Me'M Denkfabrik für Wirtschaftsethik

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CRITICAL ECONOMIC ETHICS

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The power of economics

- „The ideas of economists and political philosophers, both when they are right and when they are wrong, are more powerful than is commonly understood. Indeed the world is ruled by little else. Practical men, who believe themselves to be quite exempt from any intellectual influences, are usually the slaves of some defunct economist." John Maynard Keynes: General Theory (1936: 383)
- "I don't care who writes a nation's laws, or crafts its treatises, if I can write its economics textbooks." Paul Samuelson (probably 1995;1915-2009, author of "Economics", sold 4 million copies)
- Politician (and normal citizens) are laymen in economic matters. They need economic expertise. They get it from neoclassical/neoliberal economists.

Politics in favour of capital – The example of Jörg Asmussen

- Economist, studied in Bonn, under Prof. Axel Weber, who later became president of the Deutsche Bundesbank, suggested by his student, and after that chairman of the board of UBS.
- Asmussen was appointed Undersecretary (in 2003), later State Secretary of the German Federal Ministry of Finance (red-green alliance [1998-2005], black-red [grant] alliance [2005-2009]).
- Supported bank deregulation and an extension of the market of asset-backed securities.
- "An internationally competitive 'financial center Germany' is one of the most important condition for economic growth and more jobs… The removal of meaningless regulations in the financial sector and the expansion of securitizations provides companies with more capital in a good and cost-effective manner." Contract of the black-red [grant] alliance [Koalitionsvertrag], 2005, own translation.
- After the bubble burst, Asmussen, among others (bankers, economic "experts"), helped Minister of Finance Peer Steinbrück „to look into the abyss" [of toxic assets in the bank's balance sheets]. "The legacy of Asmussen are the 480 Bill. Euro the German taxpayer is held liable in order to safe German banks." Jens Berger, www.nachdenkseiten.de, 12/17/2013
- In 2012, Asmussen was appointed to the ECB Executive Board (monitoring the austerity programs in the Eurozone).
- In 2013, Asmussen was appointed as State Secretary of the German Federal Minister of Labour and Social Affairs (Andrea Nahles, SPD).

The Normativity of Economics

- “Economics is essentially a moral science and not a natural science. That is to say, it employs introspection and judgments of value.” John Maynard Keynes, 1938
- “The first task of integrative economic ethics is to see through the alleged value-free condition or ethical neutrality of the market’s inherent logic as it is understood in ‘pure’ economics by means of an ethical-critical elucidation of its normative basis.” Peter Ulrich: Integrative Economic Ethics, 2008, p. 101.
- Economics is IN FACT a “moral science”. It addresses the economy (the market) from the “economic point of view”.
- There is no such thing as a neutral, value-free social science.
- Claiming value-freedom for one`s own scientific endeavors, like (neoclassical) economists do, amounts to arrogating what one says about the subject matter (the economy) is beyond ethically doubt.

Why (economic) ethics?

- There are only two types of knowledge:
  - Orientation (judgemental) knowledge (Jürgen Mittelstrass): normative → How to judge things? Definition of problems.
  - Instrumental knowledge: positive → What is the case (so that I know how to influence objects in the world successfully)? Solving problems (against resistance). Ethically highly problematic, NOT neutral.
- Ethics (normativity) is inescapable.
- Integrative Economic Ethics [IEE] (Peter Ulrich) makes explicit what is implied in the allegedly purely "positive" and "neutral" mainstream economic thinking on the competitive market economy. IEE critically asks if the (at least implicit) normative claim that the logic of the market is legitimate can be maintained. → Critique of economism which is "the ultimate and perhaps most powerful major ideology of all time" (Peter Ulrich, IEE, p. 6). Economism = the market principle is the moral principle.
- IEE, or and ethics-integrated economics, does not look at the subject matter (competitive markets) from scratch (as positivism does), but together and against mainstream economics. There is no such thing as an "objective" reality, but only an reality with meaning for us. – Also: Mainstream economic thinking in fact guides economic actors – economic actors as well as economic policy.

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- Economism = the market principle is the moral principle. The market principle should rule the world.
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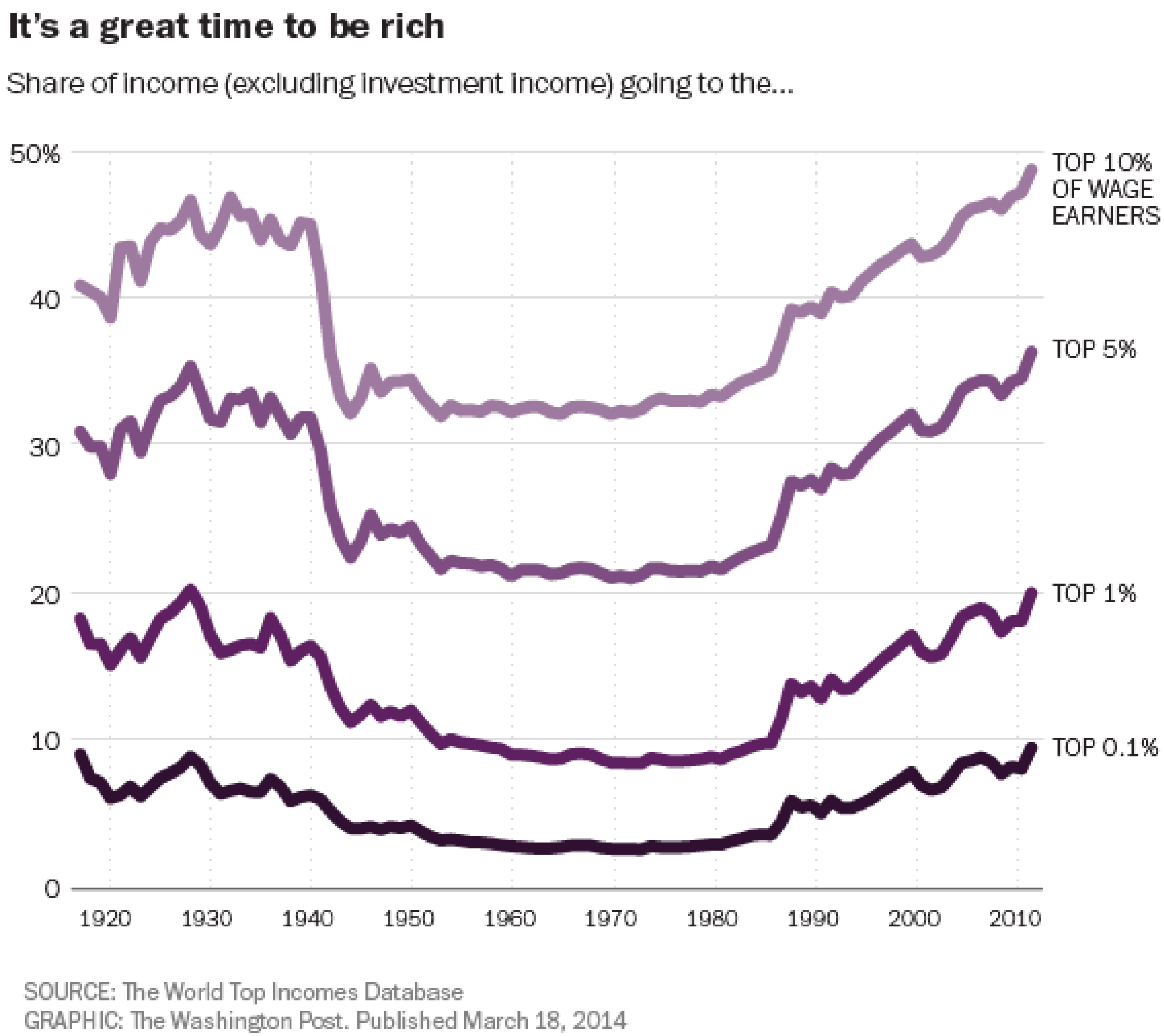
The Normativity of Economics I: „Rationality“ and the homo economicus

- Common sense of economics: “If people act rationally in a competitive market, the outcomes will be efficient”, that is good, justified, just.
- Example: The financial crisis is the result of a lack of rationality.
- “Rationality” = instrumental rationality = the will and the ability to achieve (usually: financial) success; the more the better.

Excursion: The bail-out success

- “Income inequality increased by more in the first three years of the crisis to the end of 2010 than it had in the previous twelve years, before factoring in the effect of taxes and transfers on income… After taxes and transfers, the richest 10 per cent of the population in OECD countries earned 9.5 times the income of the poorest 10 per cent in 2010, up from 9 times in 2007.” OECD, 15/05/2013
- In the US, 95% of the real US GDP growth of the 2009-2012 „recovery“ time accrued to the top 1% of income eaners. (Piketty/Saez 2013)


It's a great time to be rich
Share of income (excluding investment income) going to the...
50%
40
30
20
10
0
1920
1930
1940
1950
1960
1970
1980
1990
2000
2010
TOP 10% OF WAGE EARNERS
TOP 5%
TOP 1%
TOP 0.1%
SOURCE: The World Top Incomes Database
GRAPHIC: The Washington Post. Published March 18, 2014

The Normativity of Economics I: „Rationality“ and the homo economicus

- Homo economicus = epitome of instrumental rationality
- “Homo economicus can be seen to maximize almost anything at all.” (James M. Buchanan) → formal concept. H.O. can NOT be empirically refuted. (H.O. might even have “moral preferences” in his utility function.)
- Behavioural economics: Just claims to refute the empirical validity of H.O., but does not reject the (wrong) bindingness of “rationality”: People often make “stupid” decisions. – Also, “rationality” on the side of the addresses of theory: as customers.
  - “Everything in economics depends on behavior. Any economic consultation therefore aims to influence human behavior.” www.fehradvice.com

Profit maximization

- Profit maximization is the most prominent manifestation of utility maximization.
- Profit *maximization* means to do *whatever it takes* to increase profits (or shareholder value) *as much as possible*.
- Two misconceptions:
  - Profit maximization is already long-termism. „Long term profit maximization“ is a pleonasm. „Short term profit maximization“ is an antilogy.
  - The beneficiary of profit maximization is the ever-changing investor. It is about his or her long-term, “sustainable” track record. It is not about the enduring existence of the corporation.

Profits and ethics I

- Profit-maximization is ethically not justifiable. It is not the “profit principle”, but the moral principle which is to rule in the end. Without acknowledging the primacy of ethics it is not possible to legitimate any course of action.
- The one who maximizes profit "is done" with the other, and has "no more to say" to him or her. "In other words, he tramples the roots of humanity underfoot." Georg Wilhelm Friedrich Hegel (1807)
- Homo economicus regards other people just in terms of the effects they are able to generate (for example: purchasing power, productivity). He is inaccessible to the legitimate claims they could address to him.
- The one who maximizes profit treats others according to their power to influence the profitability of corporate conduct. With this, he or she directly violates the Categorical Imperative, "to treat humanity, whether in your own person or in the person of any other, always at the same time as an end and never merely as a means to an end." Immanuel Kant.

Profits and ethics II

- Profits is not the final measure of good corporate conduct, but one aspect among others.
- Capital is not the "principal" of business.
- Making profits is legitimate. Profit-maximization is illegitimate a priori.

The New Radicalism in Management

- "Value creation should be established as the paramount objective of all management endeavours. There still are huge potentials for setting radical cuts in an unprejudiced manner." McKinsey, 2001
- Profit maximization = actively eliminating all outer-market considerations and values (meaning, fairness)
- "We see our strength in detecting solid companies with are, as such, run well, but whose owners do not do enough to unlock its full potential. Such a company sometimes needs to go through a process of radical transformation. If the plan succeeds, substantial value added can be achieved." Pinkerton/Cinven: „Private equity ist effizienter als der öffentliche Aktienmarkt", Finanz und Wirtschaft, 5. Mai 2004, S. 23.

The destruction of the "social market economy"

- Social market economy = embedded market economy (Karl Polanyi)
  - From above: social security, regulation (e.g. licensing), „mixed economy“ (not everything is „privatized“), trade barriers
  - From below: a culture of moderation. Profitability is just one consideration among others.
    - These considerations other than profitability are eliminated – for example via incentive systems, forced ranking, EVA, opportunity cost thinking.

The Normativity of Economics II: The „efficiency“ of free, competitive markets

- “The invisible hand [of markets] usually leads markets to allocate resources efficiently.” Mankiw, Principles of Economics, 5th ed., p. 11
  - An increase in “efficiency” is called an “improvement”, “better”.
- “Efficient” (useful, good) for whom?
- The utilitarian version of “efficiency”: good for “society as a whole” (Mankiw). It is about “the greatest amount of happiness altogether”; “the world in general“ should „gain“ (John Stuart Mill). The “sum total” (A. Smith) of values is to be increased or maximized.

The failure of utilitarianism

- Good for "society as a whole" is not "good for everybody":
- "It is inevitable that reforms designed to remove sources of inefficiency in the economy will create some losers as well as winners… But the costs experienced by some individuals or communities are not sufficient reason to forego reforms that are of substantial net benefit to the community as a whole." [Australian] Productivity Commission (2004)
- In utilitarianism, individuals have no rights. Only "the world" or "the community" (Bentham) has rights. People just *represent* portions of utilities of the "fictitious body", as "the sum of the interests of the several members who compose it" (Bentham). We, the individuals, have to sacrifice ourselves for "the interest of the community", that is for (GDP-) growth.
- Utilitarian economics offers a justification for economic growth. And for competition as the driver for growth.

Competition as a process of creative destruction (Schumpeter)

- Competition creates winners as well as losers.
- The market process = exchange (trade) + competition
- Exchange = "creation" (of jobs) = win-win
- Competition = "destruction" (or at least pressure on jobs)
- The market process = win-win-lose
- There is growth only when the losers manage to find a new job (or to "improve" their market position).
- „Free trade does the reverse [of creating jobs]. It eliminates jobs." "Economic progress [i.e. growth] has two legs. One is eliminating jobs with new technologies, the other finding new tasks for workers… Both job creation and destruction go hand-in-hand… [There are] unrecognized advantages [with regard to growth] of job destruction… The future of the economy [= growth] rests on the country's willingness to endure the pain of job destructions, as well as find ways to facilitate job creations." Richard B. McKenzie (1988)

Utilitarian economics as ideology

- Exchange is the visible part of the market process. Competition is mostly invisible.
- "The 'hiding hand' of the market, which prevents you from knowing who and presumably what caused your loss of a job in your factory, tends to diffuse the resentment [against free trade], I think." Jagdish Bhagwati (1996)
- → Legitimizing self-responsibility for copying with losing in the "market game", mostly by concealing the destructive features of market process.
- "The rationale for open economies is that, in principle, the gains will outweigh the losses for the country as a whole; thus, the winners can afford to compensate the losers." Kapstein (1996: 26). (Kaldor-Hicks compensation criteria)
  - If they actually would compensate the losers, growth would be lower or inexistent, as the pressure would vanish.

Competition as the driver for economisation

- Impersonal competition is the all-pervasive feature of our times.
- Competition compels to growth, and leads to the economisation of our lives.
- "Competition produces … a kind of impersonal compulsion which makes it necessary for numerous individuals to adjust their way of life." Hayek, 1978, p. 189
- „People say that in the competitive struggle, economic lives are destroyed. This, however, merely means that those who succumb are forced to seek in the structure of the social division of labour a position other than the one they would like to occupy. It does not by any means signify that they are to starve..." Ludwig von Mises, 1936.
- The compulsion into entrepreneurship:
  - Education becomes "investing in human capital"
  - Stress management
  - Economisation of "friendship": "There are only two types of people in this world, and the sooner you discover this, the happier, more fulfilled and successful you'll become -- even if it means dumping your best friend, neighbor, or, yes, even your mother… You need to rid your life of Leeches and replace them with Energizers." Robert Pagliarini, CBS MoneyWatch, 2011

The two basic questions with regard to competition

- Is it still worthwhile to endure the stress of competitive pressures in exchange for ever more goods and services? Does the economy still serve the “good life”? To what extent to we want to live a life as “human capital investors”?
  - Skidelsky/Skidelsky: How much is enough (2012), Wilkinson/Pickett: The Spirit Level: Why Equality is Better for Everyone (2010).
- Should the more competitive market participants – and should capital – be allowed to compel the rest to an ever more “economic” way of life?
- → An option for market restraint (“protectionism”).

Is there a business case for ethics?

- Tacit assumption: Ethics is about "external effects". These are not internal to market competition.
  - "A corporation should act morally responsible simply because immoral behaviour does not pay. Moral behaviour is advantageous in the long-run." Heinrich von Pierer, former CEO and chairman of Siemens
  - "The win–win perspective to CSR": "Growing support for the business case among academic and practitioners is evident. Generally, the business case for CSR is being made by documenting and illustrating that CSR has a positive economic impact on firm financial performance."
    Carroll/Shabana: The Business Case for Corporate Social Responsibility: A Review of Concepts, Research and Practice, International Journal of Management Reviews (2010), p. 100, 102
- It would be impossible to maximize profits without doing the right thing. → Legitimization of profit maximization. Assertion: harmony between ethics and profits.

The business case and the Pareto principle

- Efficiency à la Pareto: If nobody looses, and at least someone wins, this is called “efficiency enhancement”. Pareto-efficiency = ethics of win-win.
- “That which emerges from such voluntary trading is 'efficient' ... (and) it is a relatively small step which allows us to replace the word 'efficient' with 'just'.” James M. Buchanan, 1977. p. 128 f.
- Measurement of advantages: “status quo”. (There must be some “preagreement base for the measure of cooperative surplus”, Buchanan, 1991, p. 204). The status quo is not in the past, but in the future. → What looks like a loss, needs to be regarded as an investment. → Justification of homo economicus.
- Example: justifying Wall Street bail-outs:
  - “It is difficult to pass a bill that commits so much of the taxpayers' hard-earned money… But given the situation we are facing, not passing a bill now would cost these Americans much more later.” George W. Bush, 9-23-2008
  - "I am convinced that this bold approach [$700 billion bailout package for financial firms] will cost American families far less than the alternative — a continuing series of financial institution failures and frozen credit markets unable to fund economic expansion.” Henry Paulson, 9-21-2008

Why the ethics of win-win fails

- Homo economicus only considers the interests (rights) of those who have *the power* to influence his balance sheet of profits and losses.
- Only “key stakeholders” are considered. These are “powerful stakeholders”.
- “In the long run” = time which potentially powerful opponents usually need to realize their power.
- This ethics without morals in an ethics of the right of the powerful.

CSR as ideology

- "By examining CSR in the context of the political economy of late capitalism, the book puts the emphasis back on the fact that most large corporations are fundamentally driven by profit maximization, making CSR initiatives merely another means to this end. Rather than undermining or challenging unsustainable corporate practices CSR is exposed as an ideological practice that actually upholds the prominence of such practices." Fleming, Peter: The End of Corporate Social Responsibility, 2012.
- Granted that minimum wages (or living wages) mark the lower limit for a fair remuneration for a work effort, why there still are so many companies paying wages below these lines? According to the business case, fair pay would need to pay off for capital.
- Corporations like Google, Starbucks, Apple, Facebook, or Intel, via base erosion and profit shifting, hardly pay any taxes on their billions of profits anymore. Eric Schmidt (chairman of Google): "I am very proud of the structure that we set up. It's called capitalism. We are proudly capitalistic." According to the business case, this "pride" must fail in terms of long-term profits. Realistic?

CSR as ideology

- Jack Welch („Neutron Jack“) raised the shareholder-Value of General Electric from $14 bill. To $400 bill. between 1981 und 2001. Via: mass layoffs, forced ranking (10% of the workforce were deemed „low performers“ and must be fired, every year), environmental pollution, PCB polluted wastewater in Pittsfield, contaminated soils in the neighborhood, GE knew, lobbying against environmental protection. „But, hey. Welch‘s job was to maximize shareholder value, not to be a corporate statesman. That‘s why he was anointed ‚manger of the century‘.“ Robert Reich, Supercapitalism 2008, p. 77f.

The Problem of Exigibility

- „Companies under supercapitalism no longer have the discretion to be virtuous. Competition is so intense that most corporations cannot accomplish social ends at a cost to their consumers or investors, who will otherwise seek and find better deals elsewhere. Even if individual consumers or investors believed in the virtuousness of a particular sacrifice, absent laws requiring all companies and therefore all other consumers and investors to forebear as well, the individual's action would have to effect." Robert Reich: The Case Against Corporate Social Responsibility, 2008
- "Resolving externality ... [or ethical] problems is the legitimate domain of the government in its rule-setting function." Jensen, M. C. 2002

The need for regulation

- In modern, and large, societies, moral bindingness alone is too weak and represents excessive demands for everybody.
- Responsible conduct of the single actor needs to be supported by legal bindingness (sanctified rules).

Individual ethics	vs.	Institutional ethics
Moral bindingness	vs.	Legal bindingness

- The institutional framework is to be designed so that the responsible business is not left out to dry.
- Principle of Autonomy → The foundation of the modern, liberal state under the rule of law [Rechtsstaat]

The need for global regulation

- Individual states have lost their political (democratic) sovereignty.
- Interviewer: „The struggle over presidency is in full swing. What is the prior task for the soon to be elected president of the US?" Greenspan: „We are lucky that the political decisions in the US, thanks to globalization, have been widely replaced by global market forces. With the exception of national security, it does not matter that much who will be the next president. The world is governed by market forces." *Alan Greenspan (2007)*
- "In today's hyper-competitive global economy, there is no reliable 'third way' for countries to avoid continued liberalization and market-oriented reforms." *Kenneth Rogoff (2006)*
- "Market compliant democracy". *Angela Merkel (2011)*

The need for global regulation

- Motto: end the global economic war on market shares and the favour of capital. → Global economic ceasefire agreements.
- With regard to external effects: Global coordination so that a country regulating its economy will not lose in global competition.
- With regard to internal effects: Protecting the people from excessive competitive pressures.
  - Tariffs are middle-instruments: They allow trades, but they constrain them.
  - (Re-)Taxing capital on a global stage; end tax havens
  - Stop TTIP
- The vision: an embedded market economy = the pure logic of the market (in the dimension "rationality" and "competition") is constrained and moderated.
- Do we still want to grow? Do we need to grow? If so, who forces us to growth?
- Precondition: Overcoming economism