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Research Paper

Profit and Public Value: A Welfare Comparison of Enterprise Models

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Abstract:
This paper investigates the behavioural incentives and societal outcomes associated with private, public, and charitable enterprises, assessing their relative performance through the lens of Total Economic Welfare. Drawing on theoretical models and empirical illustrations—such as the privatization of British Telecom and public sector inefficiencies in energy and health—the analysis challenges common scepticism toward profit motives. It argues that market competition and the pursuit of profit can drive innovation, efficiency, and consumer surplus, while state-owned and charitable organizations, despite benevolent aims, often suffer from inefficiencies, accountability deficits, and limited scalability. The paper concludes that private enterprises, when properly regulated, produce the highest overall welfare for society by aligning incentives with performance and value creation.

Keywords:
Profit Motive, State-Owned Enterprises, Total Economic Welfare, Consumer Surplus, Public versus Private Ownership, Market Efficiency, Charitable Organizations, Economic Incentives

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In the aftermath of World War II, the United Kingdom embarked on an ambitious experiment: it nationalized vast swathes of its economy—coal, steel, railways, telecommunications[1]—placing them under government control with the dream of fairness, equality, and public welfare.[2] Enterprises like British Rail and British Telecom were driven not by profit but by a sense of national duty.[3] While this holds a hopeful aspiration, it also reveals a deep-seated societal distrust of profit-driven motives.

The pursuit of profit[4] is central to private enterprise, but what behaviours does it unleash? Rephrased:
What actions must private firms take to maximise profits?

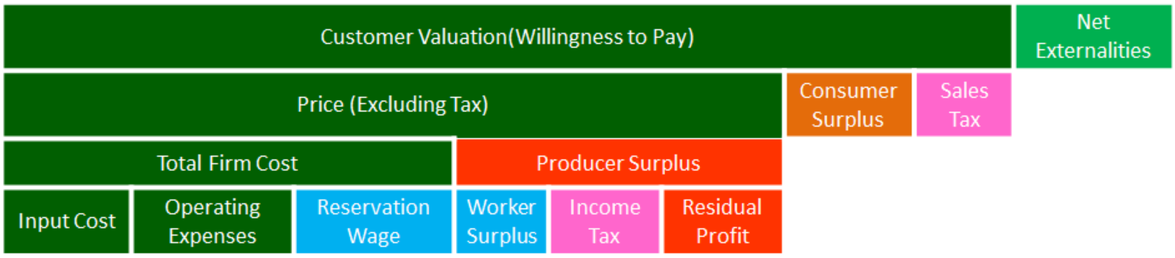
By definition, profit is the residual between selling price and total cost.[5] In its most basic formulation, a firm seeking to increase profit may choose to:

- Raise prices—causing consumers to pay more.
- Reduce total costs—potentially encouraging unethical practices such as cutting corners, underpaying employees, or tax evasion.

Such concerns have significantly contributed to scepticism surrounding profit motives.[6] While it is undeniable that some firms engage in harmful or exploitative behaviour, these cases should not be seen as representative of the whole sector. In many instances, such fears are overstated, failing to account for a fundamental market reality: to survive, businesses must compete.

To avoid confusion between performance-based incentives and corporate income tax, the concept of "profit maximization" will be expressed as "producer surplus maximization" using the following model.[7]

Figure 1: Constitution of Profit



First, in a competitive market, firms cannot arbitrarily raise prices.[8] For homogeneous goods, prices are determined by market equilibrium; [9] for differentiated products, firms may attempt to charge above-average prices, but only insofar as they do not erode consumer surplus. Marketing theory introduces a concept nearly equivalent to consumer surplus—Customer Delivered Value (CDV)[10], which largely determines a firm's competitive strength. To remain viable, a firm's CDV must not fall below that of its competitors.[11] Since CDV is effectively constrained by market competition, a firm can only achieve price premiums by offering a higher customer valuation than its rivals. This necessitates constant adaptation to shifting consumer needs and discovery for unmet demand.

At a practical level, this is precisely what firms do: they identify and meet the needs of specific market segments. This generates a remarkable diversity of services: beyond barbershops, salons are tailored for women, children, and even pets. Some businesses provide pet boarding services, others specialize in dog walking.[12] Certain roles focus on elder care, such as assisting with bathing, while others serve newborns, including postpartum caregivers.[13] In recent years, occupations only imaginable in stories have emerged—sleep coaches,[14] wake-up assistants, conversation partners, naming consultants, and more.

Second, it is innovation and operational efficiency—not unethical practices—that provide firms with effective means of reducing total costs. Total costs consist of raw materials, labour, and other indirect expenses. The unit prices of raw materials and labour are primarily determined by market equilibrium. What firms can influence, however, is the number of materials and labour they consume, along with their indirect expenses. Cost advantages require efficiency gains driven by innovation and careful management.[15]

The variety and affordability of goods today are largely the result of ongoing technological and managerial innovation—much of it motivated by the pursuit of profit. James Watt's steam-engine scaled only when expanding colonial trade created paying customers;[16] Ford's moving assembly line[17] unlocked mass-market automobiles; and modern business-model shifts[18]—chain stores, mail-order catalogues, e-commerce, livestream retail—flourished because profit beckoned.

Conversely, unsustainable or exploitative practices are penalized by market competition. This includes the use of cheaper raw materials, misleading marketing, or reducing quality in ways that are not immediately visible to consumers. In the short term, such strategies may inflate profits. Yet, in competitive and transparent markets, these behaviours are difficult to sustain and will be eliminated.[19]

The above two aspects of analysis exemplify that while private enterprises are not selfless angels, market competition compels them "to do hard things well." As Bezos noted,[20] through investing heavily in technology, data mining, and AI, Amazon has revolutionized logistics and customer service.[21] Its obsession with customer satisfaction—manifested in faster deliveries, single-click ordering, and proactive refunds—has reshaped e-commerce globally. Behind the scenes, the firm's tireless efforts to reduce costs through utilising warehouse robots, route optimization,[22] and supplier negotiations[23] have improved productivity by leaps and bounds. While this has sparked debates about market and labour power, Amazon's behaviour reflects the underlying incentives of a profit system: satisfy customers, be efficient, and innovate constantly. The result is a high consumer surplus, high firm surplus, and wide access to affordable goods.

Distrust of merchants and profit-seeking behaviour has existed almost since the very birth of commerce. In China's two-thousand-year history, merchants were ranked at the bottom of the social hierarchy; [24] in Shakespeare's works, they are portrayed in an unflattering light.[25] Yet, the pursuit of profit by private enterprises is not a calamity. Without such profit-driven behaviour, we would return to a state of scarcity and monotony. It is this profit motive that sustains day-to-day functioning of the economy: people go to bed without worrying whether bread and milk will still be available the next morning or if an Uber arrives when needed.

The second question is this:
If enterprises were instead owned by governments or charitable organizations, could they perform better than profit-driven private firms?

Sceptics of private enterprises often call for greater government involvement in the provision of essential goods and services. This rationale has led to the creation of state-owned enterprises (SOEs) not only in socialist states like the former Soviet Union, China, and Vietnam but also in many developing countries and even advanced economies including the United Kingdom, France, and Japan. [26] Despite noble intentions, SOEs often underperform relative to their private counterparts.

One major reason is the multiplicity of goals they are expected to pursue: advancing public interest, meeting employee demands, and funding the state. This creates a classic "multiple principals, single agent" problem, as described in game theory.[27] The resulting goal conflict frequently leads to inefficiency and waste. When one agent is made responsible to many stakeholders with divergent priorities, accountability becomes diluted. State-owned enterprises are also prone to capture by vested interests. Rather than serving the broader public good, they often serve internal departments or affiliated political groups.[28]

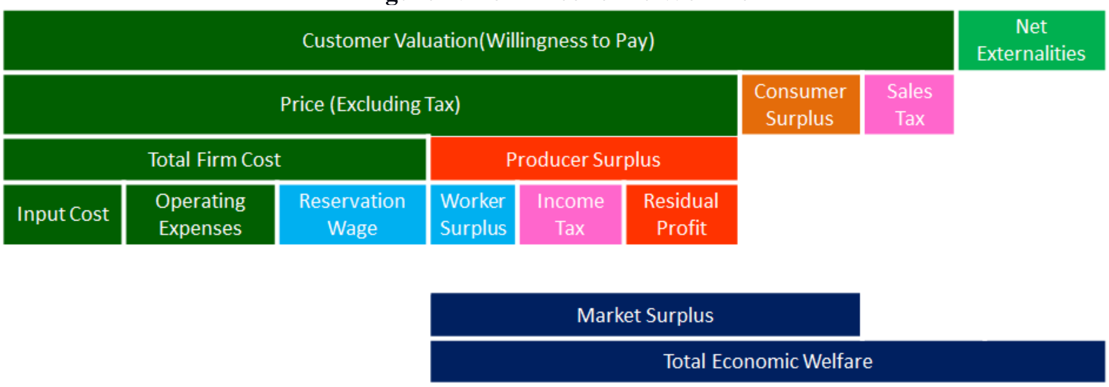
To further assess whether such performance is "better" or "worse," we need a single, unified standard of measurement. This essay utilises the "Total Economic Welfare" model as the primary criterion. "Better" behaviour is defined as that which results in higher Total Economic Welfare, and vice versa.

Total Economic Welfare is the sum of the following five components:

- Worker Surplus: returns delivered to human capital[29]
- Taxes: transferred financial contributions provided to society[30]
- Residual profits: returns delivered to investors[31]
- Consumer surplus: value created for consumers
- Net externalities: impacts on non-contractual third parties[32]

Together, these elements reflect the total value that a firm creates—or destroys—for society.

Figure 2: Total Economic Welfare



Without profit pressure and competitive forces, state-owned enterprises often struggle to pay close attention and effectively respond to customer needs.[33] As a result, customer valuation tends to be lower than that of private firms. Similarly, lacking sufficient incentives to conserve resources and improve efficiency, their raw material costs and overhead expenses are typically higher than those of private enterprises.[34] For example, under Tokyo's "Hydrogen Society" initiative, the average cost of constructing a hydrogen fuelling station was approximately ¥500 million (£ 2.55 million)—over five times the cost of a conventional petrol station. [35]

Since:
Total Economic Welfare = Customer Valuation – Total Firm Costs + Net Externalities,
a state-owned enterprise will inevitably generate lower total economic welfare than a private firm—unless it possesses a significant advantage in terms of net externalities. However, on externalities, government enterprises often face weaker soft constraints—such as media scrutiny, consumer pressure, or reputational risk—since these variables can be managed or influenced by the state itself.[36] In many economies, government-connected firms may also face looser regulatory oversight, such as exemptions from environmental regulations. For example, in China, the majority of state-owned enterprises have operated for years despite failing to meet national emissions

standards. Local governments, prioritising economic growth and employment, often delay enforcement or provide penalty protection, leading to persistent air and water pollution in industrial regions.[37]

Particularly, due to inefficiency and resource waste that weaken supply capacity, sectors controlled by government enterprises often breed shortages—harming consumer interests.

Figure 3: Market Equilibrium for Private and Public Enterprises

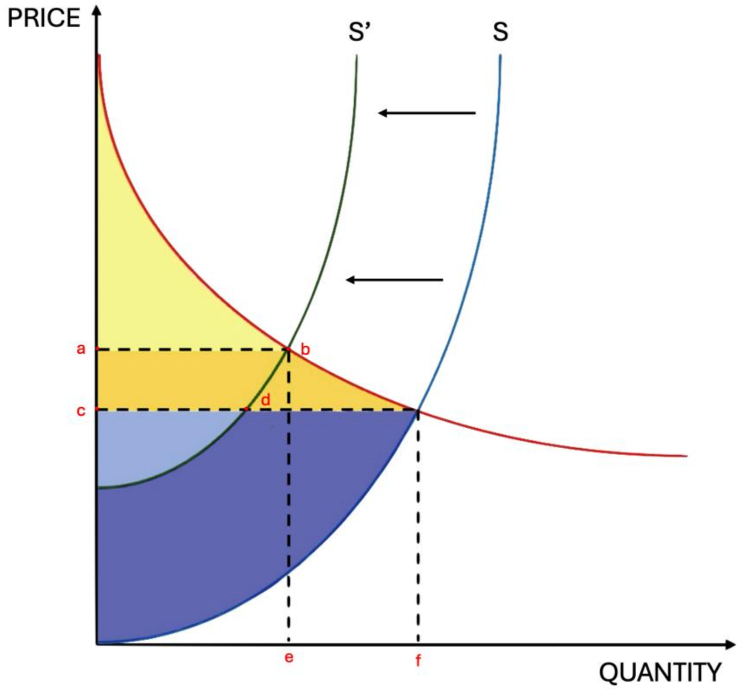


Figure 3 formalises these welfare effects. A leftward shift of the supply schedule from S (private enterprise) to S′ (public enterprise) moves the market equilibrium from point *(f, c)* to *(e, b)*, raising prices and reducing quantities. The adjustment eliminates the orange region, previously belonging to consumer surplus.

Precisely because of these issues, the UK government was forced to privatize the nationalization movement, mentioned at the beginning of this paper.

Consider the case of British Telecom (BT). Prior to its privatization in 1984,[38] BT was a state-owned monopoly characterized by long waiting times for phone line installation, outdated infrastructure, and lack of customer service. After privatization, along with the removal of anti-competition practices, BT faced new competition, such as TalkTalk.[39] The company was forced to invest in digital switching, internet infrastructure, and mobile services. As a result, waiting times decreased dramatically, service quality improved, and prices gradually dropped due to market competition.[40] Privatization encouraged innovation and efficiency, substantially increasing consumer surplus and overall social value. This scenario demonstrates how the shift from public to private ownership can realign incentives and drive behaviour that better serves the public interest, even if the enterprise is no longer explicitly "public."

Charities represent a third model. Like public enterprises, they do not pursue profit—but unlike them, they often operate in competitive markets, where they need to maintain consumer surplus. Their goals are typically altruistic: improving social conditions, addressing inequality, and reducing harm. In the Total Economic Welfare model, this creates a paradox: although charitable organizations may generate larger positive externalities, they are unlikely to surpass private firms in customer valuation or cost control. Accordingly, every additional unit of external benefit must be offset by an equal—or even greater—reduction in producer surplus. This presents two problems:

First, because charities cannot accumulate profits, they have no internal source of growth; without additional donations, they cannot scale up or provide more services to society.[41] A striking example is the Bill & Melinda Gates Foundation, the world's largest private charity, with an endowment of $70 billion.[42] Despite its scale, the Foundation faces limits on expansion. In its Sound Families Initiative in Washington State, an estimated 26,500 people were homeless, yet the program supported housing for just over 1,000 families—serving less than 4% of those in need.[43] This shortfall reflects not apathy but the limited funding capacity to enormous demands.

Second, the decoupling of funding from performance allows internal inefficiencies to persist over time without facing direct financial penalties. Take Oxfam, a UK-based international charity, as an example. While Oxfam has a noble mission—fighting global poverty[44]—it has faced several operational and financial challenges: scandals, mismanagement, and high overheads. These reports have eroded public trust and reduced the effectiveness of its aid delivery.[45]

Furthermore, even well-funded NGOs may generate distortions. When Bill & Melinda Gates Foundation launched public health campaigns in Africa,[46] many local doctors left hospitals to join the Foundation's programs, undermining existing healthcare systems.[47]

Not all profit-driven private enterprises are honest or benevolent, and market economies are not without flaws. However, appropriate government intervention can mitigate such problems. Progressive taxation can reduce income disparities,[48] while legal regulations and industry standards can constrain harmful behaviour. Ultimately, the conclusion is clear. Though comforting to believe that public or charitable ownership leads to better outcomes, data suggests otherwise. Private enterprises, when properly regulated, optimise total value for society. The size of the cake they create is bigger, even if its division appears less generous. It is not good intentions but well-aligned incentives that yield the most sustainable and beneficial behaviours.

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