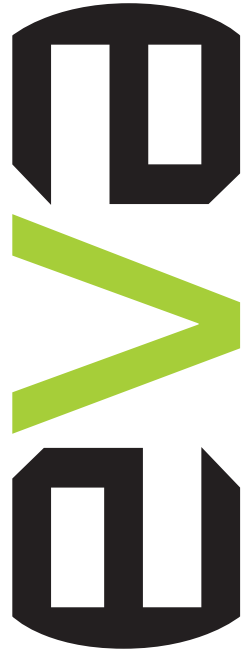


Paul Lillrank

# BACK TO BASICS

– *Why we need to revive  
the bourgeois enterprise*



## SUMMARY

In the aftermath of the financial crisis of 2008 free enterprise was once again seen as a failure. However, the current economic crisis makes it clear that Big Government is not the answer to our economic woes.

Professor Paul Lillrank argues that the answer is bourgeois enterprise, which is the best – and perhaps only – way to create sustainable growth. But in order to do that, the bourgeoisie must find its way back to the basic virtues of entrepreneurial capitalism: prudence, courage, hope and love.

The core strengths of bourgeois mentality are its central precepts of value creation, innovation, accumulation of material and intellectual capital, and a perception that man should get what he deserves through the appreciation given by others in the market.

Prof. Lillrank's advice for friends of entrepreneurial capitalism is: "Speak out." The bourgeois mentality needs to be represented and articulated better in the political debate. Currently the bourgeoisie is pitted against the rest in the struggle between different political mentalities.

Paul Lillrank is professor at the Department of Industrial Engineering and Management, School of Science, Aalto University, Finland and Chairman of the Nordic Healthcare Group Ltd.

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# 1. Introduction

In the 1970s university student scene in my country, becoming an entrepreneur was unthinkable. As employment for recent graduates was insecure, students demanded public action. An official within the Ministry of Education suggested that students might start their own businesses. The gentleman, who's surname in Finnish (Kurri) quite unfortunately means "skimmed milk", got ridiculed all over the media. Government or big business was the employment of choice. Entrepreneurship was perceived as sinful, not much better than organized crime.

Now the situation is different. Recently I interviewed a group of students at Aalto University for an exchange program. I used the opportunity to ask what they wanted to do after graduation. Two thirds said they could very well think of becoming entrepreneurs. Some even had ideas they were developing. Aalto University, with its Venture Garage and Venture Sauna has become a hub of entrepreneurs with Rovio

**If sustainable growth is expected, the bourgeoisie must find its way back to the basic virtues of entrepreneurial capitalism**

Entrepreneurs see opportunities, develop innovative solutions and take risks. Some of them fail. Others may thrive, some even excel.

But entrepreneurship also has a dark side of predation, rent-seeking, and recklessness<sup>1</sup>. It looms there like original sin. At times predation and excesses lead to speculative crashes. This explains, at least partly, why entrepreneurship was perceived as morally questionable in the 1970s.

The financial crisis of 2008 inspired many lefties to dust off their 1960s anti-capitalist rhetoric. Free enterprise was once again seen as a failure, because it could not provide uninterrupted increase in middle class living standards. Big Government was asked to clamp down. However, the current economic crisis makes it clear that that a government can behave as recklessly as any bank, and that regulation can create more problems than it solves. If sustainable growth is expected, structural reforms are needed to restrict the reach of governments, and the bourgeoisie must find its way back to the basic virtues of entrepreneurial capitalism, prudence, courage, hope and love. While these are accepted and embraced in some sectors of society,

Corp., the creator of Angry Birds, as the flagship. The mood has, indeed changed.

Entrepreneurship is the engine of wealth creation, the sunny side of capitalism.

in some others the anti-business mentality is still going strong. The purpose of this article is to shed light on that mentality, and discuss what capitalism might learn from its critics, even from its enemies.

## 2. The Concept of Mentality

Mentality here means deeply rooted patterns of thinking and action, shared mental models and intellectual operating systems.

Political mentalities have been described in different terms. Deirdre McCloskey<sup>2</sup> sees them as combinations of virtue that form the aristocrat, ascetic, peasant and bourgeois mentalities. David Priestland<sup>3</sup> uses the term "caste" for social groups as self-interested entities seeking economic advantage, and also as embodiments of ideas and life-styles, which they often seek to impose on others. The basic castes are merchant, soldier and sage.

Mentalities are not on-off, black-white, but distributed in various strengths and combinations like psychological traits. There are the hard cores at the extremes, but also large middle-of-the-road groups combining bits and pieces from here and there. As an operating system, mentalities represent conceptions of society, the moral universe, and sources of power. Different mentalities struggle for legitimacy, dignity, and freedom to pursue their objectives.

## 3. Political Mentalities

The foremost virtue of the **aristocrat** is courage, shown in war and tournaments. Heroic service on the fields of battle used to be rewarded by property. As generations passed, inheritance turned into entitlement and revenue without the owners having to get involved in labour, production or trade.

In the modern world the traditional aristocracy as a political force is next to extinct. But the aristocratic mentality lives on, taking new forms. An aristocratic position is inherited, or perceived as building on inherent capabilities that give the right to rule.

Like blue blood, ethnic membership can't be taken away. White supremacy and racism go naturally with the aristocratic mentality. In less extreme forms

**Aristocratically minded politicians and electorates fail to adjust to reality even when debts keep piling up**

it is present in the defenses against competition from emerging economies and immigrants. We can't compete on low wages, the argument goes; we are entitled to the high-paying, high-skilled jobs. The workers' aristocracy seeks to erect trade barriers; lift the drawbridge and protect the insiders with first-in-last-out rules. The young, the immigrants and the outsiders are all thrown in the moat.

The aristocracy has always sought to protect its dwindling fortunes by taking on debt to preserve a lifestyle assumed to be their birth right. Aristocratically minded politicians and electorates fail to adjust to reality even when debts keep piling up. The sovereign debt crisis is a crisis of a failing aristocratic mentality.

*The central precepts of the aristocratic mentality are power and entitlement.*

The primary virtue of the **ascetic** sage is temperance. The ability to restrain desires is proof of contact with the divine, or a superior insight into the workings of the universe. The ascetic comes basically in two shapes, the cleric and the clerk. While the aristocrat rules with the sword, the ascetic rules with the word.

### **The ascetic rules through administrative procedures**

The clerks in their service rule through administrative procedures.

When the ascetic allies fully with the aristocrat, totalitarian control of mind and body ensues. In less drastic forms the modern ascetic is the do-gooder one-upping the masses, the petty bureaucrat harassing entrepreneurs, the scientist predicting catastrophes, the politician claiming authority to manage happiness, and the social worker knowing exactly what constitutes a good life.

*The central precepts of the ascetic mind are sacrifice, knowledge, and rules.*

The **peasant**, as McCloskey uses the term, depicts the proletariat, the coolies and the workers who have only their labour to sell. Thus, the peasant is not to be confused with the freeholding farmers of the Nordic societies and the American frontier. In a stratified society where aristocrats effectively block social mobility and ascetics preach submission, the peasant gets it better by begging for mercy, by being humble and pitiful, never showing off any gains or rejoicing in betterments.

The peasant has no incentive to improve or innovate. The peasant owns little, if any capital and has little sense of property rights and the care of capital assets. He exploits the commons, and grabs what he can without responsibility or remorse, because the big decisions are made somewhere far above his pay grade.

The Industrial Revolution mightily improved the material position of the peasant. Machines do the heavy lifting. But the peasant mentality did not disappear. It migrated to the outskirts of society, to be held by a new underclass, those incapable of entering the mainstream through education or entrepreneurship.

While the bourgeois revolution diminished the ranks of the idle rich, the welfare society has created a new underclass of the idle poor.

Traditionally, peasants have rioted and slaves rebelled. The modern peasant mentality is expressed as populism, a political movement that rejects explicit ideology and claims the superiority of common sense. The left-wing populist peasant wants more handouts from the masters. The populist peasant of the right doesn't want to share the spoils of the national bourgeoisie with strangers. Both left- and right-wing populists rage against the machine that is not producing and sharing enough.

*The central precepts of the peasant mentality are pity, redistribution, fatalism in the face of the system, and irresponsible exploitation of the commons.*

Prudence together with hope and courage drive the **bourgeois** mentality. Through innovations in trade and industry, the bourgeois seeks to control his fate and establish prosperity. Prudently listen to the customers and respond to their needs. Conduct experiments and learn from mistakes.

The bourgeois mentality differs from the others principally in its conception of value. To the aristocrat, revenues flow by a divine, traditional, or enforced order. To the ascetic, market prices and speculation are abhorrent. To the peasant, production is of less interest than distribution of the gains. To the bourgeois, value is earned in economic exchanges. To get the buyer to voluntarily part with his money, you have offer something that is perceived as valuable.

### **The modern peasant mentality is expressed as populism**

### **The bourgeois gets what it deserves by creating value for customers, or failing to do so**

Businesses serve society by making goods and services available. Productivity is to achieve more with less. Prudence in business calls for sensitivity about value, both now and in the future. The bourgeois need to calculate and control the cost of production, estimate demand, and set prices properly. The bourgeois gets what it deserves by creating value for customers, or failing to do so.

With creation comes destruction. The automobile replaced the horse, and the PC drove the typewriter industry into the ground. Lacking vision and hope, the aristocrat mentality resists change and clings to the old. The ascetic, always wary of developments that could undermine their authority, is skeptical of everything new. Both aristocrats and ascetics approve of innovations only if they do not destroy anything.

*The central precepts of the bourgeois mentality are value creation, innovation, accumulation of material and intellectual capital, and a perception that man should get what he deserves through the appreciation given by others in the market.*

While most of the world has become, or is furiously becoming middle class, the bourgeois mentality is thinly represented and not well articulated. The aristocrats and ascetics, allegedly representing the peasant, dominate the chattering classes. The bourgeoisie has lost its confidence, not least because it has allowed itself to be influenced, even corrupted by the other mentalities.

### **The bourgeoisie has allowed itself to be corrupted by the other mentalities**

## **4. Corrupting Combinations**

**Aristocratic bourgeois:** The bourgeoisie is, and has always been, susceptible to the lure of the aristocracy. With it, achievement turns into entitlement and monopolies replace free competition. Crony capitalism has two key features: business activity loses any relation to, and often clashes with, the wider public interest; and business merit is separated from business reward.

When a bank, or any business, claims it is too big to fail, it exposes the aristocratic mentality, the modern equivalent of a position in society allowed by divine right. When executive pay loses all reasonable connections to profitable growth, new aristocratic entitlements are espoused. When risk takers claim the profits, but roll over losses to the taxpayer, the aristo-

cratic mentality has invaded the state and its economic policies. Turning into an aristocracy, the bourgeois lose its virtues, and with them dignity and legitimacy. The new class has to retreat into walled communities. The anti-capitalist sentiments of the Occupy Wall Street movement are a rage against crony capitalism.

**Aristocratic ascetics:** Originally, the ascetic was a man of letters rather than deeds. An ascetic could turn to bourgeois enterprise by establishing charities that do not turn a profit. Saving the world one child at a time, however, is tedious to the aspiring ascetic. The state gives easier access to the levers of power. Ascetics can get hold of them by lending their power over the ignorant masses to the service of the state aristocracy. Throughout history, the wrath of divine beings, the inevitable course of history, the forces of nature, or the rampancy of killer viruses have been able to stir electorates, and prompt politicians to make funds available to the ascetic's pursuit of power and dignity. The modern aristocratic ascetic is busy harnessing government powers to engineer happiness to the masses.

**Aristocratic peasants:** Handouts, rather than own effort, determine the peasant's position in life. In a welfare society, individual masters are replaced by an impersonal system. The connection between effort and reward that was never strong anyway weakens still further. Disappointed with its share, the peasant feels resentment, a lingering feeling of injustice. If the society would be "just" – whatever that means – everybody, except the richest one per cent, would be better off.

Equality of opportunity has not succeeded in creating an equal and enlightened society. The task of managing the remaining peasants was left to the clerks. Many of them have adopted a peasant mentality. Tax revenue equals the commons that are there to be exploited, with no sense of the responsibility that goes with ownership. The peasant asks to be pitied; welfare recipients can't gratefully count their blessings, and never admit any betterment. The peasant mentality can't comprehend the idea of progress through productivity. The worse the outcome, the more resources can be claimed. Public services managed by the peasant mentality never improve. The aristocratic peasant claims entitlement to a standard of living, even if the money needs to be borrowed.

### **The peasant mentality can't comprehend the idea of progress through productivity**

## 5. The Bourgeois and the Rest

In the struggle between mentalities, the bourgeoisie is pitted against the rest. The dividing line is prudence, the conception that value needs to be painstakingly created, that consumption needs to be preceded by production, that innovation can't be implemented without pain, and that the appreciation of others in a free market should determine who deserves what.

Politically the bourgeoisie is represented by classical liberalism and market conservatism. Its opponents on the right are the new aristocracy of crony capitalists drawing shame on the bourgeois enterprise. On the left, there are the resentful aristocrats demanding entitlements, the ascetics peddling decline, and the pitiful peasants asking for the right to exploit the

**Bourgeois enterprise, when it goes back to the basics, can succeed where others have failed**

commons. They depict the bourgeoisie as driven by simple self-interest, while the aristocrat and the ascetic see themselves as the proper guardians of the welfare of the peasant,

and as the solution to global problems. Essential welfare and educational services for the poor can only be financed through taxes collected by the aristocrat, defined and rationed by the ascetic and produced by the clerks.

The bourgeois can point to the innumerable failures of state aristocracy, the undisputable shortcomings of ascetic do-goodery, and the futility of peasant rebellions. The main argument, however, is to show how bourgeois enterprise, when it goes back to the basics, can succeed where others have failed. The revival of entrepreneurial capitalism gains credibility from the emergence of the Fourth Sector in India and other developing countries.

## 6. The Fourth Sector – Revival of the Bourgeois Mentality

In developing economies where aid has failed to deliver development, and the public sector is incapable of organizing efficiently, entrepreneurs take matters in their own hands. As Christopher Meyer has argued, a new form of mixed-value capitalism is emerging<sup>4</sup>.

The First Sector is ordinary for-profit business, the Second is central and local government, the Third is charity. The Fourth is a hybrid of the First and the Third. It tends to steer clear from government money and influence. In India, these entrepreneurs are driv-

en by charitable visions, such as reducing unnecessary blindness (Aravind), selling reading glasses for three dollars (Scojo Vision), or providing affordable cardiac care to the masses (Narayana Hrudayalaya). They do not think of the poor as peasants, empty vessels into which welfare can be poured, but as active customers who know the value of money and of the services they need.

These ventures are organized as companies with profit and loss statements and balance sheets, managerial accounting and operations management. They may accept charitable donations, but do not want to depend on them. Rather they charge for their services according to capability to pay – progressive pricing – and offer services to the very poor for free. They use the ordinary channels of corporate finance, for which they need to prove they are viable businesses. The following anecdote illustrates the differences between the sectors.

**The Fourth sector is a hybrid of the First and the Third**

Once upon a time in far-away India there was a smart consultant working with hospitals. He had developed a process analysis and improvement method with great potential. One day he went to make his pitch to the directors of four different hospitals.

- Dear Director. With my method and my help, you can cut one million of your costs, while improving quality and patient satisfaction. For my services I charge one hundred thousand, half now and half when the results are confirmed.

The director of the First Sector private for-profit hospital eyed the consultant with interest. He did some quick calculations on his smartphone.

- Well, sounds like a decent deal to me. When can you get started?

The consultant went to work, delivered the results and collected his pay. At the end of the fiscal year the hospital management's bonus pool was fattened by nine hundred thousands.

The director of the Second Sector public hospital looked at the consultant suspiciously.

- I do not understand what you are talking about. Why should we want to cut a million from our costs? Don't you see, we are already lacking resources. We would rather want you to help us get us a million more in government funding. Go away!

The director of the Third Sector charity hospital looked at the consultant with her watery eyes.

- Young man. You understand, we are a charitable institution. We are here to help sick people in need. We are not concerned with our costs. We use everything we can get in charitable contributions. If you work for us pro bono, we can offer you vegetarian meals in our canteen and a cot in our dorm.

The consultant had a housing loan and four small children, so he politely declined.

The director of the Fourth Sector hospital listened attentively to the consultant. He asked a few questions, pulled out an Excel spreadsheet and made some quick calculations.

- Very well. Please get started as soon as possible with our surgical department. If you are successful, you can have the same deal with internal medicine.

The consultant rolled up his sleeves and in due course delivered the results. At the end of the fiscal year, the hospital announced it would cut its prices and expand its capacity.

The Fourth Sector entrepreneurs reject the aristocratic-ascetic top-down, do-good mentality and employ the tools of the bourgeois to help the poor. They do market research, listen to customers, work hard to

understand how value is co-created in producer-customer interactions.

Socially minded enterprises are ac-

countable first and foremost to the customers who define their revenue stream, not to absent charitable donors. To fulfill their missions they need to expand and grow, therefore they need to control costs and show profit.

In the developing world the Fourth Sector creates innovative business models. In the developed world, Social entrepreneurship takes back welfare services from the aristocrat-ascetic. In the U.K. Social Impact Bonds (SBI) have been devised as a financial instrument connecting venture capital with social goals. Investors buy bonds that are used to design and deliver a service, such as rehabilitation of young criminal offenders, by employing best-known practices. If the effort is successful by pre-defined outcome criteria, they will earn a profit; if not, they will take a loss.

In Finland public primary care is mired with long waiting lines and poor service. Consequently several entrepreneurs see opportunities to develop innovative solutions, such as high-volume, low cost, rapid access

dental care (Megaklinikka), family doctors on wheels (Doctagon), or outcome-based occupational health-care (Hoffinanco).

The collapse of the Soviet economic model made it clear, that the public sector is not suited to the production of goods. Services are no different. In public organizations the aristocratic mentality demands that employees are entitled to their positions, no matter what they produce to the people. The ascetic mentality insists that the provider knows what is good, and people cannot be allowed to choose.

Even allowing for the argument, forcefully made by Amartya Sen, that access to education and health-care are basic capabilities that enable freedom and equality, the question remains, why do they have to be produced by public bureaucracies?

The bourgeois corporation emerged as an organizational solution to manage economic risk, capital accumulation, and efficient production. A governance structure based on shareholders, boards, and management needs to strike a balance between the claims of various stakeholders. Shareholders demand returns, but these will not materialize, unless customers are satisfied, competitors are kept at bay, and employees remain productive and motivated. The Fourth Sector demonstrates, how a better organizational architecture can replace a worse one and put the bourgeois mentality into the service of people.

## 7. Conclusion – Back to Basics

Capitalism is pragmatic and flexible. It learns from its critics and sometime absorbs them in its fold- for good or bad. The basic bourgeois mentality is based on the conception of value as determined in markets with free choice. Value creation requires prudence in production and concern for customers. Outcomes are more important than procedures. If you create value to your customers, they will reward you – and you earn it.

### Fourth Sector entrepreneurs employ the tools of the bourgeois to help the poor

## Endnotes

- <sup>1</sup> See Mulgan (2013).
- <sup>2</sup> See McCloskey (2006 and 2010).
- <sup>3</sup> See Priestland (2012).
- <sup>4</sup> See Meyer (2012).

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