



Monopsony and Social Innovation—Predictably Bad Outcomes from Bad Processes

Stephen Goldsmith | March 3, 2010

As I write this column I am listening to my iPod and typing on my new Dell computer. Both of these products impressed me from a range of competing choices, so I utilized my resources and purchased them. As a consumer, I benefited from the forces of competition that pressed these technology companies to create better, faster, cheaper products and introduce them quickly into the marketplace. Contrast that with the way we deliver and consume social services—from education to homeless services, from welfare to job training.

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Contrast that with the way we deliver and consume social services—from education to homeless services, from welfare to job training. Government dominates the sector, sometimes monopolizing the delivery system and other times functioning as a monopsonist, acting as the sole purchaser. A person in need of services rarely has any choice about where they get help, and the established government and nonprofit providers fight furiously to preserve their incumbency.

Unsurprisingly change occurs slowly in this area. Even when new techniques for delivering social services work, they rarely scale up quickly—if at all. That's because a political economy has replaced a market economy, and the incentives are very different. The result is ineffective spending on education, job readiness, and similar services that are supposed to benefit the young and poor. Despite the resources expended for their benefit, the poor still lack market power and still lack the sort of choices that drive innovation.

Education is the poster child for this problem with less than 50% of minority children graduating from urban high schools. Leaving school without marketable skills, the unemployment rate for black youths nationwide is nearly 35%. Despite being targeted by a host of educational and social programs, these young people are growing up ill-prepared for economic success and ill-equipped for participation in democracy.

Because the public sector dominates social services, it exhibits the sort of institutional inertia inherent in government action. But the poor performance of our public institutions is nearly always blamed on insufficient funding, rather than the failure of the program to actually meet the public need.

The mechanism of a political economy produces the perverse consequence that poor performance often qualifies an agency or program for more funding. For example, when I was mayor of Indianapolis, every year the central city public school system would lose students and gain revenue (In contrast, poorly



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performing private schools would simply disappear, allowing for the ‘creative destruction’ that makes room for innovation).

So, what’s the alternative approach? How can we induce innovation and new delivery systems that can right the ship in time to avoid a collision, not only with the iceberg of public indebtedness, but in time to prevent another generation being lost to social dysfunction and intergenerational dependence?

The answer is to choose policies that move young people from being passive consumers of public services into tax-paying, productive members of society.

Social spending, including education and social services must be engineered to create new wealth and net new taxpayers. Innovation in education and social service areas requires both demand and supply tools. This means giving users of services—including students—more choices so they can drive demand. But it also requires that federal, state and local government force open the door so that a new set of social entrepreneurs can demonstrate and scale promising approaches. In *The Power of Social Innovation*³, my coauthors and I highlight several examples of these principles in action.

Turning Out the Status Quo in New York City

New York City Mayor Michael Bloomberg has pried open the door for innovation through the use of three tools—rigorous performance management of existing government systems, creation of a significant innovation fund in the mayor’s office, called the Center for Economic Opportunity’s (CEO) Innovation Fund and through the injection of new providers and social entrepreneurs into the New York Schools system.

Mayor Bloomberg created CEO in 2006 to design and execute anti-poverty initiatives. CEO partners with an array of city agencies to study what works in poverty reduction across the country and to adapt innovative ideas for application in the city. The Innovation Fund provides seed capital for these projects—and the fund is able to quickly enhance or eliminate funding for an initiative depending on its impact.

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Also beginning in late summer 2002 Bloomberg charged school superintendent Joel Klein with turning around the city’s struggling school system. The effort was dubbed “Children First ” to signal a departure from the “old way ” of putting the needs of the adults in the system ahead of those of the children they were there to serve.

As expected, Klein faced opposition from strong political interests, including labor groups as well as from the school system’s own bureaucracy.

Undeterred, Klein rejected many of the institutional education players who had dominated central decision making and recruited instead advisers predisposed to take risks and innovate, many of whom came from the top levels of fields outside education. From Caroline Kennedy to Jack Welch to former investment bankers and management consultants, Klein surrounded himself with talent and expertise that brought a fresh way of looking at school reform.

Klein wanted to start a number of more independently governed public schools, and partner, force more principal authority and accountability and partner with creative nonprofits to widen school choice by introducing more charter schools.



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Klein aggressively pursued these options to open 333 new public schools, created a principal academy and school-based budgeting, and created more than eighty charter schools between 2002 and 2009. The new schools, most often created by breaking down large high schools into smaller “schools within schools,” utilized a nonprofit organization-- New Visions for Public Schools-- as the key school developer. All told, New Visions created ninety-six small schools — a maximum of five hundred students per school — with \$70 million in outside funding.

In creating these schools, New Visions set a core performance metric. Dubbed “80/92,” it challenged all schools in the initiative to graduate at least 80 percent of their students and reach 92 percent attendance rates. A New Visions study conducted in year five showed a 78.5 percent on-time graduation rate for the class of 2006 (compared with a city-wide rate of 60 percent) and an 85 percent average attendance for the 2005–2006 school year.

Innovation as a Core Value

These efforts aren’t without their critics since progress is often uneven. Defenders of the status quo and others often insist on waiting long periods for proof of concept, but this is counterproductive. Too often we have seen civic entrepreneurs whose new ideas, passion, and organizational ability swept away hopelessness and replaced it with opportunity. In so doing, they prove that energetic and creative citizens can produce truly important results. But there will be bumps in the road. Just as some new products will fail in the market—think the Edsel or New Coke—without experimentation, the stagnation of existing but ineffective institutions guarantees failure of a different sort.

We need to force innovation into social and educational delivery systems. Innovation means

more than just new or larger programs. That can take the form of innovative new policies, technologies that makes existing systems work better, or the introduction of new providers and the competitive dynamic of choice that drives innovation in the marketplace.