

# Editorial

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## KEYWORDS

ENTREPRENEURIAL FORMS, INSTITUTIONAL DIVERSITY, ROLE OF THE MARKET AND THE STATE, NONPROFIT ORGANIZATIONS, SOCIAL CAPITAL AND ECONOMIC DEVELOPMENT.

Diversity matters, both at the firm and at the macro-economic level. This is the driving mission of JEOD. While the importance of diversity is already quite well recognized in other disciplines as a major source of wellbeing and quality of life, an open discussion on diversity in economics (meaning both diversity of enterprise types and diversity in the possible combinations of public and private sector roles in different economic systems) has long been taboo. JEOD wants to remove this anomaly.

The urgency of this mission has never been as evident as it is now, during the deep and prolonged crisis that started in 2007 and is now at the center of the world economy. Indeed, the crisis has shaken many long-held tenets on the sustainability of the free market model and even on its ability to satisfy peoples' needs. Since the mid 1970s, and even more after the collapse of the Socialist regimes – which gave the impression that a single model had prevailed (the “end of history” evoked by Fukuyama<sup>1</sup>) – an increasingly strong wind of market fundamentalism had blown from New York and Washington, deeply influencing the approach to economic policy worldwide.

## The focus on a single model

The vision blowing in that wind maintained that the best way to trigger human progress was through the allocation mechanism of mostly self-regulated markets, provided property rights and few other institutions

<sup>1</sup> Fukuyama F. (1992), *The End of History and the Last Man*, New York, Free Press.

were enforced. The main implication of this approach was the need to shrink state intervention and to leave more room for private initiatives. This resulted in a massive wave of privatizations, also involving particularly sensitive public interest services.

Furthermore, a non trivial lemma identified the shareholder-owned enterprise as the ideal company model while prescribing that firm efficiency be measured exclusively by the ability to create value for its shareholders – i.e. maximizing profits. The space for not purely profit-maximizing entrepreneurial and organizational forms was marginalized and restrained. Cooperative firms of all sizes and family-owned businesses were looked upon as a relic of the past. It was believed that these archaic or eccentric entrepreneurial forms were surviving only due to outdated traditions, special legal protection and/or state intervention. Even new phenomena like social enterprises and shareholder companies subscribing to corporate social responsibility were regarded as hopelessly idealistic. This brand of market fundamentalism pervaded other spheres as well, influencing political thought and promoting the notion that the economic logic of the free market should apply to all social dynamics.

### **The failure of the profit maximization model and resilience of other forms of enterprise**

The results produced by the implementation of this economic model did not fully meet expectations, even before 2007. Globalization and liberalization ignited intense growth in several emerging countries but many other nations were left behind. Deep inequality in income and wealth distribution grew almost everywhere. In the rich countries, the middle and low classes were able to temporarily preserve their living standards only by resorting to a remarkable accumulation of private debt. In most countries public debt was not curbed at all. Privatizations resulted neither in more efficiency nor in improved customer satisfaction.

At the same time, not purely profit-seeking enterprises were not disappearing as predicted, and instead continued to thrive. Cooperatives kept growing in the traditional sectors (e.g. agriculture, finance etc.) and even expanded to new segments of the economy such as the newly privatized social and health services. Social enterprises emerged as a new effective solution to the provision of several public interest services. Family-owned businesses kept populating many sectors. Corporate social responsibility made its way into many mid- and large-sized companies.

The effects of the Great Financial Crisis that started in 2007 further testify to the limits of a model based entirely on free markets, which has proven to be unsustainable. At the peak of financial instability, all of the champions of the free market (including Goldman Sachs) had to beg for state support to avoid bankruptcy, and in the process dealt an irreparable blow to the intrinsic logic of the free market model. The crisis also induced a major slowdown of global economic growth. The hit was most intense where the degree of reliance on unfettered markets was largest: in the rich countries. The GDP of these countries dropped significantly, and the costs of the stabilizing interventions caused huge deficits, escalating public debt to dangerous levels. Thus, the private sector debt crisis was transformed into a public sector debt crisis. In order to contrast speculative attacks on sovereign debts several countries had no choice but to cut public expenditures, largely shedding welfare policies.

Meanwhile, at the firm level, the supposedly obsolete enterprises based on a not purely profit maximizing model proved generally more resilient to the crisis. Important examples may be found in the banking sector (where, by and large, cooperative and community banks did not have to ask for public funding and continued lending even as the large banks triggered a credit crunch) as well as in production

cooperatives (where, in general, reduced sales did not translate into job cuts or increased reliance on public income support measures).

### **Restoring a healthy debate on the issue of diversity**

Thus, experiences before and during the crisis confirm that diversity matters also in the design of economic systems. Accordingly, it is important to promote an open discussion on the underpinnings and the implications of such diversity, which has been conspicuously absent from the scientific debate since the 1970s. Indeed, mainstream economics has played a significant role in determining the current situation, both by failing to question the underpinnings of the neoclassic economic paradigm and by promoting market fundamentalism in the teachings of business schools. Restoring a healthy debate on the issue of diversity is precisely the chief aim of JEOD.

The underdevelopment of this vein of research may itself be explained by the fact that the prevailing extreme pro market view tended to underplay the extent and importance of market failures. Indeed, not only public institutions, but also different entrepreneurial and organizational structures respond to diverse challenges and, in turn, impart different incentives to the involved players in order to address those challenges. The wrong entrepreneurial choice can often exacerbate instead of solving the failure. Let us offer two among the many possible examples. First, consider the failed attempt in several advanced countries to curb the cost of social, educational and health services by entrusting the provision of those services to for profit enterprises. It turned out that the cost of those services was increased due to the need to generate a profit margin and to the transaction costs related to the contracting out procedures. Though initially disfavored, the non profit providers eventually emerged as the least costly solution. Second, consider how the liberalization of the banking sector produced extremely different results depending on different incentive structures: in the case of profit maximizing banks, the type of incentives given to top management through the bonus system – which was considered a good way to align the managers' and the shareholders' interests – unintentionally raised the short-termism of the sector and greatly contributed to the debt overhang behind the systemic risk that eventually caused the crisis. In contrast, in the case of cooperative and community banks, where the bonus system was virtually absent, the top managers continued to lend prudently and used deregulation to improve the support to their clients and communities. This latter example provides further elucidation of how inappropriate organizational choices contribute to building microeconomic fragilities that may turn into macroeconomic instability. In the case of the financial sector, the skewed incentive system for top executives likely resulted in heightened systemic risk via the search for larger size (worsening the Too Big To Fail problem) as well as via the creation of entirely new and unsustainable business segments (e.g. the subprime mortgages and the pyramids of structured finance built on them).

We are obviously aware that the issue of diversity is not a total novelty even in economics. For example, much attention has been devoted to explain how different set-ups may emerge and what their implications are, focusing in particular on the diversity between private enterprise and public sector institutions, and analyzing the different principles on which their actions are based. However, the issue has not received the continuous and generalized attention it deserves. Also, analyzing enterprise diversity has often been confined to the industrial organization sphere or to the dissimilar behavior of firms of different sizes. Less attention, if any, was devoted to studying diversity along more promising lines, like analyzing the

differences between aims and governance forms. Much research is needed in particular to understand how and to what extent entrepreneurial and organizational diversity can help the economy and society to cope with market failures.

Diversity of entrepreneurial forms even in the same sector should be more deeply examined at the micro and macro levels. This can make the economy more resilient and improve the functionality of the markets. For example, at the micro level, how can entrepreneurial diversity reduce the gap between supply and demand? As, for instance, when a sector includes consumer-owned enterprises, consumers' welfare is improved through a direct effect – whereby consumer-owned producers respond to the needs of the people – coupled with an indirect effect, since also traditional for profit firms may end up producing more of the goods and services that are useful to consumers, rather than supplying the outputs that are most profitable to them.

At the macro level, for example, diversity can act as a stabilizer of the price system and make the economic system more sustainable. Cooperatives, social enterprises and even family-owned businesses tend to rely more than shareholder companies on long-term contractual arrangements that imply an intrinsic resistance towards ample but short-term fluctuations in prices and wages. And this can help prevent markets from becoming dysfunctional when (as John Maynard Keynes recognized) they are exclusively driven by purely speculative motives.

Further, debate on the topic of diversity should also examine how entrepreneurial variety can contribute to making the economic system more resilient and sustainable. Since it implies that more than one production model is employed at any given time, diversity enhances competition and guarantees that, in case of failure, not all producers end up being distressed concurrently.

The importance of entrepreneurial and organizational diversity goes even beyond the economic sphere and has a significant impact on individual freedom. Entrepreneurial pluralism entails the pursuit of goals that are different from profit maximization, and in doing so it enables people to engage in the production of goods and services that would not be produced otherwise – despite the fact that they meet peoples' needs and increase social welfare. Diversity ensures a closer match between economic activity and the social preference function.

## **The launch of JEOD**

The many reasons outlined above, which show why the field studying diversity in entrepreneurial and organizational forms should be broadened and given continuity, compelled us to launch this new journal. The program JEOD seeks to carry out tries to take full advantage of and put in practice the insights recently offered by Nobel laureate Joseph Stiglitz: "... we need to encourage a variety of alternative forms of economic organization. We ... have focused too long on one particular model, the profit-maximizing firm, and in particular a variant of that model, the unfettered market. We have seen that that model does not work, and it is clear that we need alternative models. We need also to do more to identify the contribution that these alternative forms of organization are making to our society, and when I say that, the contribution is not just a contribution to GDP, but a contribution to satisfaction." (Stiglitz, 2009, p. 359).<sup>2</sup>

We believe the time is now ripe for developing a new scientific outlet to facilitate an open debate on entrepreneurial and organizational diversity. Although publications dealing with specific alternative types

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<sup>2</sup> J.E. Stiglitz (2009), "Moving Beyond Market Fundamentalism to a More Balanced Economy", *Annals of Public and Cooperative Economics*, Volume 80, Issue 3, 345-60.

of enterprises already exist, JEOD will focus more generally on diversity among entrepreneurial models and on the role played by diversity in the market and economic systems at large. JEOD seeks to serve as the principal outlet for theoretical and empirical research on the entrepreneurial phenomenon in its myriad of forms, with a strong emphasis on the determinants and the effects of entrepreneurial diversity and comparison between different types of enterprise and aims as well as diversity within particular forms (e.g., different ownership and governance models, companies organized to take social responsibility into account, entrepreneurial networks). It will also focus on new forms, such as social enterprises.

Our aim is to publish high quality, path-breaking papers making them freely available online at [www.JeodOnline.com](http://www.JeodOnline.com) in an open-access format. JEOD is an international and multidisciplinary journal seeking contributions from various disciplines including economics, history, law, philosophy, political science, social psychology, and sociology. We are currently accepting submissions of single articles to JEOD, which will be handled electronically via Editorial Manager and subjected to double-blind peer review. We are also open to proposals for entire issues edited by a guest editor looking at specific topics from a transdisciplinary perspective.

JEOD is published by Euricse (European Research Institute on Cooperative and Social Enterprises) and supervised by a Scientific Committee and Editorial Board, both composed of leading scholars from around the world in the various disciplines included in the list above.

We look forward to a fruitful debate and hope you will join us!

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