

Paul Krugman - New York Times Blog

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John Galt and the Theory of the Firm

Via David Atkins at Digby's place, Bloomberg Businessweek has a great piece about how an Ayn Rand-loving hedge fund guy is driving Sears into the ground.

One quirk, by the way, is that he doesn't meet with his division heads in person; it's all by video link. And look, I've seen that movie — probably a Syfy original, but I don't remember (better than Sharknado, anyway); clearly, this guy doesn't even exist, he's a computer-generated hologram being manipulated by an evil IT guy.

But back to the economics: Eddie Lampert's big idea is that markets and competition rool, so he's forcing the different parts of Sears to compete for resources just as if they were independent firms, with individual division profitability the only criterion for success. According to BB, it's not going well; but they don't get much into the broader issues.

The first issue that should pop into anyone's head here is, if the different divisions of Sears have no common interests, if the best model is competition red in tooth and claw, why should Sears exist at all? Why not just break it up into units that have no reason not to compete?

For that matter, why should any large firm exist? Why not just have small firms, or maybe just individuals, who make deals for whatever they need?

Of course, that's not how we do things. We may live in a market sea, but that sea is dotted with many islands that we call firms, some of them quite large, within which decisions are made not via markets but via hierarchy — even, you might say, via central planning. Clearly, there are some things you don't want to leave up to the market — the market itself is telling us that, by creating those islands of planning and hierarchy.

Now, why exactly that's true — why some things are better done through market mechanisms, while others are better done through at least a bit of command-and-control — is a deep issue. Oliver Williamson (pdf) got a Nobel for helping elucidate some aspects of that issue (although that may not mean much to you, considering some of the people who've gotten Nobels).

The thing is, however, that for a free-market true believer the recognition that some things are best not left up to markets should be a disturbing notion. If the limitations of markets in providing certain kinds of shared services are important enough to justify the creation of command-and-control entities with hundreds of thousands or even millions of workers, might there not even be some goods and services (*cough* health care *cough*) best provided by non-market means even at the level of the economy as a whole?

So in a way Eddie Lampert is being consistent: he's putting his money (or actually his investors' money) where his ideology is, and applying market-worship to the internal management of his own

company.

Of course, the purity of the experiment is sort of spoiled by the likelihood that there isn't actually any such person, that he's just a hologram. But still.

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