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Putting value creation back into “public value”: from market-fixing to market-shaping

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ABSTRACT

In conventional economics, value creation occurs in the private sector with the state limited to correcting for “market failures”. Public management scholars have developed the term “public value” to describe how public sector managers can engage citizens in shaping effective policy. A more ambitious concept of public value rejects the “market failure” framework and puts public value at the centre of the economy. Public value is created by public sector actors creating and co-shaping markets in line with public purpose. This direction-setting role enables different sectors to collaborate to address major societal challenges, such as climate change and inequality.

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1. Introduction

The attempt to justify and describe the distinctive value created by government and public-sector actors has a long intellectual pedigree. Terms such as “public interest” and “common-” or “public good” have been a focus for political philosophers going back to Aristotle (Etzioni 2014). More recently, the concept of “public value” has been developed by scholars in the public management and administration field (see, *inter alia*, Moore 1995; Stoker 2006 O’Flynn 2007; Bryson, Crosby, and Bloomberg 2014; Alford et al. 2017). This concept of public value emphasizes how public sector managers have an important role in mediating between the need for efficient and procedurally correct services and the engagement of citizens in developing public services and policy.

This paper examines the intellectual origins of this notion of public value and argues that it relies on an intellectual framework derived from conventional economics where the role of the public sector is largely reactive, focussed on correcting market failures to enhance economic efficiency. The concept of market failure emerged out of neoclassical welfare economics as an abstract theoretical concept rather than a framework for guiding policy. However, it has been interpreted and employed by policymakers as a justification for public policy intervention and in doing so relegated the role of the public sector to one of “market fixing”. This tendency has limited the theoretical development of the concept of public value and perhaps helps explain why it has not become a more powerful policy frame outside the confines of public administration and the “third way” Anglosphere politics of the early 2000s. We argue public value theory needs to be

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founded on a collective understanding of value creation where markets are viewed as co-created by the private and public sectors, rather than being created by the former and “fixed” by the latter.

Our argument draws upon Karl Polanyi’s (1957) insight that capitalist markets and indeed economic growth itself result from the interaction between different sectors of the economy, including the private sector, the public sector and civil society organisations. Thus, to separate out “public” from “market value” is misguided. Instead, public value should be understood as a way of measuring progress towards the achievement of broad and widely accepted societal goals (for example, a rapid but orderly transition to a net-zero carbon economy). Such goals can only be achieved through collaboration between both private and public sectors, which together, via the process of innovation, co-create and co-shape markets (Mazzucato 2016). As innovation and economic growth have not only a rate but also a direction (Mazzucato and Perez 2015), the role of the public sector in this market co-creation process is to create public value through providing public purpose. The notion of public purpose draws on Galbraith (1973), who warned against the dangers of public activity being captured by private purpose.

The paper is structured as follows: In [section 2](#), we review the concept of market failure and public choice theory as the intellectual basis for the modern framing of debates around public value. [Section 3](#) briefly discusses the emergence of New Public Management as the dominant paradigm in public policy itself and traces how the modern version of public value arose as a reaction to this in Anglo-Saxon democracies. In [section 4](#) we develop our broader notion of public value creation.

2. The economics of public value: fixing markets

Who creates value? The private sector is explicitly acknowledged as a value creator and the process of private firms creating value has been analysed extensively, most notably in economics, business- and management studies. In economics, the production function framework represents the microeconomic theory of value whereby businesses create value by combining capital (both tangible and intangible), labour and technology (Solow 1957; Romer 1989). In business studies, value is understood as being created inside the company by combining managerial expertise, strategic thinking and a dynamic division of labour between different workers (Bloom and Van Reenen 2007). In recent decades a “resource”-based theory of the firm has extended this understanding to how dynamic capabilities are created (Teece, Pisano, and Shuen 1997). Key debates in this literature examine governance structures, for example the limits of shareholder value (Lazonick and Tulum 2011; Kay 2012), and new ways to conceptualise value (Porter and Kramer 2002; Teece 1996).

What is the role of the public sector in the economic theory of value creation? In economics, public actors are recognised as having a role in terms of “fixing” market failures (explored below) or “enabling” value creation by investing in areas like skills, research, and education, which are key, for example, to the development of technology and for a skilled workforce (the labour input). The state can also redistribute value through taxation. But there is no clear role for the public sector to create value itself. Hence, the term “public value” does not exist in economics. Social value can be created

through welfare analysis, tied to how a policy can make different actors “better off” in terms of their utility calculations (Bergson 1938), but this fixing and redistributing function is not about value creation itself.

Market failure theory (MFT) provides a clear delineation of why and when the public sector should intervene in an economy. It has its origins in neoclassical welfare economics and takes the first fundamental theorem (FFT) of welfare economics (Arrow 1951) as its starting point. The FFT states that markets are the most efficient allocators of resources under three specific conditions: (1) there is a complete set of markets, so that all supplied/demanded goods and services are traded at publicly known prices; (2) all consumers and producers behave competitively (that is, all agents are price-takers); and (3) an equilibrium exists. Under these three conditions, the allocation of resources by markets is Pareto-optimal (no other allocation will make a consumer or producer better off without making someone else worse off) and the state has no role at all in the value creation process.

Violations of any of the three assumptions lead to inefficient allocation of resources by markets, i.e. market failures. If markets are not Pareto-efficient, then everyone could be made better off through public policies that correct the market failure. MFT suggests that governments intervene to “fix” markets when the market fails due to positive externalities, negative externalities, and information asymmetries. In the case of positive externalities created by “public goods” (such as herd immunity or basic research) the state must produce what the private sector doesn’t (vaccines and basic research), and in the case of negative externalities (like pollution) the state must devise market mechanisms to internalise external costs (e.g. carbon taxes).

A first point to note about MFT is that it was an abstract theory rather than a formalised framework to guide public policy. Some eminent economists have rejected the market failure justification for policy intervention since the assumptions described above – perfect information, completeness, no transaction costs or frictions – have never been empirically demonstrated (Coase 1960; Stiglitz 2010). Rather, markets are always incomplete and imperfect, and hence not “constrained Pareto-efficient”; they are never in a situation where a government (a central planner) may not be able to improve upon a decentralised market outcome, even if that outcome is inefficient (Greenwald and Stiglitz 1986).

Furthermore, even if we accept the conditions, Pareto efficiency turns out to be practically useless in the real world of capitalist democracies as it implies that a single loser would have a veto over any policy. This led to the development of a more utilitarian “net welfare benefit”-type analysis to guide policy decisions, whereby instead of actual Pareto improvements, the test was whether the net welfare benefits for the winners should be greater than the net costs for the losers (Hicks 1939). This was usually measured by estimates of gross national income in lieu of a better proxy for welfare. This approach then generates a justification for government redistribution via taxation and spending, with the winners compensating the losers. This is one of the main theoretical justifications for cost-benefit analysis (Tucker 2018).

Despite the concerns of some economists, the underlying intellectual framework of MFT began to gain policy traction in the 1960s and 1970s in advanced economies with the emergence of “public choice theory”. This attempted to apply neoclassical welfare economics to the study of political decision-making. Public choice theory considers how

the actions of agents (voters, bureaucrats, and politicians) involved in policy could be considered from an economic efficiency perspective, whereby those agents, including government agents, are assumed to be self-interested in the same way that private markets actors are assumed to be in neoclassical theory (Buchanan and Tullock 1962; Mueller 2004). While in markets the existence of competition and the profit motive tends to enforce efficient decision-making, in collective decision-making processes (i.e. politics and public administration) the same disciplining framework does not exist. Policy making is thus considered to be subject to capture by certain interest groups, in particular those most able to influence policymakers due to reasons of power or money. This is particularly the case because rational voters have little reason to take an interest in political decisions since most voting decisions have only a very tiny impact on the voters' lives: the "problem of collective action" (Olson 1965). In public administration, the lack of competitive pressures leads to "bureau-maximising" behaviour, whereby departments and agencies look after their own survival rather than the "common good".

Given this, even where there are clear examples of market failure, it is not always the case that government intervention would result in a more efficient outcome. Rather, there could also be "government failure", whereby decisions aimed at improving welfare make things even worse than they would have been under conditions of market failure (Le Grand 1991). With this approach, market failure is only a necessary but not sufficient condition for governmental intervention (Wolf 1989). The sufficiency results from an assessment that the gains from the intervention outweigh the associated costs due to "governmental failures" (Tullock, Brady, and Seldon 2002), such as capture by private interests (nepotism, cronyism, corruption, rent-seeking) (Krueger 1974), misallocation of resources (for example, "picking losers") (Falck, Gollier, and Woessmann 2011) or unfair and damaging competition with private initiatives ("crowding out") (Buiter 1977).

From this perspective, there is a trade-off between two inefficient outcomes, one generated by free markets (market failure) and the other by governmental intervention (government failure). The solutions advocated by some economists focus on correcting failures such as imperfect information (Stiglitz 2010). Solutions advocated by public choice scholars (Buchanan and Tullock 1962) focus on leaving resource allocation to markets (which may be able to correct their failures on their own) or the creation of market-type discipline within public agencies.

3. Public value management: a response to new public management

In business schools, mainly in the US, welfare economics and public choice theory influenced the development of "New Public Management" (NPM). In essence, NPM argued that to address the risks of government failure described above, governments should adopt strategies from the private sector to maximise value in the public sector (Hood 1991; Osborne and Gaebler 1993). Key NPM concepts included the need to introduce some equivalent of the profit motive in the public sector to improve performance, for example, efficiency targets; the related "principle-agent problem" whereby there was an inability for the public (citizens) to hold public sector employees accountable in the way shareholders could hold a corporation's managers accountable (ameliorated by contracting out and/or privatisation of services); and the idea that the government should limit itself to technical efforts to counter various forms of "market

failure” (for a more detailed review, see Bozeman 2007, 55–63). In doing so, this would minimise government failure and enhance public sector efficiency by introducing market discipline (Lane 2002).

NPM policies were widely implemented in advanced economies in the 1980s and 1990s, in particular in the UK, New Zealand, and Australia (Hood 1995). By the mid-1990s, however, concerns were growing about the effectiveness of this policy regime. The term “public value” first appeared in the public administration/public management context as a response to the perceived weaknesses of public choice theory and NPM in steering public policy. Scholars at Harvard University’s Kennedy School of Government and Harvard Business School, notably Mark Moore (1995), working with public sector executives, developed a strategic framework for public sector managers as an alternative to NPM. Moore argued that a strategy for creating public value and for introducing new policies involves more than simply importing private sector practices and market discipline. Rather, it concerns the management of trade-offs between three domains: 1) the identification of the public value an organisation seeks to produce (which will be distinctive from that which the private sector produces); 2) the “sources of legitimacy and support” that are relied upon to authorise the organisation to take action; and 3) the resources necessary to sustain the effort to create that value. In contrast to private sector strategies, strategic management in the public sector has a longer-term focus, attends to larger issues with significant impacts on performance rather than incremental issues that affect productivity, and concentrates on ends rather than means (Moore 1995, pp. 162–184).

Particular emphasis is placed on the role of the public manager in managing policy development and negotiating (public) purpose with politicians, leading public deliberation and “social learning”. The political and philosophical aspects of public performance management are at least as important as the technical aspect. To produce value, public officials must consider the entire “value chain”, which starts with inputs and moves to the production processes (e.g. policies, programmes, activities) used to transform the inputs into outputs, which then affect a client (e.g. citizen, beneficiary, etc.), which leads to the social outcome that was the intended aim of the activity. In contrast, NPM approaches usually focus on just one part of the value chain; for example, traditional-line item budgeting is focused almost exclusively on “inputs” (e.g. staff costs).

Moore’s understanding of public value proved to be especially influential in English-speaking countries, mainly because this is where NPM influence was also strongest (Stoker 2006). In the UK, the New Labour government, informed by Tony Blair and Bill Clinton’s “Third Way”, began to develop the idea of public value as a yardstick for measuring policies and institutions’ effectiveness. Kelly, Mulgan, and Muers (2002), who were advising Blair’s government, argued that public value should be concerned with outcomes (rather than outputs), including equity, ethos and accountability; the means used to deliver these outcomes; and with the generation of trust and legitimacy in government. Public value is not created by governments through the provision of services, laws and regulations, but “... determined by citizens” preferences, expressed through a variety of means and refracted through the decisions of elected politicians’

(Kelly, Mulgan, and Muers 2002, 6). This approach to public value contrasted with NPM by putting the public itself, via democratic influence and public deliberation, at the heart of the concept.

Preferences can also be incorporated into policy by more actively involving citizens and service users in the design and delivery of services. To enable this, public providers must become more visibly responsive and more participatory than merely consultative. There is a need for more direct, innovative and creative opportunities for users to participate in the “script” of public services (Leadbeater 2004). Users need to receive services according to their needs, but also to play a role as “co-designers” and “co-producers” in the shaping and delivery of that service.

This notion of “co-production” (Ostrom 1996) became popular in academic and think tank circles in the UK in the mid to late 2000s (Bovaird 2007; Stephens, Ryan-Collins, and Boyle 2008). To enable co-production, an “adaptive state” would be required with public sector organisations needing to develop the capacity to learn for themselves and “factor in aspects of the authorisation environment that ensure responsiveness to changing public needs” (Bentley and Wilsdon 2003). User-shaped and personalised services are, therefore, valuable sources of public value.

Particular experiments on building public value through new forms of engagement between the state and citizens have been informed by this approach. The work by the Government Digital Service (GDS) team in the UK Cabinet Office made it a point to reject the idea from New Public Management of citizens as “customers” and “clients”, focusing instead on the role of citizens as users. This involved completely redesigning GDS, and its main product gov.uk, to be focused on user needs and user design (Greenway et al. 2018).

Limitations of public value management theories

Broadly speaking, the public management literature described above reacted to the dominance of New Public Management regimes not by challenging the fundamental assumptions lying behind notions such as market failure, but by attempting to develop frameworks that substitute the “consumer” for the “citizen” and thus bring politics/democracy back into the process of public sector decision-making. Public value is then basically conceptualised as a “third way” of justifying the existence of public services and public managers beyond traditional Weberian-type top-down bureaucratic management and new public service management regimes (Pollitt and Bouckaert 2004). Public value is theorised as a means of reconciling the tension between democracy and bureaucracy, the basic idea being that public servants must be accountable both to politicians and also to the wider public/consumers of services – the “authorisation environment” (Moore 1995).

The implication in regard to measurement is that the public itself must be an active participant in the measurement of public value. Much of the literature is focussed on how best to do this, for example, opinion polls, stakeholder workshops, “consensus conferences”, citizens’ juries. Relatedly, economists have attempted to “monetise” public value via techniques, such as contingent valuation (see Cowling 2006 for a review). But there is little consensus on which of these forms of engagement is most accurate or useful. There is also concern that the public tends to hold contradictory views on certain issues at the same time, that views can change over time and that there is a danger that such an

approach paradoxically undermines standard democratic processes and power imbalances (Feldman and Khademian 2002; Rhodes and Wanna 2007). Measurement is also complicated by the fact that public value creation tends to occur at the end of the value “chain”, e.g. when people’s lives improve (outcome rather than output), potentially many years after the policy was enacted. This contrasts to the private sector where the value can be seen to be created upstream at the point of purchase of a product.

A number of critiques of public value as applied to public management (henceforth PVM) and public service reform have emerged. A common critique is that it is excessively vague (Oakley, Naylor, and Lee 2006; Rhodes and Wanna 2007; Sekera 2016). Various different proponents have argued it should be seen as a “paradigm”, a “model”, a “heuristic device”, a “story”, and that “perhaps the ambiguous nature of public value and its various applications fuels its popularity – it is all things to all people.” (Rhodes and Wanna 2007, 408). Some scholars have argued that PVM can be seen as a political project, which attempts to legitimise neo-liberal theory and market rationality, and downgrade democracy. Implicit in the theory, it is argued, is the idea that public managers are being asked to “rebel against standard politics and usurp the democratic will of governments” (Rhodes and Wanna 2007, 413). The result of this may be that the citizen participation process becomes a means of enhancing the legitimacy of public managers rather than a truly democratic process (Dahl and Soss 2014). According to this critique, PVM avoids foundational political economy questions of power and conflict and “substitutes ‘managed democracy’ for more democratic forms of rule based on shared power” (ibid, p497).

A further limit with PVM is that it restricts its domain to that of public services and public sector management rather than the more ambitious goal of a broad framework for public and economic policy, including, for example, science and innovation policy, industrial- and macroeconomic-policy.

4. Towards a theory of collective public value creation

A more positive theory of public value requires beginning with a notion of the public good not as a correction to a failure, but as an end in itself; an objective that can only come about if linked to a process through which value is created. In this sense, it needs a new building block for guiding and legitimising public policy. As indicated by Kenneth Arrow (1962), while a market failure approach can be utilised to understand why, for example, private firms underinvest in R&D, it is not so useful in guiding the direction of public investment in R&D, because of the inherent uncertainty involved in the outcomes from such investment. Indeed, Arrow called for alternative approaches to analysing public investment and policies for innovation.

Critically, the market failure justification implies that pure private markets/private goods can exist independently of public or collective action. While the role of institutions are admitted (North 1991), the role of different voices coming together to form the notion of the public itself is left mainly to sociology, not economics. Nelson (1987) notes that, “There is no satisfactory normative theory regarding the appropriate roles of government in a mixed economy” (p. 556) and no theory that captures the complex variety of institutional arrangements that people have developed to solve collective problems. Just as pure public goods are rare, so too are pure private goods. Babysitters

or household sharing of everyday appliances such as lawnmowers involves no government intervention or regulations, but does involve collective or “public” negotiation. Hence, the “market failure” dichotomy is not particularly useful.

Markets as outcomes

We propose an alternative approach that begins with the notion of public value as collectively generated by a range of stakeholders, including the market, the state and civil society. Key here is the emphasis on value creation at the core: not “public” value but value itself – with a clear delineation of the role of the different actors that are central to its formation. While in economics value is, in essence, created inside businesses and only facilitated by the public sector, in this view value is co-created and requires a stakeholder understanding of capitalism itself (Hall and Soskice 2001).

This view draws on the work of economist Elinor Ostrom (2005) who described the very complex structures and relationships of various types of institutions. She shows that a radical state-private division is, to use her word, barren. In developed economies, there are many types of organisations. Non-partisan government regulators, state-funded universities and state-run research projects, for example, are quite different. Besides, the crude binary state-private division fails to capture the many ways in which all institutions create and destroy value. In addition, Ostrom’s (1990) emphasis on common pooled resources and her interest in shaping systems, so that they take into account collective behaviour, can help shape new policy tools.

This more collective view also benefits from a different understanding of the market itself, with the market as an outcome of the interactions of individuals, firms and the state, as discussed in the work of Karl Polanyi (1957), and “embedded economies”, as discussed by Granovetter (1985). Polanyi argues that capitalist market societies are constituted by two opposing movements – the laissez-faire movement to expand the scope of the market, and the protective countermovement that emerges to resist the disembedding of the economy that the so-called “self-regulating market” entails. As Polanyi (1957, 146) noted, “The road to free markets was opened and kept open by an enormous increase in continuous, centrally organized and controlled interventionism . . . Administrators had to be constantly on the watch to ensure the free working of the system”.

All groups in society have participated in this project, including the capitalists themselves, who throughout history have acted to effectively “save capitalism from itself” (ibid: 45–70). In this sense, the work of trade unions in fighting for an eight-hour working day and workers’ rights (even those benefitting non-unionised workers) are fundamental to market creation.

If value is created collectively a first question becomes what capabilities, resources and capacities are needed for this value to be created inside all the different organisations, including those in the public sector, private sector and civil society? In the same way that a theory of private value creation benefits from a resource-based theory of the firm (Penrose 1959), so does a public value notion. Indeed, it is by sidelining the notion of value as only created in business and facilitated or redistributed by the public sector that the question of capabilities is missed. The work by Teece (1996) on the dynamic capabilities of the firm becomes equally necessary for the public sector (Kattel and Mazzucato (2018)).

A collective theory of value creation requires understanding investment and production capacity in all actors. Indeed, a theory of public value needs to also understand the productive capacity and capabilities of the state. And if the state loses that capacity it will lose, its “absorptive capacity” – hence be unable to understand technological and market opportunities (Cohen and Levinthal 1990). Public policies should not be seen as simple corrections to the (market failure) problem of positive externalities, but as objectives in and of themselves. These requires imagination, investment and capabilities. One of the biggest lessons of the Covid-19 crisis was that state capacity to manage a crisis of this proportion is dependent on the cumulative investments that a state has made on its ability to govern, do and manage (Mazzucato and Kattel 2020). While the crisis was serious for all, it was especially a challenge for countries that ignored the needed investments in their dynamic capabilities (Kattel and Mazzucato 2018).

Similarly, instruments like taxation are no longer about correcting externalities, but about market creation itself. Adam Smith’s notion of the free market was free from rent and this distinction between rent and profits requires tools to incentivise creation not extraction of value (Mazzucato 2018). Thinkers such as Ricardo, Mill and even Adam Smith recognised that unfettered markets were often inefficient, prone to capture by special interests and could have negative distributional outcomes without ongoing intervention by the state. In particular, there was a distinction made between productive profits on the one hand and economic rents that represented unearned income deriving from arbitrary control over resources, on the other. These authors argued that the primary role of taxation, for example, rather than internalising externalities caused by identified “market failures”, should be to tax away rents accruing from the monopolistic ownership of factors of production, in particular, land (Ryan-Collins, Lloyd, and Macfarlane 2017, 37–64). In the classical view, rents did not accrue from market “imperfections” as in market failure theory, but from the inherent imbalances in economic and political power that characterised dynamic capitalist economies.

Thus, the focus is on the economic and political processes, institutions and conditions that enable public value creation – and equally on how to counter public value extraction – across sectors and economies (Mazzucato 2018). The role of the state is key here, since it is the only institution with the power to shape markets and direct economic activity in socially desirable directions – or “missions” – to achieve publicly accepted outcomes (Mazzucato 2013, 2016). Similarly, many government interventions enable markets to function, such as legal codes, public policies, antitrust policies, university scientists and physical infrastructure (Nelson 1987, 550; Deakin et al. 2017). In many cases, government “is better regarded as a useful actor in its own right, and even as a precondition for other institutions to work decently, than as an actor reluctantly involved because they do not” (Nelson, 1987p. 556).

Evolutionary and institutional economists and economic sociologists have paid particularly close attention to the interaction between the state and commercial actors in the generation of innovation and economic growth. Markets are always institutional constructs and this requires asking not why markets fail, but rather what conditions are required for “getting the work done”? (Nelson 1987). In particular, in the area of technological development, governments have played a key role in promoting innovation (Perez 2010; Block and Keller 2011; Mazzucato 2013, 2016). The broad and deep presence of public organisations across the entire innovation chain requires understanding the more active role that public organisations play in providing patient, long-term finance (being “investor of first

resort”) and in areas of high risk/uncertainty, with the risk-averse private sector entering only later. This applies across range of key sectors including IT (Block and Keller 2011), biotechnology (Lazonick and Tulum 2011), nanotechnology (Motoyama, Appelbaum, and Parker 2011) and renewable energy (Mazzucato and Semieniuk 2018). Research in the US suggests that, contrary to the public perception, private Venture Capital funds have focused on financing firms mid-stage, which had previously received early-stage financing by public programs, like the SBIR program (Keller and Block 2013).

Whereas mainstream economic theory has emphasized the role of state in supporting the supply-side of the production and innovation process (e.g. by providing the public goods of good education and training and early-stage R&D funding) evolutionary economists have pointed to the key role of demand side activities in steering the direction of innovation, including procurement (Edler and Georghiou 2007; Uyarra and Flanagan 2010; Lember, Kattel, and Kalvet 2013). A simple analysis through the existence of positive or negative externalities is then not enough to understand this entrepreneurial role, a role that, for example, was essential for all the technologies that are in our smart products (Internet, GPS, mobile phones, etc.) (Mazzucato 2013).

Public value in this conception is broader than the version developed in the public administration literature, which largely confines itself to the delivery of public services – or a legitimisation of the role of the public servant – rather than the role of government in shaping effective markets and the wider public outcomes that are broadly recognised as desirable. Such outcomes would include ecological sustainability, a more even distribution of wealth and income, high-quality care for the elderly and fulfilling work.

Here, the state is viewed as having a potentially important macroeconomic role, going beyond a simple Keynesian counter-cyclical or stabilisation function, with a stronger directional push (Mazzucato et al 2020) Indeed, many of the technologies listed above came from “mission-oriented” investments where the state laid down the path – to go to the moon or in modern days to fight climate change (Mazzucato 2021). Missions require different actors to come together, so while the state can play the role of setting a direction, the bottom-up solutions that follow create an economic multiplier from cross-sector investments. This is then not a top-down model of public administration but one where decentralized group of public agencies work together on major challenges to provide R&D funding and overcome network failures; a “developmental network state” (Block and Keller 2009; see also Breznitz and Ornston 2013).

Public value should thus be as much concerned with the direction of growth (and the macroeconomic implications) as with the microeconomic structure of government agencies. The question should be how to shape and co-create markets, not just how to correct them.

A new framework

This notion of collective value creates a new agenda to reinvigorate a theory of public value that can address the production of goods and services in the economy (including public services), where the “public” part of that production engages in questions that involve both the economic sphere as well as the organisational sphere. The focus is on how public organisations interact with private and civil society actors to deal with the major challenges facing society – with a focus on the need to collaborate and interact widely across the economy.

For this purpose, a mission-based approach where direction setting is followed by cross-actor, cross-sector and cross-disciplinary interactions provides a useful way forward (Kattel and Mazzucato 2018; Mazzucato 2021). Missions can focus on the interactions between different actors over specific landscapes (the health sector, the creation of liveable cities, the digital economy) but with a special eye on dynamic interactions.

If public value is to truly serve the public, finding new interactive ways to engage with the public is key. Instead of seeking consensus, it should be acknowledged that public value is inherently contested in the political arena where “differing interests are resolved and conflict and argument lead to decision and action” (Stewart and Ranson 1988). Finding ways for public policy to interact in genuine ways with citizens and social movements will be key part of any society’s ability to collectively create value (Leadbeater 2018). Here, of course, there are many lessons that can be learned from the contributions from public value theory described earlier. In particular, the concept of citizen involvement and co-production could, for example, be central to how to think about the co-creation of mission-setting (Mazzucato and Semieniuk 2021; Kattel et al. 2018).

Furthermore, if the public part of value creation is guided by different criteria from the private sector, it must also be evaluated differently. Rather than checking which market failure has been corrected, the question is what form of new market has been created? New evaluation indicators are needed to capture the economy-wide benefits of such policies, including the (un/intended) dynamic spillovers and the “additionality” – making things happen that would not have otherwise occurred. For this purpose, it is essential to move beyond cost-benefit analysis and allocative efficiency approaches to embrace a more dynamic notion of efficiency (see Kattel et al. 2018 for an elaboration). Table 1 captures key differences in evaluating a “correcting market failures’ vs ‘creating’ public value’ process.

Table 1. Approaches to public value: correcting failure vs. creating public value.

	Correcting failures	Creating public value
Justification for the role of government	Market or coordination failures: Public goods Negative externalities Imperfect competition/information “public value failure” (Bozeman)	All markets and institutions are co-created by public, private and third sectors. Role of government is to ensure markets support public purpose, also by involving users in co-creation of policy
Business case approach	Ex-ante cost-benefit analysis employing allocative efficiency, i.e. assuming all else remains equal (prices/relationships etc.) and incorporating possibility of government failure.	Focused on systemic change to achieve mission – dynamic efficiency (including innovation, spillover effects and systemic change).
Underlying assumptions	Possible to estimate reliable future value using discounting and backward-looking datasets. System is characterised by equilibrium behaviour	Future is uncertain because of potential for novelty and structural change; system is characterised by complex behaviour, non-linear feedback loops
Evaluation	Focus on whether specific policy solves market failure and whether government failure avoided (Pareto-efficient).	Ongoing and reflexive evaluation of whether system is moving in direction of mission via achievement of intermediate milestones and user engagement. Focus on portfolio of policies and interventions, and their interaction.
Approach to risk	Highly risk averse; optimism bias assumed	Failure is accepted and encouraged as a learning device

5. Conclusion

In this paper, we have argued for a rethink of the concept of public value that broadens its application beyond the public management and administration sphere. To do so, we argue it is necessary to reject the “market failure” framing under which public value scholars and policymakers have developed the concept. Rather than seeing public value as something that occurs when the public sector corrects market failures or successfully mediates the trade-off between democracy and efficiency, we argue public value creation must involve the public sector setting a direction and public purpose for private and public actors to collaborate and innovate to solve societal problems. This is a “market-shaping” and/or “market-creating” role rather than a “market-fixing” role. It is inherently positive rather than negative in framing. It also requires an ontological shift – rather than markets being seen as abstract phenomena that “work by themselves”, they are better understood as outcomes of the interactions between public and private actors, following Karl Polanyi.

This is not to say that the existing literature on public value does not have its strengths, in particular, the focus on citizen engagement and co-production. For direction setting and market shaping to be democratically legitimate requires bottom-up pressure and distributed experimentation to complement and steer ambitious leadership. But it’s clear that the immense challenges of modern-day capitalism can only be confronted through different actors coming together to co-create value by each investing time, energy and imagination on how to solve problems. To do so will require the public sector to develop new dynamic capabilities to explore and experiment, and to learn by trial and error, within the context of the pursuit of societal missions. This can be enabled by an evaluation framework that encourages risk taking, accepts failure and evaluates progress against the achievement of long-term goals rather than on addressing specific market failures.

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