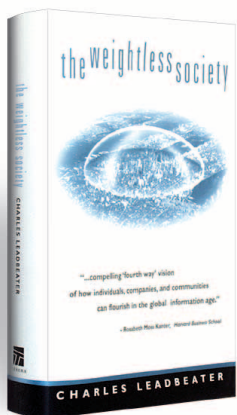




# Executive Book Summaries®



By Charles Leadbeater

## Living in the New Economy Bubble

# THE WEIGHTLESS SOCIETY

### THE SUMMARY IN BRIEF

It's hard to keep a sense of balance these days. The turbulent economy in which we all make our living constantly throws things out of kilter. At times we seem blessed. The generation, application and exploitation of knowledge is driving modern economic growth. Most developed economies make money out of thin air: We produce nothing that can be weighed, touched or easily measured. We make our living providing service, judgment, information and analysis, whether in a telephone call center, a lawyer's office, a government department or a scientific laboratory. This is the knowledge economy.

Yet many of us feel uncertain, stressed, insecure and less in control of our lives. Our powerlessness is not a personal failing, but an institutional one. Institutions seem paralyzed. They were designed for another era. We are on the verge of a global, twenty-first century knowledge economy, yet we rely on national institutions inherited from the nineteenth century. We are scientific and technological revolutionaries, but political and institutional conservatives.

In this summary, Charles Leadbeater describes how we can create the organizations to unleash and spread the benefits of the knowledge economy. We can't retreat from modernization, but must instead embark on a wave of radical innovation in basic political, social and economic institutions. We must create the weightless society.

The weightless society, according to Leadbeater, is optimistic. Globalization is good. If we turn our back on the global economy, we turn our backs on the most vital force in modern societies: the accelerating spread of knowledge and ideas. A thriving knowledge society must be cosmopolitan and open, reward talent and creativity, and invest in people and education. Knowledge societies are democratic and dissenting, open to new ideas from unusual sources, and boasting cultures in which authorities and elites are constantly questioned and challenged.

The pages that follow offer a fascinating detailed glimpse into the weightless society of the knowledge economy.



## CONTENTS

### When Ignorance Works

Page 2

### The Driving Forces Of the Knowledge Economy

Pages 2, 3

### A Piece of Cake

Pages 3, 4

### Knowing to Compete

Page 4

### Creating Knowledge

Page 5

### Evolutionary Innovation

Pages 5, 6

### Entrepreneur

Page 6

### The Networked Economy

Page 6

### The Intelligent Region

Pages 6, 7

### The Ethic of the New Economy

Page 7

### Who Should Own Knowledge?

Page 7

### Is the New Economy Green?

Pages 7, 8

### Creating Social Capital

Page 8

### PART I: LIVING ON THIN AIR

## When Ignorance Works

Compare your house with your grandparents.' Your house is packed with equipment whose inner workings you are ignorant about — computers, faxes, telephones, digital televisions, CD players and microwaves. Your domestic life is built on a foundation of ignorance. Your grandparents, on the other hand, knew how things in their house worked because these items were mechanical. Although our society is far richer in knowledge, you are more ignorant than your grandparents were.

Ignorance isn't bliss, but it's a lot better for us than we generally think. Ignorance is a good measure of just how rich and productive our societies have become. Ignorance allows us to be efficient. We can rely on other people's knowledge. We specialize and combine our knowledge with others to create new products and businesses. For example, Finnish mobile telephone manufacturer Nokia combines engineering knowledge with consumer styling and sophisticated software. Nokia is a place where scientists, engineers, product designers and consumer marketing specialists combine talents.

We are learning to trust the knowledge of other people, allowing ourselves to be ignorant where they are knowledgeable. We don't need to know how a cell phone works; it would be a waste of time to find out. As the knowledge economy becomes more developed and our lives more interdependent, the ability to trust the knowledge of other people will become more vital. All of us are made richer by our ability to remain ignorant while other people do the learning and inventing for us. Ignorance is efficient because it helps us economize on knowledge. That's the power of the division of labor in the knowledge economy. ■

## The Driving Forces Of the Knowledge Economy

Your father probably had a steady, predictable and dependable career which carried him through a well-earned, properly funded and enjoyable retirement. Today, you might be self-employed, independent and working from home. If so, you are a "portfolio worker," armed with a laptop, a modem and some contacts. You

are also what Peter Drucker calls a "knowledge worker." Simply put, you live by your wits.

### *We're Going on a Bear Hunt*

To go it alone is risky, demanding and stressful. Yet to rely upon larger organizations and institutions, companies, and trade unions isn't much of an improvement. Where can you turn to find greater security in an environment as hostile as the modern global economy? The unlikely answer lies in a children's book, *We're Going on a Bear Hunt*. In it, a family sets out to find a bear, but runs into daunting obstacles: deep mud, a cold river, a dark forest and a violent storm. At each obstacle, the family chants, "We can't go under it. We can't go over it. We'll have to go through it." That's the challenge we face. We have to steel ourselves to press on because there is no going back.

### *Financial Capitalism*

Three forces drive the new economy: financial capitalism, knowledge capitalism and social capital.

The first, financial capitalism, allows the world's financial system to switch vast resources around the globe in an instant. A dealer in London can buy stocks in Lebanon, government bonds in Thailand and futures in Brazil, all while sipping a café latte. Combine these powerful and volatile financial flows with fragile emerging economies equipped with feeble, sometimes corrupt, and poorly regulated financial systems, and you have a recipe for disaster. And that's exactly what happened with the rolling financial collapse of 1998.

The answer is not to retreat, but to push for the creation of a more globally interconnected and regulated economy. The task is to maintain beneficial long-term

(continued on page 3)

**The author:** Charles Leadbeater is a writer, consultant and advisor to Prime Minister Tony Blair's Downing Street Policy Unit.

Copyright© 2000 by Charles Leadbeater. Summarized by permission of the publisher, Texere, 55 East 52nd Street, New York, NY 10055 (and for the UK, Commonwealth, Europe and open markets, Penguin Books Ltd., 27 Wrights Lane, London W85TZ). 260 pages. \$27.95. 1-58799-001-6.

**Published by Soundview Executive Book Summaries** (ISSN 0747-2196), 10 LaCrue Avenue, Concordville, PA 19331 USA, a division of Concentrated Knowledge Corporation. Publisher, George Y. Clement. V. P. Publications, Maureen L. Solon. Editor-in-Chief, Christopher G. Murray. Published monthly. Subscriptions: \$195 per year in U.S., Canada & Mexico, and \$275 to all other countries. Periodicals postage paid at Concordville, PA and additional offices.

**Postmaster:** Send address changes to Soundview, 10 LaCrue Avenue, Concordville, PA 19331. Copyright © 2001 by Soundview Executive Book Summaries.

**Available formats:** Summaries are available in print, audio and electronic formats. To subscribe, call us at 1-800-521-1227 (1-610-558-9495 outside U.S. & Canada), or order on the Internet at [www.summary.com](http://www.summary.com). Multiple-subscription discounts and Corporate Site Licenses are also available.

### The Driving Forces Of the Knowledge Economy

(continued from page 2)

global investment flows to emerging markets and innovative economies while taming speculative excess.

#### **Knowledge Capitalism**

The second driving force is “knowledge capitalism.” Knowledge capitalism is the drive to generate new ideas and commercialize them. This process of creating, disseminating and exploiting new knowledge is the dynamo behind rising living standards and economic growth. Collaboration is the driving force behind the creativity reflected in knowledge capitalism.

#### **Social Capital**

That collaboration gives rise to the third driving force, social capital. Trusting and being able to rely on others reduces the risk inherent in the new economy. That’s because the larger the range of people you can depend on, the less risk you will experience. In order to succeed, we must reach a point where we are an innovative and inclusive society. We cannot write off a percentage of our people through poor schooling, poverty and unemployment. We must move away from the winner-takes-all mentality that leaves most people at the bottom. We invest in new institutions of social solidarity.

These three forces are driving modern economies. It’s no coincidence that they are all intangible. When they work together, the economy hums and society seems strong and creative. When they are at odds, society is in danger of fragmenting and becoming more volatile. The task is to combine finance, knowledge and social capital in a virtuous circle of innovation, growth and social progress. The goal of politics in the twenty-first century should be to create societies that maximize knowledge, the wellspring of economic growth and democratic self-governance. ■

### A Piece of Cake

There is no better example of the power of the knowledge economy than a simple recipe. Each year at Christmas, millions of people give cookbooks. This exchange is an annual, global knowledge transfer on a vast scale. A few thousand cookbook writers around the world distill their knowledge and deliver it to millions of cooks. It’s a worldwide upgrade of the software which runs our kitchens.

#### **Tacit vs. Explicit**

There are two kinds of knowledge, tacit and explicit. Tacit knowledge is that which you acquire by experience. It’s best communicated by example. Explicit

### Myths About the New Economy

#### **Myth 1: Learning is the Only Key to Success.**

In the knowledge economy, the ability to unlearn is more important than the ability to learn. Unlearning is harder than learning, but absolutely necessary if companies and organizations are going to survive challenges.

#### **Myth 2: Information is Always Valuable.**

What counts is not the accumulation of information, but what we do with it. Information must be turned into understanding and insight. What sets entrepreneurs apart is not their raw information processing power, but their capacity for insight and imagination.

#### **Myth 3: Formal Education is the Best Model for Learning.**

Having more college graduates than ever before is not necessarily a great idea. If more people have degrees, the value of having just a college degree will go down. Consequently, many professional organizations try to boost the earning power of their members by creating more and more professional qualifications. Thus we have created qualification inflation. As more have these advance certifications, the value goes down. Two other qualifications will become more important than education: experience and entrepreneurship. In a society where virtually everyone is formally educated to high standards, the skills and qualities that cannot be taught will gain greater value.

#### **Myth 4: We Live in a Time of Endless Choice and Opportunity**

The new economy is supposed to open up endless choices for consumers, but it’s just not true. The global economy is instead dominated by a few global brands like Nike, Armani and Calvin Klein. The new economy does open up countless opportunities to make a living any way you want, but it also means a greater chance of failure.

knowledge, on the other hand, is codified in reports and books. Explicit knowledge is easier to transfer, but less rich. For example, there are two ways of delivering a recipe — tacitly or explicitly. You may have learned how to create a beautiful chocolate cake by watching your mother make one. That was the transfer of tacit knowledge. The same recipe in a cookbook or posted on the Internet will transfer the knowledge faster, and to a lot more people.

(continued on page 4)

### A Piece of Cake

(continued from page 3)

#### Commoditizing Knowledge

Knowledge about how to cook has become a commodity. Instead of acquiring our own knowledge, we economize and buy the book. Imagine for a moment that you have invented the perfect chocolate cake recipe. You can exploit this two ways. One is by making cakes. But there is a limit to how many cakes you can make, and each one costs money to produce. If, however, you perfect the recipe, and sell it, there is no practical limit on how many you can produce, at very little cost. ■

#### Knowing to Compete

Our generation is the beneficiary of an unprecedented tide of formal knowledge which is lifting us up. That knowledge is coming from a combination of scientific research, a concerted investment in education, and the spread of information technology.

Together, these “push” factors are making available unprecedented amounts of valuable know-how. And another powerful set of competitive pressures is pulling companies toward know-how as a durable source of competitive advantage. Companies are driven to invest more in assets that weigh nothing but which are of great

### How Waterford Globalized

Shortly after he took over Waterford Wedgwood, the Irish fine goods company, Tony O'Reilly commissioned research to determine if U.S. consumers knew Waterford crystal came from Ireland. If they did, it would be important to keep production in Waterford. If they didn't, he reasoned he could outsource production elsewhere more cheaply so long as quality was maintained. The study found most consumers thought of Waterford as a brand, not a place. Outsourcing began. Waterford's distinctive assets were intangibles — brand names, design traditions and know-how.

value: brands, research and development, and new approaches to building customer loyalty.

The message for companies is clear. Most of their value comes from “stealth assets” like brands, research, patents and other intellectual property. The tangible assets recorded on most corporate balance sheets are often no more than a fraction of the total worth of a company. The gap between the value of a company's tangible assets and its true worth, known as the market-to-book ratio, is especially large for service and high-technology companies. ■

## PART II: COMPANIES

### Corporate Collapse

Each day, we pick up, without thinking, the intelligence of others, embedded in easy-to-use products. The manufactured products we use and enjoy embody the knowledge and skills of thousands, and were made possible by the contributions of Frederick Winslow Taylor.

Born into a privileged family, Taylor suffered from poor eyesight and debilitating headaches that kept him out of Harvard. Instead, he took a job as a patternmaker. By day, he was a laborer, but in the evening he dined with family and friends who owned factories. This dual perspective of work and business, combined with a fanatical attention to detail and abhorrence of waste, encouraged him to develop theories of scientific management.

In *The Principles of Scientific Management*, published in 1911, he became a prophet of one of the dominant ideologies of our times: that we should make ourselves more efficient and productive by applying scientific methods to work. His ideas helped create mass manufacturing industries that produced the consumer affluence of the last century. He turned organizations into well-oiled machines. His ideas are at work in every

McDonald's, and has shaped our schools with their standardized tests and specialization.

Corporations took Taylor's ideas and applied them to not just the shop floor, but also other aspects of production. However, by the end of the century, competitive forces, particularly foreign ones, meant a shift in attitude. Workers began to be cross-trained and multi-skilled. Teamwork became the mantra. There was panic and confusion, dressed up as strategy and renewal.

Now, at the beginning of the twenty-first century, the giant corporation has a new lease on life. Global organizations are exploiting opportunities for economies of scale, and selling to global markets. A new breed of corporate giant is being created through global consolidation, with mergers such as Daimler-Benz and Chrysler, BP and Amoco, and Exxon and Mobil.

Yet in much of the rest of the economy, the old corporate regime is being stripped down and new organizations are slowly emerging. These have little hierarchy and encourage teams while rewarding initiative. The most successful companies in the new economy will be mutants and hybrids in software, communications, media and biotechnology. ■

### Creating Knowledge

A company's health depends on whether it has the flow of ideas it needs to renew its products. If the knowledge flow runs dry, so will the company's reservoir of know-how. A company has to excel at finding and generating knowledge and then protect that intangible asset through branding, patents and copyrights. The process is full of difficulty. Visible knowledge is easily imitated, while intangible knowledge is more complex. Companies that will succeed will figure out how to create knowledge one of two ways: through incremental knowledge creation or through radical innovations.

*Incremental* knowledge creation involves the transfer of best practices through an entire company. Take, for example, the case of 42 almost identical food plants within the same company. A study showed that the best plants were three times more efficient than the worst. If the best practices of the high-performance plants are transferred to the worst plants, the savings are astonishing.

*Radical* knowledge creation, on the other hand, moves fast. For example, the U.S. computer industry developed an "intelligence network" to spot new ideas among bright graduate students on the theory that there are more innovative ideas outside their companies than inside. They develop and test radical new ideas and learn from failure.

To engage in radical innovation, a company often has to be open to ideas from the outside and from unusual sources, quick to recognize and reward talent, open to counter-cultural ideas, and able to combine know-how with other assets and skills such as finance and marketing. The best companies combine both radical and incremental knowledge generation. They improve their productivity, quality and cost performance continually while being open to radical, new ideas. ■

### Evolutionary Innovation

We all know an innovative company when we see one. Dell Computers created a new industry by combining just-in-time manufacturing with telephone sales and home distribution. McDonald's created an industry by developing standardized cooking methods and training workers to deliver low-cost hamburgers, just in time, in hygienic conditions. Charles Schwab forced its competition to take e-commerce seriously by launching an online financial services business. They all created new products or industries by innovating new business models. But the process is anything but easy, since it typically requires a new organization and new processes, new incentives and a new culture. Here's how to go about it:

- **Diversity:** Evolution needs diversity. Bring out-

### The Knowledge-Creating Company

The knowledge-creating company of the future will be good at learning and unlearning and will embrace eight principles:

**1. Cellular Structure:** Know-how companies will be cellular. They act on their own to satisfy basic needs and in concert to achieve more complex tasks.

**2. Self-Management:** The cellular company practices self-management and self-organization of motivated, educated and ambitious workers. People will self-manage within a clear set of values and corporate goals, so there will be less bureaucratic oversight.

**3. Entrepreneurship:** All organizations will become more entrepreneurial. Entrepreneurship, which is the ability to spot and take advantage of opportunities in the face of uncertainty, needs to spread throughout the entire organization.

**4. Equity Pay and Membership:** Organizations will need to be held together by a sense of membership. Knowledge-creating companies will resemble clubs, which have distinctive, self-regulating codes of behavior and values. There is equity pay and opportunities for people to pursue their interests.

**5. Deep Knowledge Reservoirs:** A strong company needs to be sustained by deep reservoirs of knowledge. It must acquire and generate specialized expertise and know-how. A company can't be a loose collection of generalists.

**6. Integration:** The ability to integrate diverse skills and complementary resources will become more critical. Companies are knowledge integrators.

**7. The Holistic Company:** Public legitimacy is a vital asset. Companies that want to harness new ideas into new products will have to establish public trust.

**8. Collaborative Leadership:** A knowledge-creating company needs to be an enterprise rather than a business; an organization with a purpose. Entrepreneurial companies are a purpose in search of assets. Leaders must create that sense of purpose and must engage in a constant search for creative collaboration, promoting a culture of curiosity and inquisitiveness, attacking complacency, encouraging dissent, dispute and creative abrasion.

siders in when possible. Develop networks that include educational institutions, research laborato-

(continued on page 6)

### Evolutionary Innovation

(continued from page 5)

ries, suppliers and competitors.

- **Selection:** Companies must allow good ideas to be tried while weeding out bad ones. Reward good efforts, as well as good proposals that didn't make the cut, to encourage further idea generation.
- **Replication:** Once selected, a good idea has to spread. Turn good ideas into new products, processes or routines.
- **Organizations and Environments Innovating Together:** Companies have to change with their environment as well as change the environment. Form partnerships. Rather than retaining exclusive rights to a patent, companies can license that technology to others, spread the idea, and become a global leader through partnership.
- **Equilibrium Punctuated by Disruption:** Long periods of incremental change are punctuated by explosions of creativity. Companies must be capable of continual incremental change but also radical reinventing.
- **Design for Evolution:** Successful companies are

### The Personalized Company

As human capital has become more critical, large companies are finding it harder to recruit, retain and motivate the talent they need. Workers are simply demanding more in terms of corporate culture, benefits and work-life balance. Companies that fail to address these issues will make themselves vulnerable to competition in labor markets.

In the last three decades, there has been a dramatic increase in the number of women with children in the workforce. This shift creates demands by mothers and fathers for a better balance between work and family life. Companies that employ a diverse workforce will have to respond, or lose a vast source of talent. Women are more likely to turn down a job or leave a company because it does not provide family-friendly policies, individualized career planning, sound anti-discrimination policies, or flexible work times.

better at learning, adapting and evolving. Companies must design organizations, and promote a culture that is cellular, self-managing, entrepreneurial and quick to adapt. ■

## PART III: ENTREPRENEURS AND NETWORKS

### Entrepreneurerve

The knowledge economy will not be the sole preserve of global companies. It will breed a rich undergrowth of entrepreneurial high-growth companies who will be the source of many of the brightest and best ideas. Of these, the most important will be the knowledge entrepreneurs. The assets they will trade on — know-how, skill, good judgment — are intangibles.

Entrepreneurship involves two main ingredients: sensing opportunity and mobilizing resources. Entrepreneurs spot value in ideas, resources and people that large companies often overlook. They excel at rapidly mobilizing resources to exploit opportunity.

We are witnessing the emergence of a new entrepreneurial generation, willing to take risks. They're not just looking for profit, though. They value their independence and want a sense of achievement from building a business or even changing society. ■

### The Networked Economy

Successful global companies are really networks of information, knowledge and relationships. Take, for example, Visa, the credit card company. It isn't a company at all, but an alliance of banks brought together

into an international settlements system. Visa is a service owned by 20,000 financial institutions that offer credit card services. Visa handles \$650 billion in consumer transactions per year, yet it is nothing more than a brand and a set of relationships. ■

### The Intelligent Region

Silicon Valley is known for its high-tech industry. There, in a congested space, more and more intelligence has been packed, making it the largest agglomeration of knowledge capital in the world. It also has the world's highest concentration of venture capitalists. The region's economy is a network of social ties that stretch from universities to companies, from venture capitalists to lawyers, from large companies to small.

Entrepreneurship thrives there because once an idea emerges, its creator is embraced by a network of venture capitalists and advisors, who help bring in companies and managers with complementary skills and assets. It is these ties that let Silicon Valley adapt to changing conditions and stay at the forefront of the new economy. It exemplifies the connection between innovation, collaboration, relationships and social capital. Like

(continued on page 7)

### The Intelligent Region

(continued from page 6)

Silicon Valley, the global economy is evolving into a patchwork of regions and urban agglomerations. The social and political communities fostered by the new economy are likely to be regional and city-based rather than national. These will be intelligent regions. ■

### The Ethic of the New Economy

Trust and cooperation are as critical to success in the modern economy as self-interest. People share and act on ideas when they trust one another. Yet many of our traditional bases for trust have been eroded by social and economic change. Established institutions are suffering from a malaise, if not a crisis, of trust. Large companies cannot be trusted to deliver security. The political system is treated with widespread cynicism. We need to embark on a wave of innovation in both public and private institutions to reform them to inspire and reproduce trust among workers, consumers and financiers.

As the character of the economy continues to shift

toward global production and trade of intangible services, trust will only become more important. As the international division of labor expands, so we depend on goods we barely understand, made by strangers, in factories thousands of miles away. And entrepreneurial cultures thrive when there is a high tolerance for well-intentioned failure, when people are trusted enough to be given a second and third chance. How will trust be seen in the new economy? In one of four distinct ways:

- **The role of contracts will be extended from commerce into other areas, such as government, to set clear yardsticks of acceptable behavior.**
- **To win public trust for innovation, we need to establish a transparent, publicly accountable system of trusted, expert third parties who will assess risk on our behalf.**
- **We need to improve procedures for injured consumers or workers who feel they have been treated unfairly to obtain redress, perhaps through arbitration.**
- **We must create a society where information is open and accessible.** ■

## PART IV: THE KNOWLEDGE SOCIETY

### Who Should Own Knowledge?

Who should own knowledge in the new economy? The old ideas of ownership embodied in the far right notions of private ownership coupled with the free market and the far left notion of collective, public ownership won't work in the new century. We need to innovate new forms of ownership that are both postcapitalist and postsocialist.

The traditional idea of company ownership is a myth. All over the world, managers justify decisions on the grounds that they have to deliver value to the ultimate owners of the business, the shareholders. In theory, all power flows down from the shareholders.

This account of shareholder ownership is one of the most powerful fantasies of corporate life. Ownership is not a simple concept. Ownership confers the right to possess, use and manage an asset, to earn income from it, to claim an increase in its capital value.

But a knowledge-based form differs markedly from this model in both practice and theory. The core to a knowledge-based company is the know-how of the people who work there. The critical issue is how these people are combined. A know-how business is created when people come together, give up their individual property rights over their work, and jointly invest these rights — temporarily — in the enterprise. Property rights are pooled by a social contract among peers, not by the top down

delegation of power from shareholders to managers. That fundamental distinction, between social contract and hierarchy, has far reaching implications in the way knowledge companies will be organized and owned.

The rise of the knowledge economy will encourage hybrid ownership that combines the public and the private. The old capitalism was founded on strong property rights; the new economy will be founded on fuzzy, pooled property rights and will only come to life with new forms of ownership. ■

### Is the New Economy Green?

Has the Holy Grail — a new economy in which economic growth can be combined with environmental sustainability — appeared on the horizon? It is an alluring promise. For decades, the demands of economic efficiency and environmental sustainability has been at odds. Regulations designed to protect the environment have been opposed by industry because they threatened to raise costs and undermine competitiveness. Electorates have been presented with a dilemma: Consume less or degrade the environment for your children and grandchildren.

If the promise of a green and prosperous future is to be realized, it will not be through technology alone. The new

(continued on page 8)

### Is the New Economy Green?

(continued from page 7)

economy will benefit the environment only if it gives rise to social, commercial and organizational innovations which change our attitude toward basic economic activities like consumption, investment and ownership.

#### *Dematerialization*

The new economy is driven by information. As we consume more entertainment and information, and use more computers and software, we will produce more and more with less energy and material. Physical products are becoming lighter. Building technology allows us to enclose more square footage with less material. Consumers can download songs digitally rather than buying and storing a CD. Shopping online consumes less energy than driving to the mall. The confluence of two trends — dematerialization and virtualization — means the economy should become less material intensive and therefore more environmentally friendly.

The effect may be more pronounced in the services sector of the economy, as we shift away from manufacturing. As consumers grow more affluent and more satiated, they spend more on services and less on basic goods. ■

---

### Creating Social Capital

Why do financiers find it difficult to come up with ways to lend a few hundred dollars to poor people with no credit rating, or a few thousand to budding entrepreneurs with no track record in business? There is nothing stopping us, other than our lack of will and ingenuity. It can and is being done, on a small scale for now.

A good place to start looking for a model is Shorebank. The Chicago bank has broken through the superficial and outmoded divide between charity and commerce, social purpose and profits. Shorebank invests in social capital creation, and does it so well, it makes a financial return comparable with any bank in the United States. Shorebank began in 1973 when four Chicago bankers bought an ailing bank which was the last financial institution left in a poor neighborhood.

The bankers saw that capital was flowing out of the neighborhood, homes were in a state of disrepair, property values were falling, store owners were quitting, and there were fewer and fewer employment opportunities available. Shorebank began lending money for rehabilitation of rundown houses to people who ordinarily wouldn't pass bankers' credit requirements. Repayment was structured to meet the needs of the borrower. The bank now has a capital base of \$77 million and assets of \$725 million.

### *The End of Tax and Spend*

We are in the midst of a chronic crisis in the balance between tax and spending. Too much social spending delivers too little lasting benefit. Our tax systems will find it increasingly difficult to finance these growing demands. Traditional tax and spend policies are no longer sustainable. The new economy will make it more difficult to raise money for public spending through the old tax system. Taxpayers will be increasingly unwilling to pay more in tax unless they see lasting benefits. More social spending will have to become social investment. But that will require radical changes to the structure, culture and organization of the public sector. Public spending must deliver lasting social capital.

Tax collection will become tougher and tougher, as money becomes electronic and inventories will no longer be physical and countable. Our industrial-age tax system is clearly in trouble. We must create an intelligent tax system based on four principles for raising funds for social investment:

- 1. The system must be able to adapt to the speed of the society around it.** Old style entitlement systems can't continue to function beyond their usefulness. Pensions and social security systems must be rearranged so that investment decisions are placed in the hands of individuals, towns and regions.
- 2. The social investment system must be capable of matching the diversity of the needs it serves with financing from different sources.** The financing must be matched to the activity that is being financed. For example, pensions must be funded from investment income rather than by transferring resources from one group of the population to another.
- 3. The scale of the challenge posed by an aging population, the rising demand for education, and growing inequality requires society-wide response.**
- 4. Developing countries face a service revolt as well as a tax revolt.** People want to see results. ■

---

### Closing Thoughts

We must not retreat into narrow nationalism. That would be like our ancestors a century ago trying to retreat from the cities to their country communities. The knowledge economy goes to the heart of issues of global equality and development. There is no one best route into the knowledge economy. The production of new ideas within schools, colleges, companies and teams can be organized in a vast array of ways, while firms, governments and societies have a widening array of choices about how to organize themselves. ■