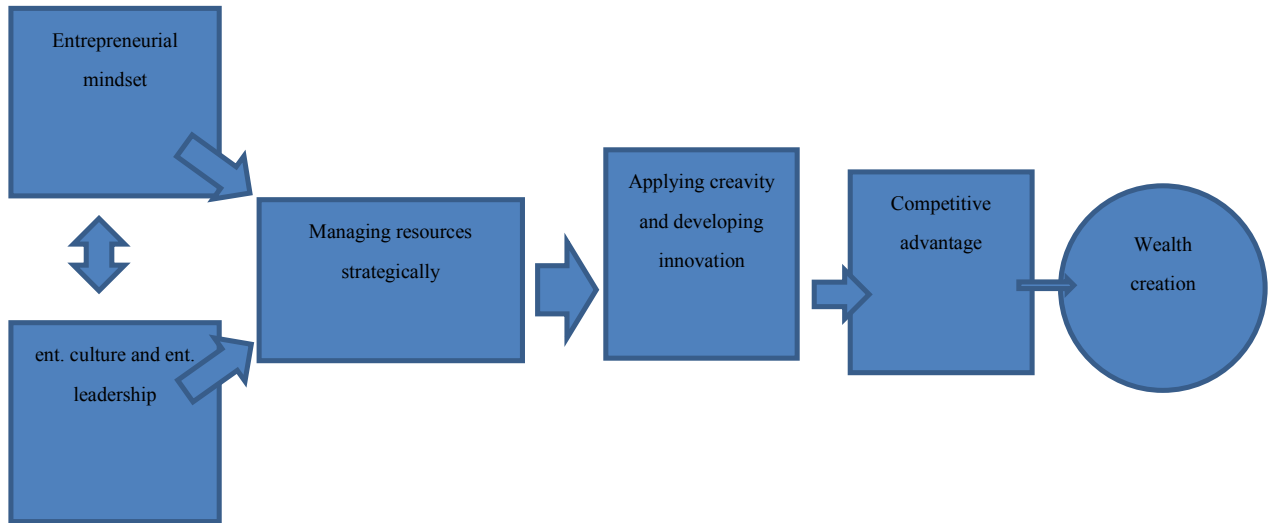


Fig 1: A Model of Strategic Management

Source: Ireland, R. D., Hitt, M. A. ve Sirmon, D. G. (2003), A model of strategic entrepreneurship: The construct and its dimensions, *Journal of Management*, 29 (6), pp. 963–989.

Entrepreneurial strategies are becoming more and more important for both new as well as established enterprises. Because of increasing environmental dynamics and increasing global competition, enterprises, regardless of their age or size, must to build more entrepreneurial strategies on the purpose of surviving. Strategic entrepreneurship refers to firms' pursuit of superior performance via simultaneous opportunity-seeking and advantage-seeking activities. Both small and large firms face impediments while pursuing strategic entrepreneurship (Ketchen et al.2007). These entrepreneurial strategies are said to be related to better company performance. They aim to build on the identification of opportunities for coping with global competition by their own competitive advantages. This is where the fields of *entrepreneurship* and *strategic management* intersect.

Arguments involving strategic entrepreneurship build on four main assertions about the nature of strategic entrepreneurship. First, as its name suggests, strategic entrepreneurship is the melding of the strategy and entrepreneurship domains. Firms pursuing strategic entrepreneurship engage in both the opportunity-seeking activities required by entrepreneurship and the advantage-seeking activities required by strategy (Ireland *et al.*, 2003).

Strategic entrepreneurship is entrepreneurial action with a strategic perspective. In the words *Strategic Entrepreneurship* of Venkataraman and Sarasvathy (2001), entrepreneurial action is the 'Romeo on the balcony.' One could also consider entrepreneurial action to be strategic action with an entrepreneurial mindset. In short, strategic

entrepreneurship is the integration of entrepreneurial and strategic perspectives in developing and taking actions designed to create wealth (Hitt et al., 2001).

In addition to “classical” variables that describe entrepreneurship, some authors manage to create interest on organizational and strategic variables. Zahra & Dess (2001) argue that the integration of different views is a key to more fruitful research in entrepreneurship, and specifically name strategic management as a most promising area to be integrated into entrepreneurship research. The positive outcomes of such an integration can be observed in real business life, where entrepreneurial enterprises are more inclined to engage in strategic management practices than more established enterprises which are by nature more conservative. Entrepreneurship and strategic management both have made their unique and valuable contributions to management theory. Although their foci differ, both are inevitably interrelated, and are often complementarily supportive of each other (Ireland *et al.*, 2003). Meyer & Heppard (2000) remark that the two fields are in fact even inseparable, forming two sides of the same coin, since the research results of the one cannot fully be understood without the other (Barney & Arkan, 2001).

Entrepreneurship is an essential element for economic progress as it manifests its fundamental importance in different ways: a) by identifying, assessing and exploiting business opportunities; b) by creating new firms and/or renewing existing ones by making them more dynamic; and c) by driving the economy forward – through innovation, competence, job creation- and by generally improving the wellbeing of society (Cuervo et al., 2015).

No entrepreneur or enterprise, however successful and big, can continue to hold a place of leadership unless it recognizes that modern business operates in a world of galloping change which creates new problems, risk and opportunities and for which they have to mobilize the enterprise’s resources before changes make their impact felt. To do successfully, the entrepreneur and enterprise should know where this firm is going and how the firm will get there (Okpara, 2007).

At the center of Schumpeter’s theory of competitive behavior is the assertion that Schumpeter ideas on innovation and economic development are best summarized in his book, *The Theory of Economic Development* (Schumpeter, 1934). His classical definition of development includes:

“(1) The introduction of a new good – that is one with which consumers are not yet familiar – or of a new quality of a good. (2) The introduction of a new method of production, that one not yet tested by the branch of manufacturing concerned/.../(3) The opening of new market/.../(4) The conquest of a new source of supply of raw materials or half-manufactured goods/.../(5) The carrying out of new organisation of any industry/.../” (Schumpeter, 1934, p. 66).

Schumpeter’s definition therefore equates entrepreneurship with innovation in the business sense; that is identifying market opportunities and using innovative approaches to exploit them. However, although Schumpeter’s definition embodies a characteristic of entrepreneurship that is widely recognized today, namely, innovation, it still retains some ambiguity that has meant the debate regarding a definition of entrepreneurs/hip continues; although, to some extent, this reflects the definition of innovation, in particular whether it relates to incremental or quantum changes.

Moreover, unlike the Knight perspective, for example, the Schumpeterian entrepreneur need not be a risk taker or business owner, for example. Indeed some (Drucker, 1985) have argued that entrepreneurship reflects merely the creation of a new organization and that any individual who starts a new business venture is an entrepreneur; even those that fail to make a profit. Although, it could be argued that this corresponds to Schumpeter’s ‘opening of a new market’ (Ahmad and Seymour, 2008). Creative destruction implies, though, that entrepreneurship and the activities associated with it have temporal limits. A new product is introduced or a new venture is launched and it lasts until another supplants it. Many firms begin as entrepreneurial ventures only to abandon their entrepreneurial roots as they grow into large corporations with greater levels of complexity and bureaucracy.

4. Conclusion

The strategic entrepreneurship which includes opportunity- and advantage-seeking behaviors contributes to our understanding of how firms create wealth. Firms that identify potentially valuable opportunities but are unable to exploit them to develop a competitive advantage will not create value for their customers or wealth for their owners.

Firms that build competitive advantages but lose their ability to identify valuable entrepreneurial opportunities are unlikely to sustain those advantages over time. Essentially, they will discontinue creating wealth for their owners. Therefore, all of firms, new and established, small and large, must engage in both opportunity-seeking and advantage-seeking behaviors. Analysis of strategic entrepreneurship in business and industry sectors, public and private, would also be extremely useful to confirm its existence and compare similarities and differences. This will provide further insight into strategic entrepreneurship.

In point of fact, this concept details the strategic management discipline through which exploration is used to identify entrepreneurial opportunities by which these opportunities are exploited to create firm wealth. From this point of view, strategic entrepreneurship facilitates firms' efforts to identify the best opportunities and then to exploit them with the discipline of a strategic business plan. The objective of strategic entrepreneurship is to create continuously competitive advantages. And this process lead to maximum wealth creation.

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