Analyzing Making Profit A Public Good

Table Of Contents

1. Abstract

This paper considers profit as a public good, where economics is aligned with social welfare. Here the usual notion of "profit- benefiting the private interests" is being examined from a different point of view. This paper emphasizes the theory of shared value, bringing benefits to society in the long term. In the course of the analysis, a simple and intuitive version is presented, and some of the problems confronting empirical attempts to measure the distributive incidence of public goods are resolved. Assessing the extent to which various public goods should be provided, determining how the provision of public goods affects the desirability of income redistribution, and providing a meaningful description of the distribution of well-being. The objective is to identify how the distributive incidence of a public good affects the extent to which the good should be provided. This paper takes the position that businesses should take the initiative in making the modern economy more inclusive. To achieve this ideal, the traditional goal of profit maximization or the maximization of shareholder wealth, in the case of publicly held companies, needs to be re-conceptualized in terms of creating value for all groups that contribute to the process of value creation.

Keywords: public good, social enterprise, profit-maximization, corporate social responsibility, free markets, social welfare, welfare capitalism.

2. Introduction

The COVID-19 pandemic, refugee crises, and climate change have exposed the need for public goods that are likewise global, and the world rendered even more unequal therefore a new language of "prosperity" and "welfare" will have to be explored. What are public goods, and how can they be supplied globally? The government plays a significant role in providing goods such as national defense, infrastructure, education, security, and fire and environmental protection almost everywhere, often referred to as "public goods". Public goods are of economic and developmental interest because of their provisioning, to varying degrees, essential to the smooth functioning of society economically, politically, and culturally and because of their close connection to problems concerning the regulation of externalities and the free-rider problem. Without infrastructure and their protection goods cannot be exchanged, votes cannot be cast, and it would be harder to enjoy the fruits of cultural production but due to their connection to externalities and the free-rider problem, the provision of public goods raises profound economic and ethical issues.

Rather than serving as a means to achieve social welfare, profit has always been the primary objective of business practice resulting in constraints on the practice of prosocial business management. However, there has been a marked shift in the way people view businesses after the 2008 global financial crisis. Businesses are beginning to be thought of as profit-maximizing entities while this is true for a few entities, most companies work to create value for not only their shareholders but also for their customers and employees. The movement now in capitalism is addressing societal challenges through market-based solutions. Companies are creating measurable business value by identifying and addressing social problems that intersect with their business. This is what is termed 'Creating Shared Value' (CSV).

3. Profit as a Public Good

In a welfare economy, profit appears when production and distribution are organized by maintaining commodity relations. In a capitalist economy, individuals or companies own the capital assets. The general market's supply and demand govern how commodities and services are produced. In this system, businesses would manage the markets by competing with one another to captivate the market, with the government taking a backseat. Capitalist society is a profit-maximizing society, so their involvement in important industries will hamper the basic services that are offered to common people at affordable prices. If big players get involved in rendering basic services which were offered by the government then they can only be afforded by the wealthy and affluent members of the society. Having said that that, both public and private sectors are important for the growth and development of the nation but seeing the size of the population, the literacy rate of citizens, and the unequal distribution of income it can be said that the government should have more control over the assets of the nation to overlook that the resources are fully utilized and equally distributed among citizens.

3.1 What is a Public good?

A public good is a commodity or service that every member of a society can use without reducing its availability to others. Typically, a public good is provided by a government and funded through taxes. For example town road, park, or school. National defense is a public good. A public good may also be a basic need such as access to clean air and drinking water. The main distinctive factor of a public good is that they are non-rivalrous and non-excludable. Non-rivalrous means that the goods do not decrease in supply as more people consume them. Non-excludability means that the good is available to all citizens.

Every nation makes its own decisions on which goods and services should be considered public goods, and this is reflected in their national budgets. Global institutions, where they exist, often lack the legal authority to enforce regulation and taxation or the institutional capacity to coordinate the needs of all citizens in the world and across generations. The coordination challenge is also bigger. Global institutions deal with national governments, as opposed to individual citizens. National governments have very different incentives from individual citizens, both economic and political, and many struggle to provide public goods even within their own countries. For instance, the ratification of the Paris Agreement was both a success and a testament to the limitations of international coordination. By making allowances for countries' different needs and responsibilities, the agreement takes into account the welfare of each country. For instance, WHO defines global public goods like polio eradication initiatives, effects of alcohol and tobacco consumption, information systems for communicable diseases, and regulations aimed at stopping the cross-border movement of communicable diseases. The river basin management model in the EU, for example, has advantages for all the countries the river flows through, including some that are not EU Member States. In the summary report of the International Task Force on Global Public Goods, which was co-chaired by Ernesto Zedillo and Tidjane Thiam, the concept is defined as, “Global public goods are those whose benefits could in principle be consumed by the governments and peoples of all states.[1] Examples include mechanisms for ensuring financial stability, the scientific knowledge involved in the discovery of a vaccine, and international regulations for civil aviation and telecommunications. Once such global standards and systems are established, they are available to all states, and consumption of the good by one state or its people in no way reduces its availability to others.”

Advocates for this kind of government spending argue that its economic and social benefits significantly outweigh its costs, pointing to outcomes such as improved workforce participation, higher-skilled domestic industries, and reduced rates of poverty over the medium to long term. Critics argue that it poses a burden on taxpayers and that goods can be more efficiently provided by the private sector. For instance, EU governments and institutions are promoting alternative sources that can contribute to development finance if aid pledges are not met. From the G20 to the European institutions, official pronouncements view private sector activity and resources as key for delivering public goods and aim to diversify and enhance sources of financing and develop new financial instruments, thus reducing the burden on the public purse.

4. Social and Economic implications of Profit maximization

4.1 On Income Inequality

One of the greatest anomalies of our time is the widening gap in income and wealth in most societies between the rich and privileged few, and the masses at the bottom of the social pyramid who are often mired in abject poverty. While the prevalence of poverty in the face of phenomenal growth stems largely from the state’s failure to perform its traditional functions in a manner that equalizes opportunities for all members of society, business also bears a major share of the blame for an economic system that has become increasingly non-inclusive. For

[1] 2006. International Task Force on Global Public Goods. “Meeting Challenges: International Cooperation in the National Interest.” *Summary Report of the International Task Force on Global Public Goods*. Stockholm: Erlanders Infologistics Vast AB.

instance, concerns about inequality can also lead to political unrest and instability. A proper welfare state in a healthy capitalist system should be financially and politically sustainable, provide social benefits that reduce inequality, reduce the opportunity cost of economic activities such as labor participation, and involve a progressive tax system. Generally, the role of the state in a capitalist society is to provide the legal framework within which individuals can pursue their economic self-interest without jeopardizing the same rights held by other people and to ensure that the collective well-being of society is achieved and shared by all. Business enterprises will be the principal force of change in capitalist society because, among the various institutions that comprise modern society, they have proven to be by far the most adaptive to emergent technological, market, political, and cultural change.

5. Case studies

5.1 Strategies used by Corporates for Profit maximization

A lot of case studies exist across industries and geographies, "Novartis Arogya Parivar" in India is bringing health education and access to medicines to more than 10 million villagers, opening a new and profitable market for the company and improving health outcomes for consumers. Innovations like ICICI Bank Ltd's rainfall-based crop insurance, now insuring 12 million small-holding farmers, are bringing financial inclusion as well as benefiting ICICI.

Grameen Bank- Grameen Bank is a microfinance organization and community development bank founded in Bangladesh. It makes small loans known as microcredit or Grameen Credit. It is founded on the principle that loans are better than charity to interrupt poverty. Their objective is to promote financial independence among the poor and encourage all borrowers to become savers so that their local capital can be converted into new loans to others. Their work is based on groups of five prospective borrowers who meet regularly with the Grameen Bank field manager and two of the five prospective borrowers are granted loans. If, after a probationary period, the first two borrowers meet the terms of repayment, then loans are granted to the remaining group members. Peer pressure acts as a replacement for traditional loan collateral. The Grameen model has come to symbolize an efficient means of helping the poor by providing them with opportunities to help themselves. More than 97 percent of Grameen's loan recipients have been women. Since 1995, Grameen has funded 90% of its loans with interest income and deposits collected, aligning the interests of its new borrowers and depositors-shareholders. The last 15 or so years have seen phenomenal, worldwide growth in poverty-focused microfinance programs, those that provide credit, savings, insurance, and other related services to the poor, especially poor women. The number of Forward poor clients reached by microfinance institutions was 106,584,679 at the end of 2007, up from 7,600,000 in 1997, according to the State of the Microcredit Summit Campaign Report 2009.[2] While much of this growth stemmed from the massive scaling up of Grameen Bank and other large-scale institutions that were established in the 1980s and 1990s, a significant part was due to the establishment of start-up programs that subsequently scaled up to reach significant numbers. More microfinance institutions (MFIs) are expected to be established in the coming years, as the microfinance movement gains ground. They will have a particularly important role to play in reaching people in underserved countries and regions.

SELCO Foundation- For the last three years Selco Foundation has strived to experiment with several financial instruments that could then be replicated and scaled in other parts of the developing world, focused on SDG7-driven livelihood interventions. These interventions, the ecosystem access for livelihoods, include technology innovation, training and capacity building, appropriate regulation, and linkages to markets and raw materials. The range of their financial products ranged from very poor segments to reduced interest rates for those having access to slightly more mature ecosystems. The innovations have to consider the maturity of the livelihood philanthropic monies may end up subsiding the wrong link leading to unsustainable interventions. The various implementations of Decentralized Renewable Energy

[2] State of the Microcredit Summit Campaign Report 2009

(DRE) solutions like solar, make the option long-term and sustainable. The ecosystem required for the DRE-focused livelihood interventions has not only enabled several families to come out of poverty but also made them a part of the formal banking push poor families multiple rungs up in the social and financial ladder. Based on data from the last 5 years, having implemented more than 100+ sustainable energy-driven livelihood solutions, with more than 6000 entrepreneurs and enterprises, the solutions have been broadly categorized into micro, small, medium, and large with an indication of the typical end-user segments, financial institutions, and credit terms that apply for each.[3]

Solar Philippines- The largest developer of solar rooftop power plants in Southeast Asia. This is an in-house team of solar energy experts backed by a proven track record with the largest commercial plants in the country.[4] The company's avowed vision is to end "energy poverty" by providing cheap and reliable electricity to every Filipino by the year 2022, a lofty goal indeed considering that 10 percent of the country today has no access to electricity. According to a company press release, the firm intends to devote half of its resources to remote areas of the country that currently remain unserved or poorly served by electric utilities. They invest heavily in the production of solar panels to serve the energy needs of poor communities through the application of new production technologies which are more cost-effective than coal-fired power generating facilities. Solar-generated energy is one of a class of products with network externalities which have the characteristic of being subject to increasing returns, the more its production is scaled up and its customer base expands, the lower the cost of producing additional amounts.

[3] selcofoundation.org

[4] https://www.solarphilippines.ph/about-us/

5.2 Welfare capitalism

In economics, the welfare capitalism definition refers to privately owned businesses offering welfare services to employees. Welfare capitalism can also be included in government-supported welfare policies. Socialism and welfare capitalism share some key traits but are vastly different when it comes to how social services are distributed. In nations that practice socialism, the government controls most of the basic goods and services. Socialist economies also are responsible for financing, organizing, and administrating social services to the people. In welfare capitalism, businesses own most of the goods and services, not the government. Governments work with Businesses to provide welfare services to the citizens. Today, most modernized Western nations practice welfare capitalism like the United States, Canada, United Kingdom, and Germany. All of these nations differ in the degree to which welfare capitalism operates, however. The most common example is an organization offering healthcare, disability, life, vision, and dental as part of their hiring package. In 2020, the pandemic only underscored the crucial role of the welfare state, as large populations lost their livelihoods and the economic fallout reached all regions of the world. Welfare measures and social security initiatives were undertaken by governments across the world to mitigate the crises brought about by the pandemic.

The government provides very basic standards by which employers must abide, such as minimum wage standards. Anything above the minimum required by the government is at the employer's discretion. Recently, companies have begun to invest even more in corporate social responsibility initiatives, employee welfare programs, and perks provided by the business to satisfy employees. Companies have found that employees make fewer demands and are more productive when they are happier, so companies such as Google have spent millions of dollars making their businesses enjoyable places to work.

5.3 Non-Profit models

Nonprofits vary widely in purpose and type, ranging from hospitals and universities to NGOs and community kitchens. Nonprofits sharply differ from for-profit firms, which exhibit stronger procyclicality and little smoothing. For example, “Hindustan Unilever’s Sustainable Living Programme”, has undertaken initiatives like “Project Shakti”, wherein rural women, as well as the company, have benefited. In this initiative, rural women are empowered by basic training in running a business and doing the sales and distribution of the products. This way, Hindustan Unilever earns revenue as well as provides a means of livelihood to many women entrepreneurs. The consumers too get products that depend on their individual needs.

Implementation of inclusive business models (IBMs), solutions that provide access to economic opportunities to low-income communities in a manner that will make businesses more viable and sustainable. The IBM logic is, the sustainability of a business can only be achieved in a sustainable community; a community characterized by widespread poverty and great income inequality is not sustainable; therefore, addressing the social and economic needs of society is in the strategic interest of business. Ibms should therefore be encouraged and supported by government agencies, multilateral organizations, NGOs, and other social institutions. The United Nations Development Program, the United Nations’ primary instrument for social development, has long realized the importance of partnering with the private sector, business in particular, in the implementation of its worldwide network of developmental programs.[5] United Nations Development Program Philippines has for some time been working in close partnership with businesses and business associations in pursuing the un’s Sustainable Development Goals (SDGs) in the country. A recently published comprehensive report prepared by this agency jointly with the Philippine Business for the

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[5]UN’s programs for global development are encapsulated in its report, “Transforming our world: 2030 agenda for sustainable development”, which targets 17 Sustainable Development Goals (sdgs) for the year 2030 (https://www.un.org/pga/wp-content/uploads/sites/3/2015/08/120815_outcome-document-ofSummit-for-adoption-of-the-post-2015-development-agenda.pdf).

Environment showcases several IBMs being implemented across the country, quietly transforming the countryside by contributing in varied ways to the attainment of country-specific SDGs.[6]

Jollibee Food Corporation- The corporation's Farmer Entrepreneurship Program is plausibly the most publicized IBM in the Philippines, perhaps partly for the reason that it carries one of the most recognizable brands in the country today, but mainly because of Jollibee's extensive supply chain which touches the lives of many of the very poor all across the land. During the six years 2008-2014, the flagship program of the Jollibee Group Foundation, working in partnership with the Catholic Relief Services Philippines, National Livelihood Development Corporation, and several local community organizations, trained close to 2,000 farmers in supplying agricultural inputs not only to the Jollibee Food Corporation but also to other institutional buyers, including restaurants, supermarkets, and food manufacturers. Through the years, the program has provided technical assistance and managerial training to farmer-entrepreneurs from 15 provinces all over the country, all of whom are themselves potential employers and income providers.[7]

6. Challenges

1. Adding a corporate social responsibility objective will not necessarily increase social welfare. Firms with multiple shareholders that pursue goals in addition to, or instead of, profits are saddled with a few significant burdens. There is a separation of ownership and management for publicly traded firms and private firms with multiple owners. In such cases, the owners must

[6] UN's Sustainable Development Goals (successor to the Millenium Development Goals) appear to tacitly assume that overall social development is the algebraic sum of achievements along all the 17 SDGs.

[7] Farmer Entrepreneurship Program, see http://jollibeefoundation.org/farmerentrepreneurship-program/. See also http://www.inclusivebusinesshub.org/the-farmer-entrepreneurshipprogram-how-jollibee-group-foundation-empowers-small-scale-farmers-in-the-philippines/

develop a mechanism to measure and monitor the manager's performance on the social goal.[8] Profits are a relatively clear and easily quantified metric on which all owners can agree. Measuring progress toward a social goal is far more difficult and is particularly troubling for firms with many owners, each of whom may have a different idea of how to measure progress. It is now conventional wisdom that when managers are given great discretion over corporate investment policies, they tend to serve disproportionately their own interests, however, well-intentioned managers may be.

2. Social ventures, by providing goods and services at prices that do not cover all of their costs, effectively subsidize the products and services they provide. Local providers of the same good or service don't have that luxury. Social enterprises therefore run the risk of undermining local businesses and the development of that economy. For instance, the reasons for the decline in garment production in Africa between 1981 and 2000. It was found that used clothes donations explained 40% of the decrease in production and 50% of the decrease in employment.[9]

3. The world will continue to fail to provide global public goods. Many institutions that provide public goods today did not appear on their own but formed in response to demand. Public education in the United States developed in response to citizens' demands in a technologically advancing world. The IMF was established after the Great Depression and World War II as countries recognized the need to promote global financial stability. For instance, despite the wide network of welfare schemes, India still has a large ground to cover in healthcare and education spending, even when compared to other developing countries. India is also facing

[8] Michael C Jensen, 2000, Value Maximization, Stakeholder Theory and the Corporate Objective Function

[9] Frazer, Garth, 2008, "Used-clothing donations and apparel production in Africa," The Economic Journal, 118 (532), October, 2008, 1764-1784.

challenges in unemployment, hunger, and overall Human Development.[10] The welfare schemes that constitute India's social protection architecture have not been able to adequately address the gamut of developmental challenges as long-term capacity-building projects in education, healthcare, and employment remain under-utilized.

4. Often, resources within the society are constrained in developing economies, and resources with the government are often limited. Consider the case of India: as per the Companies Act of 2013, corporations must spend 2% of their average annual profits of the past three years to address social issues and challenges facing society. While the mandatory approach does solve some societal problems, this approach severely undermines the role that corporations can play in solving primary challenges such as education, healthcare, poverty alleviation, rural development, and environmental sustainability.

5. Private benefits will reflect social benefits as long as there are no "externalities." Externalities are, by definition, costs, and benefits that are not realized by either the producer or consumer. The easiest example, and one that appropriately causes much concern, is pollution. If carbon emissions have a social impact beyond the cost to the firm of the fuel that produces the emissions, which is almost certainly the case, anything that involves the use of those fuels will be overproduced, imposing an inefficiently high cost on society.

6. Market failure when there is asymmetric information- Certain markets where there is significant asymmetric information may fail without appropriate market design or government intervention.[11] Healthcare is one sector where such issues are most salient, and many Western countries have adopted systems that are not entirely free-market based.

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[10] "India's Public Spending on Healthcare Lowest in BRICS Nations: DEA Secy," Business Standard, May 13, 2021, https://www.business-standard.com/article/current-affairs/india-s-public-spending-on-healthcare-lowest-in-brics-nations-deasecy-121051301220_1.html

[11] Akerlof, George, "The Market for Lemons: Quality Uncertainty and the Market Mechanism," The Quarterly Journal of Economics, 84 (3), Aug, 1970, 488-500.

7. The widespread practice of offering freebies by politicians, across party lines and for electoral benefits, drains public finances that can be used instead for more concrete policy initiatives. The vote-bank compulsions and likely electoral dividends accrued from such tailor-made schemes complicate their reconfiguration based on actual needs that can prevent overlaps, ensure better targeting, and prevent misuse of resources.

7. Recommendations

1. Business firms can co-align the financial interests of their owners and those of the other groups that have a stake in the business. Focusing primarily on the economic interests of stakeholders ensures the production of maximum economic value by the business enterprise, and, eventually, maximum returns on capital. For example, paying workers higher-than-market wages and improving their working conditions make them more productive and highly motivated in their job performance.[12] Creating customer value through improved product quality and customer service leads to higher demand and enhanced sales revenue. Both of these strategies contribute positively to long-run profits.

2. Externalities, which justifies a role for targeted government intervention- In the case of carbon emissions, a tax that accounts for the social cost of the pollutants will cause buyers and sellers of carbon fuels to make decisions based on the social costs. There is no good substitute in these cases for appropriately targeted government intervention. The appropriate response for individuals is to play their role as citizens in encouraging the appropriate policy response.

3. It is worth emphasizing that to an extent market information is also a product that can be traded like any other good or service, and hence there will be a useful role for profit-maximizing firms engaged in the business of collecting and providing information, to reduce information asymmetries, acknowledge that settings with significant asymmetric information could call for

[12] Akerlof and Yellen 1990

government interventions, for example, mandatory auto insurance, Carfax in the used car market, or credit bureaus in financial markets.

4. Development and implementation of inclusive business models (ibms), solutions that provide access to economic opportunities to low-income communities in a manner that will make businesses more viable and sustainable. They are implemented by incorporating low-income populations in the firm's supply chains to ensure, a continuous source of well-trained and highly capable workers, constant and reliable supplies of raw materials, and steady increases in sales revenue from poor customers who benefit from low-priced versions of their products and services. In this way, the long-run viability of the business is assured. For example, locators in the various special economic zones that are situated all over the country can pursue similar joint programs to achieve the same results.

8. Conclusion

The next transformation of businesses will lie in creating economic value that creates value for society by addressing its needs and challenges. Realigning business models with societal needs is going to be the next big evolutionary change for Indian corporations. The need of the hour is the involvement of people in corporations who understand the meaning and imbibe the meaning of shared value within their organizations. We recognize that there are limitations and qualifications to the profit-maximizing model, most of which can be addressed most effectively by appropriate government action. However, these qualifications do not undermine the basic argument that firms trying to maximize profits are generally socially beneficial. The government and key policymakers should encourage companies to understand the concept and adopt it for social good. Businesses must incorporate the shared value paradigm in their business models so that it truly has a transformational impact on all the key stakeholders.

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