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Schumpeter's theory of leadership: a brief sketch

Panayotis Michaelides

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Abstract: So far, it has hardly been recognized that the great Austrian thinker Joseph Alois Schumpeter had developed a general theory of leadership. In this paper, we analyze how leaders promote change by building on Schumpeter's understanding of entrepreneurial leadership which fuses the concepts of entrepreneurship and leadership. Also, we analyze Schumpeter's *shift in emphasis* regarding his leadership theory. Specifically, Schumpeter in his early works defined entrepreneurs as individuals whose acts have significant effects on firms. However, in his late works he seems to have realized the need to extend further the boundaries of his early approach, to account for social forces.

Keywords: Schumpeter, entrepreneurship, leadership, society

Introduction

It has hardly been recognized that the great Austrian theoretician Joseph Alois Schumpeter had developed a sketch of a general theory of entrepreneurial leadership. Given the presence of central elements of Schumpeter's *oeuvre* in most leadership theories, it is surprising that so little attention has been paid to this great thinker as an intellectual source for leadership theories.

In this context, we analyze the Schumpeterian theory of "entrepreneurial leadership" and investigate how leaders, according to Schumpeter, can promote change. The concept of entrepreneurial leadership fuses the concepts of "entrepreneurship" and "leadership". This paper develops the construct of "entrepreneurial leadership", drawing on Schumpeter's *oeuvre*.

The remainder of the paper is structured as follows: The second section offers briefly some background knowledge on the concept of entrepreneurial leadership; the third section presents a brief outline of Schumpeter's sketch of a theory of leadership; a fourth section focuses on Schumpeter's *shift in emphasis* regarding the concept of leadership; Finally, the fifth section concludes.

On entrepreneurship and leadership: a brief comment

Undoubtedly, understanding the links between leadership and change is extremely important given that change is traditionally linked to leadership. Meanwhile, entrepreneurship has long been recognized as a driver of development (e.g. Kuratko and Hodgetts, 1989). Also, the so-called neo-managerial theory (e.g. Boston et al., 1996) focuses on innovation (e.g. Light, 1997). The literature suggests several conditions that encourage entrepreneurial action where the leader's task is to "mobilize" the resources of the firm and its creditors (see Brazeal and Herbert, 1999; Howell and Higgins, 1990; Morris and Jones, 1999; Jelinek and Litterer, 1995).

But, what are the challenges faced from the perspective of the various theories of leadership? Leadership theories emphasize the relations among three key factors: (i) the leader, (ii) the followers, and (iii) the environment. While theories of leadership in the management literature abound, we focus on the perspectives of leadership that have emerged recently and are relevant to the context outlined above, i.e. leadership leading to innovation (Gupta et al., 2004).

In this framework, first, the so-called neo-charismatic/transformational leadership made its appearance probably in response to more traditional theories where the leader's role was rather "instrumental" (e.g. path-goal theory [House, 1971] and operant conditioning [Podsakoff et al., 1982]) and focuses on how leaders could initiate super-ordinate performance (Bass, 1985). Second, the so-called team-oriented theories emphasize exactly this ability of leaders to 'initiate' high levels of involvement (Graen and Uhl-Bein, 1995). Third, the so-called value-based leadership approach (House and Aditya, 1997) argues that leaders put forward an ideologically attractive vision (Conger and Kanungo, 1987).

In brief, components of leadership theories relevant for entrepreneurial leadership, based on Gupta et al. (2004), are: (a) Articulate a compelling vision;

(b) Initiate economic change; (c) Face organizational change; (d) Manage a complex environment; (e) Promise that the change will lead to extraordinary outcomes; (f) Initiate exceptional commitment from the personnel; (g) Grant credit from the organizational creditors to finance the new venture; (h) Convince that the goals can be accomplished.

In this sense, the actions of entrepreneurial leaders signal the "enactment" of new combinations and this calls for the execution of the aforementioned entrepreneurial leadership roles. These roles provide the conceptual framework for the construct of a theory of leadership drawing on Schumpeter's works. In what follows, we will take a look at his work.

Entrepreneurial leadership in Schumpeter's *Oeuvre*

As we know, in the *Theory of Economic Development*, Schumpeter claimed that his aim had been "to answer the question how the economic system generates the force which incessantly transforms it" (Clemence, 1951: 158–9) because development consists in "such changes in economic life as are not forced upon it from without but arise by its own initiative, from within" (Schumpeter, 1934: 63).

According to Schumpeter, economic development is accompanied by growth, i.e. sustained increases in income; however quantitative growth does not constitute development *per se*. He wrote: "[W]hat we are about to consider is that kind of change arising from [...] the system *which so displaces its equilibrium point that the new one cannot be reached from the old one by infinitesimal steps*. Add successively as many coaches as you please, you will never get a railway thereby" (Schumpeter 1934: 64, emphasis added).

Development depends upon 'innovation'. More precisely, this concept covered the following five cases: "1. The introduction of a new good [...] or a new quality of a good. 2. The introduction of a new method of production [...]. 3. The opening of a new market [...]. 4. The conquest of a new source of supply [...]. 5. The carrying out of the new organisation of any industry" (Schumpeter, 1934: 66).

In this spirit, Schumpeter used the term 'technological progress' to characterize these changes (Scherer 1992: 1417), which account for the greater part of economic development. He distinguished this process from growth due to the

gradual increase in population and capital. He wrote: 'The slow and continuous increase in time of the national supply of productive means and of savings is obviously an important factor in explaining the course of economic history through centuries, but it is completely overshadowed by the fact that development consists primarily in employing existing resources in a different way, in doing new things with them, irrespective of whether those resources increase or not' (Schumpeter, 1942: 65).

As we know, Schumpeter labelled the carrying out of new combinations 'enterprise' and the individuals 'entrepreneurs', and what made these individuals special was the fact that they had the capacity to exploit the new possibilities offered (Prendergast, 2006: 255). In the words of Ebner (2006: 504): "It follows that novelty needs to be forced upon the majority of economic agents, as progress in general is basically a result of force and confrontation".

Meanwhile, Schumpeter defined production as the combinations of materials and forces (Schumpeter, 1942: 65); however, the producer *is not an inventor*. Following Scott's formulation: 'Schumpeter emphasized the role of the entrepreneur in development. He is the man who sees that the new combination is made. He is to be distinguished from the capitalist (who bears the risk) and from the inventor (who has the ideas), although it is possible for one man to be all three' (Scott, 1998: 104).

It is along these lines of reasoning that Schumpeter drew a sharp distinction between the roles of entrepreneurs and managers. He believed that "the entrepreneur is concerned with change' whereas the manager is 'concerned with routine problems'" (Scott, 1998: 104). According to Scott (1998: 104), the difference between the manager and the entrepreneur had already been stressed in *Theory of Economic Development*. "Carrying out a new plan and acting according to a customary one are things as different as making a road and walking along it' (Schumpeter, 1934: 85). He even stressed the difference between an entrepreneur and a manager with the following words: 'everyone is an entrepreneur only when he actually 'carries out new combinations', and loses that character as soon as he has built up his business, when he settles down to running it as other people run their businesses'" (Schumpeter, 1934: 78).

According to Schumpeter (1934), any departures from existing routines involved certain difficulties (Prendergast, 2006: 255-6):

- One of them arose from the fact that the success of any project depended on the capacity of entrepreneurs to see things differently.
- Also, the 'force of habit' was an obstacle to change.
- Moreover, there was the reaction of the social formation against one who wishes to do something new given that there was a general tendency for a social group to condemn any deviating conduct by one of its member.
- Finally, resistance manifested itself primarily among those groups threatened by innovation.

Thus, as Schumpeter emphatically argued, "[l]eadership [...] does not consist simply in finding or creating the new thing but in so impressing the social group with it as to draw it on in its wake" (Schumpeter, 1934: 88). As we know (see e.g. Prendergast, 2006: 256), Schumpeter's entrepreneur was motivated by (Schumpeter, 1934: 93): (a) the dream to found a private kingdom and / or a dynasty; (b) the will to conquer, the impulse to fight, to prove oneself superior to others, to succeed for the sake, *not of the fruits of success*, but of success itself; (c) the joy of getting things done, or simply of exercising one's energy and ingenuity. As Ebner (2006: 504) put it: "entrepreneurship is driven by motivations that are alien to the rationalist foundations of capitalist civilisation".

In this framework, Schumpeter concluded that entrepreneurship was "a special case of the social phenomenon of leadership" (Schumpeter, 1928: 379) and argued that "this relation between entrepreneurship and general leadership is a very complex one and lends itself to a number of misunderstandings" (Clemence, 1951: 254). Schumpeter believed that entrepreneurship is "essentially a phenomenon that comes under the wider aspect of leadership" (Clemence, 1951: 254–5). Moreover, for Schumpeter "the type of man defined as a "leader" overthrows the existing order and creates a new direction" (Shionoya 1997: 38).

In fact, in his *Capitalism, Socialism and Democracy*, Schumpeter seems to have taken a different view. There, Schumpeter developed his idea of antithesis between the entrepreneur and the manager. He claimed that the bureaucratization of the big enterprise (i.e. the transformation of entrepreneurial activity into a routine process conducted by managers and technical personnel), would lead to the final decline of the big enterprise and, thus, of capitalism.

In what follows, we will take a look at Schumpeter's mature works on leadership, when he apparently realized the need to extend further the boundaries of his older approach.

Schumpeter's shift in emphasis

In his early writings, Schumpeter advocated 'methodological individualism' (Shionoya, 1990: 202), which gave priority to an atomistic view of society over a holistic one. For Schumpeter (1908: 91), who originally coined the term, methodological individualism "just means that one starts from the individual in order to describe certain economic relationships". Of course, according to Hodgson (2007), methodological individualism is neither a universal principle of social science, nor an obligatory rule for all social scientists. According to the same author, Schumpeter (1954: 888) invented the term 'sociological individualism' to describe 'the doctrine that the self-governing individual constitutes the ultimate unit of the social sciences'. Regardless of the fact that there is no broad consensus on the sense and usage of 'methodological individualism', the term 'sociological individualism' coincides with what many theoreticians, nowadays, describe as 'methodological individualism' (see Hodgson, 2007).

In fact, as we know Schumpeter in his mature works changed considerably his conception of leadership (Swedberg, 1991: 172-3). A major manifestation of this shift in emphasis is the fact that he was sincere enough to admit that "the entrepreneurial function need not be embodied in a physical person and in particular in a single physical person" (Schumpeter, 1965: 51). For Schumpeter the entrepreneurs constantly renewed the capitalist class, as the more successful among them systematically showed the propensity of becoming capitalist-owners themselves (Schumpeter, 1934: 78-9). Only the bureaucratization of the big enterprise, through the subordination of the entrepreneurs to managers, could lead trust-ified capitalism to socialism: "The perfectly bureaucratized giant industrial unit [...] ousts the entrepreneur and expropriates the bourgeoisie as a class which in the process stands to lose not only its income but what is infinitely more important, its function" (Schumpeter, 1942: 134). "Thus the same process that undermines the position of the bourgeoisie by decreasing the importance of the functions of entrepreneurs and capitalists, by breaking up protective strata and institutions, by creating an atmosphere of hostility, also

decomposes the motor forces of capitalism from within" (Schumpeter, 1942: 161-62).

Schumpeter's emphasis on societal factors was evident both in *Business Cycles* and, mainly, in *Capitalism, Socialism and Democracy*. In *Business Cycles*, Schumpeter referred to leadership as being "relatively insignificant in itself" (Schumpeter, 1939: 227). Also, in *Capitalism, Socialism and Democracy*, he wrote: "mankind is not free to choose...things economic and social move by their own momentum and the ensuing situations compel individuals and groups to behave in certain ways whatever they may wish to do— not indeed by destroying their freedom of choice but by shaping the choosing mentalities and by narrowing the list of possibilities from which to choose" (Schumpeter, 1947: 129–30).

In fact, a main argument of *Capitalism, Socialism and Democracy* is that the entrepreneur becomes less and less important: "For, on the one hand, it is much easier now than it has been in the past to do things that lie outside the familiar routine – innovation itself is being reduced to routine. Technological progress is increasingly becoming the business of teams of trained specialists who turn out what is required and make it work unpredictable ways. The romance of earlier commercial venture is rapidly wearing away, because so many more things can be strictly calculated that had of old to be visualized in a flash of genius. On the other hand, personality and will power must count for less in environments which have become accustomed to economic change – best instanced by an incessant stream of new consumer's and producer's goods – and which, instead of resisting, accept it a matter of course" (Schumpeter, 1942: 132). As Ebner (2006: 507) emphatically argued: "the leadership function of entrepreneurship would become obsolete in terms of personal leadership".

Of course, Schumpeter still stressed the importance of individual entrepreneurs, albeit in a different institutional setting: e.g. a production engineer in the Research and Development department of a large firm could be regarded as an 'entrepreneur' in Schumpeter's sense of the word. Thus, despite envisaging the demise of the entrepreneurs and their partial replacement by a new mode of economic organization (Freeman, 1982), he never completely abandoned his initial model of the entrepreneur.

Schumpeter's late writings also seem to admit the limits that society imposes on the leader's activity and it is in this context that Schumpeter (1951: 153) in his

mature writings argued that the choices open to individuals are *not* unlimited (see Prendergast, 2006). But, the definite *response* to objective opportunity is not *uniquely* determined and thus depends, at least partly, on the actions of leaders. In other words, his mature writings clearly show that Schumpeter's was aware of the fact that leaders are constrained by social forces (Prendergast, 2006: 264).

This shift in Schumpeter's *oeuvre* from an "individualistic" to a "holistic" point of view could be regarded as a shift in emphasis in his theoretical system. Meanwhile, it expresses Schumpeter's shift from "entrepreneurial leadership" – closely related to "charismatic/transformational" leadership – to an "instrumental" leadership approach, as he seems to have realized the need to extend further the boundaries of his older approach to incorporate the social momentum.

Schumpeter's shift in emphasis could have been due to a Marxian thesis that individuals are not able to determine the social momentum. Their own energy is shaped by the productive forces in the context of the Capitalist Mode of Production and is determined by the 'social capital'. As a result, the 'social capital' is always more than a sum of the individual capitals. More precisely, the core of Marx's thesis was that the leader (i.e. typically a manager) had an "instrumental" role and performed a rather "coordinating" function, but there was nothing special, in the general case, about any particular leader, a thesis that Schumpeter himself came to advocate in his mature writings, as demonstrated earlier.

Conclusion

In the increasing competition that capitalist firms face, the recent management literature has observed the need for a more "entrepreneurial" approach (Brown and Eisenhardt, 1998). In this context, a type of "entrepreneurial leader" has made its appearance that is said to be distinct from the other forms of leadership. This paper made an attempt to link this approach to Joseph Alois Schumpeter, and our analysis demonstrated that Schumpeter's *oeuvre* provides an excellent sketch of entrepreneurial leadership by fusing the concepts of "entrepreneurship" and "leadership".

The perspective of leadership that has emerged in recent years and is relevant to the context outlined above is 'Schumpeterian leadership' capable of sustaining

innovation. In this paper, in Schumpeter's early work, entrepreneurial leadership was viewed as a discrete theoretical construct based on (individualistic) innovative initiative and opportunities (e.g. Lumpkin and Dess, 1996). However, as we have seen, Schumpeter's *oeuvre* underwent changes involving *shifts in emphasis* with regard to the nature of the entrepreneur, since greater emphasis was placed, in his late writings, on the interaction between the leader and the dominant social sphere.

This *shift in emphasis* raises the question of Schumpeter's intellectual debts to the work by other economists, such as Karl Marx. The potential Marxian influence behind Schumpeter's move towards a less individualistic approach to leadership is a fine example for future investigation.

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