Reimagining the Platform Economy

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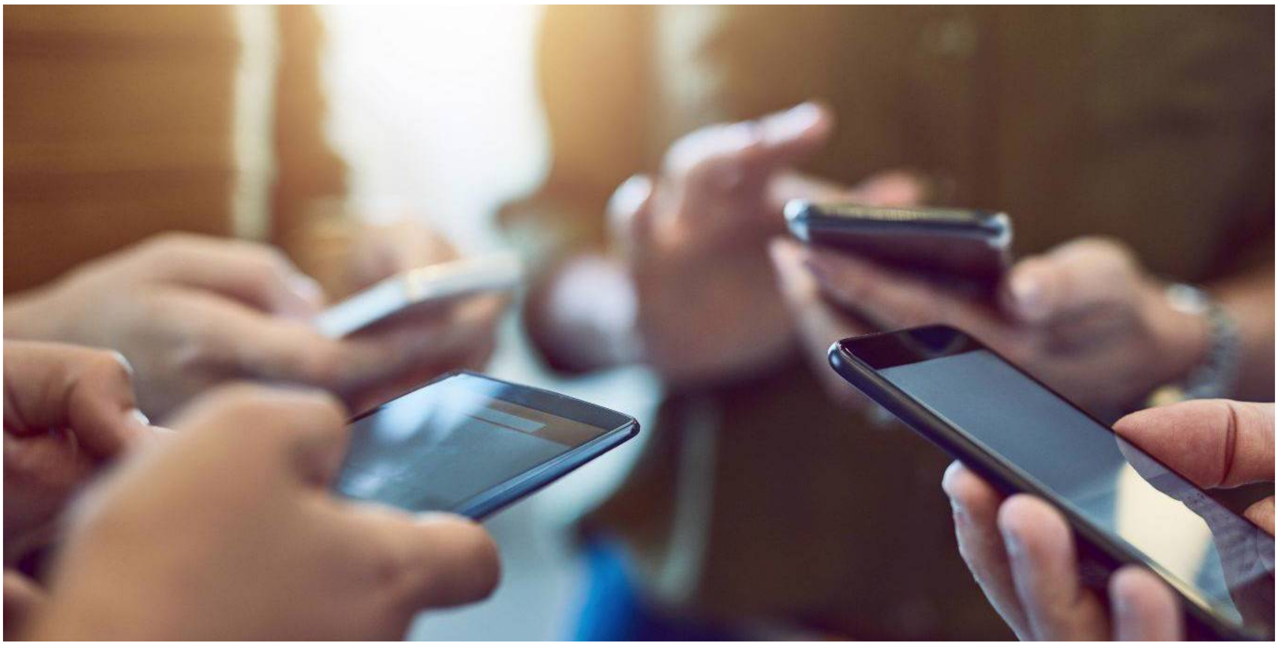

Today's digital economy has grown up around a business model of data and wealth extraction, confounding traditional antitrust paradigms and undermining the public and social value that otherwise could be derived from technological innovation. The state can redress these problems, but only if it reclaims its proper role.

LONDON – As Donald Trump's presidency careened to its ignominious end, with a mob of his supporters storming of the US Capitol, Facebook and Twitter banned the US president for inciting the violence. With that act, the scope of the political power wielded by Big Tech became impossible to ignore.

Whether these platforms have too much political power is a debate that is just beginning. Their outsize economic power, though, is unquestionable. The combined market capitalization of the five largest US tech platforms – Alphabet (Google), Amazon, Apple, Facebook, and Microsoft – rose by $2.7 trillion in 2020. Following the addition of Tesla to the S&P 500, the Big Six tech firms now represent nearly one-quarter of the index's valuation. And with the spread of COVID-19, the leading digital platforms have become de facto essential service providers, enabling a mass transition to remote and isolated living.

And yet the political pressure on Big Tech has continued to rise. There is a growing consensus that platforms have been abusing their power, driving profits by exploiting consumer privacy, crushing the competition, and buying up potential rivals. In Germany, a provisional ruling by the Federal Court of Justice against Facebook has set a precedent for disabling data-extractive business models more generally. In the United Kingdom, an expert panel is completing an inquiry into whether giants like Google should be broken up, and how regulatory institutions and capabilities can be strengthened to rein in Big Tech. And in Australia, the government is following through on a number of regulatory proposals designed to redefine its approach to the industry.

Moreover, the European Union has proposed two major legislative packages – the Digital Services Act and the Digital Markets Act – to overhaul its tech governance regime. The OECD is seeking to establish new global standards for measuring the value derived from digital innovation and taxing the leading platforms. And in the United States, a long congressional investigation has, like the EU authorities, concluded that the leading tech firms are not merely engaging in ad hoc anti-competitive behavior, but rather have amassed so much market power as to require extensive regulatory scrutiny.

With US President Joe Biden's administration focusing first and foremost on tackling COVID-19, questions about the future of tech regulation remain on the backburner – for now. But how aggressive will the US be in considering new regulations when Biden's team shifts its attention to Big Tech? What capabilities does effective regulation require? US leaders must seize the unique opportunity they have to shape global standards. But to do so, they will have to revisit antitrust enforcement as well as look beyond it. The question is not just what a better platform economy would look like, but what kind of innovation ecosystem is needed to build it.

No Free Lunch

New schools of antitrust theory are already racing to fix the cracks in the current legal paradigm. Since the 1970s, the principle of consumer welfare has dominated antitrust jurisprudence, based on the assumption that the best way to assess the health of a market is to identify practices that disadvantage consumers. But with Google, Amazon, Facebook, and others offering "free" services to their users, the calculus has changed. Even if the leading platforms were to pay their users, they could still end up ahead, because one of the main sources of value in these markets lies in amassing user-generated data with which to sell or drive targeted advertising.

Regulators therefore need to look at the other side of the equation, particularly the supplier marketplace. Even if consumers are not being harmed directly, there is the question of how Google treats content creators, how Amazon treats sellers, how Uber treats drivers, and how Facebook treats merchants.

With a monopoly position in internet search, Google can direct traffic to its own properties, displayed to users in order to capture advertising revenue that previously went to an ecosystem of web-content providers. With a wealth of data on buyer preferences, search queries, and so forth, Amazon can displace existing merchants by offering its own comparable product, requiring them to compete for visibility by purchasing Amazon advertising (or hiking its price). The concern is not simply that platforms might extract too much and provide too little to users; it is that they can leverage their position to disempower and exploit the merchants and content providers in their ecosystem.

Because digital platforms tend to fall outside of the existing antitrust framework, we need a new tool kit, with new metrics of market power, and a clear definition of platform power in particular. But outdated theories are only one part of the story. When modified to account for new realities, market-power arguments tend to conclude that the major platforms should be broken up, and key mergers rolled back. But if we push these new theories further, it also follows that some digital services should be considered social infrastructure.

In any case, the economics of platforms is different from the economics of traditional offline and one-sided markets. Policymakers therefore need to reconsider some of their most basic assumptions, asking themselves whether they are even focusing on the right things.

Cui Bono?

A key challenge is to determine how the value of data diverges from the value created by providing a data-generating service. Platforms have the power to shape how decisions are made, which in turn can alter the value of the data being amassed. The implication, as Google co-founders Larry Page and Sergey Brin foresaw in a 1998 paper, is that advertisers or any other third-party interest can embed mixed motives into the design of a digital service. In the case of internet search, the advertising imperative can distract from efforts to improve the core service, because the focus is on the value generated for advertisers rather than for users.

As this example shows, it is necessary to ask who benefits the most from the design of a given service. If a platform's core mission is to maximize profits from advertising, that fact will shape how it pursues innovation, engages with the public, and designs its products and services.

Moreover, it is important to understand that even if antitrust authorities were empowered to break up companies like Google and Facebook, that would not eliminate the data extraction and monetization that lie at the heart of their business models. Creating competition among a bunch of mini-Facebooks would not weed out such practices, and may even entrench them further as companies race to the bottom to extract the most value for their paying customers.

Given how these practices have evolved within the digital services sector, policymakers need to go further, reimagining the foundations and principles on which the platform economy rests. Otherwise, grand efforts to dismantle dominant players or transform platforms into social infrastructure will simply make extractive practices more diffuse, in the process normalizing them as intrinsic features of digital markets.

But digital markets do not *have* to be extractive and exploitative. They could be quite different, but only if we ourselves start to think differently. We need to recognize, as Adam Smith did, that there is a difference between profits and rents – between the wealth generated by creating value and wealth that is amassed through extraction. The first is a reward for taking risks that improve the productive capacity of an economy; the second comes from seizing an undue share of the reward without providing comparable improvements to the economy's productive capacity.

The Roots of the Platform Economy

For the past half-century, corporate governance has rested on the notion of shareholder value. The result is an economy in which it is increasingly important to differentiate firms that are actually driving innovation from those that are not. There is no shortage of firms that are engaged merely in financial engineering, share buy-backs, and rent-seeking, extracting gains from actual risk takers while under-investing in the goods and services that generate value.

The digital economy has accelerated this conflation of wealth creation and rent extraction, making it all the more difficult to differentiate between the two. The issue is not just that financial intermediaries are shaping how value is created and distributed across firms, but that these extractive mechanisms are embedded within user interfaces; they are baked into digital markets by design.

The dominant platforms have been able to orient the broader innovation ecosystem around the technologies of rent-seeking and wealth extraction. Recommendation algorithms mediate between advertising incentives and microtargeting demands (encouraging practices that lead users to give over more data for fewer benefits); and user interfaces are designed to maximize data collection by fostering addiction.

The proliferation of such practices shows why we need to focus more on the "how" of wealth creation, and less on the "bottom line." An economy that produces wealth from privacy-respecting innovations would not function anything like one that encourages the systematic exploitation of private data.

But building a new economic foundation will require a shift from the shareholder model to a stakeholder model that embodies a deeper appreciation of public value creation. Wealth and other desirable market outcomes are collectively co-created among public, private, and civic domains, and should be understood as such. Policy analysis and corporate decision-making can no longer be guided solely by concerns about maximizing efficiency. We now also must consider whether wealth generation is actually improving society and strengthening the ability to respond to social challenges.

Wealth Without Value

After all, the fact that platforms are creating wealth does not mean they are creating public value. A firm with access to massive amounts of data and network effects could, in theory, use its position to improve social well-being. But it is unlikely to do so if it is operating under a framework that prizes the generation of advertising revenue over everything else, including the performance of products and services.

Unfortunately, the incompatibility of these various objectives is not always clear to see; and even if the antitrust paradigm is fine-tuned to account for value and data extraction, legal and regulatory action at the level of individual platforms may not be enough. The Big Tech giants did not emerge from a vacuum. Many, in fact, are reaping the rewards of risks taken earlier by entrepreneurial states.

Today's platforms evolved according to the logic of both the underlying digital technology and the overarching innovation ecosystem, which itself has been shaped to fit the advertising business model. In this context, if we tackle market power without addressing value extraction, or if we address value extraction without tackling market power, the job will remain incomplete.

Developing a different kind of platform economy will require pushing for bold industrial and innovation policies to shape the direction of technology and of the innovation ecosystem. For example, imagine an economy where public procurement and common market standards altered not just privacy protections but also the ownership of data. Under the current dispensation, we are all uncompensated data laborers. Our decisions online and even offline – from our search histories and physical locations down to every movement of our cursors – fuel an engine of increasing returns that accrue to a few dominant firms.

But the foregone compensation, here, is not really about remuneration (the value of one's individual data production is miniscule, amounting to perhaps a few dollars per year). Rather, it is about the broader effects on digital services, which could be improved and made even more valuable if users were the top priority. This vision of structural change is not necessarily anti-Apple, anti-Google, or anti-Amazon. It is an argument against any firm whose primary business is to privatize public value through extraction, privacy violations, and similar other practices.

The State Must Stand Up

There are a number of ways to start addressing these deeper issues. We would point first to the need for coordinated procurement, industrial, and regulatory policies to set the direction – rather than just the rate – of innovation. The key is to develop a better understanding of the state's entrepreneurial potential for creating and shaping markets. Historically, public investment has created the foundation for many of the technologies that we rely on today, not least the internet itself.

At a more fundamental level, policymakers need to recognize that all markets, all economies, and all innovation ecosystems are directional. They tend to favor some kinds of innovation over others, depending on the overarching incentive structure and other factors. This tilt reflects not so much consumer demand as the influence of power, which is allocated according to ownership of resources and decision-making over how value is distributed. When it comes to platform governance, we need an entrepreneurial state to take a proactive role in determining how value is created and allocated.

A second crucial step is to start differentiating between the various data-extractive features of each Big Tech platform. Platform-based models are not necessarily data-extractive, but they are and will continue to be data-intensive. How data are used, and which data are collected in the first place, are therefore paramount questions. If personal data are used for micro-targeted advertising, we should ask whether the platform is in the business not only of identifying but of creating consumer desires through subtle forms of psychological manipulation.

Remember, the founders of Google have long known that advertising incentives fuel a divergence between creating value for users and creating value for advertisers. We now need to consider what a post-advertising internet might look like. If indiscriminately harvesting data from users without their unambiguous consent is no longer viable, how would digital start-ups redirect their time, talent, and energy?

This concern extends to Big Tech's other advantages – including its significant lead in artificial intelligence, talent recruitment, and research capacity, and a commanding position from which to amass valuable, highly granular data sets. Alphabet (Google's parent company), Amazon, Facebook, and others are not simply digital marketplaces; they are the proprietors of rich data portfolios that can be leveraged to digitalize more and more areas of life through the Internet of Things. As such, they are already positioned as core providers of public services and infrastructure.

Among the dominant players, the competition is not just for market share or consumers. There is a race to convert the entire offline world into an online web of data nodes, which will be used to organize even more human behavior around the imperatives of data generation and extraction. The alternative is to push for more emancipatory models of digitalization that ensure that the value being created by new technologies is directed toward social and public goods, rather than being monopolized.

Finally, we need the public sector to start investing in itself again. Governing online platforms requires more than just "gov-tech," McKinsey consultants, or advisers from Silicon Valley. The state needs to develop its own capacity to understand and respond effectively to new risks. The fact that Big Tech itself is driving the public sector's digital transformation does not bode well for the state's future regulatory and operational independence.

The state needs to be able to scrutinize, investigate, and govern the complex realities of the platform economy. It needs the know-how to demand the right kind of data from private platforms and enforce effective transparency. And it needs to step up and start pursuing opportunities for investment and public-purpose innovation. It is time to think more broadly about what it would mean to have a platform economy that actually respects privacy, enhances human agency, and fosters civic discourse.

Correction Feb 8, 2021 11:04UTC

In the second paragraph, the tech platforms' market capitalization rose by $2.7 trillion, not $2.7 billion.

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