

## THE CRISIS OF CAPITALISM: AN OPEN DEBATE

### 1. THE CAPITALIST SYSTEM IS UNDER SIEGE: THE URGE OF A GENERAL RETHINKING

“The capitalist system is under siege. In recent years the capitalist system has been viewed as a major cause of social, environmental, and economic problems. Companies are widely perceived to be prospering at the expense of the broader community ” (Porter and Kramer, 2011, p. 1).

This is the incipit of a sort of manifest for a new brand of capitalism by M. Porter e M. Kramer (from now on P.K.), appeared in the first issue of 2011 of the Harvard Business Revue.

In conclusion, they say: the moment for a new conception of capitalism is now; society’s needs are large and growing, while customers, employees, and a new generation of young people are asking business to step up.

It is very important, I believe, that such explicit signs of preoccupation come from one of the true scientific-ideological hearts of capitalism, such as the Boston’s Harvard University.

The sense of drama of the expressions quoted, as well as of other possible quotations from the text of P.K., is, in my view, suitable for a world where finance, that has invaded all resorts, care only for the net surplus of every transaction, or group of transactions. Buy cheap and sell dear, independently from circumstances and effects, seems to have become the basic saying of our times.

Accordingly the text of P.K. must be taken as an authoritative cry of alarm and its considerations and proposals must be taken seriously.

It is true that the text here commented has more the air of a pamphlet than of a scientific paper, but, as I will try showing, it contains also an interesting fragment of a very ambitious theoretical downturn.

### 2. A STILL REACTIVE SYSTEM OR A AGONISING BODY?

In the pages of P.K., obviously worried for the present difficulties of capitalism itself, I see one of the few positive signals of the

system. A system that instead of mirroring in its past successes, pays attention to its present difficulties, shows *in vivo* that it has yet something to teach to the humanity as a whole.

As aficionado of old critical approaches, I rejoice in seeing that it implies a big change in the attitude of some economists towards social reality. The firms of the P.K.'s world do not have a simple task (e.g. to maximise profits over a reasonably short period); but they are seen as maximising their net returns over a much longer period, where everything changes. What does it mean?

I would be inclined to see in it just a retching of the basic neoclassical assumption, according to which, the single firm, true molecule of the market, must take care only of maximizing its profits in the short run, leaving to the magic of invisible hand the wondrous transformation, in the very long period, of private vices into public virtues.

What do P.K. mean, when they speak about sheared value?

Value is defined as benefits relative to costs, not just benefits alone. However, businesses have rarely approached societal issues from a value perspective but have treated them as peripheral matters. This has obscured the connections between economic and social concerns.

First of all: why value, disused as it is by the great majority of today's economists, instead of the apparently simpler and more evident price? Shared by whom?

May be it is only an *ex ante* perception of the social implications of every firm's decision. But if that perception remains hazy as it remains, as far as I know, in P.K.'s paper, it's difficult to insert it in the usual decision-making mechanisms. It will always be something inherently uncertain and questionable.

### 3. AN ITINERARY OF RESEARCH

To begin from the beginning, the incubator of the recent ideas of Porter is presumably the theme of clustering, already present in the forth book of the Principles of Economics, by Alfred Marshall (1920), incomprehensibly bypassed by the main stream of economic thought and rediscovered on the ground a century after, by Porter (1990) and a few others.

What is Porter's Cluster?

"Clusters are geographic concentrations of interconnected companies, specialized suppliers, service providers, firms in related industries, and

associated institutions (for example, universities, standards agencies, and trade associations) in particular fields that compete but also cooperate” (Porter, 1998, p. 197).

The distinctive line between Clusters and entities apparently similar, as e.g. the Industrial Districts, is due to one or more investments coming mainly from outside the place, (Cluster) acting as a trigger of business, or instead as a slow and meandering process of specialization of a community, focusing gradually on certain activities, but on closer inspection affecting its overall style of living in some specific kind of product (Industrial District).

The virtual final state, changing in every moment, would be constituted not by a vector of hypothetical long range equilibrium prices, but by a multiplicity of self-reproductive social bodies employing in the best way their provision of factors of production (natural and historically produced) to satisfy a continuously changing worlds group of needs. At the end of this *raisonnement* we find a sort of generalization of the ricardian law of countries’ specialization, but which takes account also of institutional and cultural factors.

Both these conceptions (Cluster and Industrial District) suggest a dynamical reading of the world as populated not by Nation-States but by Clusters, proto-Clusters and remains of Clusters; and/or by Industrial Districts, proto-Industrial Districts and remains of Industrial Districts.

That does not mean ignoring other socio-economic entities (e.g. The Nation-State, the single firm or the family unit), but only that the engine of growth and progressive articulation of the world, consists of groups of people located in stable, self-reproducing communities.

Now, referring specifically to the cluster, all that means that considered the apparent incapacity, with some exceptions quoted by P.K., of present oligopolistic competition to turn automatically private vices into public virtues as requested by the theory, we need – say P.K. – that the enterprise, particularly the big one, must bear directly and explicitly also the social or natural negative effects of its productive process in its strategic view. The direction – which I agree with as far as I understand it – appears clear but it is still a long way to Tipperary.

#### 4. THE SHARED VALUE

So far we agree with P.K., but at least two questions remain open: a) the way to reach that U-turn; b) the role of the value

concept. I start here an analysis that I will develop in other papers, quoting an illuminating example from P.K.'s paper:

“Waste Concern, a hybrid profit/non profit enterprise started in Bangladesh 15 years ago, has built the capacity to convert 700 tons of trash, collected daily from neighbourhood slums, into organic fertilizer, thereby increasing crop yields and reducing CO2 emissions. Seeded with capital from the Lions Club and the United Nations Development Programme, the company improves health conditions while earning a substantial gross margin through fertilizer sales and carbon credits” (Porter and Kramer, 2011, p. 7).

As a result of several widely opened explorations of the worlds business ground, P.K. attribute to their Company, supposedly single-product to simplify, four different utility functions to be reconciled with its function of profitability:

- a) those of the inhabitants of the Cluster where the Company has its head;
- b) those of its subcontractors, considered as a homogeneous aggregate, wherever located;
- c) those of its customers, wherever located;
- d) those of humanity as a whole.

First of all I must notice that, without giving some sort of weight to each of them, the problem remains indeterminate. And by the way, P.K. do not tell us, at least in this paper, how to weigh these four partners of the Company.

## 5. A WORLD OF PLACES?

Let us dwell on an aspect of the construction that gives ground for the sharing of the value of things between the inhabitants of a cluster and the Companies that work there.

This postulate is equivalent to taking, as unit of the analysis, instead of an eluding commodity, a group of humans, spatially located. Here we border the marshallian idea of economic nation (Marshall, 1919, pp. 13-23).

What value? This is the problem. Certainly not the normal long term price of commodities, with which the economists work normally, albeit implicitly. Since the reality in which we live is characterized by a differentiated oligopoly, does it make sense to speak of a tendency of the market price to normal price, or value of

a commodity changing continuously in the very long term? I believe it doesn't.

#### 6. LOOKING BACK TO SOME ITALIAN POST-WAR EXPERIENCES

Let's examine a case, which fits reasonably well, I believe, in Porter's current studies. What may mean: reconciling the Company's profit function with the function of social utility of a place, proposed by P.K.? It can mean, for example, weighing the various plans of production of Olivetti with the supposed peculiarities and preferences of Canavese people. And vice versa, to collocate possible development plans of the Canavesians within the operative strategy of Olivetti.

This constitutes an unusual situation for economic studies in which, *ex ante*, the needs of Olivetti are introjected by the population of the Canavese and/or the recognised needs of Canavesians are incorporated in the Olivetti strategies.

This does not mean (notice!) allocating the profits of the Olivetti, whatever their origin, to meet certain needs of the Canavese, but to discuss the long term needs of, and possibilities for the simultaneous progress of Olivetti and of the Canavese in advance, around a table, simultaneously and constructively.

With the placement of *ex ante* comparison, everything would be done in the light of sun (of the future? Who knows!).

#### 8. LOOKING FOR A PRACTICAL SOLUTION, THEORETICALLY SOUND

The solution of the complicated problem just sketched here, is only the tip – I think – of the very thing for which P.K. strive, that is to reconcile *ex ante* public and private interest. However, it is not entirely clear, at least to this writer, if putting *ex ante* the confrontation would increase the uncertainty to a point where shared value starts to decrease.

To carry the idea on a practical level we can think, for instance, of a bicameral system in the cluster or industrial district, which covers the presence of representatives of the place on the board of directors of the Company and representatives of the Company in the local Council. Of course, with well-calibrated golden shares and veto rights and possibly not interfering with each other. I realize there is a lot to think before such a plan can become workable.

We should determine the penalties, and the institutions to impose sanctions and enforce the ruling for infractions to the rules

laid down, in full concert, by the local authority and the Company. Wanting to be picky, perhaps also the bishopric of the prevailing religion might have a subdued voice.

*Il va sans dir* that the decisions of those Boards should be binding for both, the Company and the local authority, not to speak of every inhabitant of the place, or member of the Company. Shortly, it should enter in the prevailing style of thinking and living of the locality, as well as in the strategy of the Company.

In the dynamism of life, branches of the Company located elsewhere, or collectivities allied to the one here considered, pose continuous, and/or sporadic problems of representation into political and business decision-making organisms. The danger is obviously a degeneration of the governing bureaucracy.

## 9. PARADIGMATIC CHANGES

I realize that this conception implies a dramatic reorientation of the mindset of businessmen and public officials, as well as of economists, politicians and legislators, with a lot of blurring among the existing frontiers of public and private law. In short, we should disassemble rights of public and commercial, national and international law, and reassemble them on new lines.

Anyway, all this implies that the political structure of the world should undergo a great change, disassembling the current policy of sovereign nation-states and companies (not less sovereign in their sphere), to one in which places (clusters or districts) are sovereign states, and Companies have explicit and coordinated (or subordinated?) relief. At the limit, a new inter-local code for external transactions will regulate the exchanges between Turin-cars and Parma-hams, etc.

Note, in passing, that the jealous control of the quality of its typical product would pass, as it should be, from the clusters or industrial districts who buy to those who sell. Every place, like every company, will receive aid, if needed, from the national or worldly institutions, according to the reputation of fairness and accountability gained by its behavior over time, and not on the basis of a social accounting full of imperfections and tricks! In this conception there is more than a scent of the well known “economic chivalry” by Alfred Marshall.

The rating of every place would be not related to its simple solvency, but rather, to the overall reputation of fairness and efficiency of every cluster-district. And it would not be emitted by a private ratings company, with the inherent risks, but by a specialized and severely controlled world’s authority.

At the end of this purely virtual process, we can think of a kind of specialization of the production sites (territorial division of labor), which are for natural and/or historical reasons the more adapt clusters and/or districts, better conformed to a certain kind of production and relative style of living, comprehending all the material and cultural factors of production. This virtual perfect specialization of territory changing, however, kaleidoscopically in every moment is just a target reachable only *ad infinitum*, however useful, in the meantime, to orient ourselves in the hubbub of the world process of change.

#### 10. THE BLURRING AMONG PRIVATE AND PUBLIC LAW

What would be the gist of all this? That in the structure of our society there would be a trend, invisible to the naked economic eye, wherein the potential development of places and Companies would be in the hands of a myriad of joint committees politically like (in the formal protection and utilization of local *joie de vivre*, as perceived in the different places); and business like (to avoid the repression of the precious spirit of entrepreneurship).

This implies, needless to say, a broad and incisive redesign of existing legislation, with striking changes everywhere on the divide between public and private law.

It also means, in other words, bringing into discussion the general political, economic, anthropological aspects, interacting dialectically, in different forms, in the formation of located-communities. The social welfare function of the community and the earnings function of the Companies should find an *ex ante* compromise between social problems and the promotion of an effective pursuit of profit; an objective, this one, which Porter has been chasing for a long time.

#### 11. THE PANDORA'S BOX

Summarizing, in terms of economic theory, the whole P.K.'s discourse reopens the old quarrel on the theory of value.

The general problematic of value – says Heilbroner – is the effort to tie the surface phenomena of economic life to some inner structure or order (Heilbroner, 1983 p. 254).

A reopening, this one, which would draw a very different scenario from that postulated by the common view of economists, where the dynamics of prices is supposed to be the visible manifestation of

an inherent tendency of the structure of prices of commodities, to converge on the structure of long run prices, i.e. values. But if the production function of a commodity (i.e. the satisfier of a group of needs) changes continuously for technical or cultural reasons, as it happens in our dynamic world, the usual architecture of price-value breaks down. And so the economist must redefine his job.

With this return, in a different perspective, to the origins of economic discourse, P.K. demonstrate that the intrepid analysis of social phenomena can help us to understand the inner links among them more than the most sophisticated mathematical implementation of the prevailing view. In their excursions P.K. found some inner links among social phenomena that cannot be reached through the pawed avenues of the economic common view.

This seems to me the deepest meaning of the overall message coming from P.K.: companies, (and scholars and politicians, GB) must take the lead in bringing business and society back together at whatever cost, and as early as possible, I would add, in order to escape apocalypse.

To conclude: through their bold deciphering of the warning signs of capitalism in the flesh, P.K. have, in fact, reopened the Pandora's box of the role of the time honored, (but scarcely studied) theory of value, usually confined to the back room of the Old Curiosity Shop, in the explanation of socio-economic phenomenology.

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## ABSTRACT

According to some Harvard economists – among whom Michael E. Porter and Mark R. Kramer – capitalism as a system is experimenting now a crisis more serious than the usual ones. They maintain that it must be faced with a deep change in the way of conceiving and doing business. Their *big idea*: “involves creating economic value in a way that also creates value for society by addressing its needs and challenges. Businesses must reconnect company success with social progress. Shared value is not social responsibility, philanthropy, or even sustainability, but a new way to achieve economic success”. Accordingly, companies should tailor their projects in such a way to take account *ex ante* of implied social costs. The authors emphasize the difference of this approach from the current practice of compensating *ex post* the places hit by their presence. In this comment, some practical limitations of such a project, and some implications of the approach proposed for economic theorizing, are discussed.

## RIASSUNTO

### *La crisi del capitalismo: un dibattito aperto*

Nella valutazione di un gruppo di economisti di Harvard il capitalismo come sistema attraversa una crisi più seria del solito, che deve essere fronteggiata con un cambiamento del modo di fare impresa. Si tratterebbe, soprattutto per le companies transnazionali, di passare dal commisurare i loro progetti di azione ad una massimizzazione dei ricavi monetari netti su di un periodo abbastanza breve, come oggi accade, ad un approccio che contemperi *ex ante* i propri ricavi con i costi sociali intravvedibili. In questo commento si sottolineano alcuni limiti di tale progetto e si patrocina una soluzione più radicale del problema con lo spostare apertamente alla fase del progetto di investimento il superamento di eventuali conflitti col bene pubblico dei luoghi investiti, pur senza nascondersi i rilevanti problemi di ri-ordinamento giuridico che ne discenderebbero. Incidentalmente si nota che l'approccio suggerito implica una rimessa in discussione della teoria del valore economico oggi dominante.