



RECONSTRUCTING THE ECONOMY FOR THE 21ST CENTURY

Vision paper of the Impact Economy
Foundation

Impacteconomyfoundation.org

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Executive Summary

A sustainable and inclusive reconstruction of our economy is overdue

Many recognise the need to reconstruct the economy in a way that can bring prosperity to all, now and in the future, by simultaneously generating material wealth and health while conserving nature. Until now, this reconstruction captured the need to transform the economy to address key long-term challenges – hunger, poverty, inequality – and avert long-term crises – e.g. climate change and biodiversity loss.

The COVID-19 pandemic forces us to reconstruct a resilient economy, now

Before COVID-19, reconstruction was important and urgent but still optional. The COVID-19 pandemic, however, has left the economy so damaged that it needs to be reconstructed with massive governmental intervention. In addition, it demonstrated the need for an economy that is much more resilient in the face of the accumulating crises we already face and the new challenges the 21st century will bring.

We need to create a resilient, sustainable and inclusive economy

The problem is that we have no viable alternative for the current system. The question is thus: how can we create a resilient, sustainable and inclusive economy? We believe the answer lies in realising an impact economy, a market economy revolving around the common good.

The problem of the current economy is that it ignores the common good

A troubling pattern of the current economic system is that it is generating problems instead of solutions. The reason is simply that it does well at what it is designed to do: maximising short-term profit and financial returns and satisfying the immediate needs of consumers. The global economy, by design, does not cater to the common good in terms of human well-being, fairness, the respect of rights and the preservation of nature.

Our current system persists as it has many attractive qualities and punishes those who deviate

Despite all these failings, our current economic system has brought prosperity to many, and there has been no better alternative. One has to recognise its attractive qualities: it has infused (specific kinds of) efficiency, rationality, entrepreneurship and meritocracy into the economic process. It is also persistent; it rewards those who adhere to the pursuit of self-interest at the expense of the common good, while those who pursue the common good – be it individuals, governments or businesses – will be less successful.

The impact economy is a market economy revolving around the common good

An impact economy is a market economy that provides the values, information and incentives that optimise the common good and enables people to pursue their own preferences, ideas and projects to satisfy their needs while having a positive impact on society.

The impact economy can be effective in addressing the challenges of the 21st century

Because the current economy optimises productivity in terms of short-term financial gains, many resources (human, natural, financial) are used sub-optimally, or even counterproductively to welfare productivity (conceived as the fulfilment of well-being, rights and fairness). In contrast, the impact economy can massively increase welfare productivity, which will greatly increase the resilience of our society. In short,



an impact economy harnesses the power of markets, entrepreneurship, innovation and technology for the common good.

The impact economy is feasible due to 21st century science and technology

Until recently, an impact economy would not have been feasible, as it requires providing market players with information about their impact on society. Recently, though, modern data collection, computing and information transmission technologies and scientific progress on measuring impact have made this possible.

The impact economy can successfully spread, as it already has deep roots

First, the impact economy has deep roots in human nature. The majority of people combine self-oriented preferences with prosocial preferences. Second, the impact economy has deep roots in economic practice. Throughout history there have been many examples of people and communities engaging in economic behaviour based on reciprocity, trust and professional purpose. Third, people are increasingly finding ways to use market mechanisms to realise positive impact.

Pockets of the impact economy already exist

A fast rising number of social enterprises are using business models to promote the common good. Similarly, there is a growing group of impact investors that aim to use their money for the good of society by investing in social enterprises and other initiatives that both create a positive return to society and a financial return to the investors. On the other hand, businesses traditionally aimed at profit seeking are also increasingly paying attention to their impact on society.

Existing movements can grow into an impact economy with the right support

The challenge is how to upscale existing practices and movements to a systemic level. This is a multi-dimensional, multi-stakeholder effort to induce a co-evolution of regulation, business practices, investor practices, consumer behaviour, reporting practices, professional and academic training and technology towards the impact economy.

Effectuating the impact economy starts with the human and intellectual foundations

To realise the impact economy, we need to broaden the group of businesses that aim to realise impact and deepen the integration of impact into businesses. This requires developing enabling practices:

- A culture that provides shared purpose and values of an impact economy
- A cohesive architecture for the impact economy
- Universal and standardised measurement, valuation and reporting of impact
- Availability of high quality, and preferably, real-time information and data on impact at low cost
- Government regulation and policies that require transparency and incentivise positive impact

Let us come out of the COVID-19 tragedy wiser and stronger

The COVID-19 pandemic is a human tragedy in terms of lives diminished, destroyed and lost that nobody has wanted. Given that it has happened, though, we should use this window for change to rise from the ashes wiser and stronger, as a phoenix. We invite you to join us in building an impact economy.

Reconstructing the

economy

for the

21st century

How can we create a resilient, sustainable and inclusive economy?

A sustainable and inclusive reconstruction of our economy is overdue

Many recognise the need to reconstruct the economy in a way that can bring prosperity to all, now and in the future, by simultaneously generating material wealth. In the past decades, our economic system has already generated several major short-term and long-term global crises. An acute short-term example is the financial crisis of 2007-08. Crises that can pose great long-term damage include our fossil fuel dependency leading to a climate crisis threatening inhabitability of the planet, our encroachment of natural habitats causing a biodiversity crisis by bringing a million species to the brink of extinction, an unequal accumulation of capital resulting in an inequality crisis and a tragic twin health crisis of lifestyle diseases due to overconsumption in developed countries and undernutrition in developing countries.

The COVID-19 pandemic forces us to reconstruct a resilient economy, now

If the above crises were not enough, the COVID-19 pandemic has created the largest public health crisis in a generation and the largest economic crisis in a century: UNDP calls the COVID-19 pandemic the “greatest challenge we have faced since World War Two.”¹

Before COVID-19, reconstruction was important and urgent but still optional. The COVID-19 pandemic has left the economy so damaged that it needs to be reconstructed with massive government intervention. In addition, it shows the need for an economy that is much more resilient, in the face of the accumulating known crises and the new challenges the 21st century will bring.

We need to create a resilient, sustainable and inclusive economy

The problem for those convinced of the urgent need for change is that we have no viable alternative for the current system. To date, despite many efforts, no feasible alternative to the current self-interest market system has emerged, with governments shaving off the roughest edges and acting as safety net.

This means we should push ourselves and address the difficult question heads on: how can we create a resilient, sustainable and inclusive economy?

The Impact Economy Foundation believes the answer lies in constructing an impact economy, a market economy that provides the values, information and incentives that optimise the common good and enable people to pursue their own needs, ideas and projects. An Impact Economy provides freedom to its participants, individuals and organisations alike, but also requires an active role for governments to set the rules of the game in such a manner that they promote the common good. The realisation of the impact economy was a great opportunity before the COVID-19 emerged and has now arguably become a hard necessity.

¹ <https://www.undp.org/content/undp/en/home/coronavirus.html>

What is the problem?

The problem of the current economy is that it ignores the common good

A troubling pattern of the current economic system is that it is generating many crises and fails to solve crises, endogenous or exogenous. The past 50 years it has generated climate, biodiversity, financial, health and overconsumption crises. Either governments come to the rescue and pay the bill – such as in the case of financial crises – or they fail and the challenge remains unresolved – such as in the case of the climate crisis. Although one could argue the degree to which COVID-19 is a result of our economy, it is clear that the economic system has been unable to weather this shock.

The fact is that the global economy is not fit for the 21st century - by design. It does well what it is designed to do: maximise short-term profit and financial returns for capital providers and the satisfaction of the immediate needs of consumers with a purse. It is unsurprisingly abysmal at preventing or solving societal problems, as it has never been designed to do so. This is a problem, as the 21st century will see many new challenges due to unprecedented technological, economic and social change.

The global economy, by design, does not cater to the common good in terms of human well-being, fairness and the respect of rights or the preservation of nature – except if they coincide with self-interest. This leads to so-called negative and positive externalities: effects on society that are not priced and thus ignored by the market. Businesses and consumers lack both the information and incentives to prevent societal problems, as these are negative externalities: the costs are not reflected in the prices or profits of those causing them. A business does not pay, for example, for the biodiversity loss, inequality or zoonoses risk it creates. From a social perspective, this has led to a culture where businesses and consumers do not know about nor assume responsibility for such ‘externalities’.

Similarly, businesses lack the information and incentives to develop solutions to collective societal problems, as these are positive externalities (public goods). There is no incentive to invest in medicines that can cure lots of people but are not, or not very, profitable. There is hardly a business case for products that cater to the ‘bottom of the pyramid’.

Governments have – to varying degrees – shaven off some of the roughest edges of the self-interest economy, but its core ideal stands.

Our current system persists, as it has many attractive qualities and punishes deviations

Despite all of these failings, however, our economic system has brought prosperity to many and there has been no better alternative. To understand how to change, one needs to understand and appreciate its many attractive qualities. For starters, it is very efficient, as it brings a rationality to allocating resources throughout the economy. In addition, it promotes a certain kind of freedom: consumers and businesses are provided few restrictions in what to do. Third, it enables entrepreneurship and competition, which lead to



innovation and efficiency. Also important is that – at least in some ways – it is meritocratic: wealth depends on your success in the marketplace and not on social position.

In addition to its attractive qualities, it is successful because it resonates with one universal, cross-cultural human instinct: self-interest. Various cultures can adapt the system, but at a basic level, people find it natural to understand the expectations and norms of the system. A key reason it persists is that it benefits those who adhere to it and punishes those who deviate. Those agents (be it individuals, enterprises or countries) who pursue their own interest within the system will be more successful than those who try to pursue the common interest.

Finally, it is a coordinated system made out of intellectual, ethical, cultural, economic, business, professional and political aspects. Each part of society plays its role and there is (also cross-border) consensus on how markets should work.

Hence, it is not surprising that the many justified critiques of the current system have not yielded an alternative. Such an alternative must be better, viable, and systematic. Often proposals to change the system are inefficient (such as blunt government intervention) or assume unrealistic human behaviour (such as the self-sacrificial ‘consume less’). Other times, the proposals for change are good in themselves, but cover only a specific part – better values, climate policy, tax, ‘culture’, greed, short-termism. These changes often will not be successful as they do not fit in with the wider system.

The impact economy can harness the power of markets for good

The impact economy is a market economy revolving around the common good

An impact economy is a market economy that provides the values, information and incentives that optimise the common good and enables people to pursue their own preferences, ideas and projects to satisfy their needs and have a positive impact on society.

For starters, the impact economy is geared towards optimising the common good. This common good consists of dimensions of well-being, fairness and a respect of rights. Optimising this common good requires conserving and increasing various capitals: human capital (e.g. health and productivity), intellectual capital (e.g. knowledge and data), social capital (e.g. trust and rules) and natural capital (e.g. climate, forests and fertile soils).

The impact economy provides information and incentives that promotes and enables market players to optimise long-term value creation for society. Currently, companies are rewarded for the short-term profits they create for shareholders, and virtually all information about the economy concerns prices and profits. In an impact economy, businesses will publish impact statements showing not only the financial value they create for shareholders, but the natural, social and human value they create or diminish for all stakeholders in society. Similarly, consumers in an impact economy will see the true price of products, the price including all external costs. Information is a necessary but not sufficient condition for an impact economy; to optimise the allocation of resources, it should also pay to do the good thing. Businesses that create more

good should pay less taxes than those who create less good. Products that create risks for the environment or health should be more expensive than those without such risks.

An Impact Economy provides freedom to its participants, individuals and organisations alike, but requires an active role for governments to set the rules of the game in such a manner that they promote the common good. In addition, as is the case in current economies, an impact economy will consist of a private sector and a public sector, with different countries opting for different boundaries between the two. Organisations in the public or semi-public sector, such as municipalities, public schools or public hospitals, can benefit as much from the information and incentives provided by an impact economy as organisations in the private sector.

An impact economy also requires a culture that provides professionals, consumers and policy makers with a shared purpose, understanding and competence for creating positive impact.

Finally, the impact economy is a market economy. It harnesses the effectiveness and efficiency of markets, entrepreneurship and competition. In addition, it gives individuals and organisations the freedom to pursue their own ideas and projects. The underlying value system is that the economy expects participants to simultaneously satisfy their own needs and have a positive impact on society. All enterprises are social enterprises and all investors are impact investors.

The impact economy can be effective in addressing the challenges of the 21st century

The impact economy can massively increase productivity, fairness and resilience, by increasing welfare productivity (conceived as the fulfilment of well-being, rights and fairness). Currently, lots of financial, human and natural capital is employed to efforts that create little to no value to society. All the billions or trillions invested in tech have arguably led to quite little progress in terms of human life quality. In the impact economy, critical resources, such as talent and money, will go into those areas that actually create value to society and reduce inequality.

An impact economy will also greatly increase the resilience of the economic system. First, activities that create risks, such as food systems that create the risk for animal diseases or obesity, will be less profitable than those that prevent such risks. Second, by focusing on long-term value, businesses will take the longer view and invest in long-term resilient supply chains and building reserves that optimise long-term value instead of maximising short-term profits. Finally, by creating information, competences and expectation about societal value creation by businesses, an impact economy enables businesses and professionals to find solutions and innovations to societal problems much quicker. In short, an impact economy harnesses the power of markets, entrepreneurship, innovation and technology for the common good.

The impact economy is feasible due to 21st century science and technology

Until recently, an impact economy would not have been feasible as it requires providing market players with information about their impact on society. The technology, data infrastructure and science to gather



the data, compute the impact and communicate the impact were not yet available. Due to modern data collection, computing and information transmission technologies and scientific progress on measuring environmental and social impact, however, this has become possible. Although impact measurement and valuation is a young science, and there are currently no standards, it is technologically feasible.

The impact economy can successfully spread as it already has deep roots

First, the impact economy has deep roots in human nature. Although a vast majority of people have selfish instincts, scientific research has shown that the majority of people actually combine selfish preferences with prosocial preferences. Only a minority of people act wholly on the basis of selfishness. Hence, the dual nature of the impact economy – focused on realising the needs of the self and of society – aligns much better with the preferences of most people than the self-interest economy.

Second, the impact economy has deep roots in economic practice. Throughout history there are many examples of business activities primarily focused on self-interest. But there have also been many examples of people and communities engaging in pro-social economic behaviour: business and trade activities based on reciprocity, trust and professional purpose. The rationalisation and globalisation of markets has magnified the various aspects of human economic behaviour. Arguably, in the last century it mainly magnified the selfish impulses of people by enabling and stimulating profit-seeking and consumption.

Third, the impact economy has strong roots in recent progressive business movements. This century, people are increasingly finding ways to use market mechanisms to magnify prosocial human tendencies. Whereas Corporate Social Responsibility in the 20th century was arguably also an effort by smart companies to prevent government intervention and boost their reputation, the first two decades of 21st century has seen genuine and fresh ideas to employ markets for good: sustainable business, impact investing, social entrepreneurship, shared value, stakeholder value creation, etc. These ideas draw on normative foundations in the UN Declaration of Human Rights, the UN Sustainable Development Goals and intellectual foundations of broad welfare notions, translating them into business practices.

Initiating the impact economy requires growing a system around diverse movements around positive business impact

Pockets of the impact economy already exist

A fast rising number of social enterprises are using business models to promote the common good. For example, the highly successful US outdoor apparel brand Patagonia strives to minimise the production of new clothes and uses its profits to conserve nature. The Dutch Chocolate brand Tony's Chocolonely aims to eradicate slave labour and poverty from the cocoa industry by producing sustainable chocolate.

Similarly, there is a growing group of impact investors that aim to use their money for the good of society by investing in social enterprises and other initiatives that both create a positive return to society and a

financial return to investors. It is estimated that the amount of impact investing will reach 300 billion USD in 2020.²

On the other hand, businesses traditionally aimed at profit seeking are also increasingly paying attention to their impact on society. The share of S&P 500 companies that published sustainability or corporate responsibility reports rose from 20% in 2011 to 86% in 2018.³ A large number of institutional investors in Europe and North America also now apply some form of environmental, social and governance (ESG) criteria.⁴

Existing movements can grow into an impact economy with the right support

The challenge is how to upscale existing practices and movements to a systemic level. To realise the impact economy, we need to *broaden* the group of businesses that aim to realise impact and *deepen* the integration of impact into businesses. This requires developing the soft and hard institutions that enable market players to optimise their societal impact.

This is a multi-dimensional, multi-stakeholder effort to induce a co-evolution of business practices, investor practices, consumer behaviour, regulation, reporting practices professional and academic training and technology towards the impact economy. Various components are needed:

- A culture that provides shared purpose and values of an impact economy, an economy that enables its participants to fulfil their own needs while contributing to the common good.
- A cohesive architecture for the impact economy that provides the information *and* incentives that enable the optimisation of impact and rewards creation of value to society, ensuring the integrity of the system
- Universal and standardised measurement, valuation and reporting of impact: each organisation in the impact economy should report impact statements alongside their financial statements
- Availability of high quality and, preferably, real-time information and data on impact at low cost, enabling meaningful and effective steering and reporting on impact
- Government incentives and policies that promote transparency and positive impact

² McKinsey. (2018, February). A closer look at impact investing. Retrieved from: <https://www.mckinsey.com/industries/privateequity-and-principal-investors/our-insights/a-closer-look-at-impact-investing>

³ GAI. (2019). Flash report: 86% of S&P 500 Index[®] Companies Publish Sustainability Reports in 2018. Retrieved at: <https://www.gai-institute.com/press-releases/article/flash-report-86-of-sp-500-indexR-companies-publish-sustainability-responsibility-reports-in-20.html>

⁴ Connaker, A., & Madsbjerg, S. (2019, 17 January). The state of socially responsible reporting. Harvard Business Review. Retrieved from: <https://hbr.org/2019/01/the-state-of-socially-responsible-investing>



Effectuating the impact economy starts with laying down the human and intellectual foundations

We believe kick-starting the impact economy requires five main activities:

1. Creating a community of impact professionals who can work on the building blocks, standards, and competences needed to construct the impact economy.
2. Designing the impact economy to provide the cohesive vision and architecture required to start building.
3. Developing concrete regulatory and policy proposals for the impact economy, enabling policy makers and businesses to start building the impact economy.
4. Standard incubation for impact and impact statements to realise reliable, available and universally standardised data on impact.
5. Creating the new professional identity and corresponding professional standards required for people working in, and towards, the impact economy.

Let us come out of the COVID-19 tragedy wiser and stronger

The COVID-19 pandemic is a human tragedy in terms of lives diminished, destroyed and lost. Nobody wanted this. Given that it has happened, though, we should use this window for change to rise from the ashes wiser and stronger, as a phoenix. Let us put aside all the reasons why it cannot happen. We invite you to start with the hard but rewarding work of building an impact economy.



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