

Chapter 1

Introduction



Economic growth and prosperity are key topics on the political agenda. Despite intensive research, we still have only incomplete answers to questions such as: “Why do some countries and regions prosper, while others fall behind?”, or “Why are certain countries and regions more seriously hit by exogenous shocks and suffer for long periods of time while others show quick recovery?”

This book focuses on regional sources of growth and the responsiveness of regions to global and national developments. Although there are many growth-relevant factors at the national and international level, zooming in on the regional level shows considerable differences in the effect of such factors across regions. Not only is there considerable diversity across regions with regard to their resources for growth, such as knowledge, talent, and behavior, regions may also considerably differ in their response to global and national challenges. We go, however, beyond the recognition that ‘regions matter’ for economic growth, by analyzing long-term trajectories of regional development in the sense of regional economic and social histories. The main claim that we make in this book is that there are deep historical roots that determine the relative economic performance of regions today. In short, not only do ‘regions matter’, but perhaps even more importantly, ‘history matters’.

In the tradition of Joseph A. Schumpeter (1934), we emphasize entrepreneurship and innovation as important sources of economic growth. Our analysis shows that there are substantial differences in the levels of available knowledge, entrepreneurship, and innovation activity across regions, in earlier times as well as today. Investigating these differences, we find significant correspondence between the historical and the current levels of these factors. We show that historical traditions of entrepreneurship and innovation activity have an effect on regional growth and prosperity today.

The empirical analyses in this book are confined to Germany, and cover a time period of a nearly 120 years, from the year 1900 until today. Germany provides us with a particularly interesting case study for the analysis of long-term developments because the country was the focal point of a number of disruptive shocks to the

framework conditions of the social, political, and economic environment beginning in the early twentieth century. Main disruptions include the disastrous events of World War I, followed by a shift from an imperial regime to democracy in 1918, national turmoil in the post-war years causing hyperinflation in 1923, the world economic crisis of the late 1920s and early 1930s with the subsequent rise of the Nazi regime, the destructive results of World War II followed by massive in-migration of expellees from former German territories, and occupation by Allied Powers. After World War II, the country was divided into a Soviet controlled communist East Germany, while West Germany adopted a western-type market economy. Some forty years later, East and West Germany were reunified, bringing about a shock transformation of socialist East Germany to a market economy with severe and long-lasting economic problems. These disruptive shocks allow us to analyze the role of formal and informal institutions for regional development.

A key starting point for our research is the observation that regional differences in the level of entrepreneurship (measured by self-employment and new business formation) tend to be rather persistent over the long period of our analysis. Given the disruptive changes to the socio-economic framework conditions in Germany, we argue that finding a persistent level of regional self-employment and new business formation reflects a regional culture of entrepreneurship. Such a regional entrepreneurial culture can be understood as an informal institution that ‘survives’ drastic changes to the formal institutional framework. Chapter 2 introduces the notion of formal and informal institutions, and provides a detailed characterization a regional culture of entrepreneurship. Based on this characterization we discuss the role of a regional entrepreneurial culture for regional development, and provide an overview of possible reasons for the persistence of regional entrepreneurship.

Chapter 3 provides important basic information for the analyses that follow. We first give a brief overview of German history since the early twentieth century (Sect. 3.1). We then introduce the primary data sources that are used in the analyses. Finally, we describe the regional structures of self-employment and new business formation in both the early twentieth century and today (Sect. 3.2).

Chapter 4 investigates the persistence of regional levels of entrepreneurship in three different scenarios. Scenario I highlights West Germany during the years 1976–2014, a time that was characterized by rather stable economic and institutional framework conditions. Scenario II looks at the development of self-employment and new business formation in West Germany beginning in 1907 and carrying through until 2014, a much longer period that includes a number of drastic disruptive changes. The third scenario focuses on East Germany during the period 1907–2014. This scenario is particularly interesting because of the 40 years of Soviet imposed socialist ideology in East Germany, and the shock transformation to a market economy system after the dissolution of the socialist East German state. The empirical evidence suggests that East German regions with high levels of historical self-employment were able to cope with the challenges of the transformation process relatively well. This can be regarded a clear indication of the important role played by entrepreneurship and an entrepreneurial culture in regional development.

In Chap. 5, we analyze the particularly interesting case of East Germany in more detail. The historical realities of East Germany provide us with a “natural laboratory” in which to investigate the interplay between formal and informal institutions. After enduring 40 years of socialist institutions and anti-entrepreneurial policies, reunification of East Germany with West Germany in 1990 brought about the almost immediate installation of a western-type market economy. During the 40 years of communism in post WWII East Germany, West Germany was developing a capitalist market economy. Looking more closely at the East German example allows us several levels of analysis. First, we can examine the impact of the socialist institutions and policies on regional self-employment and entrepreneurial activity. Second, we are able to make a comparative analysis of the regional dynamics of entrepreneurship between the socialist era and after. Finally, we can accomplish a comparative, multilevel, side-by-side analysis of entrepreneurial activity and self-employment between East and West Germany—so to say ‘an international comparison within one country’—, and observe the relative impacts of formal and informal institutions on regional growth.

Chapter 6 analyzes the effect of entrepreneurship on regional development. We find indeed that those regions with high levels of historical self-employment (a measure of entrepreneurship) experience higher growth rates today. According to our analysis, the mechanism behind this empirical regularity is that high historical self-employment rates apparently imply high current start-up rates that, in turn, have a positive effect on growth.

In Chap. 7 we investigate the link between historical levels of self-employment, historical knowledge sources and regional innovation activity today. A special focus of the analysis is on current levels of new business formation in technology intensive industries that can be regarded as particularly important for regional growth. We find that historical knowledge sources and an entrepreneurial tradition play a significant role in the number of start-ups in innovative industries. The results show that a considerable part of the knowledge that constitutes an important source of entrepreneurial opportunities is deeply rooted in history.

We test our conjecture that a regional tradition of entrepreneurship indicates a regional entrepreneurship culture in Chap. 8 by analyzing data about the personality traits of the local population. We find a significant positive relationship between the historical level of self-employment in a region and the presence of people with an entrepreneurial personality profile today. An aggregate entrepreneurial personality profile of the local population is not only associated with higher current levels of new business formation, but also with higher levels of innovation activity today. In the final chapter, Chap. 9, we summarize the results of our research, draw conclusions for theory, discuss policy implications and outline avenues for further research.

All in all, our empirical analyses of the growth trajectories of German regions demonstrate that history plays a critical role in economic development. Specifically, a culture of entrepreneurship can be extremely resilient and persistent over long periods of time, and has the ability to survive extraordinarily disruptive shocks to the political, social and economic framework conditions. This clearly demonstrates that critical sources of regional development are deeply rooted in the past, and that

previous activities and experiences do significantly shape current developments. Our analyses open up diverse avenues for future research. Our book is a “call to arms” for integrating history, institutions, and culture into any reasonable analysis that aims at understanding regional development. We demonstrate that accounting for historical factors is particularly relevant for an understanding of why certain regions experience a concentration of entrepreneurship and other regions do not. It goes without saying that the design and development of political programs that intend to foster regional entrepreneurship and growth must consider the historical, institutional and cultural environment of specific regions in order to be effective.

Reference

Schumpeter JA (1934) *The theory of economic development*. Harvard University Press, Cambridge (repr. Transaction, New Brunswick 1983)