REBALANCING CAPITALISM

Statement of the problem:

Contemporary capitalism due to its excessive creation of financial means – money and credit – has upset a healthy balance among its various means and ends. Imbalances always degrade systemic sustainability. Moderation and self-correction are the hallmarks of sustainable equilibrium, the service in due proportion of all parts of the system. Health and well-being, flourishing, depend on balance and prevention of excess. This was the insight of Aristotle, of Old Testament guidance to "have mercy, do justice, and walk humbly with Thy God", of the Middle Path of the Buddha, of the Chinese concept of the Tao, and of the Qur'an's guidance not to "transgress the balance (*Mizan*)".

Our present dynamics of capitalism underserve the biosphere which sustains our civilization, the natural capital upon which human happiness depends, and our social capital by facilitating divisive politics and a narcissistic hedonism. The problem before us is not capitalism but maldistribution of power among its component capitals. We do not properly value financial, social, human, intellectual, moral, and natural capitals.

Financial capital is overvalued while the other capitals necessary for well-being are undervalued.

At the dawn of the Industrial Age in Holland, Scotland, England and their colonies in North American, financial capital was scarce and the other capitals (coal and iron ore deposits, farmland, forests, fish, clean air, and labor power) were readily available. The price of financial capital was high but low for natural, social and human capitals. This the new capitalism system as so insightfully described by Adam Smith in his book *the Origins and Causes of the Wealth of Nations*, privileged financial capitalism by giving it legal ownership rights of first access to wealth created. The older Common Law of property and contract was not revised to impose on owners responsibility for the cost of the consequences of enterprise – externalities, be they low living standards for workers or degradation of the environment.

As the impact of capitalism grew in the Nineteenth Century, the Common Law and statutes evolved a more comprehensive program of tort liability in negligence and strict liability to force enterprises to be prudent in what they produced and how they did so. In the late Nineteenth and early Twentieth Century, as the social welfare state bureaucracies emerged and evolved, the state became a supervising partner of the capitalists.

But the inner discipline of capitalism continued to privilege financial capital until today.

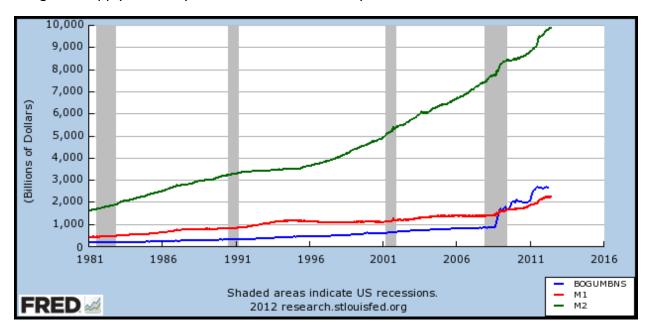
In the 1970's a false anthropology under the name of the "Agency Problem" dictated the use of financial incentives as the guide for personal ambition and decision-making in capitalist enterprises. This led to systemic focus on short-term monetization of enterprise and systemic

neglect of long-term asset accumulation. Such a capitalism directed income and wealth to the top 10% which had access to financial asserts. Returns paid to labor and vital social assets such as education, health, and the Rule of Law, and to nature were stingy by comparison.

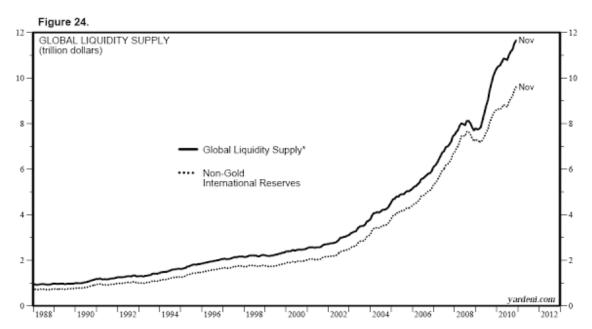
In the 1980's sophisticated mechanisms of finance for the creation of money, credit, and contract rights to share in future wealth creation -central banking, trading markets for securities of all kinds (options, futures, currencies, and derivatives) created vast amounts of liquidity, driving down the price of financial capital. Today there is no dearth of financial capital, so much so that billions of dollars are available to companies such as Uber and Tesla which do not earn profits.

On the other hand, no investment has been made to make up for depletions and disruptions in the supply of Natural Capitals.

The global supply of money has increased dramatically:

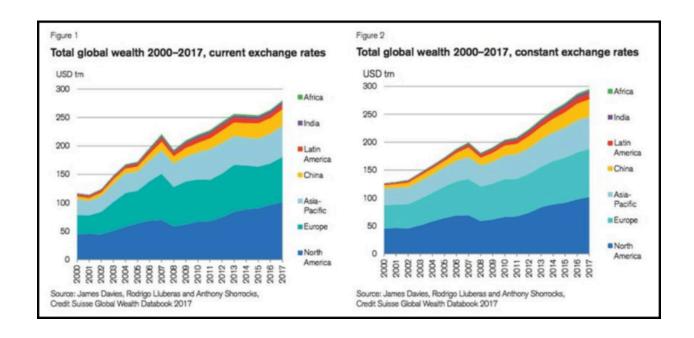


Recent growth in world liquidity is:



Non-gold international reserves plus Fed's holdings of US Treasures and Agencies.
 Source: Federal Reserve Board.

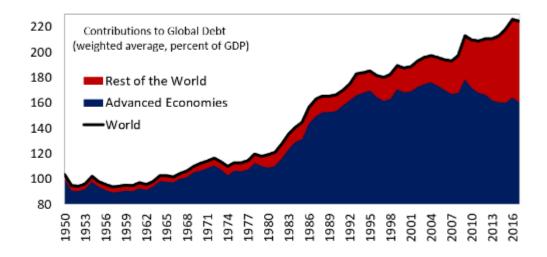
Total global wealth as of 2017:



Global debt has also grown apace:

A history of debt

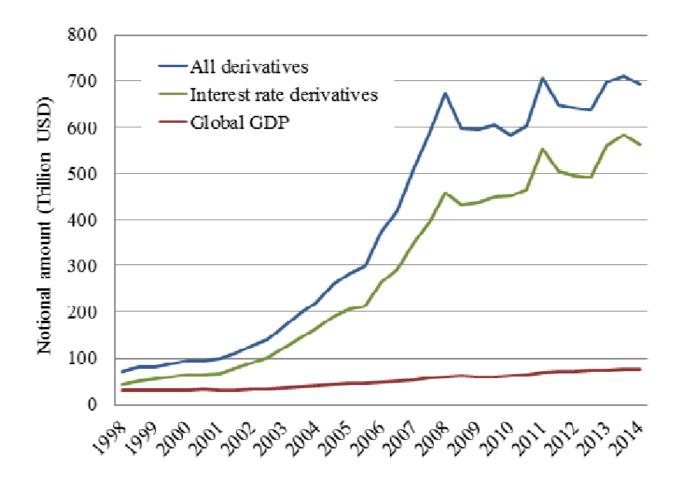
While global debt has risen dramatically since 1950, the global debt ratio came down in 2017.



Sources: Global Debt Database and authors' calculations.

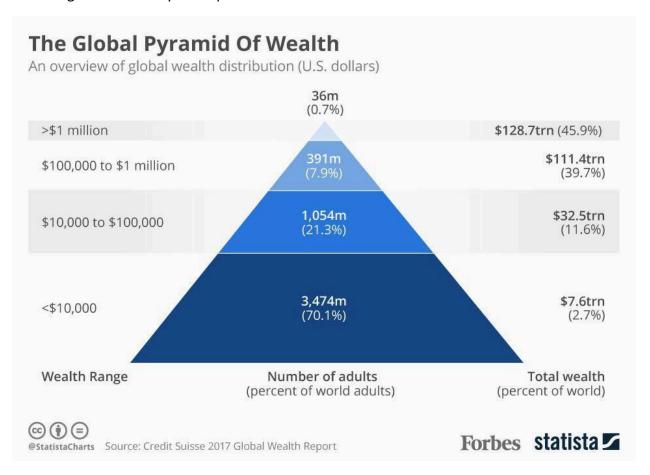


Notional value of all derivatives has grown:



Notional value of OTC derivatives at June 2018 was \$595 trillion. Gross market value was \$10 trillion.

Share of global wealth by the top 1% in 2017 was:



Today we need to urgently restore the health of capitalism by decreasing the returns to finance and increasing the returns to natural, social and human capitals.

Only by energizing and expanding the power of social, human and natural capitals can our civilization achieve the 17 Sustainable Development Goals agreed to by the governments of the world.

The active use of robust social, human and natural capitals will minimize the risks of an imbalanced climate, mean-spirited populism, corruption and abuses of human rights.

- 1) We need new metrics for the measurement of impacts good and bad of enterprise.
- 2) We need an alternative way to value enterprises to off-set the influence of the nominal prices set by financial markets and used for speculation and excessive diversion of liquidity to the few and far between.
- 3) Such metrics will permit better "steering" of investment and enterprise towards optimal outcomes. Better metrics will lead directly to better governance of firms. They will permit owners, boards of directors, and managers to focus more on stewardship responsibility.
- 4) The express purpose of the firm, the theory of the firm, must transition from seeking short-term cash profit, to a more comprehensive and balanced achievement of accumulation of capitals as assets supporting sustainable human fulfillment.
- 5) Leadership of capitalism must be entrusted to a cadre of newly recruited and trained Impact Professionals

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