

Academics should be feeling pretty pleased with this debate, regardless of the stance which they take. Men who have made stupendous amounts of money seem to really, really want to be remembered for the profundity of their thoughts rather than their mere financial success. Mr Gates, with his concept of creative capitalism, joins Mr Soros with his invention of 'reflexivity'.

They both appear to subscribe to Keynes' famous aphorism "The ideas of economists and political philosophers, both when they are right and when they are wrong, are more powerful than is commonly understood. Indeed the world is ruled by little else. Practical men, who believe themselves to be quite exempt from any intellectual influence, are usually the slaves of some defunct economist". So the way to be remembered is to have a Great Idea.

Mr Gates' idea stands up rather better than that of Mr. Soros. Indeed, we can see reflections of it in Keynes' 1933 remark that "The decadent international but individualistic capitalism in the hands of which we found ourselves after the war is not a success. It is not intelligent. It is not beautiful. It is not just. It is not virtuous."

Capitalism faces a similar problem of legitimacy now, and it is this which I believe Mr. Gates is attempting to address. When Keynes wrote, output in America had just fallen by 30 per cent. There were millions of unemployed living at near-starvation levels in the richest country in the world. We have moved on enormously since then. The cornucopia which capitalism was to unleash in the second half of the 20th century seemed barely conceivable.

But there are profound – and perfectly reasonable – misgivings about the reward structure of contemporary capitalism. Financial capital has created a crisis, and no-one, least of all the bankers themselves, knows how deep this will prove to be.

Yet the risk/reward structure in the industry has been wholly asymmetrical. The expensive Mayfair and Central Park apartments, the country seats in the Cotswolds, the mansions in the Hamptons, these will still belong to the bankers, even if they are made unemployed. The problem is that millions of others might be as well. In any event, the re-building of banks' balance sheets can only take place at the expense of the personal sector. Everyone else pays for the bankers' mistakes.

This would not really matter if there were not, exactly as in the 1930s, a much more sinister rival political and economic system on offer to the developing nations of the world. As we know, markets and democracy are much better at delivering prosperity – in its widest sense - than central planning and authoritarianism. But it did not seem like that in the 1930s, when the seeming success of the Soviet Union contrasted with the apparent decadence of capitalism. Now, we have as the main rival to America for global hegemony China, controlled by a regime which has slaughtered, by various means, the best part of 100 million of its own citizens.

Mr Gates is really calling for a general re-evaluation of the ethics of business, of which he gives a specific example. It is not true to say that, if this were to happen in some way, capitalism and the workings of markets would automatically be compromised and impeded. Scarcely a market in the history of the world has operated in line with the paradigm of unconstrained profit maximisation.

I think it is quite unfair for William Easterly to dismiss this idea in the phrase ‘Moral exhortation has a very limited effect on most people’s behaviour’. In the example he gives, of \$4 gas prices, he is correct. But the moral code of capitalism’s elite is not exactly subject to the same set of simple incentives.

Our knowledge of how behaviour and attitudes either spread or are contained across networks has increased enormously in the past decade. In terms of the demand for gas, in the short-run we might reasonably ignore the potential effects of such social interaction. Individual tastes and preferences can be assumed fixed, so in general an increase in price will reduce demand.

But in markets where social interaction is important, where tastes and preferences can be altered directly by the behaviour of others, such impacts can swamp the immediate impact of monetary incentives. So, for example, the more CEOs who reject huge contractual bonuses when their company underperforms – which Willie Walsh at British Airways has just done – the more likely it is that others will follow the example. It is not guaranteed, but it becomes more likely.

Of course, we know that these types of networks tend to be robust but fragile. ‘Robust’ in the sense that the prevailing attitudes and behaviour on them are in general robust with respect to small disturbances. Disturbances such as BA’s CEO rejecting his bonus, or Bill Gates calling for creative capitalism, each have only a small chance of spreading across the system. But these systems are ‘fragile’ in the sense that every so often, an event, which need be no different in magnitude than any other, *will* percolate widely across the system.

Economists’ understanding of how social norms and ethics evolve is highly imperfect. But in the real world these are of great practical importance. Mr Gates’ perception is that a change in attitude *is* needed amongst Western business leaders. He believes this would speed up economic development. But it is even more important in order to continue to secure the allegiance of non-Western nations not just to the idea of markets and capitalism, but to the political system of liberal democracy.

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