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How the Hope of Profit Engenders Economic Behaviors

Jacky Tang

Abstract:
The hope of profit creates incentives rooted in the prospect of residual profits, motivating firms towards cost minimisation, revenue maximisation, and innovation, but potentially also towards opportunism or externalising social costs. Whether such behaviour is better or worse requires an evaluation of which ownership structures magnify societal welfare. While profit incentives may cause cost-cutting behaviours and inefficient resource allocation in private industries, the absence of it government and charity-run industries often leads to a higher quality baseline in essential services, better welfare, and reduction in deaths.
By focusing on an unregulated baseline, the article employs Hart et al.'s (1996) model of optimal ownership structure to sort industries into four quadrants based on varying hidden-harm potential and innovation-payoff levels. Under each quadrants, case studies on welfare, customer satisfcation, and service quality are provided and analyzed. Overall, it argues that an economy made up entirely of public and charity-run enterprises would, on balance, engender better behaviour.

Keywords: Profit incentives; Cost-cutting; Provisional model; Optimal ownership structures; Economic behaviors;

The hope of profit creates incentives rooted in the prospect of residual profits, motivating firms towards cost minimisation, revenue maximisation, and innovation, but potentially also towards opportunism or externalising social costs. Whether such behaviour is better or worse requires an evaluation of which ownership structures magnify societal welfare.

Profit-seeking companies work best in markets where cutting corners rarely hurts anyone and new ideas are worth a lot. Government or charity organisations work better in the larger group of essential services—health, elderly care, water—where hidden shortcuts can be deadly and big breakthroughs are rare. Since these essential services absorb most of the money we spend and shape everyday well-being, an economy made up entirely of public and charity-run enterpris-

es would, on balance, engender better behaviour.

In what follows, the article identifies the intrinsic, unregulated behaviours that the hope of profit engenders, then contrasts them with the behaviours of government and charity ownership. Next, it employs Hart et al.'s (1996) model, utilising a graph to sort industries into four quadrants, with each quadrant having an optimal ownership structure. Finally, by evaluating the weight of those quadrants, the article demonstrates that an economy run entirely by governments and charities would, on balance, engender better overall behaviour than the hope of profit.

The hope of profit operates before any laws, taxes, or watchdogs intervene, so measuring a regulated firm would tell us as much about government rules as about profit itself. To compare fairly, this article focuses on the unregulated baseline. What owners would do if profit were their only guide, then sets that baseline against a world where the profit motive is absent, because every enterprise is run by a government body or a charity.

1. Behaviour Engendered by the Hope of Profit

Profit maximisation rewards any action that raises net cash flow. When quality is hard to verify, that stake often drives covert cost-cutting. This is done by thinning nurse staffing in care homes, deferring utility safety checks, or cheapening food supply inputs. The real-world toll is measurable: U.S. nursing homes taken over by private-equity funds saw a 10% jump in resident mortality, attributable to lower nurse hours and higher use of antipsychotics (Gupta et al., 2021). Tirole (2017) calls such behaviour "the dark side of efficiency," where visible costs fall, but welfare does not improve.

Beyond covert cost-cutting, intrinsic profit seeking encourages price exploitation when there is asymmetric market power. In pharmaceuticals, the median launch price of a new U.S. drug in 2023 climbed 35% from the previous year. Analysts attribute the rise to monopoly list prices after patenting or acquisition (Beasley, 2024). The price hike of antiparasitic medication Daraprim from US$13.50 to US$750 overnight illustrates the same dynamic (Sifferlin, 2015).

Further, without liability or emissions limits, a firm can minimise its private costs by pushing the financial burdens of pollution onto the public (Coase, 1960). Empirical work on U.S. waterways finds that counties downstream of industrial plants suffered significantly worse health outcomes before the Clean Water Act imposed discharge permits (Keiser & Shapiro, 2019). Without government intervention, profit motives create major negative externalities.

A third pattern is inefficient resource allocation. Global advertising will reach almost US$1 trillion in 2025, with up to US$68 billion lost annually to ad fraud—resources devoted to grabbing market share rather than improving products (Zenith, 2023; Woodford, 2022). Simultaneously, listed U.S. companies are forecast to spend over US$1 trillion on share buy-backs in 2025, diverting cash from investment to short-term share-price support (Chakravarty et al., 2024; Mackenzie, 2025). Both behaviours are privately rewarding, yet socially wasteful.

2. Behaviour Engendered by Charity & Government-Owned Enterprises

The defining feature of charities and state enterprises is their non-distributive constraints: any operating surplus must be ploughed back into the organisation or the public purse rather than paid to private owners. That legal structure reshapes managerial incentives and, before any outside regulation intervenes, generates certain broad behavioural tendencies:.

Because managers cannot appropriate residual profits, they are rewarded for expanding reach or improving quality. U.S. data shows that nonprofit hospitals direct about 20% more of their budgets to uncompensated care than for-profit hospitals with similar revenues (Duggan, 2000). In infrastructure, after at least 5,000 French water systems moved from private to municipal control, tariffs fell 16% while pipe replacements accelerated (Chong et al., 2006). Such behaviour supports Hansmann's (1980) contract-failure claim that nonprofits thrive where users must trust quality they cannot observe. Simultaneously, the absence of a hard profitability target leads to over-expansion: Niskanen's (1971) bureau-supply model predicts that public managers, judged on budgets rather than profits, may keep growing output even when marginal social benefit is low.

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Public deficits are often covered by tax revenue or parliamentary appropriation. Kornai's (1986) examination of socialist enterprises found chronic overruns because managers anticipated state bailouts. A meta-study of an OECD city solid-waste and water services reported that in-house municipal provision costs 7–9% more than competitively bid contracts offering identical services (Bel & Warner, 2008). Empirical work on air-traffic control, postal delivery and rail services similarly detects higher unit costs under public ownership, suggesting the cushion of a soft budget dilutes daily cost discipline.

Public managers answer to elected officials, not shareholders, and those officials operate on electoral calendars. Shleifer and Vishny (1994) document how this link encourages "overstaffing, overspending, and contract direction toward political allies." A recent study of Indian state electricity boards shows operating losses 40% higher in election years, driven by under-priced power supplied to favoured constituencies (Min, 2019). Similar patterns appear in U.S. public transit, where capital spending spikes just before local elections and then subsides, disrupting long-term project efficiency (Altshuler & Luberoff, 2003). Finally, without equity upside, managers who champion risky projects bear reputational costs if those projects underperform. Studies of national telecom companies before liberalisation reveal significantly slower adoption of digital switching and mobile technology relative to new private entrants (Boylaud & Nicoletti, 2001). In pharmaceuticals, public research labs rarely undertake costly late-stage trials without private co-investment (Cockburn & Henderson, 1998).

3. Analytical Framework

Which ownership structure engenders better behaviour depends on the sector. We can apply the framework by Hart et al. (1996) on a coordinate plane. The horizontal axis measures how badly hidden cost-cutting can hurt users—the hidden harm-potential *b(e)* in the model. The vertical axis records how much society gains when providers innovate—the parameter *p(i)*. Placing sectors on that plane yields four stylised zones (shown in Figure 1).

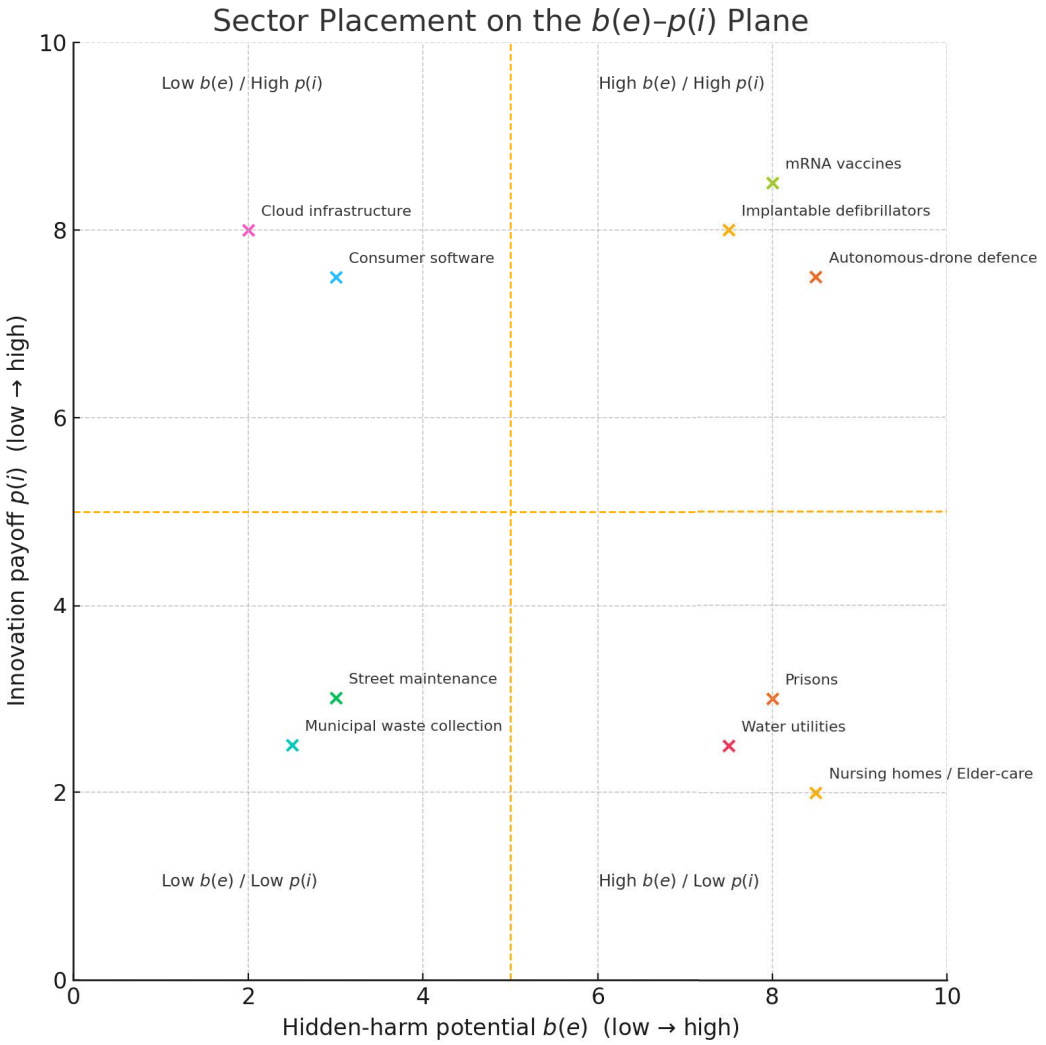

Figure 1 Sector Placement on the b(e)-p(I) Plane

The optimal ownership in each quadrant may be neither a structure nor a hybrid. For the purpose of the article, each subsection below only compares the two.

3.1 Low-harm and High-innovation

When *b(e)* is low and *p(i)* is high, undercover skimping does little damage while successful innovation delivers large benefits. Since cost-cutting only creates nuisances, the intrinsic profit motive's appetite for experimentation and speed outweighs the modest safety risk. Placing such a market under government or charitable monopoly would weaken breakthrough efforts without a commensurate gain in consumer protection. Unregulated private ownership is therefore welfare-superior.

3.2 High-harm and Low-innovation

Where *b(e)* is high and *p(i)* is low, hidden shortcuts can cause serious injury or death, while technological advance offers scant benefit. For an unregulated profit-seeker, every undisclosed cut yields guaranteed savings, downside is unlikely detection, and the upside from genuine innovation is negligible. A government or charity may operate with some slack, but it lacks built-in incentives for protecting users, and political or donor scrutiny can expose failures. In this quadrant, the safety dividend from removing private residual claims outweighs softer budgets.

3.3 Low-harm and Low-innovation

When hidden cost-cuts and breakthrough ideas barely matter, the goal is simply to service with the least waste.

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An unregulated, profit-seeking firm trims slack, but because big R&D pay-offs are absent, it diverts savings into zero-sum pursuits. Industry data show that routine consumer-service companies devote about 5-7% of revenue to advertising, and U.S. firms in mature sectors channel roughly half of net earnings (≈8% of revenue) into share buy-backs (Zenith, 2023; Lazonick, 2014). Together, those moves consume ≈13-15% of each dollar earned without improving street sweeping.

A public or charitable provider, by contrast, faces no incentive to advertise or repurchase shares. They are less efficient because managers are shielded from bankruptcy; meta-studies of water operations estimate this at 5-9% of costs (Bel & Warner, 2008). Even at high range, the cash lost from public delivery is still smaller than the combined advertising-plus-buy-back drain on the profit side. Thus, while neither structure is first-best, a government or charity operator is the less costly option.

3.4 High-harm and High-innovation

When hidden cost-cuts can do grave harm and successful innovation yields enormous social gains, sectors run by the government or profit-seekers are not the best. An unregulated profit-seeker unleashes maximum inventive effort, yet the same bonus structure rewards shortcuts that are catastrophic. The Merck Vioxx case (≈60,000 excess cardiac deaths after safety data were withheld) and the Boeing 737 MAX fiasco (346 fatalities linked to an undisclosed software fix) show how fatal that trade-off can be (Graham, 2005; U.S. House of Representatives, 2020).

Government or charity enterprises become more cautious, though the record shows they still bankroll breakthroughs through mission-funded R&D: public agencies financed the key lipid-nanoparticle work behind mRNA vaccines long before private sectors saw profit potential (Mazzucato, 2021; Azoulay et al., 2019). Delayed roll-out of innovations is a cost, yet the expected loss from a single large safety failure, measured in livelihoods, outweighs the lost surplus from slower diffusion. Therefore, while neither pure model is fully satisfactory, government or charity ownership inflicts the smaller welfare loss in this quadrant: it reins in life-threatening shortcuts and still allows breakthrough research through targeted public funding.

4. Synthesis and Conclusion

Sectors where covert cost-cuts can kill or maim, such as elderly care, hospitals, water, and basic education, sit on the high *b(e)* side of the graph; they account for roughly a sixth of OECD's GDP yet define most people's chances of living a long, decent life (OECD, 2025). By contrast, the low-harm/high-innovation corner that pure profit wins in cloud hosting and consumer apps occupies barely 5% of value added.

Inside those life-critical sectors, the stakes are measured not in convenience but in funerals. A single wave of private-equity takeovers in U.S. nursing homes coincided with 22,542 excess deaths because owners thinned nurse staffing to save money (Gupta et al., 2021). Unregulated profit can also spill into the environment we all share: before the Clean Water Act, downstream counties recorded markedly higher disease rates because industrial plants found it cheaper to dump effluent than to treat it (Keiser & Shapiro, 2019). Government and charity-run providers are not the epitome of efficiency, but they protect everyone from needless danger. Here, the absence of a dividend cheque is a life-saving brake.

At the opposite pole—low *b(e)*, high *p(i)*—profit truly does perform a social service: it turns server racks into cheaper computation, packages into one-day deliveries, and software into monthly updates. But the most dazzling cloud discount cannot offset a grandson who loses his grandmother to understaffing in a care home. This is the Rawlsian intuition: a good society first protects people from the worst outcomes before chasing marginal gains for the already secure (Rawls, 1971). Or, in Sen's language, safeguarding basic capabilities ranks ahead of adding bells and whistles to conveniences (Sen, 1999).

Add the numbers and the moral weight together, and the ledger tips toward public and charitable ownership. Profit-led tech markets may shave about US$100 billion off annual IT bills. However, profit-driven failures in trust-based sectors have already taken thousands of lives and imposed several hundred billion dollars in medical, environmental, and confidence-rebuilding costs. When readers imagine the faces behind those statistics, whether a grandparent in long-term care or a child drinking from a safe tap, the balance becomes even clearer. An econo-

my entirely focused on mission, not dividends, may lack some sparkle at the frontier of convenience, but it better honours our shared obligation to keep one another safe, healthy, and included. Behaviour bound by public purpose is, on balance, better for the collective than behaviour driven solely by profit.

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