

from the occurrence of changes in this routine itself, the emphasis in the definition of the function of entrepreneurs would have been shifted automatically to the latter. Finally there are definitions which we could simply accept. 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. Since this is a performance of a special kind only when the factors are combined for the first time — while it is merely routine work if done in the course of running a business — this definition coincides with ours. When Mataja (in *Unternehmensgewinn*) defines the entrepreneur as one who receives profit, we have only to add the conclusion of the first chapter, that there is no profit in the circular flow, in order to trace this formulation too back to ours.¹ And this view is not foreign to traditional theory, as is shown by the construction of the *entrepreneur faisant ni bénéfice ni perte*, which has been worked out rigorously by Walras, but is the property of many other authors. The tendency is for the entrepreneur to make neither profit nor loss in the circular flow — that is he has no function of a special kind there, he simply does not exist; but in his stead, there are heads of firms or business managers of a different type which we had better not designate by the same term.

It is a prejudice to believe that the knowledge of the historical origin of an institution or of a type immediately shows us its sociological or economic nature. Such knowledge often leads us to understand it, but it does not directly yield a theory of it. Still more false is the belief that "primitive" forms of a type are also *ipso facto* the "simpler" or the "more original" in the sense that they show their nature more purely and with fewer complications than later ones. Very frequently the opposite is the case, amongst other reasons because increasing specialisation may allow functions and qualities to stand out sharply, which are more difficult to recognise in more primitive conditions when mixed with others.

¹ The definition of the entrepreneur in terms of entrepreneurial profit instead of in terms of the function the performance of which creates the entrepreneurial profit is obviously not brilliant. But we have still another objection to it: we shall see that entrepreneurial profit does not fall to the entrepreneur by "necessity" in the same sense as the marginal product of labor does to the worker.

So it is in our case. In the general position of the chief of a primitive horde it is difficult to separate the entrepreneurial element from the others. For the same reason most economists up to the time of the younger Mill failed to keep capitalist and entrepreneur distinct because the manufacturer of a hundred years ago was both; and certainly the course of events since then has facilitated the making of this distinction, as the system of land tenure in England has facilitated the distinction between farmer and landowner, while on the Continent this distinction is still occasionally neglected, especially in the case of the peasant who tills his own soil.¹ But in our case there are still more of such difficulties. The entrepreneur of earlier times was not only as a rule the capitalist too, he was also often — as he still is to-day in the case of small concerns — his own technical expert, in so far as a professional specialist was not called in for special cases. Likewise he was (and is) often his own buying and selling agent, the head of his office, his own personnel manager, and sometimes, even though as a rule he of course employed solicitors, his own legal adviser in current affairs. And it was performing some or all of these functions that regularly filled his days. The carrying out of new combinations can no more be a *vocation* than the making and execution of strategic decisions, although it is this function and not his routine work that characterises the military leader. Therefore the entrepreneur's essential function must always appear mixed up with other kinds of activity, which as a rule must be much more conspicuous than the essential one. Hence the Marshallian definition of the entrepreneur, which simply treats the entrepreneurial function as "management" in the widest meaning, will naturally appeal to most of us. We do not accept it, simply because it does not bring out what we consider to be the salient point and the only one which specifically distinguishes entrepreneurial from other activities.

¹ Only this neglect explains the attitude of many socialistic theorists towards peasant property. For smallness of the individual possession makes a difference only for the petit-bourgeois, not for the socialist. The criterion of the employment of labor other than that of the owner and his family is economically relevant only from the standpoint of a kind of exploitation theory which is hardly tenable any longer.

Nevertheless there are types — the course of events has evolved them by degrees — which exhibit the entrepreneurial function with particular purity. The “promoter” to be sure, belongs to them only with qualifications. For, neglecting the associations relative to social and moral status which are attached to this type, the promoter is frequently only an agent intervening on commission, who does the work of financial technique in floating the new enterprise. In this case he is not its creator nor the driving power in the process. However, he may be the latter also, and then he is something like an “entrepreneur by profession.” But the modern type of “captain of industry”¹ corresponds more closely to what is meant here, especially if one recognises his identity on the one hand with, say, the commercial entrepreneur of twelfth-century Venice — or, among later types, with John Law — and on the other hand with the village potentate who combines with his agriculture and his cattle trade, say, a rural brewery, an hotel, and a store. But whatever the type, 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. This is the rule, of course, and hence it is just as rare for anyone always to remain an entrepreneur throughout the decades of his active life as it is for a businessman never to have a moment in which he is an entrepreneur, to however modest a degree.

Because being an entrepreneur is not a profession and as a rule not a lasting condition, entrepreneurs do not form a social class in the technical sense, as, for example, landowners or capitalists or workmen do. Of course the entrepreneurial function will lead to certain class positions for the successful entrepreneur and his family. It can also put its stamp on an epoch of social history, can form a style of life, or systems of moral and aesthetic values; but in itself it signifies a class position no more than it presupposes one. And the class position which may be attained is not as such an entrepreneurial position, but is characterised as landowning or

¹ Cf. for example the good description in Wiedenfeld, Das Persönliche im modernen Unternehmertum. Although it appeared in Schmoller's Jahrbuch in 1910 this work was not known to me when the first edition of this book was published.

capitalist,¹ according to how the proceeds of the enterprise are used. Inheritance of the pecuniary result and of personal qualities may then both keep up this position for more than one generation and make further enterprise easier for descendants, but the function of the entrepreneur itself cannot be inherited, as is shown well enough by the history of manufacturing families.¹

But now the decisive question arises: why then is the carrying out of new combinations a special process and the object of a special kind of “function”? Every individual carries on his economic affairs as well as he can. To be sure, his own intentions are never realised with ideal perfection, but ultimately his behavior is moulded by the influence on him of the results of his conduct, so as to fit circumstances which do not as a rule change suddenly. If a business can never be absolutely perfect in any sense, yet it in time approaches a relative perfection having regard to the surrounding world, the social conditions, the knowledge of the time, and the horizon of each individual or each group. New possibilities are continuously being offered by the surrounding world, in particular new discoveries are continuously being added to the existing store of knowledge. Why should not the individual make just as much use of the new possibilities as of the old, and, according to the market position as he understands it, keep pigs instead of cows, or even choose a new crop rotation, if this can be seen to be more advantageous? And what kind of special new phenomena or problems, not to be found in the established circular flow, can arise there?

While in the accustomed circular flow every individual can act promptly and rationally because he is sure of his ground and is supported by the conduct, as adjusted to this circular flow, of all other individuals, who in turn expect the accustomed activity from him, he cannot simply do this when he is confronted by a new task. While in the accustomed channels his own ability and experience suffice for the normal individual, when confronted with innovations he needs guidance. While he swims with the stream in the circular flow which is familiar to him, he swims against the

¹ On the nature of the entrepreneurial function also compare my statement in the article “Unternehmer” in the Handwörterbuch der Staatswissenschaften.

stream if he wishes to change its channel. What was formerly a help becomes a hindrance. What was a familiar datum becomes an unknown. Where the boundaries of routine stop, many people can go no further, and the rest can only do so in a highly variable manner. The assumption that conduct is prompt and rational is in all cases a fiction. But it proves to be sufficiently near to reality, if things have time to hammer logic into men. Where this has happened, and within the limits in which it has happened, one may rest content with this fiction and build theories upon it. It is then not true that habit or custom or non-economic ways of thinking cause a hopeless difference between the individuals of different classes, times, or cultures, and that, for example, the "economics of the stock exchange" would be inapplicable say to the peasants of to-day or to the craftsmen of the Middle Ages. On the contrary the same theoretical picture¹ in its broadest contour lines fits the individuals of quite different cultures, whatever their degree of intelligence and of economic rationality, and we can depend upon it that the peasant sells his calf just as cunningly and egotistically as the stock exchange member his portfolio of shares. But this holds good only where precedents without number have formed conduct through decades and, in fundamentals, through hundreds and thousands of years, and have eliminated unadapted behavior. Outside of these limits our fiction loses its closeness to reality.² To cling to it there also, as the traditional theory does, is to hide an essential thing and to ignore a fact which, in contrast with other deviations of our assumptions from reality, is theoretically important and the source of the explanation of phenomena which would not exist without it.

¹ The same *theoretical* picture, obviously not the same sociological, cultural, and so forth.

² How much this is the case is best seen to-day in the economic life of those nations, and within our civilisation in the economics of those individuals, whom the development of the last century has not yet completely drawn into its stream, for example, in the economy of the Central European peasant. This peasant "calculates"; there is no deficiency of the "economic way of thinking" (*Wirtschaftssinnung*) in him. Yet he cannot take a step out of the beaten path; his economy has not changed at all for centuries, except perhaps through the exercise of external force and influence. Why? Because the choice of new methods is not simply an element in the concept of rational economic action, nor a matter of course, but a distinct process which stands in need of special explanation.

Therefore, in describing the circular flow one must treat combinations of means of production (the production-functions) as data, like natural possibilities, and admit only small¹ variations at the margins, such as every individual can accomplish by adapting himself to changes in his economic environment, without materially deviating from familiar lines. Therefore, too, the carrying out of new combinations is a special function, and the privilege of a type of people who are much less numerous than all those who have the "objective" possibility of doing it. Therefore, finally, entrepreneurs are a special type,² and their behavior a special

¹ Small disturbances which may indeed, as mentioned earlier, in time add up to great amounts. The decisive point is that the businessman, if he makes them, never alters his routine. The usual case is one of small, the exception one of great (*utro actu great*), disturbances. Only in this sense is emphasis put upon "smallness" here. The objection that there can be no difference in principle between small and large disturbances is not effective. For it is false in itself, in so far as it is based upon the disregard of the principle of the infinitesimal method, the essence of which lies in the fact that one can assert of "small quantities" under certain circumstances what one cannot assert of "large quantities." But the reader who takes umbrage at the large-small contrast may, if he wishes, substitute for it the contrast adapting-spon-taneous. Personally I am not willing to do this because the latter method of expression is much easier to misunderstand than the former and really would demand still longer explanations.

² In the first place it is a question of a type of conduct and of a type of person in so far as this conduct is accessible in very unequal measure and to relatively few people, so that it constitutes their outstanding characteristic. Because the exposition of the first edition was reproached with exaggerating and mistaking the peculiarity of this conduct, and with overlooking the fact that it is more or less open to every businessman, and because the exposition in a later paper ("Wellenbewegung des Wirtschaftslebens," Archiv für Sozialwissenschaft) was charged with introducing an intermediate type ("half-static" businessmen), the following may be submitted. The conduct in question is peculiar in two ways. First, because it is directed towards something different and signifies doing something different from other conduct. One may indeed in this connection include it with the latter in a higher unity, but this does not alter the fact that a theoretically relevant difference exists between the two, and that only one of them is adequately described by traditional theory. Secondly, the type of conduct in question not only differs from the other in its object, "innovation" being peculiar to it, but also in that it presupposes aptitudes differing *in kind* and not only in degree from those of mere rational economic behavior.

Now these aptitudes are presumably distributed in an ethically homogeneous population just like others, that is the curve of their distribution has a maximum ordinate, deviations on either side of which become rarer the greater they are. Similarly we can assume that every healthy man can sing if he will. Perhaps half the individuals in an ethically homogeneous group have the capacity for it to an average degree, a quarter in progressively diminishing measure, and, let us say, a quarter in a measure above the average; and within this quarter, through a series of continually increasing singing ability and continually diminishing number of people

problem, the motive power of a great number of significant phenomena. Hence, our position may be characterised by three corresponding pairs of opposites. First, by the opposition of two real processes: the circular flow or the tendency towards equilibrium on the one hand, a change in the channels of economic routine or a spontaneous change in the economic data arising from within the system on the other. Secondly, by the opposition of two theoretical apparatuses: statics and dynamics.¹ Thirdly, by the opposition who possess it, we come finally to the Carusos. Only in this quarter are we struck in general by the singing ability, and only in the supreme instances can it become the characterising mark of the person. Although practically all men can sing, singing ability does not cease to be a distinguishable characteristic and attribute of a minority, indeed not exactly of a type, because this characteristic — unlike ours — affects the total personality relatively little.

Let us apply this: Again, a quarter of the population may be so poor in those qualities, let us say here provisionally, of economic initiative that the deficiency makes itself felt by poverty of their moral personality, and they play a wretched part in the smallest affairs of private and professional life in which this element is called for. We recognise this type and know that many of the best clerks, distinguished by devotion to duty, expert knowledge, and exactitude, belong to it. Then comes the "half," the "normal." These prove themselves to be better in the things which even within the established channels cannot simply be "dispatched" (erledigt) but must also be "decided" (entscheiden) and "carried out" (durchsetzen). Practically all business people belong here, otherwise they would never have attained their positions; most represent a selection — individually or hereditarily tested. A textile manufacturer travels no "new" road when he goes to a wool auction. But the situations there are never the same, and the success of the business depends so much upon skill and initiative in buying wool that the fact that the textile industry has so far exhibited no trustification comparable with that in heavy manufacturing is undoubtedly partly explicable by the reluctance of the cleverer manufacturers to renounce the advantage of their own skill in buying wool. From there, rising in the scale we come finally into the highest quarter, to people who are a type characterised by super-normal qualities of intellect and will. Within this type there are not only many varieties (merchants, manufacturers, financiers, etc.) but also a continuous variety of degrees of intensity in "initiative." In our argument types of every intensity occur. Many a one can steer a safe course, where no one has yet been; others follow where first another went before; still others only in the crowd, but in this among the first. So also the great political leader of every kind and time is a type, yet not a thing unique, but only the apex of a pyramid from which there is a continuous variation down to the average and from it to the sub-normal values. And yet not only is "leading" a special function, but the leader also something special, distinguishable — wherefore there is no sense in our case in asking: "Where does that type begin then?" and then to exclaim: "This is no type at all!"

¹ It has been objected against the first edition that it sometimes defines "statics" as a theoretical construction, sometimes as the picture of an actual state of economic life. I believe that the present exposition gives no ground for this opinion. "Static" theory does not assume a stationary economy; it also treats of the effects of changes in data. In itself, therefore, there is no necessary connection between static theory and stationary reality. Only in so far as one can exhibit the fundamental form of the

tion of two types of conduct, which, following reality, we can picture as two types of individuals: mere managers and entrepreneurs. And therefore the "best method" of producing in the theoretical sense is to be conceived as "the most advantageous among the methods which have been empirically tested and become familiar." But it is not the "best" of the methods "possible" at the time. If one does not make this distinction, the concept becomes meaningless and precisely those problems remain unsolved which our interpretation is meant to provide for.

Let us now formulate precisely the characteristic feature of the conduct and type under discussion. The smallest daily action embodies a huge mental effort. Every schoolboy would have to be a mental giant, if he himself had to create all he knows and uses by his own individual activity. And every man would have to be a giant of wisdom and will, if he had in every case to create anew all the rules by which he guides his everyday conduct. This is true not only of those decisions and actions of individual and social life the principles of which are the product of tens of thou-

economic course of events with the maximum simplicity in an unchanging economy does this assumption recommend itself to theory. The stationary economy is for uncounted thousands of years, and also in historical times in many places for centuries, an incontrovertible fact, apart from the fact, moreover, which Sombart emphasised, that there is a tendency towards a stationary state in every period of depression. Hence it is readily understood how this historical fact and that theoretical construction have allied themselves in a way which led to some confusion. The words "statics" and "dynamics" the author would not now use in the meaning they carry above, where they are simply short expressions for "theory of the circular flow" and "theory of development." One more thing: theory employs two methods of interpretation, which may perhaps make difficulties. If it is to be shown how all the elements of the economic system are determined in equilibrium by one another, this equilibrium system is considered as not yet existing and is built up before our eyes *ab ovo*. This does not mean that its coming into being is genetically explained thereby. Only its existence, and functioning are made logically clear by mental dissection. And the experiences and habits of individuals are assumed as existing. How just these productive combinations have come about is not thereby explained. Further, if two contiguous equilibrium positions are to be investigated, then sometimes (not always), as in Pigou's Economics of Welfare, the "best" productive combination in the first is compared with the "best" in the second. And this again need not, but may, mean that the two combinations in the sense meant here differ not only by small variations in quantity but in their whole technical and commercial structure. Here too the coming into being of the second combination and the problems connected with it are not investigated, but only the functioning and the outcome of the already existing combination. Even though justified as far as it goes, this method of treatment passes over our problem. If the assertion were implied that this is also settled by it, it would be false.

sands of years, but also of those products of shorter periods and of a more special nature which constitute the particular instrument for performing vocational tasks. But precisely the things the performance of which according to this should involve a supreme effort, in general demand no special individual effort at all; those which should be especially difficult are in reality especially easy; what should demand superhuman capacity is accessible to the least gifted, given mental health. In particular within the ordinary routine there is no need for leadership. Of course it is still necessary to set people their tasks, to keep up discipline, and so forth; but this is easy and a function any normal person can learn to fulfil. Within the lines familiar to all, even the function of directing other people, though still necessary, is mere "work" like any other, comparable to the service of tending a machine. All people get to know, and are able to do, their daily tasks in the customary way and ordinarily perform them by themselves; the "director" has his routine as they have theirs; and his directive function serves merely to correct individual aberrations.

This is so because all knowledge and habit once acquired becomes as firmly rooted in ourselves as a railway embankment in the earth. It does not require to be continually renewed and consciously reproduced, but sinks into the strata of subconsciousness. It is normally transmitted almost without friction by inheritance, teaching, upbringing, pressure of environment. Everything we think, feel, or do often enough becomes automatic and our conscious life is unburdened of it. The enormous economy of force, in the race and the individual, here involved is not great enough, however, to make daily life a light burden and to prevent its demands from exhausting the average energy all the same. But it is great enough to make it possible to meet the ordinary claims. This holds good likewise for economic daily life. And from this it follows also for economic life that every step outside the boundary of routine has difficulties and involves a new element. It is this element that constitutes the phenomenon of leadership.

The nature of these difficulties may be focussed in the following three points. First, outside these accustomed channels the individual is without those data for his decisions and those rules of

conduct which are usually very accurately known to him within them. Of course he must still foresee and estimate on the basis of his experience. But many things must remain uncertain, still others are only ascertainable within wide limits, some can perhaps only be "guessed." In particular this is true of those data which the individual strives to alter and of those which he wants to create. Now he must really to some extent do what tradition does for him in everyday life, viz. consciously plan his conduct in every particular. There will be much more conscious rationality in this than in customary action, which as such does not need to be reflected upon at all; but this plan must necessarily be open not only to errors greater in degree, but also to other kinds of errors than those occurring in customary action. What has been done already has the sharp-edged reality of all the things which we have seen and experienced; the new is only the figment of our imagination. Carrying out a new plan and acting according to a customary one are things as different as making a road and walking along it.

How different a thing this is becomes clearer if one bears in mind the impossibility of surveying exhaustively all the effects and counter-effects of the projected enterprise. Even as many of them as could in theory be ascertained if one had unlimited time and means must practically remain in the dark. As military action must be taken in a given strategic position even if all the data potentially procurable are not available, so also in economic life action must be taken without working out all the details of what is to be done. Here the success of everything depends upon intuition, the capacity of seeing things in a way which afterwards proves to be true, even though it cannot be established at the moment, and of grasping the essential fact, discarding the unessential, even though one can give no account of the principles by which this is done. Thorough preparatory work, and special knowledge, breadth of intellectual understanding, talent for logical analysis, may under certain circumstances be sources of failure. The more accurately, however, we learn to know the natural and social world, the more perfect our control of facts becomes; and the greater the extent, with time and progressive

rationalisation, within which things can be simply calculated, and indeed quickly and reliably calculated, the more the significance of this function decreases. Therefore the importance of the entrepreneur type must diminish just as the importance of the military commander has already diminished. Nevertheless a part of the very essence of each type is bound up with this function.

As this first point lies in the task, so the second lies in the psyche of the businessman himself. It is not only objectively more difficult to do something new than what is familiar and tested by experience, but the individual feels reluctance to it and would do so even if the objective difficulties did not exist. This is so in all fields. The history of science is one great confirmation of the fact that we find it exceedingly difficult to adopt a new scientific point of view or method. Thought turns again and again into the accustomed track even if it has become unsuitable and the more suitable innovation in itself presents no particular difficulties. The very nature of fixed habits of thinking, their energy-saving function, is founded upon the fact that they have become subconscious, that they yield their results automatically and are proof against criticism and even against contradiction by individual facts. But precisely because of this they become drag-chains when they have outlived their usefulness. So it is also in the economic world. In the breast of one who wishes to do something new, the forces of habit rise up and bear witness against the embryonic project. A new and another kind of effort of will is therefore necessary in order to wrest, amidst the work and care of the daily round, scope and time for conceiving and working out the new combination and to bring oneself to look upon it as a real possibility and not merely as a day-dream. This mental freedom presupposes a great surplus force over the everyday demand and is something peculiar and by nature rare.

The third point consists in the reaction of the social environment against one who wishes to do something new. This reaction may manifest itself first of all in the existence of legal or political impediments. But neglecting this, any deviating conduct by a member of a social group is condemned, though in greatly varying degrees according as the social group is used to such conduct

or not. Even a deviation from social custom in such things as dress or manners arouses opposition, and of course all the more so in the graver cases. This opposition is stronger in primitive stages of culture than in others, but it is never absent. Even mere astonishment at the deviation, even merely noticing it, exercises a pressure on the individual. The manifestation of condemnation may at once bring noticeable consequences in its train. It may even come to social ostracism and finally to physical prevention or to direct attack. Neither the fact that progressive differentiation weakens this opposition — especially as the most important cause of the weakening is the very development which we wish to explain — nor the further fact that the social opposition operates under certain circumstances and upon many individuals as a stimulus, changes anything in principle in the significance of it. Surmounting this opposition is always a special kind of task which does not exist in the customary course of life, a task which also requires a special kind of conduct. In matters economic this resistance manifests itself first of all in the groups threatened by the innovation, then in the difficulty in finding the necessary cooperation, finally in the difficulty in winning over consumers. Even though these elements are still effective to-day, despite the fact that a period of turbulent development has accustomed us to the appearance and the carrying out of innovations, they can be best studied in the beginnings of capitalism. But they are so obvious there that it would be time lost for our purposes to dwell upon them.

There is leadership *only* for these reasons — leadership, that is, as a special kind of function and in contrast to a mere difference in rank, which would exist in every social body, in the smallest as in the largest, and in combination with which it generally appears. The facts alluded to create a boundary beyond which the majority of people do not function promptly by themselves and require help from a minority. If social life had in all respects the relative immutability of, for example, the astronomical world, or if mutable this mutability were yet incapable of being influenced by human action, or finally if capable of being so influenced this type of action were yet equally open to everyone, then there would be

no special function of leadership as distinguished from routine work.

The specific problem of leadership arises and the leader type appears only where new possibilities present themselves. That is why it is so strongly marked among the Normans at the time of their conquests and so feebly among the Slavs in the marshes of the Pripet. Our three points characterize the nature of the *function* as well as the *conduct* or behavior which constitutes the leader type. It is no part of his function to "find" or to "create" new possibilities. They are always present, abundantly accumulated by all sorts of people. Often they are also generally known and being discussed by scientific or literary writers. In other cases, there is nothing to discover about them, because they are quite obvious. To take an example from political life, it was not at all difficult to see how the social and political conditions of France at the time of Louis XVI could have been improved so as to avoid a breakdown of the *ancien régime*. Plenty of people as a matter of fact did see it. But nobody was in a position to do it. Now, it is this "doing the thing," without which possibilities are dead, of which the leader's function consists. This holds good of all kinds of leadership, ephemeral as well as more enduring ones. The former may serve as an instance. What is to be done in a casual emergency is as a rule quite simple. Most or all people may see it, yet they want someone to speak out, to lead, and to organize. Even leadership which influences merely by example, as artistic or scientific leadership, 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. It is, therefore, more by will than by intellect that the leaders fulfil their function, more by "authority," "personal weight," and so forth than by original ideas.

Economic leadership in particular must hence be distinguished from "invention." As long as they are not carried into practice, inventions are economically irrelevant. And to carry any improvement into effect is a task entirely different from the inventing of it, and a task, moreover, requiring entirely different kinds of aptitudes. Although entrepreneurs of course may be inventors

just as they may be capitalists, they are inventors not by nature of their function but by coincidence and vice versa. Besides, the innovations which it is the function of entrepreneurs to carry out need not necessarily be any inventions at all. It is, therefore, not advisable, and it may be downright misleading, to stress the element of invention as much as many writers do.

The entrepreneurial kind of leadership, as distinguished from other kinds of economic leadership such as we should expect to find in a primitive tribe or a communist society, is of course colored by the conditions peculiar to it. It has none of that glamour which characterises other kinds of leadership. It consists in fulfilling a very special task which only in rare cases appeals to the imagination of the public. For its success, keenness and vigor are not more essential than a certain narrowness which seizes the immediate chance and *nothing else*. "Personal weight" is, to be sure, not without importance. Yet the personality of the capitalistic entrepreneur need not, and generally does not, answer to the idea most of us have of what a "leader" looks like, so much so that there is some difficulty in realizing that he comes within the sociological category of leader at all. He "leads" the means of production into new channels. But this he does, not by convincing people of the desirability of carrying out his plan or by creating confidence in his leading in the manner of a political leader — the only man he has to convince or to impress is the banker who is to finance him — but by buying them or their services, and then using them as he sees fit. He also leads in the sense that he draws other producers in his branch after him. But as they are his competitors, who first reduce and then annihilate his profit, this is, as it were, leadership against one's own will. Finally, he renders a service, the full appreciation of which takes a specialist's knowledge of the case. It is not so easily understood by the public at large as a politician's successful speech or a general's victory in the field, not to insist on the fact that he seems to act — and often harshly — in his individual interest alone. We shall understand, therefore, that we do not observe, in this case, the emergence of all those affective values which are the glory of all other kinds of social leadership. Add to this the precariousness of the

economic position both of the individual entrepreneur and of entrepreneurs as a group, and the fact that when his economic success raises him socially he has no cultural tradition or attitude to fall back upon, but moves about in society as an upstart, whose ways are readily laughed at, and we shall understand why this type has never been popular, and why even scientific critique often makes short work of it.¹

We shall finally try to round off our picture of the entrepreneur in the same manner in which we always, in science as well as in practical life, try to understand human behavior, viz. by analyzing the characteristic motives of his conduct. Any attempt to do this must of course meet with all those objections against the economist's intrusion into "psychology" which have been made familiar by a long series of writers. We cannot here enter into the fundamental question of the relation between psychology and economics. It is enough to state that those who on principle object to *any* psychological considerations in an economic argument may leave out what we are about to say without thereby losing contact with the argument of the following chapters. For none of the results to which our analysis is intended to lead stands or falls with our "psychology of the entrepreneur," or could be vitiated by any errors in it. Nowhere is there, as the reader will easily satisfy himself, any necessity for us to overstep the frontiers of observable behavior. Those who do not object to *all* psychology but only to the *kind* of psychology which we know from the traditional textbook, will see that we do not adopt any part of the time-honored picture of the motivation of the "economic man."

In the theory of the circular flow, the importance of examining motives is very much reduced by the fact that the equations of the system of equilibrium may be so interpreted as not to imply any psychic magnitudes at all, as shown by the analysis of Pareto

¹ It may, therefore, not be superfluous to point out that our analysis of the rôle of the entrepreneur does not involve any "glorification" of the type, as some readers of the first edition of this book seemed to think. We do hold that entrepreneurs *have* an economic function as distinguished from, say, robbers. But we neither style every entrepreneur a genius or a benefactor to humanity, nor do we wish to express any opinion about the comparative merits of the social organization in which he plays his rôle, or about the question whether what he does could not be effected more cheaply or efficiently in other ways.

and of Barone. This is the reason why even very defective psychology interferes much less with results than one would expect. There may be rational conduct even in the absence of rational motives. But as soon as we really wish to penetrate into motivation, the problem proves by no means simple. Within given social circumstances and habits, most of what people do every day will appear to them primarily from the point of view of duty carrying a social or a superhuman sanction. There is very little of conscious rationality, still less of hedonism and of individual egoism about it, and so much of it as may safely be said to exist is of comparatively recent growth. Nevertheless, as long as we confine ourselves to the great outlines of constantly repeated economic action, we may link it up with wants and the desire to satisfy them, on condition that we are careful to recognise that economic motive so defined varies in intensity very much in time; that it is society that shapes the particular desires we observe; that wants must be taken with reference to the group which the individual thinks of when deciding his course of action — the family or any other group, smaller or larger than the family; that action does not promptly follow upon desire but only more or less imperfectly corresponds to it; that the field of individual choice is always, though in very different ways and to very different degrees, fenced in by social habits or conventions and the like: it still remains broadly true that, within the circular flow, everyone adapts himself to his environment so as to satisfy certain *given* wants — of himself or others — as best he can. In *all* cases, the *meaning* of economic action is the satisfaction of wants in the sense that there would be no economic action if there were no wants. In the case of the circular flow, we may also think of satisfaction of wants as the normal *motive*.

The latter is not true for our type. In one sense, he may indeed be called the most rational and the most egotistical of all. For, as we have seen, conscious rationality enters much more into the carrying out of new plans, which themselves have to be worked out before they can be acted upon, than into the mere running of an established business, which is largely a matter of routine. And the typical entrepreneur is more self-centred than other types,

because he relies less than they do on tradition and connection and because his characteristic task — theoretically as well as historically — consists precisely in breaking up old, and creating new, tradition. Although this applies primarily to his economic action, it also extends to the moral, cultural, and social consequences of it. It is, of course, no mere coincidence that the period of the rise of the entrepreneur type also gave birth to Utilitarianism.

But his conduct and his motive are “rational” in no other sense. And in *no* sense is his characteristic motivation of the hedonist kind. If we define hedonist motive of action as the wish to satisfy one’s wants, we may indeed make “wants” include any impulse whatsoever, just as we may define egoism so as to include all altruistic values too, on the strength of the fact that they also mean something in the way of self-gratification. But this would reduce our definition to tautology. If we wish to give it meaning, we must restrict it to such wants as are capable of being satisfied by the consumption of goods, and to that kind of satisfaction which is expected from it. Then it is no longer true that our type is acting on a wish to satisfy his wants.

For unless we assume that individuals of our type are driven along by an insatiable craving for hedonist satisfaction, the operations of Gossen’s law would in the case of business leaders soon put a stop to further effort. Experience teaches, however, that typical entrepreneurs retire from the arena only when and because their strength is spent and they feel no longer equal to their task. This does not seem to verify the picture of the economic man, balancing probable results against disutility of effort and reaching in due course a point of equilibrium beyond which he is not willing to go. Effort, in our case, does not seem to weigh at all in the sense of being felt as a reason to stop. And activity of the entrepreneurial type is obviously an obstacle to hedonist enjoyment of those kinds of commodity which are usually acquired by incomes beyond a certain size, because their “consumption” presupposes leisure. Hedonistically, therefore, the conduct which we usually observe in individuals of our type would be irrational.

This would not, of course, prove the absence of hedonistic motive. Yet it points to another psychology of non-hedonist character, especially if we take into account the indifference to hedonist enjoyment which is often conspicuous in outstanding specimens of the type and which is not difficult to understand.

First of all, there is the dream and the will to found a private kingdom, usually, though not necessarily, also a dynasty. The modern world really does not know any such positions, but what may be attained by industrial or commercial success is still the nearest approach to medieval lordship possible to modern man. Its fascination is specially strong for people who have no other chance of achieving social distinction. The sensation of power and independence loses nothing by the fact that both are largely illusions. Closer analysis would lead to discovering an endless variety within this group of motives, from spiritual ambition down to mere snobbery. But this need not detain us. Let it suffice to point out that motives of this kind, although they stand nearest to consumers’ satisfaction, do not coincide with it.

Then there is 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. From this aspect, economic action becomes akin to sport — there are financial races, or rather boxing-matches. The financial result is a secondary consideration, or, at all events, mainly valued as an index of success and as a symptom of victory, the displaying of which very often is more important as a motive of large expenditure than the wish for the consumers’ goods themselves. Again we should find countless nuances, some of which, like social ambition, shade into the first group of motives. And again we are faced with a motivation characteristically different from that of “satisfaction of wants” in the sense defined above, or from, to put the same thing into other words, “hedonistic adaptation.”

Finally, there is the joy of creating, of getting things done, or simply of exercising one’s energy and ingenuity. This is akin to a ubiquitous motive, but nowhere else does it stand out as an independent factor of behavior with anything like the clearness with which it obtrudes itself in our case. Our type seeks out difficulties,

changes in order to change, delights in ventures. This group of motives is the most distinctly anti-hedonist of the three.

Only with the first groups of motives is private property as the result of entrepreneurial activity an essential factor in making it operative. With the other two it is not. Pecuniary gain is indeed a very accurate expression of success, especially of *relative* success, and from the standpoint of the man who strives for it, it has the additional advantage of being an objective fact and largely independent of the opinion of others. These and other peculiarities incident to the mechanism of "acquisitive" society make it very difficult to replace it as a motor of industrial development, even if we would discard the importance it has for creating a fund ready for investment. Nevertheless it is true that the second and third groups of entrepreneurial motives may in principle be taken care of by other social arrangements not involving private gain from economic innovation. What other stimuli could be provided, and how they could be made to work as well as the "capitalistic" ones do, are questions which are beyond our theme. They are taken too lightly by social reformers, and are altogether ignored by fiscal radicalism. But they are not insoluble, and may be answered by detailed observation of the psychology of entrepreneurial activity, at least for given times and places.

CHAPTER III

CREDIT AND CAPITAL

THE NATURE AND FUNCTION OF CREDIT¹

THE fundamental notion that the essence of economic development consists in a *different* employment of *existing* services of labor and land leads us to the statement that the carrying out of new combinations takes place through the withdrawal of services of labor and land from their previous employments. For every form of economy in which the leader has no direct power of disposal over these services, this again leads us to two heresies: first to the heresy that money, and then to the second heresy that also other means of payment, perform an essential function, hence that processes in terms of means of payment are not merely reflexes of processes in terms of goods. In every possible strain, with rare unanimity, even with impatience and moral and intellectual indignation, a very long line of theorists have assured us of the opposite.

Economics, almost since it became a science, has continually resisted the popular errors which cling to the phenomenon of money — quite rightly. This has been one of its fundamental services. And whoever thinks through what has been said so far

¹ The line of thought that is expounded fundamentally unchanged in the following has in the meantime received valuable substantiation and improvement from the investigations of A. Hahn in his *Volkswirtschaftliche Theorie des Bankkredits* (1 ed. 1920, 2 ed. 1926). The reader is expressly referred to this original and meritorious book, which has essentially advanced our knowledge of the problem. Also in many respects parallel is W. G. Langworthy Taylor in *The Credit System*. Perhaps the post-war phenomena and the discussions of the rôle of bank credit in boom and depression have removed from what I have to say much of the appearance of a paradox. To-day every theory of the business cycle considers the fact of "additional credit" in prosperity and takes account of the question, raised by Keynes, whether the cycle may be mitigated by being influenced from the money side. This does not yet mean the acceptance of my point of view. But it must lead to it. Cf. also my article "Kreditkontrolle" in the *Archiv für Sozialwissenschaft und Sozialpolitik* (1925). Recently Robertson, in *Banking Policy and the Price Level*, has arrived at similar results (cf. on this Pigou, *Economic Journal*, June, 1926).