

## How to foster entrepreneurship. A liberal's critique of the status quo in Switzerland

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Ever since Schumpeter's gale (namely, the concept of *creative destruction*), liberalism has cultivated an intimate relationship to entrepreneurship – entrepreneurs embody the creative power of free markets, and conversely one assumes entrepreneurs to be inclined to a liberal social order. How does this reciprocal relationship come about? Different explanatory patterns exist. One of them runs as follows: Liberalism is based on the recognition of universal individual rights. Freedom rights directly give rise to the possibility of entrepreneurial activity, and indeed the right not to be prevented from such activity.

According to the [Economic Freedom in the World Index](#) co-published by the [Liberal Institute](#), Switzerland remains the country with the highest economic freedom in Europe and the fourth-largest in the world in 2019. And also with regard to entrepreneurship, Switzerland reaches record levels due to its [highly attractive startup ecosystem](#). So all good? Not quite. As always, the devil is in the details.

This author, who founded a Swiss startup (Syntherion) which was supported by a federal program (Innosuisse and SNF), who has served as startup coach and judge (Start Summit, Vroom, MassChallenge Switzerland, Kickstart) and runs a startup community (Startup Grind Geneva), argues self-critically that some state actors in the startup ecosystem play a harmful role in a dual sense when it comes to sparking improvements or making particularly early-stage startups thrive. On the one hand, counterproductive programs to foster or accelerate startups are put in place since they impair the ecosystem in the longer run by diminishing economic freedom which is key to prosperity – e.g. countries that rank high in the Economic Freedom in the World Index are also well-off, and, vice versa, those that rank low suffer from a poor economic performance. On the other hand, regulators such as the FINMA are encouraged to strike a balance between legal certainty and lean regulation.

### **A general objection: Hayek's pretense of knowledge in Swiss entrepreneurship**

A supposed strength of the Swiss startup ecosystem are the numerous industry academia collaborations and transfers which either provide direct sponsorship without

taking equity (e.g., [Bridge: Proof of Concept](#) by Innosuisse and SNF)<sup>1</sup> or cash-free coaching and networking platforms (e.g., [AIT](#) or [VentureLab](#)). By liberals, such programs to foster entrepreneurship using tax money at the end of the day must be considered a harmful intervention into the market undermining economic freedom, and thus slowing down the economic development in the long run. It amounts to a pretense of knowledge when politicians, bureaucrats or so-called experts that are appointed as judges by those programs claim to know which startups (reviewing their cases for a few minutes only without having skin in the game) and/or markets have the highest potential. Even though professional or private investors might also do a poor job at assessing the quality of startups (see for example the tremendous waste of capital at [WeWork](#)), the crucial difference is that they (in the example: Softbank) suffer the consequences of their decisions too (in lieu of transferring them to others that are not responsible).

The bottom line for liberals is clear: The politically mandated allocation of resources in the form of start-up and innovation promotion replaces the market-based mobility of goods on the basis of prices. Prices that have been formed on free markets have the important function of carrying elementary information between market participants. They express the constantly changing appreciation for certain goods and are therefore able to allocate scarce resources to those uses which are prioritized by a large number of people, and not only by some politicians, bureaucrats or ill-informed experts. In other words, in the undisturbed market process, the wrongly speculating entrepreneurs who spend too much on production factors are systematically sifted out in favor of more efficient entrepreneurs (who are more economical with production factors). If politics (in the broad sense of the word) then interferes with these free price formation mechanisms – even if this involves well-intentioned promotions of entrepreneurship – it distorts relative prices and confuses the entire economic system. This gives politics an unnecessary high amount of power: by exercising control over subsidy funds, they can make subsidy recipients dependent on their goodwill and thus also secure their votes.

### **A sound argument?**

Wouldn't the liberal stance leave us with a too radical conclusion because it would provoke the question what other party will then enable the value-generating (and, thus, socially desirable) transition from research results to technology and solutions to business problems instead. Furthermore, critical economists such as Paul Collier (in his latest book "the future of capitalism") would strike a blow for pragmatism instead of indulging in a discourse on principles. In this vein, one could argue that supporting

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<sup>1</sup> It is important to distinguish a personal and systemic view on the Bridge grant which the author received as well: The former entails gratitude, the latter criticism.

entrepreneurship (even financially with tax money) is in the public interest since this measure contributes to economic and social progress – particularly by tackling the funding gap, known as the «valley of death» where the grant-making chain breaks down for many innovative projects, no more research funding is available and venture capital is not yet available. It further helps keep the economy internationally competitive (which protects jobs) and creates new jobs at startups which drive innovation, etc. On this basis, one could thus argue that such measures are legitimate since they have a positive return. Yet, such a counter-argument is difficult to buy, at least as long as it is not backed up by evidence. And at least some known facts speak a different language: The [failure rate](#) among startups is high and Switzerland is no exception here. Besides, liberals don't have anything against fostering startups (quite the opposite as we saw at the beginning of this article), the point is just that the state is not the right actor as knowledge is decentralized. Even if public spending is relatively low in the overall funding mix, it is sufficient to distort free markets (which becomes transparent once we investigate the systemic consequences of interventions). Other stakeholders such as professional investors and, first and foremost, the (potential) clients of a startup know better if and how many resources should go to a company.

For markets to work (and markets are the best tool we know to generate prosperity), it's crucial that actors bear responsibility for their (investment) decisions, that they have skin in the game. If citizens or taxpayers in Switzerland deem entrepreneurship and early-stage ventures important, they don't need or pay the state for that, but can become involved themselves, e.g. by becoming co-founders, employees or investors. Even the latter is more realistic and less elitist than it looks like at first glance since initiatives (startups) such as [investiere.ch](#) decrease the entry barriers by allowing common people easy and direct access to Swiss startups.

### **The example of FinTechs: What the state ought to do instead?**

From the above, it does not follow that the state becomes dispensable in the Swiss startup ecosystem. Just its role needs to be redefined, being aware that even in a liberal country like Switzerland the crude libertarian view according to which there ought to be no government at all (von Mises) is too far from practical relevance. In this light, the state should be content with setting up general conditions and the regulatory framework, respectively. The plea is twofold and consists, on the one hand, of striking a good balance between legal certainty and lean regulation when it comes to fintech and new technologies. An illustration is in order and given by the example of blockchain: A recent [study by Avenir Suisse](#) spells out our plea by making the following statement: "Essentially, the law should be changed only in areas where it is not yet DLT<sup>2</sup>-compatible. But these changes have to be made as soon as possible." The time

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<sup>2</sup> Distributed ledger technology.

to act is now because current regulation in Switzerland stunts innovation and technological progress. An example where regulation does not accommodate new technology is fund regulation necessitating a central custodian which is not synchronized with the nature of a decentralized environment promoted by blockchain. Yet, regulation which is currently in place prohibits fund transactions without custodians, which in turn limits the advantages of blockchain.

Therefore, regulation should be made that is technology neutral. Wherever possible and reasonable, FINMA should be exploiting the potential of regtech more fully too by making machine-readable regulation available.

The second part of our plea aims at preventing overregulation which is a burden and concerning established financial firms and banks, in particular. Switzerland has been at the forefront of regulation efforts and activities. International agreements such as Basel III are implemented rigidly whereas other parts of the world (the US or China) are more reluctant or flexible (to put it nicely). This gives their banks a competitive advantage and distorts international competition. When viewed systemically, we come to the insight that this curtailment of economic freedom heavily affects Swiss startups too. If regulatory costs are high for Swiss banks, then their ability to invest into innovation and partner up with startups is reduced. In a nutshell, preserve more economic freedom on all levels.

### **The role of Swisspreneurs**

Let's close this article by detailing some implications for Swiss entrepreneurs. It's not their job to decline funding offers from public sources. Nor to rewrite regulation. However, a few lessons can be learned, among them are the following:

- Join together in interest groups and industry associations (blockchain and the [Crypto Valley](#) with its global reach are again a good example) to build pressure on policy-makers and the regulator to raise awareness of and, ultimately, bring about a leaner and technology neutral regulation which creates legal certainty too. Do not only take your own or immediate interests into account, but adopt a systemic perspective and also speak up on behalf of your customers or your *ecosystem*.
- Don't be too tempted and chase after relatively easily accessible seed funding from the state, but convince your customers or (in capital-intensive cases) wealthy cofounders or angel investors first. In line with how liberalism (or Austrian economics to be precise) portrays the entrepreneur, experimentation is a central aspect of entrepreneurship. (Veritable) risks must be taken to test whether a hypothesis, a given combination of heterogeneous capital factors is

profitable or not. The state in the mix would only delay the essential feedback cycle and put you back to your comfort zone.

- From time to time, step out of the stream of product or business development work, direct experiences, and your immediate responses to it, and engage in deep thinking – and, as special cases, creative or disruptive (Schumpeter) and holistic or systems thinking. It not only helps you to have an open, sharp, well-trained mind, but also shows, by having applied it within this paper at hand, that you found a strong ally in liberalism and Austrian economics.<sup>3</sup>

### About the author



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<sup>3</sup> The economic textbooks usually do not acknowledge the entrepreneur and his importance for the economy (Baumol, W.J. 2010. *The Microtheory of Innovative Entrepreneurship*. NJ: Princeton University Press.). The explanation for this is to be found in the focus of neoclassicism on equilibria and perfect competition. Therein, the acting person does not play a role, the agents merely react as if they were automata. The creative entrepreneur is thus missing too. Only two great thinkers of the Austrian School of Economics changed this in the earlier and mid 20<sup>th</sup> century: Israel M. Kirzner and Joseph A. Schumpeter.