1.
The 'what': Geographies of value creation

Introduction to value creation

This chapter is dedicated to the concept of value and its role within the framework in the analysis. The concept of value is the core of economic thinking and modern economics. Theories about value creation are central to economic debate, (see a brief presentation in Section 1.1). This contribution, since it is situated in the PM stream of studies, investigates broader meanings of the idea of value, coming from managerial studies contributions. The chapter, focuses with the concept that, according to Porter (1985) and others, value chain arises from contributions of managerial studies to value theory (as seen in Section 1.2). The analysis of the value chain sets the discussion on the micro-perspective of the organization or enterprise. The chapter then focuses on the concept of public value (see Section 1.3) and on social value (see Section 1.4). There is extensive background literature about these two concepts, which is complex and there is no agreement on the meaning of public or social value.

The empirical analysis (see Section 1.5) of this chapter presents the results of qualitative research conducted in 2015 that studied the potential evolution of value chains when applied to new organizations, such as collaborative economic venues. These focused on social value creation instead of economic value, even when economic value was vital to the sustainability of the organizations studied. The last section (Section 1.6) aims to assess the concept of value in the context of analysis, that of SIBs and new tools of social finance.

The aim of Chapter 1 is to both identify which categories of value are at stake when public policies are designed and evaluated, and to deepen the debate on value creation. In discourse about social finance and sector collaboration, value creation – social, public and shared is usually taken for granted. In wider literature, however, there are a number of different perspectives on the concept of value itself. It is important for all scholars to assess their own particular contexts and to decide, according to their field of research and model of intervention chosen, which is the most suitable.

1.1. Economic theories of value creation – A brief overview

What does "value" mean? There are different possible answers to this question. If we consider the dictionary of Business English (2018) [1], we find at least four definitions:

1. "Accounting: The monetary worth of an asset, business entity, good sold, service rendered, or liability or obligation acquired.
2. "Economics: The worth of all the benefits and rights arising from ownership. Two types of economic value are (1) the utility of a good or service, and (2) power of a good or service to command other goods, services, or money, in voluntary exchange.
3. "Marketing: The extent to which a good or service is perceived by its customer to meet his or her needs or wants, measured by customer's willingness to pay for it. It commonly depends more on the customer's perception of the worth of the product than on its intrinsic value.
4. "Mathematics: A magnitude or quantity represented by numbers".

The first two are the most coherent with the debate of this contribution, particularly that of economic value which most closely matches the definition used by most scholars of economic theory. Every economic theory is based on a definition of value and its use in applications. Research questions often regard value as being closely associated with the relationship between prices and goods or services, that is, the value that society gives a product or service. Classical political economists state that value is determined in production. This approach is called the Labour Theory of Value since most associated costs of production are found in labour.

Neoclassical economists argue that value is determined during the act of exchange, and therefore, place value creation in market mechanisms. This approach is called the Marginal Theory of Value. Both of these theories have been challenged and reinforced in contemporary economic debate. What is interesting is that theories of value place the concept of value at the intersection between economy and philosophy. The concept of value addresses basic questions in macro and micro economic equilibrium. Mainly it is concerned with

[1] WebFinance Inc. (2018, August 23). *Value*. Retrieved from http://www.businessdictionary.com/definition/value.html.

the issue of wealth creation, wealth distribution and the functioning of the market. As Taylor (1996) puts it:

> If we were all self-sufficient in our material lives, there would be no problem of economic value. I would produce and consume what I value and you would produce and consume what you value. However, others consume most of what each of us produces and others produce most of what each of us consumes. So the *value* of what you produce in terms of the conditions under which it can be exchanged for the things you consume will determine the level of your material life".

In the pre-monetary era, instead of the price being linked to the value produced, other labour or products were valued alongside services or products that were exchanged. This represented the basis for the labour theory of value that was first questioned by Adam Smith. He proposed a theory about the cost of production that was later developed into the exchange value theory. A brief reconstruction of the key theories of value that have come to characterize this debate follows.

The debate analysed here, focuses on the evaluation of non-economic values, like public value and social value, though in order to fully understand the topic, it is fundamental to set value theory in the wider context of economic debate.

Adam Smith gave prominence to this theory and considered that the fundamental concept of value as given in labour value theory or time value theory of pre-monetary society was insufficient to explain value creation. He said that there were several factors affecting value creation, which were not all wage-driven. Hunt (2015, p. 52) [2] frames this development in the concept of value:

> "[Smith] distinguished between market price and natural price. The market price was the actual commodity price that existed at any particular point in time in a particular market. He believed that it was regulated by the relationship between the amount of the commodity that sellers wished to sell and the quantity that buyers wished to buy at various prices. In other words, the market price was determined by the forces of supply and demand".

Smith (2005, p. 31) [3] developed the debate by stating:

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[2] Hunt E.K. and Lautzenheiser M. (2015). *History of Economic Thought: A Critical Perspective*, Routledge, Abingdon.

[3] Hunt E.K. and Lautzenheiser M. (2015). *History of Economic Thought: A Critical Perspective*, Routledge, Abingdon, p. 53.

"The word value, it is to be observed, has two different meanings, and sometimes expresses the utility of some particular object, and sometimes the power of purchasing other goods which the possession of that object conveys. The one may be called "value in use," the other "value in exchange." The things that have the greatest value in use have frequently little or no value in exchange; and on the contrary, those that have the greatest value in exchange have frequently little or no value in use. Nothing is more useful than water: but it will purchase scarce anything; scarce anything can be had in exchange for it. A diamond, on the contrary, has scarce any value in use; but a great quantity of other goods may frequently be had in exchange for it".

The Smith paradox of diamond-water introduced the issue of what is intrinsic value; that is, the value that is created through the valuer's attitude or judgements. Intrinsic value is distinct from logical decisions. Nowadays, value incorporates other variables, such as brand name, trademark, and copyright, that is usually difficult to calculate and not always accurately reflected in the market price. The concept of intrinsic value expands the debate on value to include non-economic or not priced value, and the difficulties in measuring and evaluating value are discussed throughout the book.

The labour theory of value asserts that the economic value of a good or service is determined by the total amount of socially necessary labour required to produce it. The founder of this theory, Ricardo (1817, p. 5)[4], stated that:

"Possessing utility, commodities derive their exchangeable value from two sources: from their scarcity, and from the quantity of labour required to obtain them".

Ricardo (1817, pp. 75-76) argued that:

"Some proportion of what remains of that value, after paying rent is consumed by the producers, and it is this, and this alone, which regulates profits .... Thus we again arrive at the same conclusion which we have before attempted to establish: that in all countries, and at all times, profits depend on the quantity of labour requisite to provide necessaries for the labourers on that land or with that capital which yields no rent".

In contrast, Marx[5] (Hunt & Lautzenheiser, 2015, pp. 208-209) developed the labour value theory from a very different approach:

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[4] Ricardo D. (1817). *On the Principles of Political Economy and Taxation*, John Murray, London.

[5] Hunt E.K. and Lautzenheiser M. (2015). *History of Economic Thought: A Critical Perspective*, Routledge, Abingdon, pp. 208-209.