

# THE ENTREPRENEUR ACCORDING TO J. A. SCHUMPETER AND A VIEW OF MANAGEMENT SCIENCE AND PSYCHOLOGY

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## Abstract

Global changes and growing competition in world markets cause an increasing interest in the topic of entrepreneurship and the personality of the entrepreneur as a source of innovation and competitiveness. Among the first economists who have systematically explored the issues of entrepreneurship, business, and entrepreneurs is Schumpeter. His contribution presents the concept of the entrepreneur as a dynamic theory in the context of other economic theories. Schumpeter's entire work is a celebration of the individual entrepreneur-innovator - modern entrepreneurship, representing the creative and driving force of socio-economic development, conferring system dynamics and shifting the economy forward. The text presents the different types of business according to Schumpeter, as compared with the classification of entrepreneurs from the perspective of modern management science and psychology.

**Key words:** entrepreneur, Schumpeter, economic theory, classification of entrepreneurs

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## Introduction

Companies as fundamental economic and social units of a society are one of the most important actors of modern history. They are the source of economic and technological development as well as fundamental national economic values. The quickly changing environment of global markets places demands on companies, when timely recognition of changes that are about to come and subsequent adjustment is the question of survival. Creating and maintaining a competitive advantage in an increasingly competitive environment is a permanent challenge. Entrepreneurship and the personality of entrepreneur as a source of innovation and competitiveness is becoming the subject of research for many scientific disciplines. The objective of the competitiveness policy of current European governments is to support positive entrepreneurial attitudes. The European Commission sees entrepreneurship as: “ ... a state of mind and process of creating and developing an economic activity by fusing creativity, innovation and will to bear risks with a high-quality management within a new or

*existing organization.*” (European Commission, 2003, p. 6). The term “entrepreneur” comes from French. Entrepreneurs were mediators who accepted liability for certain projects or represented interests of third parties in war conflicts. R. Cantillon (1725) defined an entrepreneur as a person bearing risks for buying for fixed prices while selling for prices that are uncertain. The will to bear risks distinguished entrepreneurs from capitalists. According to Beaudeau (1797), an entrepreneur is defined by accepting risks, planning business meetings, supervising staff who executes entrepreneur's plans for a salary and by owning production, organizational and business means. J. B. Say (1803) distinguished the profit of an entrepreneur from the profit from capital as two different concepts. Francis Walker (1876) distinguished between the offer of capital that yields interest and managing and exploiting talent in order to achieve profit (Jünger, Fialová, 2005). One of the first economists who processed the subject of entrepreneurship, business and entrepreneurs theoretically and systematically was Schumpeter. This paper presents the concept of an entrepreneur in the dynamic theory of J. A. Schumpeter in the context of other economic theories. Schumpeter's entrepreneur-innovator (i.e. modern entrepreneurship) represents a creative and driving force of the socioeconomic development providing the system with dynamics and driving economy forward. The paper presents different types of entrepreneurs according to Schumpeter and types of entrepreneurs from the perspective of modern managerial science and psychology.

## **1 The concept of an entrepreneur according to J. A. Schumpeter**

In his system, Schumpeter strictly distinguishes between the static and dynamic economy (i.e. stationary “growth” vs. dynamic “development” or “progress”). His ideal is not the perfectly competitive neo-classical static balance<sup>1</sup>, but rather a dynamic market with economic cycle: a cycle as an inevitable phenomenon pertaining to the dynamic development of economy, whose function is the realization of internally generated scientific and technical progress, in other words “implementation of innovations”. Implementing innovations into an economic system is called the act of entrepreneurship, while the carrier of innovations (initiator of development – entity bringing about a new change) is the entrepreneur.

*“Entrepreneurship is what we call new combinations, their implementation in companies, etc. Entrepreneurs are economic entities whose function is to promote new*

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<sup>1</sup> “Schumpeter did not consider accumulation of capital or depersonalized technological advancement to be the source of economic growth. In his conception, the driving force behind economic development was an entrepreneur, the innovation maker, whose motivations are based on business profit. However, the existence of such an entrepreneur requires abandoning the concept of perfect competition as theoretic explanation of how capitalist market economy works” (Sojka, 2010, p. 199).

*combinations that are at the same time an active element*” (Schumpeter, 1987, pp. 207-208). The result of entrepreneurship is represented by business profit. Its source is the implemented innovation representing a “new combination of manufacturing actors” enabling production with lower production costs when compared to the preceding combination.

According to Schumpeter, economic development essentially requires entrepreneurial mind, implementation of innovation is thus an act of entrepreneurship<sup>2</sup>, whereas the result is business profit. Schumpeter called the implementation of innovations into an economic system an act of entrepreneurship, while the carrier of innovations is an entrepreneur. Schumpeter actually saw the originality of his theory in distinguishing between an entrepreneur and a capitalist. The function of a capitalist lies in merely funding innovations, whereas he associated an entrepreneur<sup>3</sup> with the function of implementing innovations performed only during the innovation period. The result of entrepreneurship is reflected in the business profit,<sup>4</sup> the source of which is the implemented innovation enabling production at lower manufacturing costs. The creative part of an entrepreneurs requires “*entrepreneurial spirit*”, when an entrepreneur is willing and able to push through innovations, even despite rigid circumstances. Schumpeter sees the essentials of capitalism in the incessant innovative activity of private individual entrepreneurs (related to the use of capital)<sup>5</sup> and links it with the transition from a static cycle to dynamics.

J. A. Schumpeter defines capitalistic socioeconomic system as “*a system based on dynamics evoked by individual entrepreneurs, the innovation makers*” (Sojka, 2010, pp. 198-199) and its creation thus as a result of transition from statics to dynamics. “*Entrepreneurs, the innovation makers, are the result of particular historic development and as such they may only prove themselves successful on a certain level of socioeconomic development that has brought about value and institutional changes allowing for this type of behaviour*” (Sojka,

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<sup>2</sup> For more details see (Čapek, 1990), (Grochová, 2010), (Klusoň, 1994).

<sup>3</sup> An entrepreneur does not necessarily have to be an owner – see the below specified “*factory owner-merchant*”, “*captain of industry*”, “*director*” and “*founder*”. Depending on who the carrier of innovations is, we distinguish between “*competitive*” and “*trustified*” stages of capitalism. For more details see (Sirůček, 2005).

<sup>4</sup> “*Another Schumpeter’s important contribution concerns understanding and elaborating the close correlation between successful innovations and extraordinary innovation profit. Depending on the approach to innovations, Schumpeter distinguishes between a simple manufacturer and entrepreneur. An entrepreneur is a manufacturer or trader who introduces “new combinations” that yield “business profit” exceeding the usual average profit achieved by simple, innovation-passive manufacturers and traders. He strongly warns that this higher level of profit, this extraordinary innovation profit may only be achieved and maintained in the long term by those entrepreneurs who keep coming with new innovations over and over again.*” (Vlček, 2010, p. 7).

<sup>5</sup> He defines capital from the perspective of a central category of his theoretic system – innovations – as: “*a sum of money and other monetary means an entrepreneurs is left with in any period*” (Schumpeter, 1987, p. 271). Schumpeter thus rejects Marx’s concept of capital in the sense of a social production relation that allows for its appreciation.

2010, p. 198). This occurred in Europe during 18th century and the “*ultimate reversal*” came with industrial revolution at the beginning of the 19th century.

Economy changes in terms of quality through entrepreneurs' activities. There are changes in satisfying of needs, consumer preferences, technologies, organization, management and institutions. Innovation activities are of “*creative nature*” and take place under conditions of principal uncertainty. “*Therefore, the future of economy is not strictly predetermined, it is ... formed particularly by creative activities of entrepreneurs, the innovation makers*” (Sojka, 2010, p. 199).

Schumpeter elaborates broadly on his thoughts on an entrepreneur who has to overcome obstacles (technical, subjective, social), “*sails against the stream*”, “*pushes*” the system forward and endows it with dynamics. An entrepreneur faces various technical obstacles (more complicated calculation of costs and prices when compared with routine practices), circumstances of subjective nature (the necessity to surmount temptations and traditional routine activities resulting from psychological predispositions) and difficulties of social nature (reactions of the surroundings when introducing new things in consumption,<sup>6</sup> when trying to convince associates, the necessity to suppress competitors, etc.).<sup>7</sup>

Entrepreneurs-innovators have to overcome many obstacles and resistance posed against the implementation of innovations by the existing socioeconomic environment. Despite this, they keep pushing the whole system forward endowing it with necessary dynamics. “*... While in usual cycles, it is enough if a common economic entity has certain skills and experience, innovations require know-how. While such an entity goes with the flow in the generally known cycle, in case it wants to change the flow, it swims upstream. What was once a support becomes an obstacle and the known becomes unknown ...*” (Schumpeter, 1987, p. 215).

The driving force of, in particular, capitalistic economy is associated with human initiative and lies in activities of an individual and creative entrepreneur. An entrepreneur-innovator is a creative entity exhibiting wider non-hedonistic motivations for entrepreneurship and follows the profit motivation not only because of the effort to maximize consumption. There were no great innovators before capitalism, the transition to capitalism is the transition to dynamics based on innovation activity of individuals; innovators in socialism cease to exist

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<sup>6</sup> In order to succeed, an entrepreneur has to form consumers' preferences. Schumpeter observes that “*a vast majority of changes of the commodities consumed were forced by manufacturers on consumers who often resisted and had to be instructed via a mental technique of promotion*” (Pressman, 2005, p. 131-132) with reference to (Schumpeter, 1939).

<sup>7</sup> Compare (Klusoň, 1994).

as autonomous personalities and this function is taken over by the state. Let us repeat that Schumpeter valued his distinguishing between an entrepreneur and a capitalist. Schumpeter does not see in entrepreneurs any particular persons (in the same way as he did not see in a company a specific organization or institution with a certain period of existence, but he rather referred to a specific activity or operation) – his entrepreneur is not a representative of a certain profession or clearly defined class. *“The role of the implementer of a new combination may be, according to Schumpeter, played by persons of various legal or even economic statuses. They may be company owner, presidents of boards of directors, authorized officials, influential bankers or financiers. Schumpeter did not pay attention to who was or was not an entrepreneur in a joint-stock company; for Schumpeter, nobody becomes an entrepreneur once and for all and may be replaced by anybody else at any time”* (James, 1968, p. 76). The innovation implementer is an entrepreneur-innovator when performing a certain function during the innovation. An entrepreneur does not necessarily have to be identical with the owner: an entrepreneur can be anyone: according to Schumpeter, the function of an entrepreneur was never linked to particular persons; an entrepreneur is always also something else. Due to their status, various people find themselves in situations, when they perform managerial functions.

### **1.1 Typology of entrepreneurs according to Schumpeter and Miner**

In practice, Schumpeter speaks of four types<sup>8</sup> of entrepreneurs: “factory owner-merchant” (16th-18th century), “captain of industry” or president of a board of directors, etc., and “director” (manager) and so-called “founder” (an unstable element focused on founding new companies and shortly afterwards moving elsewhere).

The “factory owner-merchant” was also an owner and director and performed many different tasks (being involved e.g. in the sphere of business). The “captain of industry” is the second type of entrepreneur: e.g. a president of a board of directors or authorized official who is usually not the owner: this captain of industry actually runs the business (e.g. due to the control over shares) and does not deal with e.g. technical issues, which is a task for his teams of superiors. Another type is called the “director” (this is, however, not an “ordinary” director of a company, although these two functions may coexist in a single person or organization –

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<sup>8</sup> The word typology derives from the Greek words “tupos” meaning a sign or model and “logos” meaning a word, speech, law or term. Webster defines typology as “the study of types, symbols or symbolism”, whereas Oxford defines it as “the study of symbolic representation”. Typology is a generalizing scientific method which tries to classify selected phenomena according to similar features.

an entrepreneur thus decides e.g. about introducing new production, not only about common operations), who works for a salary, but runs the business. “Directors” do not always have to follow their motivation for unlimited profit and their actions follow different psychological motivations than in the previous cases (striving for good reputation, accentuation of the satisfaction of a job well done or feeling of responsibility, importance, performance, etc.). The fourth type is the “founder”, often a very unstable element in entrepreneurship. This type may specialise e.g. on founding new companies, but later loses interest in them and sells his share. *“According to Schumpeter, these unstable founders are often characterized with low morale. Nevertheless, they are the type that is nearest to Schumpeter's conception of pure entrepreneurs, whose function he tries to define”* (James, 1968, p. 77).

The type of an entrepreneurial personality strongly influences the type of the company being founded, its future organizational structure, control methods, growth orientation, strategy and types of markets it will enter. Nobody has yet been able to define unique features common to all entrepreneurs. At present, there are many different entrepreneurial typologies (Lang von Wins, 2004). Schumpeter's types suggest there may be significant differences between entrepreneurs the typologies and their authors try to describe. Some typologies are based on individual experience of advisors, some others on empiric research. The most elaborate typology of entrepreneurs is probably Miner's typology (2000), which is based on the existence of four main types. In order to classify an entrepreneur as a certain type, such an entrepreneur does not need to exhibit all the features. At the same time, it is necessary to remark that some entrepreneurs may exhibit features of more types (Lukeš, Nový et al, 2005).

**Performance oriented entrepreneurs** are characterized by strong performance motivation, desire for feedback concerning their performance, desire to plan and set goals for future performance. They are distinguished by strong personal involvement in their company and value identification with it, desire to learn and gain information. They believe in their own abilities, the result of their activity depends on their endeavour. **Real managers** have a positive attitude to authority, desire to compete with others, desire to succeed and manifest their power, desire to step out of the crowd and perform managerial tasks. They have a directive cognitive style. **Creators of expert ideas** are characterized with high intelligence, desire to innovate personally. They use conceptual cognitive style and try to avoid risks. These entrepreneurs like solving problems and they typically come with new ideas. **Empathic supersellers** are empathic in their cognitive style, they want to help others, they value social processes and have a strong need for harmonic social relations. These entrepreneurs are friendly and sensitive to others' problems. They consider selling power to be the decisive

element of a company's strategy. Each of these entrepreneurial types has own ways to success. It is obvious that personal characteristics of entrepreneurs significantly influence the success of the company founded. Miner pointed to the fact that companies founded by performance oriented entrepreneurs grew faster than any other types. He went on to suggest that entrepreneurs with features of several different types will probably be more successful (Lukeš, Nový et al, 2005, pp. 71 - 73).

## 1.2 Schumpeter and motivation for entrepreneurship

When reflecting on entrepreneurs, Schumpeter pays attention also to motivations. He classifies motivation variables of entrepreneurial behaviour into three basic groups, while the decisive role is not played by satisfying of “material needs” (forming the basis of economic activities and behaviour of entities). Schumpeter accentuates the will to establish “a private kingdom”, a continuing dynasty led by efforts to achieve power and independence. The second group of motivations is characterized by the will to conquer, entrepreneurs often have the “instinct of a fighter” and their activities are similar to sports fighting where *“financial result alone is not the purpose, but it is no more than a criterion of success, symptom of victory”* (Klusoň, 1994, p. 20). Motivations of the third group of entrepreneurs are joy and contentment from creating and implementing something “new” and from their own performance and abilities. Therefore, entrepreneurs search also for difficult tasks and are not afraid to take risks. According to Schumpeter, financial benefit is still important and principally irreplaceable, but he sees the core motivations of entrepreneurs especially in the second and third group.<sup>9</sup>

## 2 Schumpeter in the context of theories of entrepreneurship

As mentioned above, “entrepreneurship” is currently an interdisciplinary and fast growing area in research as well as in education, although we still do not have a comprehensive theory of entrepreneurship (Lukeš, Nový et al 2005). The existing studies of entrepreneurship use three sources – economics, psychology and strategic management (Lukeš, Nový et al, 2005).

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<sup>9</sup> *“During his life, Schumpeter refused to believe that innovation is a rational activity. He thought it to be a creative activity that could not be explained or understood as a result of rational thought process. The driving force of innovation ... is an entrepreneur”* (Pressman, 2005, p. 131). We shall repeat that with his wider thoughts on motivations, Schumpeter somehow supersedes the concept of motivations in Anglo-Saxon neoclassical tradition as well as *“traditional”* rationality of the homo oeconomicus model. For more details see (Sirůček, Džbáňková, 2006).

Economic theories of entrepreneurship have been evolving especially in the past couple of decades (e.g. Kirzener, Shane, Venkataraman, Low, Eckardt and others). Drucker's statement (1993, p. 25) claiming that *“out of all the significant economists, only Joseph Schumpeter focused on the personality of entrepreneurs and their influence on economics”* is no longer true. Economic theories explain what happens when entrepreneurs take actions, what it leads to and what impact it has on the economic system. It is the role of entrepreneurs in relation to forming market economy. An economic view of entrepreneurship usually abstracts away from an individual entrepreneur. Entrepreneurship is, due to the innovations it brings, responsible for economic development of the society. Economic approaches distinguish between entrepreneurs, managers, traders and investors. According to Shane and Venkataraman (2000), entrepreneurship is a mechanism through which societies transfer technical information to products and services and which allows for discovering and mitigating temporary imperfections of economy. A disadvantage of economic approaches is the lack of empiric confirmations of these mechanisms and inability to explain how and why individuals act entrepreneurially. Psychological approaches to entrepreneurship study researches based on characteristics of entrepreneurial personality. The area of management answers the question how entrepreneurs act and what needs to be done so that a person becomes a successful entrepreneur. It also deals with problems entrepreneurs face when their company grows. A significant contribution of this approach is the identification of factors influencing future success of entrepreneurship and how an entrepreneur may take advantage of them (Lukeš, Nový et al, 2005).

Schumpeter's definition of an entrepreneur in economic theory follows e.g. the approach of J. B. Say – *“There is in particular the well-known one that goes back to J. B. Say: the entrepreneur's function is to combine the productive factors, to bring them together”* (Schumpeter, 1987, p. 210). Schumpeter's conception is still topical and most authors use it as a basis for their treatises. His theoretic assertions were followed by P. F. Drucker (1993) and others.

Schumpeter unwinds his conception of entrepreneurship and the entrepreneur from the evolutionary nature of economy functioning, more precisely from its dynamizing factor – innovations. Every step of an entrepreneur needs to be assessed through the prism of processes of “creative destruction”. As suggested above, the term “entrepreneur” in Schumpeter's concept is (as opposed to e.g. common use in economic practice), restricted only to those who implement innovations – i.e. to innovators. Schumpeter considered entrepreneurship a deviation from a routine managerial practice, while these deviations are

accompanied with many complications and obstacles. Let us compare Schumpeter's conception and the conception of an entrepreneur as a “creative force” (human action) in more “classical” continuators of Austrian liberal economic tradition: L. E. Mises and Kirzner. L. E. Mises accentuated the dynamic nature of the market process driven by the entrepreneurial dream of achieving future profits in a world that is radically uncertain. “Neo-Austrian” I. M. Kirzner elaborates the theory of entrepreneurial discovering. According to Kirzner, an entrepreneur “searches for gaps in the market” that represent new opportunities. A good entrepreneur is characterized with “vigilance” so that he does not miss any beneficial opportunity. The reward he gets is a “surprising” profit. Unlike Schumpeter's “entrepreneurs-innovator”, in Kirzner's conception an entrepreneur is particularly an “arbitrageur”, whose main task is to fill gaps in the market. Entrepreneurial issues were also discussed by e.g. W. J. Baumol, H. Leibenstein, T. W. Schultz and others (Holman et al., 1999; Sojka, 2010).

## Conclusion

Schumpeter is one of the most often quoted authors in current economics and he has significantly influenced theories of entrepreneurship. Despite being considered, together with Keynes, to be one of the two most important personalities of economic theory of the 20th century, he is often omitted in economics textbooks. From time to time, we may hear that the time of his influence on economics is still to come and he shall become “the economist of the 21st century”.

H. Hanusch (1990) summarizes Schumpeter's conception of the entrepreneur – initiator (entity) of relevant changes with the following words: “*J. Schumpeter uses the term “entrepreneur” as a technical term referring to somebody who does something new, who succeeds with new combinations. An entrepreneur's motivation is conditioned by searching for profit, his actions are creative and risky and they are the reason for creating new things and destroying old ones. Schumpeter's entrepreneur is thus deeply involved in the process of “creative destruction” and finds himself in sharp contrast to the so-called “statischen Wirt” (static economist), whose activities are oriented mainly on cycle in circle and who can be characterized as a conservative and administrative type. After all, entrepreneurs' activity results in wavy moves of economic development. They are inherent to evolutionary processes and cannot be eliminated without excluding the evolution itself*” (Hanusch, 1990, p. 1328).

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