

## ENTREPRENEURSHIP AND ECONOMIC GROWTH: COMMENT ON HOLCOMBE

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Economic growth is determined by two elements, (a) by the available quantities of goods that can be used in the productive process and (b) by the adroitness with which these available factors of production are combined. Dealing with element (b), Randall G. Holcombe<sup>1</sup> has recently emphasized the importance of entrepreneurial activity with a valid and interesting observation. Unfortunately, he does not pursue this observation to the conclusion to which it naturally leads (and which I will therefore have to spell out in what follows), but instead tries to relate it to Israel Kirzner's theory of entrepreneurship. This makes Holcombe's analysis deficient in several respects, with the result that potentially disastrous policy recommendations might be derived from it.

The valid and interesting observation that I have in mind can be grasped from the following example given in Holcombe's article:

Somebody had the idea that if a computer mouse communicated with the computer via an infrared connection, the mouse could be used without a cord. . . . The profit opportunity arose solely because of a previously nonexistent market niche, and once that market niche appeared, it did not take very long for an entrepreneur to seize on the idea. . . . Before personal computers used mice . . . , there would have been no possibility for the insight, regardless of how far the market was out of equilibrium. . . . This entrepreneurial insight capitalized on a new opportunity, which was created by other entrepreneurial insights. (p. 54)

Holcombe here illustrates the importance of the "context" of action for economic growth. Entrepreneurial decisions are not taken in a time- and space-less vacuum, but under specific conditions, which permit the successful performance of some actions and preclude the success of other actions. Entrepreneurs thus have to choose carefully how to use their factors of production. They can only succeed if they do what, under the prevailing conditions, is most important in the eyes of the consumers. Yet, irrespective of whether they succeed or not, they change these very conditions and thus other entrepreneurial activities become successful and unsuccessful. Two general conclusions immediately follow.

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<sup>1</sup>See Holcombe (1998); page numbers throughout refer to this article.

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First, entrepreneurial judgments are "historical" judgments, that is, they have to grasp the unique combination of circumstances that actually prevails and to anticipate, in the light of ongoing events, the unique conditions that will prevail in the future. For their task is not to buy "capital" and hire "labor" to produce a "product," but to buy specific goods (infrared lamps) and to hire specific labor services (information scientists specialized in the programming of infrared lamps) to produce a specific product (an infrared mouse). Thus, only on the basis of correct historical judgments—only if they are good "historians of the future" (Mises 1985, p. 316) can they decide what is best to do here and now.

Second, it is from the outset futile to promote growth by stimulating the production of "capital goods" and "research" or "education." For it is not immaterial which factors of production are produced, because one needs specific goods and specific human services, knowledge, and capacities to accomplish what is most important under prevailing conditions. And in order to discern which specific goods and services are most important, one must be able to compare their importance in terms of a common unit, which is precisely what monetary calculation permits us to do.

Hence, an analysis of the context-dependence of action leads naturally to the conclusion that economic growth essentially depends on good historical judgments and on the possibility of economic calculation. Yet, Holcombe takes another path. He attempts to make sense of his observations in terms of Kirzner's theory of entrepreneurship, arriving at the general conclusion that "the key element in economic growth is the production of entrepreneurial opportunities" (p. 60).

The crucial point in Holcombe's argument is his claim that entrepreneurship itself creates more profit opportunities than would have existed without it: "When entrepreneurs take advantage of some opportunities, the economic environment changes, creating with it additional opportunities. Thus, entrepreneurship leads to more entrepreneurship" (p. 54). If this argument were correct then we would have to consider entrepreneurship as an activity that reinforces itself, a kind of perpetuum mobile in human action.

Yet why does entrepreneurship itself create additional profit opportunities? Holcombe is silent about this point. As I have pointed out above, entrepreneurial activity shifts the profit opportunities, that is, it creates some new opportunities while at the same time destroys others. But this does not mean that it creates more profit opportunities. In fact, how could such a claim ever be proven? It cannot be proven *a priori* because the question of how many profit opportunities exist is empirical. We can easily posit a technological development—say, for instance, the advent of computers replacing the myriad of profit opportunities associated with marginal improvements in the typewriter—that would appear to destroy more entrepreneurial opportunities than it creates. Yet this is only conjecture; there can be no empirical proof because empirically we can only observe the opportunities that are realized in fact. To weigh opportunities created and opportunities destroyed in the balance requires that we know the unknowable: how many other opportunities might have been realized had history taken a different course.

Holcombe seems to have recognized this dilemma. In fact, his only explanation for the thesis that entrepreneurship leads to more entrepreneurship does not focus on the quantity of existing profit opportunities, but on the perception of

these opportunities. He claims that entrepreneurs create a dynamic environment in which the perception of profit opportunities is facilitated. Thus he states that "most profit opportunities get noticed by entrepreneurs because they are new" (p. 50, emphasis added), and he points to the static ancient Chinese economy where "one is not likely to spot an entrepreneurial opportunity today that was not apparent yesterday" (p. 52).

However, Holcombe again fails because he does not explain why the perception of profit opportunities is facilitated by change as such. Lack of change was indeed not the only feature that distinguished ancient China from Europe, and it could well be the consequence rather than the cause of a lack of entrepreneurial spirit. Thus, Holcombe's thesis boils down to a mere assertion that cannot be proven any more than his other claim, that entrepreneurship creates additional profit opportunities. It is, furthermore, clear that Holcombe's perception thesis implies a passive view of man and thus contradicts the existence of choice. Either acting man chooses where to turn his perception, or his perception is caused by external events. Only if the former holds true can there be something like an economic science. If the latter were true, we would have to study human action in the way the natural sciences deal with their subjects.

Moreover, what political conclusions are likely to be drawn from Holcombe's view of entrepreneurship as "the engine of growth"? As he himself points out, "the emphasis shifts toward the creation of an environment within which opportunities for entrepreneurial activity are created, and successful entrepreneurship is rewarded" (p. 58). I submit that this by no means precludes government intervention. If economic growth were really stimulated by change as such, why should government not start to interfere randomly in the economy?

Hence, Holcombe's attempt to put a valid observation into the Procustean bed of Kirzner's theory of entrepreneurship leads to inescapable analytical contradictions and to possibly disastrous policy conclusions.<sup>2</sup>

#### REFERENCES

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<sup>2</sup>For a detailed critique of Kirzner's theory, see Hülsmann (1997).