

Capitalism 2.0

new horizons for managers

**4TH VIENNA
GLOBAL
DRUCKER
FORUM
2012**

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are the financial meltdown and the debt crisis
direct and necessary consequences of capitalism?*

The world has been shattered by a series of crises since the collapse of Lehman Brothers in 2008: the near shattering of the world financial system followed by a severe economic downturn across the advanced economies and the surfacing of a sovereign-debt disaster that has been building up during the past 30 years.

While the unethical behaviours and self-serving strategies of key players in the financial sector have become quite evident because of the mess, the issue has not stopped there. Many have begun to question the underlying values of the capitalist system as a whole.

The idea of “maximising shareholder value” with its obsessive focus on short-term results and pure financial measurements has been called into question in many quarters. Others have focused on what they perceive as a lack of ethical standards and values in business and a disregard for the common good.

Given the immense damage that the recent crises have inflicted on the world and its population, a robust discussion about the future of capitalism is appropriate. However, how that discussion is framed is crucial: should capitalism be tossed aside completely in favour of some other economic model or is there a way to improve the system and make capitalism work better in a new global context?

Capitalism under siege

Capitalism – and, with it, business leaders and managers – are under siege today. Populist movements on both the left and the right are offering up a slew of reactionary ideas, essentially calling for a return to a closed world. Meanwhile, businesses have lost much of their credibility with the public, as demonstrated by the recent Edelman Trust Barometer. Indeed, only government institutions have suffered a bigger drop in approval than businesses.

However, rather than be defensive and turn inward, managers must play a key role perhaps the key role – in the transformation towards a new capitalism.

We are now confronted with a fundamental question: are the financial meltdown and the debt crisis direct and necessary consequences of capitalism? Or have these things occurred due to abuses by a small minority of players – and in spite of a hugely efficient economic system that the vast majority of participants have used for positive ends?

A remarkable performance

The positives are certainly undeniable. Since 1950, according to the Groningen Growth and Development Centre, the world has enjoyed a five-fold increase in GDP per capita, even as world population has soared from 2.5 billion to 7 billion today. Growth and prosperity have not been uniform across the globe during that span but now even the poorest regions are catching up – and fast.

Many believe that Africa is poised for strong development over the next decade. Many economies throughout Latin America are already expanding rapidly. Most of Asia has been on a path of increasing wealth for some time. In short, wherever governments have been able to ensure a degree of stability and security, global corporations and local entrepreneurs have created the conditions for economic development, growth and jobs.

All the while, a steady stream of innovations in agriculture, medicine, chemistry, information technology and transportation have emerged from these businesses – not, for the most part, from governments that, at best, have created positive conditions for private enterprise to operate.

This, of course, is what capitalism is all about. And there is not the slightest shadow of evidence that any other known or conceived economic system would have achieved this mind-boggling performance in value creation and innovation in such a short timeframe.

Legitimacy lost

Why then is the image of business and managers so negative? Why are business leaders not seen as the true heroes of the post-war period?

The answer is clear: leaders – especially those in large corporations and the financial sector – have squandered the chance to be celebrated because of their arrogance, complacency and isolation from the communities that lie beyond their walls.

The push to “maximise shareholder value” started with a legitimate idea: the concept of “agency theory” as first articulated in the mid-1970s by Michael Jensen and William Meckling. But since then the pendulum has swung too far, pushing far too many executives to put a premium on short-term results over the long-term health of the enterprise.

Mounting pressure to “make the numbers” expected by Wall Street has led many corporations to engage in predatory behaviour, aggressive HR practices with knee-jerk restructurings and massive “downsizings” whenever clouds appear on the horizon and obscene remuneration policies among a self-serving cadre of management elites.

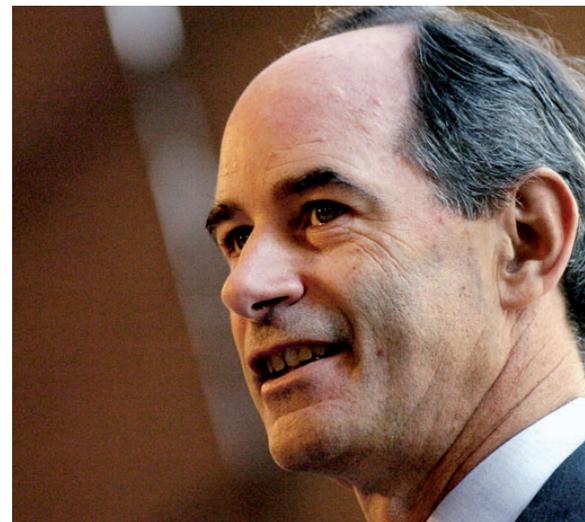
Roger L Martin, dean of the University of Toronto’s Rotman School of Management, has demonstrated how this shareholder-is-king mindset has diverted corporations from having a proper customer focus. All of these odious trends were apparent even before the financial crisis struck. CSR programmes have not helped, either. Many of these initiatives were based on a philosophy of business apologising for its success by “giving back” to society. Or worse, to divert attention from socially harmful practices.

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A critical turning point

The upshot is that despite the undeniable progress that capitalism has brought over the last 70 years, we find ourselves at a crossroads, a painful moment of truth. We need to reform capitalism as it is currently practised lest we see increasing calls to dismantle the system entirely.

The stakes are enormous. In the aftermath of the recent crises, we are confronted with an avalanche of challenges – a world population growing toward 9 billion by 2050; a fragile global financial system; an unresolved sovereign debt crisis, especially in Europe, exacerbated by a system of social protection that has become unsustainable due to the pressures of an aging population; and shortages of energy, food and water supplies in major parts of the world.

Yet, the biggest global dream at the moment is a “good” job as Jim Clifton,

CEO of Gallup, pointed out at a recent entrepreneurship conference. Given a deficit of 1.5 billion “good jobs” worldwide we can appreciate the magnitude of fulfilling that aspiration...

Each of these social challenges can be addressed only with an unprecedented

stream of innovations at all levels – products and services, business models and the practice of management itself.

Hence, the big question: can a better and stronger form of capitalism be realised? Can Capitalism 2.0 provide us with the means to create the economic foundation for a liveable world for all? And what would its underlying management model and management philosophy be?

The big levers for change

There is clear evidence that Management 1.0 with its pedigree in the industrial age will not be adequate to achieve the transformation. Hence the underlying model for Capitalism 2.0 has to be Management 2.0, based on the principles and values outlined below.

Which will be the key levers for change as we move toward a new and more effective form of capitalism and management?

First, myriad studies show that there is a huge pool of unused or underused human capacity in today’s organisations. Yet most companies do not organise work in a way that can unleash this latent energy. We need new ways of thinking. Lynda Gratton has demonstrated this in her research on “hotspots” and, more recently, in her book *The Shift: The Future of Work is Already Here*.

In the same vein, the late Peter Drucker challenged 21st-century managers to increase knowledge-work productivity to the same extent that their forebears increased the productivity of manual labour. Empowerment, autonomy and trust are essential ingredients to make knowledge work more productive – and to accelerate innovation.

Second, the entrepreneurial spirit needs to be awakened and fostered on a broad basis, within organisations and in our societies at large. Individuals must take their lives and their destinies into their own hands. And nation states have to create favourable conditions such as early education, tax incentives and the elimination of administrative hurdles.

Drucker called for us to create “the entrepreneurial society” some 30 years ago. Are we finally getting there? Sara Horowitz, the executive director of the Freelancers Union, notes that 30% of the American workforce is now employed as independent contractors. She calls this a “third industrial revolution.”



Clockwise from left:
Roger Martin
Gary Hamel
Peter Drucker
Linda Gratton

Entrepreneurialism is not confined to start-ups and new ventures. It is a key capability for all organisations, new or old, big or small. Along with entrepreneurship goes innovation. Open innovation, design thinking and frugal innovation are promising approaches to embed creative power at all levels of an organisation.

Next, a shift in values needs to take hold. Specifically, our leaders need to move from taking purely competitive stances to embracing collaboration. While competition is a major driver of efficiency in market-based economies, the potential for collaboration and mutual support in addressing key challenges is a way to increase the pie as opposed to competing for each little part of it.

A new sense of responsibility needs to be instilled on a global basis. While the challenges ahead are daunting, they have the potential to create meaning for all those engaging in economic and social activity. Establishing meaning and purpose needs to re-emerge as one of the foremost responsibilities of leadership. Simultaneously creating social and economic value should become the new standard for businesses around the globe.

Finally, the state must redefine itself in a fundamental way. In the Western world, government has evolved into a Leviathan suffocating initiative and siphoning too much financial capital from productive use. Even though many politicians are quick to point fingers at the bankers for the financial crisis, they clearly deserve some of the blame themselves for their lax oversight and the way that they have bought off voters with ever-increasing promises from election to election.

Translating all of this into action will be a tall order. There is, however, no choice. Achieving “betterness” in capitalism and management, as consultant Umair Haque calls it, is the ultimate test for human ingenuity and creativity.

Learning from alternative models

The good thing is that there are already many good alternative models to learn from and build upon. Largely unnoticed, numerous companies from the German *Mittelstand* (basically the SME sector) have survived and thrived for more than 100 years. And by achieving market leadership, they have created value and generated jobs around the world.

When it comes to solidarity and mutual support, co-operatives also boast a unique track record. Today more than 1 billion people are part of co-operatives, and the livelihoods of almost half of the world’s population are supported by such enterprises, according to the International Co-operative Alliance.

These organisations – including the Raiffeisen Banks and the Bank-Genossenschaften in Germany, Austria, Switzerland and the Netherlands – have not only made a mark with their contributions to the community they have also proven an ability to withstand crises in competitive markets better than many of their traditional capitalist counterparts.

These largely unnoticed organisations deserve special consideration during 2012, a year that the United Nations has designated as the International Year of Co-operatives. Are there not lessons to be learned from the success of this model for Capitalism 2.0 and Management 2.0?

For-profit businesses have developed alternative models, as well. There are, for example, more than 11,000 companies in America that are owned entirely or in significant part by their employees, some 13.6 million of them in total.

WL Gore, maker of Gore-Tex fabric and many other products, is a leading example. The company has some 9,000 employee-owners at 45 locations worldwide and generates annual sales of \$2.5 billion.

Graybar, a *Fortune 500* company, also has a long history of being fully employee-owned. Originally established in 1925 as part of Western Electric, it was purchased by the employees in 1929 for \$9 million. Today the \$5 billion company is one of North America’s largest employee-owned concerns, with 250 distribution centres throughout America, Canada, Mexico and Puerto Rico.

Partnerships also provide interesting clues about how to move forward. Mazars, which grew from a 50-person company after the second world war into a 13,000-employee global organisation, is an example of how value can be created using fundamentally different governance and management models based on democratic and co-operative principles.

Even though hierarchy is an inherent element at most companies, self-managed organisations offer yet another structure to consider.

Gary Hamel, for example, has written about Morning Star, a California-based tomato processing company with revenues of \$700 million and more than 400 employees. What makes the company so remarkable is that it has no bosses, titles or promotions. While the Morning Star model may not be universally applicable, it contains seeds that can be widely applied, especially when it comes to building a trust-based organisation with a truly empowered workforce.

Citizen Sector Organisations (CSOs), which include nonprofits and non-governmental organisations, also have much to teach the capitalist world. Drucker had a significant influence on the development of this sector with his book *Managing the Nonprofit Organization*.

Since the 1980s, the Citizen Sector has created jobs about three times as fast as other employers in the OECD. In Brazil, the number of CSOs has risen from about 36,000 to nearly 1 million



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over the past 20 years. Today, millions of these groups across the globe attract talented individuals who long for challenging and fulfilling work that is consistent with their personal values and goals. New hybrid value chains between CSOs and for-profit enterprises show that there are unconventional routes to address the immense social issues of today's world.

On a more fundamental level, there is a broader challenge to the Western capitalist model in the form of state capitalism as exercised in countries as different as China and Brazil. As *The Economist* outlined in its special report on the subject, this new model bears little resemblance to the disastrous spate of nationalisations in Britain and elsewhere half a century ago. China's infrastructure companies win contracts the world over.

The best national champions are outward-looking, acquiring skills by listing on foreign exchanges and taking over foreign companies. And governments are selective in their corporate holdings. Any meaningful discussion of Capitalism 2.0 needs to include an assessment of this phenomenon.

Bringing it all together

What we have here is a complex puzzle. Though a number of pieces are already in place, many more will have to be added during the coming years. Creating a new version of capitalism will require a concerted effort between all stakeholders and a great sense of urgency and responsibility.

The internet and social media can help. These tools provide all of us with a chance to share experiences, co-create ideas, learn collaboratively and innovate – and all much faster than in the past.

But in the end, it will be people, not technology, that make Capitalism 2.0 a reality. A new generation driven by passion, purpose and strong values is poised to engage for the greater good. Yet, managers, in particular must lead the way, moving beyond “business as usual” and “business as bystanders” toward the innovator and activist roles described by Joseph L Bower, Herman B Leonard and Lynn S Pain in their 2011 *Harvard Business Review* article “Global Capitalism at Risk: What Are You Doing About It?”

It is a fitting question on which to end:

What, in fact, are you doing about it? And what are you going to do tomorrow? **gf**

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MORE INFORMATION

Capitalism 2.0 – New Horizons for Managers will be the central theme of the 4th Global Peter Drucker Forum in Vienna on 15-16 November 2012

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