Regulation vs. Transformation of our Financial and Economic System

von Prabhu Guptara

Regulation is essential for creating confidence, fair play and indeed the very possibility of widespread commerce and business. But does our current kind of regulation help solve the challenges facing humanity, or is it worsening our problems? For example, if we ask who the people are who have drawn up the new Basel II regulations, how they came to be the people drawing up these regulations, what is their education and experience, what they understand to be the purpose of the new regulations, and whether they see any need to relate such regulations to the global good, we will not be surprised that they have come up with a set of regulations that will strengthen the advantage of the richer countries and the bigger banks, against poorer countries and smaller banks.

The world economy has had the abolition of poverty as one of its ostensible aims, at least since President Kennedy's Inaugural address in 1960. I recollect his stirring words: "If a free society cannot help the many who are poor, it cannot save the few who are rich...Our generation should be the first to extend the benefits of civilization to all mankind". However, while America and the world have enjoyed an unprecedented boom in prosperity since then, with the occasional bout of inflation, deflation or uncertainty on the way, we have not merely failed to abolish poverty, we have not even managed to hold the line. Today, there are more poor people in America, and in the world, than there were at President Kennedy's Inauguration (3.1 million U.S. households suffer from actual hunger, including something like 2 million children; 10 million households - that is, 31 million people - risk hunger or food insecurity, including 12 million children; and 12.5 percent of the total U.S. population lived in poverty in 2003, according to the official U.S. measure of poverty). We could expand this story from the US to the whole of the world by looking at material from the World Economic Forum, from other governments, from multigovernmental organisations and so on.

Governments, companies and individuals seem therefore to find themselves in a bind, unable to do the good that they would, doing the evil that they don't really want to - a dilemma to which St Paul drew attention some two thousand years ago.

What is the basic reason for this dilemma? It is that our aspirations for the global good clash with the economic, financial, corporate, government and multi-government structures which we have created.

For example, we talk of the need to ensure long-term sustainability or at least medium-term shareholder returns, but we have a stock market system which focuses in theory on short-term quarterly returns but in practice on moment-by-moment news and rumours.

The purpose of companies has moved from that of reducing risk to that of maximising returns.

Technology has always promised us power and choice, but we are living in what may come to be called the ETC Century (that of Erosion, Technological Transformation and Corporate Concentration). "Technological power is becoming concentrated in a corporate elite that seems to be struggling for dominance over the rest of the earth", in the view of RAFI (Rural Advancement Foundation International):

"For every Luddite trying to establish social controls over the introduction of untested technologies, there is a much more powerful elite using social manipulation to market new technologies. Any major new technology introduced into a society which is not by its nature just will exacerbate the gap between the rich and poor, and between aspiration and achievement in both environmental care and ethical transparency". (my emphasis).

More fundamentally, the global economy is built on a competitive race to grow. This is, by definition, unsustainable in a world of limited resources - though some people argue that resources are not limited, and that the market always finds substitutes, given time. Of course, markets do sort many things out, so it is possible that we may have enough time to find corrective mechanisms. Equally we may not. In chess as in business, the winners are generally those who are cautious and conservative and weigh the positive possibilities as carefully as the negative ones.

Much of our so-called "growth" (national, corporate & personal) is driven by debt. In October 2004, there was much anguished debate in the UK when the "Debt in a Decade" report from the Skipton Building Society made it known that UK household debt had reached £1 Trillion. Interestingly, the UK government had, almost exactly 4 years earlier, in October 2000, established its Task Force on Tackling Over-indebtedness to "address concerns about consumer debt in the UK by considering ways of achieving more responsible lending and borrowing". However, as Professor Kevin Keasey, Director of the International Institute of Banking and Financial Services, at Leeds University Business School in the UK, wrote in the December 2004 issue of Finance Industry Solutions:

"The problem the credit industry faces is that it needs debt levels to keep increasing if it is to meet its ongoing profit targets….transforming an industry built on pushing
credit into one that is responsible in its lending will not be an easy task" (emphasis mine)

There is the further challenge for the current economic system that what are called "goods" are not always good. More and more is not necessarily desirable: Do we really need all that we produce in terms of industry and armaments? Even in agriculture, the Common Agricultural Policy has historically consumed an enormous proportion of the EU's budget simply to store European over-production in beef, beer, milk, butter and so on, purely for the purpose of price-maintenance. Now the WTO wants us to change the world system so that subsidised rich farmers who over-produce by following unsustainable practices can dump their over-production on the rest of the world.

Never before have so many people been so rich, and yet felt so poor. Sixty four per cent of respondents, who had an average wealth of $38 million, feel financially insecure. (The U.S. Private Bank's 2000 Study on "Wealth with Responsibility", from Deutsche Bank's Forum magazine, 6/2000, page 24). One key reason is that greater globalisation of business means greater opportunities to make money quickly because of the scale of new opportunities which the traditional multinationals were in the past not properly poised to exploit...but it has become a more volatile world (how much is Bill Gates worth today?)

It has now been scientifically established that there is no correlation between happiness and wealth. People who are very poor do become happier with each additional dollar till a certain threshold is reached, then additional money adds to the sum of happiness with decreasing effect, till another threshold is reached, when the correlation reverses, and the more money you have, the unhappier you get. No wonder Bhutan and Brazil are experimenting with replacing the notion of growth. Bernard Litaer's proposal for a properly asset-based currency therefore would be a good one to adopt in the USA) are better at providing slower but more solid growth. Bernard Litaer's proposal for a properly asset-based currency therefore would be a good one to adopt in the current conditions of the world economy, provided a representative group of assets was included (including household value, for instance). It is also clearly established that the abolition of usury (see above) would more or less completely eliminate the boom-bust cycle, which is one of the key difficulties of our modern economic system, as well as eliminate the dependence of the world on ever-faster growth and the consequently increasing threats to the environment that we have had since WWII.

Lastly, we need to consider the fundamental transfer of risk from government and from financial institutions to households like yours and mine. Think of what has happened in the area of pensions or of health provision. Think of areas such as hedge funds and derivatives, where the classic Sharpe ratio should be abandoned, since it ignores the asymmetric risk component of fund positions. The problem is that there is no good substitute. Though some theoretical solutions have been proposed,
as yet they lack computational constraints and robustness. Think of credit risk transfer, where the biggest questions are being ducked. I quote from a paper on "Credit Risk Transfer" published in October 2004 by The Joint Forum established to deal with issues common to the banking, securities and insurance sectors, by the Basel Committee on Banking Supervision, the International Organisation of Securities Commissions, and the International Association of Insurance Supervisors:

"The Working Group spent considerable time discussing with market participants the related questions of how much risk is actually being transferred via credit derivatives transactions, as well as the ultimate sources of the risk protection….

In general, the Working Group believes that it would be impractical to develop a precise answer to these questions, because it would require a comprehensive survey of a very large number of market participants, including many private fund managers, and a detailed analysis of many different structured products.

I read that as an admission that no one knows how much credit risk is actually being transferred to whom; nor does anyone know the implications of this lack of knowledge; moreover, that the task "is too big to perform"! Of course, credit risk is only one kind of risk…. We have shifted from an asset and ownership based economy to one based on access and flow (interest payment is one such flow). That is why risks - and their transfer - are so crucial.

We really are living in a house of cards, in terms of the economics of our world.

By now, you may have become curious about an interesting question: how come we have created such structures which generate unsustainability? Specially when the traditional wisdom of all our societies sought to steer us away from the creation of such structures?

The reasons are our fear, greed, and lust for power. In other words, our self-orientation which is often wrapped up in fine language and imagery to do with secularism, rationalism, individualism, "freedom" and so on, rather than true God-orientation or, as we might put it in practical terms, thankfulness-towards God, love towards other human beings, and responsibility towards nature.

For example, the notion that borrowing, and by implication debt, is bad has been the received wisdom for many generations, coming straight out of the Biblical tradition. Post-War indoctrination into what I call "Popular Darwinism" or "Evolutionism" ("evolution as religion or doctrine or dogma") was a principal contributor not only to the rise of Fascism and Nazism but also to the enormous decline of faith and ethics which has taken place since then, and has changed the culture to the extent that, for example in the UK, the rules governing official credit allocation were changed in 1971, and those concerning hire purchase agreements and the personal financial services marketplace were changed in 1982. Indeed, most legislative restrictions on the charging of interest, were removed between the 1950s and the 1990s across the world. This has transformed borrowing into something not only "acceptable and necessary" but has made consumption the only meaning in life for many people. No wonder that, as the world "develops", debt continues to rise and rise across the world and in all sectors (except, from time to time, in the corporate sector). In most societies today, you can legally charge any amount of interest that some foolish or desperate customer is willing to bear. In India's case, this has resulted in the continuing serfdom (virtual slavery) of tens of millions of people to my caste, which began to be reversed with the Evangelical Revival and the work of the Clapham Group that turned the East India Company from a "gang of looters" into at least a partial blessing for India.

Similarly, our global financial and economic challenges have cultural, intellectual, psychological and emotional roots which can be countered by the right kind of spirituality. The difficulty is that most of today's spiritualities are merely individual or selfish - and it is not enough for spirituality today merely to help individuals with negative emotions. It is necessary also for spirituality to address the concrete question of how to deconstruct the structures to which I have drawn attention. Someone who is exploring that is Dr. Peter Heslam FRSA, with his Research Project on Capitalism at the University of Cambridge in England.

I would merely suggest that there are at least five varieties of spirituality, in terms of their economic and financial impact. First, there are individualistic spiritualities that are aspirin-like (including Eastern spiritualities and techniques such as yoga, tai-chi, various forms of meditation, and so on). Second, there are jujube-like spiritualities. American Fundamentalism and Indian bhakti-worship are good examples of this kind of spirituality: sweet, but perhaps too sweet. Most contemporary spirituality, Eastern and Western, remains stuck at the level of spectator sport (come to the temple or mosque, and don't bother with whether and how this relates to work or to the world). Much of contemporary Christianity betrays its own spiritual roots by being incense-like - it considers the primary purpose of life to lie in "worship" (as in the song: "the reason I live/ Is to worship You"). Actually, as far as I can understand the teaching of Jesus the Lord, a relationship with Him is meant to be dynamite-like or (to use his own imagery), like yeast or like a tree growing, breaking up everything around and making something new and greater instead: we are here to be revolutionised and to revolutionise work and the workplace and the world, while of course doing our assigned job well.
This kind of spirituality is what is required as the basis of our emerging global economic and financial system if it is to be transformed to produce the results that we all desire.

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