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IfS Discussion Paper 01/2014

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Social Science**

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A decorative graphic at the bottom of the page consists of several overlapping, swirling green lines of varying thickness and opacity, creating a sense of movement and depth.

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Abstract

This paper deals with methodological principles of Schumpeter's academic writings. Those principles led Schumpeter to create diverse works and were reflected systematically in some of his writings, where Schumpeter emerged as a theorist of science. Besides working on specific topics, Schumpeter dealt systematically with methodological issues in different works. Schumpeter's *History of Economic Analysis*, in particular, must be regarded as the one study among his diverse works, which is considered not only his latest but also his most relevant analysis concerning social sciences and the role of economics in relation to sociology, history and other academic branches. The substantial preface of the *History of Economic Analysis* can be regarded as a manual on how to refer to different academic branches and integrate them into a coherent universal social science, which is far removed from being an autistic, narrow economic science of some modern representation. Although Schumpeter's *History of Economic Analysis* has been extensively printed in several editions, the idea is that the preface especially reveals somewhat neglected thoughts in Schumpeterian discourse. While Schumpeter is mostly regarded as a pioneer of evolutionary economics, this paper argues that Schumpeter could also, perhaps primarily, be interpreted as a well-reasoning institutionalist aiming at a universal social science. From today's point of view, Schumpeter is a truly interdisciplinary theorist.

Keywords: economics; sociology; Joseph A. Schumpeter; social science; history of economic thought; methodology

How to Read Schumpeter

Reading the diverse works of Schumpeter (1883-1950) shows that his thinking matches very well with ideas aimed at coherent universal social sciences. Schumpeter not only practiced a transdisciplinary “putting together”, he also argued theoretically in favor of his practice by mentioning cross-fertilization or the unmixed blessing (Schumpeter, 1954a: 27). His aim was far from delivering a “grand unified theory” (Uhlig, 2012: 31), but rather, as a sociologist of science, he reflected about the division of academic branches such as economics and sociology into semi-independent sciences (Schumpeter 1954a: 27). Therefore, Schumpeter was representative of an academic procedure, which did not fit with, as he said, “primitive economics” (Schumpeter, 1954a: 26). “Primitive economics” has no cooperation with other disciplines and is monodisciplinary and autistic. Spiethoff has said that Schumpeter saw himself as a “gourmet” in issues of theory (Spiethoff, 1949: 291). In a nutshell, although Schumpeter is mostly known for his discussion of the entrepreneur and his ideas of innovation, he is also a theorist providing a manual for inter- and transdisciplinary thought, which may serve as a starting point for an up-to-date debate on the integration of fragmented social sciences.

Summarizing the central issues of the argument at the beginning, four points should be acknowledged: (i.) First, from today’s point of view Schumpeter is a truly interdisciplinary theorist. He worked continuously in a perspective, which must be characterized as academic cross-fertilization. Therefore, posthumously, Schumpeter’s different articles were sorted into books as *Collected Papers in Sociology* (Schumpeter, 1953), *Political Speeches* (Schumpeter, 1992), *Essays in Socioeconomics* (Schumpeter, 1987), *Papers on Economic Policies* (Schumpeter, 1985), *Essays on Daily Politics* (Schumpeter, 1993), *Papers on Economic Theory* (Schumpeter, 1952) and articles on the history of economic thought (Schumpeter 1954b). Many contemporaries know Schumpeter’s ideas as they were developed in *Theory of Economic Development* (Schumpeter, 1963), perhaps also his book on *Business Cycles* (Schumpeter, 1939), and, of course, his arguments in

Capitalism, Socialism, and Democracy (1942)¹, but less well known is his systematization of academic development and his methodological roadmap.

The paper focuses on the principles of Schumpeter's academic thought, which led him to create diverse works and which were reflected systematically in some of his writings, where Schumpeter emerged as a theorist of science. Aside from working on specific substantial topics, throughout his life Schumpeter dealt with methodological issues. He wrote articles on rationality (Schumpeter, 1991), on *Positivism in Economics* (Schumpeter, 1914a), on *Mathematical Methods in Economic Theorizing* (Schumpeter, 1906), *How to Study Social Sciences* (Schumpeter, 1915), "Gustav Schmoller und die Probleme von heute" (Schumpeter, 1926), and many more articles. Referring to books, his 1908 book *Das Wesen und der Hauptinhalt der theoretischen Nationalökonomie* (Schumpeter, 1908) started with methodological reflections, with a chapter entitled "methodological individualism", and his book *Epochen der Dogmen- und Methodengeschichte* (Schumpeter, 1914b, published in English as *Economic Doctrines and Method* in 1954) was certainly a major contribution to methodology in economics. Despite these many different works, Schumpeter's *History of Economic Analysis* (Schumpeter, 1954a) must be viewed as the one study among his diverse works, which depicts his latest statement concerning the division of social sciences and the role of economics in relation to sociology, history and other academic branches.

The substantial preface of the *History of Economic Analysis* (1954a) reads as a manual on how to refer to different academic branches and how to integrate them into a coherent universal social science. This is far removed from being an excessively rigid and emotionally detached narrow economic science of modern representation. There is evidence here that Schumpeter must be regarded as someone who is solidly a well-studied historian of mainstream economics. This leads him to argue offensively for an institutional approach integrating economics with different social sciences and avoiding the formulation of divisional order or ranking.

¹ Ongoing publications of books on Schumpeter exist, but most of them concentrate on Schumpeter as a theorist of innovation and entrepreneurship, see e.g. Kurz and Storn (2012), Becker, Knudsen, Swedberg (2011), Andersen (2009), McCraw (2007), Heertje (2006), Shionoya (1997), Kurz (2005), Reisman (2004), Backhaus (2003), Metcalfe (1998), Moss (1996), Swedberg (1991).

Schumpeter's *History of Economic Analysis* (1954a) has been extensively printed, translated and reprinted in several editions. Especially the preface appears to be rather neglected in Schumpeterian discourse. His argumentation requires so much more attention because it has to be read as a fine synthesis of arguments developed in the first battle of methods between Carl Menger and Gustav Schmoller and the second battle of methods between Schmoller, Max Weber, and others. Over a time span of fifty years or more between the "old" classic controversies and *History of Economic Analysis*, we see that many questions have emerged in a more elegant and rigorous way. Schumpeter is mostly regarded as a pioneer of evolutionary economics, and author of the seminal books *Theory of Economic Development* (Schumpeter, 1963 [1912]) and especially *Capitalism, Socialism and Democracy* (Schumpeter, 1942), the latter containing the famous formulation of "creative destruction" (see Bögenhold, 2007). However, one may see Schumpeter mostly as a well-reasoned and guided theorist, who proved to be aware of all strands of debate in the battle of methods and beyond, and who synthesized and offered his own elaborated positions which still have much to offer. Furthermore, our argumentation shows that Schumpeter practiced an offensive dialogue with neighboring disciplines like sociology, history, political economy and psychology. Recent discussion on the need for transdisciplinary thought can learn a lot from Schumpeter.

History of Science: How Ideas Evolve

Schumpeter argues not only in favor of economic history as rendering a service to economic theory, but also in favor of "a sort of generalized or typified or stylized economic history" (Schumpeter, 1954a: 20) which includes institutions like private property, free contracting, or government regulation.

According to Schumpeter, there are four main reasons to study history. First of all, it has pedagogical advantages. He argues that for students it is very difficult to approach a field without knowing how it relates to the specific historical time. For thorough understanding, a historical background is required. One could affirm that methods presently in use already embody what has been done in the past, and what is not a part thereof is no longer important and not worth considering. However, present methods and

results are meaningful only with reference to historical background. "Scientific analysis is not simply a logically consistent process that starts with some primitive notions and then adds to the stock in a straight-line fashion. It is not simply progressive discovery of an objective reality" (Schumpeter, 1954a: 4).

The second reason is that pertaining to the reading of "old" theories, one may discover other interpretations or new ideas; Schumpeter writes that "our minds are apt to derive new inspirations from the study of the history of science" (Schumpeter, 1954a: 4-5). In his discussion, Schumpeter adds an example: The productivity of this experience may be illustrated by the fact that the fundamental ideas that eventually developed into the theory of special relativity occurred first in a book on the history of mechanics (Schumpeter, 1954a: 5).

The third cause is that history can give us insights into the manner in which the human mind works. Particularly in the history of science, various types of logic are used. Scientific performances are self-revelatory by nature, that is, they reveal the mental processes that have taken place in order to arrive at a certain law or theory. "Scientific habits or rules of procedure are not merely to be judged by logical standards that exist independently of them; they contribute something to, and react back upon, the logical standards themselves" (Schumpeter, 1954a: 5). Finally, the fourth point deals with economics in particular, which is described as a unique historical process. Fundamentally this process does not differ from analogous processes in other fields of knowledge but "much more than in, say, physics is it true in economics that modern problems, methods, and results cannot be fully understood without some knowledge of how economists have come to reason as they do. In addition, much more than in physics have results been lost on the way or remained in abeyance for centuries" (Schumpeter, 1954a: 6).

Given these insightful instructions by Schumpeter as a plea for increased, or at least continuous, attempts to invest in history of economics, one also has to consider Schumpeter's writings as good exemplification of what history of economic writings can highlight. Brilliant ideas are often hidden and neglected for long periods of time. If one wants to analyze a painting hanging on a wall, one must take a few steps back to see the painting as a whole in order to get a sense of the full composition. The same applies to

dealing with science and economics specifically. History of economic thought is a neglected academic area of necessary contextualizing of knowledge, which provides a more sufficient working compass.

If students embark upon a new academic discipline such as medicine, biology or economics, they usually want to learn what is the current state of thought. The majority of people do not want to learn about the discussion that was on the agenda fifty or one hundred years ago, but instead about what the predominant portraits of recent debate are. What is uncontested terrain, what are the competing theories, and where can academic profit for future engagement be found? The difficulty is that academic progress and its change must be conceptualized as a series or process of shortcomings, which, conversely, appear as a never-ending story of failures or mistakes, to express it starkly. Evolutionary economists take it as their credo to look at the inner dynamics of change to arrive at an understanding of principles, analogous to how theoretical economists should treat their subject. One has to gain a careful understanding of the history of one's own discipline to see the bolder and fainter lines, which have led to recent discussion and the current state of the art. In this light, recent debate provides color. Our current knowledge emerges in a historically transcendent way as a snapshot in a series of academic achievements, be they failures or innovations. Economic theory evolves in specific contexts of social life and societal organization.

The Academic Division of Sciences: Towards the Idea of an Orchestra

The substantial preface of *History of Economic Analysis* discusses, in addition, "techniques of economic analysis" in which Joseph A. Schumpeter included economic sociology, economic history, psychology, political economy, statistics and others. Furthermore, Schumpeter explores the relationship between "pure" economics and sociology, psychology, philosophy and logic in detail, providing a systematic discussion of the academic landscape and division. In this discussion, he proves to be an intellectual master of multidisciplinary reflection by investigating the sociology of economics. His systematic methodological reflections in *History of Economic Analysis* (1954a) provide a key to understanding what Schumpeter achieved throughout his academic life, namely the

combining of new elements of different academic strands. Academically, Schumpeter was highly innovative all his life and provided his own methodological script on how to perform social and economic analysis.

Schumpeter discussed several independent scientific disciplines from today's standpoint such as economic history, statistics, "theory," economic sociology, political economy, and "applied fields" such as "techniques of economic analysis." In a subsequent chapter, he turned his attention to specific discussion topics such as the specific relationships between economics and sociology and between logic and psychology. Here, the reasoning is dense and much deeper than is usually assumed when coming across the conventional image of Schumpeter as a theorist of entrepreneurship. Instead, he engages in a very precise sociology of science in which diverse matching processes between individual scientific areas and traditions of thought are investigated.

In depicting the fields of economic history, statistics, "theory," economic sociology, political economy and applied fields as "techniques of economic analysis," a clear conceptual ranking in terms of order is missing. Schumpeter understands each of them instrumentally and he regards the different elements taken together as a box of tools. Obviously, economics is a synonym for "economic analysis," which is to be utilized through different academic configurations provided by the toolbox. The interplay of different branches comes up like an orchestra where different agents have different functions but even the smallest voices contribute to the success of the common enterprise.

In contrast to the history of science as a history of changing intellectual ideas, Schumpeter refers to economic history – *nomen est omen* – as a history of economic and social changes. His plea for an integration of economic history in the orchestra of economic analysis reads as follows: "Nobody can hope to understand economic phenomena of any, including the present, epoch without an adequate command of historical *facts* and an adequate amount of historical *sense*, or of what may be described as *historical experience*. The historical report cannot be purely economic but must inevitably reflect also 'institutional' facts that are not purely economic: therefore it affords the best method for understanding how economic and non-economic facts *are* related to one another and how various social sciences *should* be related to one another"

(Schumpeter, 1954a: 12-13). According to Schumpeter, most of the ongoing errors in economic analysis are due to a lack of historical competencies, which leads him to acknowledge also the fields of anthropology and ethnology: "History must of course be understood to include fields that have acquired different names as a consequence of specialization, such as pre-historic reports and ethnology (anthropology)" (Schumpeter, 1954a: 13).

With respect to statistics, Schumpeter explains that we should recognize that statistical methods are part of the tools of economic analysis because statistical figures or series of figures are of vital importance for economics (Schumpeter, 1954a: 13-14). Consequently, "an adequate command of modern statistical methods is a necessary (but not a sufficient) condition for preventing the modern economist from producing nonsense" (Schumpeter, 1954a: 14).

When discussing "theory" Schumpeter again does what could also be found in his earlier writings (e.g. Schumpeter, 1926). He writes the word "theory" with quotation marks. Schumpeter's intention was to explain that we have no precise commonly shared understanding of what we mean when we talk about theory. In this respect, Schumpeter proves to be a methodologist with profound knowledge of the philosophy of science. His set of questions includes: When does theory achieve the distinction of being "pure theory?" Why do we need studies in the history of economic thought? What about the intersections between theory, statistics, and economic history? Where are the boundaries and areas of overlap among economics, philosophy, psychology, political economy, and economic sociology? Which are the general principles of scientific processes?

Schumpeter explains that "theory" has many meanings and it should not simply be interpreted as a semantic counterpart to practice. Schumpeter (1954a: 14-20) explains that three of these meanings are of special relevance: First, theory is an explanation of causal connections. Even if more of those causalities exist, one may summarize them taken together as "theory". Second, "theory" is also a methodology at the level of paradigms, approaches and procedures, which must be discussed academically. Here, we do not expect to find empirical results but methods to achieve scientific knowledge. Third, "theory" is reserved to a semantic of general economics (see already Schumpeter, 1926:

365 ff.). Viewing this discussion, a reader feels that many items remain provokingly up-to-date and finally unsolved. In the end, Schumpeter tries to find bridges between inductive and deductive procedures in order to arrive at a theory, which should provide an advanced holistic perspective. Already the fact that theory is written with quotation marks indicates Schumpeter's strength in perceiving and acknowledging the complexity of the matter. What is currently a topic in recent science theory was already identified as problematic in Schumpeter's writings, namely that one should not take for granted the wording of theory since different types of theory and correspondingly different semantics coexist (Bunge, 1996). The question of when an academic statement receives the status of being a theory still remains on the agenda.

It is not only economic history that renders a service to economic theory, as Schumpeter argues, but also economic sociology: "Economic analysis deals with the questions how people behave at any time and what the economic effects are they produce by so behaving; economic sociology deals with the question how they came to behave as they do. If we define economic behavior widely enough so that it includes not only actions and *motives* and propensities but also the *social institutions* that are relevant to economic behavior such as government, property inheritance, contract, and so on, that phrase really tells us all we need" (Schumpeter, 1954a: 21). There are several statements where Schumpeter speaks with great appreciation about economic sociology and claims that economics has to seek or to keep closer contact with sociology because "we cannot afford [...] to neglect the developments of sociology" and especially not the "fundamental field of economic sociology in which neither economists nor sociologists can get very far without treading on one another's toes" (Schumpeter, 1954a: 25-26).

Concluding the argument, we see Schumpeter as an author clearly addressing the universe of social sciences in order to put into context elements of academic discussion, which are conventionally separated from each other. Using more recent wording, Schumpeter shows that not only does empirical data matter and in this understanding that history matters, but that sociology also matters. Of course, the angle of Schumpeter's thought is the question of an appropriate economic analysis from which he inspects and evaluates the potential of neighboring fields of research. Schumpeter states that the

academic field of political economy is widely covered by his explanation of the potential of economic sociology. Insofar as sociology deals with social, political and economic institutions, there is not much to add about what political economy can do further. A fourth field of economic analysis techniques encompasses the applied fields of modern business administration disciplines and of specialized fields of economics, such as financial or agricultural economics.

Schumpeter is also concerned with logic, philosophy and psychology, which are not summarized under techniques of economic analysis but which are discussed as a basic methodological understanding of his conceptual framework. He explains in the introduction to the relevant chapter that he uses nothing other than a philosophy of economics (Schumpeter, 1954a: 25) as a basic theoretical scientific reflection.

The most significant statement about economic psychology is contained in the following words: "Economics like other social sciences deals with human behavior. Psychology is really the basis from which any social science must start and in terms of which all fundamental explanation must run" (Schumpeter, 1954a: 27). Of course, Schumpeter is impressed by the arguments of Keynes and Keynesianism of his time, which refers to animal spirits and other behavioral foundations. Also, this type of argument matches an idea, which he presented in a different theoretical discussion on methodological individualism much earlier (Schumpeter, 1908).

Most of our pieces of evidence highlighting Schumpeter's approach are taken from the preface of *History of Economic Analysis* (Schumpeter, 1954a), which is a 1200-page book about the development of economics starting with Aristotle, which Schumpeter left uncompleted. The book was published four years after Schumpeter had passed away. His theory of science with a focus on economics in relation to other academic areas, often historically new and emerging ones, must be viewed as a sociology of scientific ideas. Schumpeter explained in his own words: "From time to time, we shall look up from our work in order to view a piece of intellectual scenery. Slightly less perfunctorily, we shall, for every one of our periods, register some contemporaneous developments in other sciences ... that were relevant or might, for one reason or another, be expected to have been relevant to the development of our own" (Schumpeter, 1954a: 25).

How Schumpeter practiced his own economic analysis

The book *History of Economic Analysis* (1954a) was the last of Schumpeter's writings. The preface provides a manual on how to interpret economics and in this sense, it is a kind of meta-economics, in other words a sociology of economics. However, all his life Schumpeter followed his manual without ever having declared it systematically. Only in his preface to *History of Economic Analysis* do we find this systematic kind of reasoning. However, in his early book *Theory of Economic Development* (Schumpeter, 1963, initially in German 1912)², Schumpeter practiced a kind of interdisciplinary investigation when he referred to behavioral foundations of the entrepreneur. "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" (Schumpeter, 1963: 90).

When Schumpeter asks about the meaning of economic action, he discusses models of rationality. All his theorizing is against practices of utilitarianism and against basic assumptions of economic theorizing. In other words, Schumpeter systematizes arguments in favor of an economics that is oriented at "real life" as opposed to axiomatic assumptions of the nature of human beings. Schumpeter discusses different motives behind entrepreneurial activities (Bögenhold 2003):

(i.) "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 especially strong for people who have no other chance of achieving social distinction." (ii.) "Then there is

² Specialists in the history of economic thought are still debating whether the first publication date was 1911 or 1912; the fact is that it was printed in 1911 but was declared as being published in 1912. Much more important is the fact that the first edition is widely unknown and until recently only very few copies were available in European libraries (a new edition was published as Schumpeter 2006). Current scholars reading the *Theory of Economic Development* in German refer to a reprint of the second edition, while English readers refer to a reprint of the revised English translation first published in 1934. The English version is not identical to the second German edition (1926), while the German first edition differs substantially from the German second edition. For example, the first German edition had a final seventh chapter (title: "The holistic view on the economy") which is largely based on sociological thought, where Schumpeter also refers very much to the issue of demographic patterns.

the will to conquer: the impulse to fight, to prove oneself superior to others, to succeed for the sake, not for 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.” (iii.) “Finally, there is the joy of creating, of getting things done, or simply of exercising one’s energy and ingenuity. ...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” (Schumpeter, 1963: 93-94).

Schumpeter provides very important elements for a psychology of entrepreneurial activity as well as for the need to invest in research on economic-related behavior at all. He clearly insists that motives, such as the need for achievement and success, can also be found within regular professions and that the financial motive is always present but never dominant. Taken together, Schumpeter specifies seemingly non-rational motives as driving forces for entrepreneurship. Economic life and related motives to participate and to compete can be compared to sports: achieving with the goal of success and receiving rewards in terms of recognition and prestige. In some way, Schumpeter portrays an eroticism of business life, which serves as the driving force of champions. Successful people have comparatively high incomes but that is very often an appreciated secondary effect and not the primary or only source of motivation.

Conclusion and Outlook

In recent decades, modern economics has yielded an increasing number of voices referring to a need to deal with human actors and their concrete motivation as driving forces of economic activity. Herbert Simon (1982) coined the (famous) term of “bounded rationality.” Much later Douglass G. North added that economics treats the issue of human motivation like a black box (North, 1990: 17). In the meantime, references to psychology have been deployed increasingly. Kahneman (2012) was recognized for his pioneering work in economic psychology. In his function as the outgoing president of the *American Economic Association*, Akerlof (2007) recently issued a plea to turn academic energy towards issues of motivation and cognitive structures. In their study *Animal Spirits* (2009) Akerlof and Shiller posited that the functioning of the whole capitalist system is heavily based upon socio-

psychological foundations. Simon, North, Kahneman, Akerlof and some further economists in the same line are Nobel laureates and practice methodologically what Schumpeter (1954a) had already suggested earlier. Sociology increasingly claims new ground and indicates the social embeddedness of institutions and economic behavior (Granovetter, 1985; Mikl-Horke, 2008; Bögenhold, 2008; Haller, 2014), which follows a script already provided by Schumpeter. His position is quite close to an institutionalist perspective, which tries to embed historical, regional and, in that sense, cultural specifics in order to gain a clear sense of empirical material, which differs internationally and historically. Reading Schumpeter is an appropriate tool for finding a way back and for shedding light on contemporary questions. Obviously, many open questions remain. One of the issues to be discussed further is the positioning of Schumpeter within so-called Austrian economics. Is Schumpeter a major actor of the Austrian school, if it exists as a unique body? Is he just a foot soldier or does he not belong to the Austrian school at all? The answer is certainly indefinite and vague, depending on how Austrian economics is defined. Another question is how the landscape of the academic division and the economic toolbox might be drawn from the viewpoint of members of different disciplines, e.g. the view of a sociologist, an economist, a historian or a psychologist. Do those academic professionals have separate tool boxes? Sixty years after Schumpeter's preface to the *History of Economic Analysis* (1954a), much of the discussion is still very relevant and Schumpeter proves to be a very important representative of a former generation of universal social scientists.

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