"A Sustainable Growth Strategy for Mitigating Financial Crises: Broadening Capital Acquisition with the Earnings of Capital."

or

"Prosperity without Austerity"

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Abstract

The current economic crisis and the conflicting mainstream stimulus and austerity strategies advanced to promote economic growth and national solvency may be viewed as disparate responses (grounded in mainstream economic theory) to the prospect (1) of inadequate present and future earning capacity of both consumers and producers to purchase what can be produced (physically, but not profitably) and (2) the inability of nations, businesses and individuals to repay existent and anticipated debt obligations. To address the crisis in a fundamentally new way that promises to promote sustainable growth, fuller employment, enhanced earning capacity for poor and working people, a higher return on private equity, and enhanced national solvency for members of the Euro-Zone, without the imposition of austerity, this presentation advances a new economic understanding of production, distribution. Contrary to the austerity and stimulus strategies (and the economic theories that are used to justify them), the new economic understanding is based on the premise that the market return on capital has a substantial, positive relation related to the distribution of capital acquisition with the earnings of capital. The prospect of a broader distribution of capital acquisition with the earnings of capital carries with it the prospect of more broadly distributed earning capacity in future years, which in turn will provide substantial market incentives to profitably employ more capital and labor in earlier years. Based on this new economic understanding, the presentation advances an entirely voluntary approach to corporate finance that will simultaneously (1) enable credit-worthy companies to meet their capital requirements in a more efficient and cost effective way and (2) open the markets for real and financial capital acquisition more fully and competitively to poor and working people by extending to them the same benefits non-recourse corporate credit and corporate finance that well-capitalized people routinely enjoy. Based on the new understanding, the effect of the enhanced voluntary system of corporate finance will (1) distribute more broadly the earnings of capital, (2) profitably employ more capital and labor, (3) reduce the need for government spending, (4) enhance the credit-worthiness of member nations, and (5) lay the economic foundation for sustainable growth.

Overview of Presentation

I. Introduction

1. The current economic crisis has been a long time in coming.
2. Only a small minority of economists and non-economists warned of its coming,
   --But no one seemed to know *when* it would come.
   (One of the basic rules of being a successful economic expert is to never put an economic number and a future date on the same page.)
3. What is a recession?
   A widespread, sustained market response to the widely perceived prospect of inadequate present and future earning capacity of both consumers and producers
   (1) to purchase what can be produced (physically but not profitably) and
   (2) to repay existent and anticipated debt obligations.

4. Unutilized Productive Capacity (two very different meanings)
   1. Static - neoclassical: capital, technology, skills held constant
   2. Dynamic - holistic: capital and technology are variable

5. The Greek Financial Crisis is a Part of the European Economic Crisis
   ...is a Part of the American Economic Crisis;
   ...is a Part of the Global Economic Crisis

6. 1. Not all nations and not all people are presently in crisis
   2. but very few are doing better now than in the year 2000.

7. The situation faced by Greece is highlighted by the following charts.
   (1) central government net debt, (2) gross domestic product,
   (3) general government revenue, (4) general government budget deficit,
   (5) 10-year bond yields of Greece and other Euro-Zone nations,
   (6) Greek unemployment rate, and
   (7) central government debt by residual maturity

8. The banks and creditor nations want to be paid and
   demand austerity from debtor nations and the vast majority of their people;
   Poor and working people want government policies
   that create and preserve jobs, and honor hard earned pensions.
   Both groups can find mainstream economists to support their position because ...

9. Mainstream economics is a house divided on what best to do:
   1. Some prescribe government austerity –> decreased public spending and debt.
   2. Some prescribe government stimulus –> increased public spending and debt.

10. These disagreements are grounded in theories that have long dominated economic, financial, and political analysis.

11. Until the recent calls for austerity by creditor banks and nations, the mainstream strategy for promoting economic recovery is a compromise of left- and right-wing government policies that facilitate
(1) capital acquisition with the earnings of capital (and also considerable government redistribution) primarily for major corporations and well-capitalized persons (generally in proportion to their existing wealth), and
(2) primarily jobs (but by no means the best or highest paying jobs) and various forms of welfare redistribution for poor and middle class people.

12. Now that this (generous for the rich and less generous for the poor) grand political compromise has hit unexpectedly hard times with no clear mainstream remedy,
the creditor banks and nations demand austerity from those least able to afford it.

13. The mainstream analysis and strategies for economic recovery share a common but unstated assumption: Namely
The broader distribution of capital acquisition with the earnings of capital
will not promote growth.
Otherwise, there would be commentary and concrete efforts to enable poor and working people to also acquire capital with the earnings of capital
... but there is none.

14. The scientific response to two or more theories that fail to solve problems is to:
– identify, suspend, and reverse shared fundamental assumptions

15. The Counter Assumption:
The broader distribution of capital acquisition with the earnings of capital
will promote growth

16. Consider a plan based on the counter assumption that promises to
1. Promote more sustainable growth,
2. Enhance the earning capacity of poor and working people
3. Enhance the capacity of national governments to raise revenue
4. Reduce the need for transfer payment and other government expenditures
5. Enhance the value of equity investments
6. Enhance the credit worthiness of national governments

II. The Binary Economic Paradigm: A New Paradigm for Understanding of Production, Distribution and Growth

1 Three Fundamental Binary Principles:

1. Labor and capital are "equally fundamental" "independent" or "binary" factors of production;
2. Technology makes capital much more productive than labor; and
3. Capital has a strong, positive, distributive relationship to growth, such that the more broadly capital is acquired, the more it can be profitably employed to increase output.
(The principle of binary growth, which is described more fully below.)

2. Capital Defined: As used in this presentation "capital" includes land, animals, structures, machines, patents, trademarks, and other capital intangibles -- anything capable of being owned and employed in production.

Different Meanings of "Capital": Real, Financial, Human, Intellectual, Social Capital

Balance Sheet	
Assets (Real Capital)	Liabilities
	Equity (Financial Capital)

Financial Capital Is a Claim on Real Capital and Its Earnings, After Liabilities Are Satisfied,

3. Binary Factors of Production: Labor and (Real) Capital

Each factor does its own work

E.g., Sawing Boards and Hauling Sacks

4. Productivity compared to Productiveness

Productiveness:

Retrospectively == Work Done

Prospectively == Productive Capacity

Productivity == $\frac{\text{(Value of) Work Done by All Factors of Production}}{\text{One Factor (Usually Labor)}}$

5. Charts Illustrating the Growing Productiveness of Capital

6. The Six Powers of Capital:

Capital can

1. replace labor (by doing work formerly done by labor);
2. vastly supplement the work of labor by doing much more of the kind of work that humans can do;
3. do work that labor alone can never do (e.g., elevators lift tons hundreds of feet in seconds; airplanes fly; scientific instruments and chemical reactions create computer chips that cannot be made by hand; fruit trees make fruit while all farmers do is assist in the process);
4. work without labor (e.g., washing machines, automatic bank tellers, gasoline dispensers, vending machines, automated factories, and fruit-bearing trees);
5. pay for itself out of its future earnings (the basic rule of business investment); and
6. distribute income equal roughly equal to the value of its output

7. The Distributive Power of Capital:

1. Just as capital has the power to do much more work than labor,
2. Capital has the power to distribute much more income than labor

8. **Price and Value: Two Theories of perfect competition:**
Conventional View: (Starting with Smith)
Things are worth the work people are willing to do to acquire them.
Binary Economic View:
Things are worth the work people are willing to do themselves
and/or the work they are willing to employ their capital to do to acquire them.

9. **The Earning Capacity (Rate of Return) of Capital** is a Function of ________:
Two Views:
Conventional View
1. the willingness of people to work at an agreed-upon wage,
2. the scarcity of capital,
and (according to the binary view):
3. ***the distribution of capital acquisition.***

9. **Binary Growth:** (A New Proposition in the History of Economic Thought)
Because demand for capital investment is dependent on
demand for consumer goods in a future period,
a voluntary pattern of steadily broadening capital ownership promises
1. more production-based consumer demand in future years and therefore
2. more demand for investment in earlier years.

10. **The Financial Impact of Binary Growth**
A broader distribution of capital acquisition, ownership, and income
1. strengthens the promise of capital to pay for itself out of its future earnings, and
2. makes profitable the employment of more (and increasingly more productive) labor and capital.

III. A Plan for the Euro-Zone

In Cooperation With The Member States, The European Central Bank Should Open
The System of Corporate (Which It Presently Facilitates) So That All People
May Competitively Acquire Capital With The Earnings of Capital.

(Note: The voluntary system advanced in this presentation is not the only one consistent with binary principles it is merely a proposal that makes the fewest changes the existing system necessary to manifest binary growth.)

1. **The General Theory Diagram**, which shows six institutions of Corporate Finance.
(1) a corporation, (2) an ownership-broadening, constituency trust, (3) a lender,
(4) a private capital credit insurer, (5) government reinsurer, and (6) the central bank.

2. **How Corporations Grow**
1. Retained Earnings (70+%)
2. Borrowed Money (25+%)
3. Sale of Stock (5 -% – in some years negative)

3. **The purpose of corporate finance** is to enable a corporation to acquire capital assets ***before*** it has earned the money to pay for them

4. **The Earnings of Capital & Retained Earnings**

"Profit (and Loss)" or "Income" Statement

Revenues	100
Minus Expenses	
Labor	-40
Supplies	-20
Interest	-10
Depreciation, Research, & Development	-10
Profit Before Taxes ("the earnings of capital")	20
Minus Taxes ;	-5
Net Profit After Taxes	15
Minus Dividends	-1
Retained Earnings	14

5. **The Distribution of Wealth in Almost All Capitalist Economies**
(in approximate terms)
1% of the people own 50% of the capital
10% of the people own 50% of the capital
90% of the people own 10% of the capital
and most of the people have a negative net worth (i.e., assets – liabilities < 0)

6. The Distribution of Wealth in Almost All Capitalist Economies Indicates that
1. Almost all capital is acquired with the earnings of capital, and
2. Very little capital is acquired with the earnings of labor.

7. **The Primary Institution Used To Acquire Capital With The Earnings Of Capital Is The Corporation.**
(The corporation is not an evil; it is a tool that can be used for good and evil.)

8. **Major Credit-Worthy Corporations**
In the USA, these eligible corporations would generally (though not necessarily) number among the three-thousand or so largest corporations.
In the Euro-Zone, it would include comparable corporations,
The next slide shows how corporations can employ corporate finance to broaden their share ownership.

9. **An Ownership-Broadening Way For Corporations To Grow Using Constituency Trusts and Third-Party Beneficiary Contracts**
(Shown on the following three-box chart)

10. **Constituency (or Ownership-Broadening)Trusts:**
National Law would authorize establishment of "constituency trusts"
(also called "ownership-broadening trusts")
which would be empowered to borrow funds
to acquire "full-return" common shares of stock
from participating corporations
for the benefit of
employees, consumers, and neighbors of the participating companies,
and welfare recipients and other poor and working people.
The employees of participating companies and other "binary beneficiaries"
incur no personal liability for the capital acquisition loans.
As to binary beneficiaries the capital acquisition credit is non-recourse.

11. **The Loan Transaction**

The bank loans funds to the trust in return for a promissory note secured by
the pledged, anticipated profits of the capital acquired,
the corporate common shares of stock to be acquired by the loan,
and market-priced, capital credit loan insurance
as a substitute for collateral.

12. The trust invests in ***"full-dividend" common shares*** of the corporation
at fair market value.
These shares would pay their full return
(net of reserves for depreciation, research, and development to maintain
the competitive productive capacity of the capital)
first to repay the capital acquisition loan obligation
and then to provide a capital source of income
to supplement wages and welfare benefits.

13. The Corporation's Capital Acquisition

With the cash received for its stock, the company makes the investment and
(if all goes according to plan)
distributes the income earned on the capital investment
to the ownership-broadening trust
which uses the funds to repay the loan obligations and
then distributes all net earnings to the beneficiaries

14. **Capital Credit Insurance As A Substitute For Collateral. (4-Box Chart)**

(If the capital investment fails ...)
To provide security for the lender-bank and to protect the corporations existing shareholders from losses resulting from corporate investments for which those shareholders stand to receive no investment gain, the lender bank purchases a capital-credit insurance from a private capital credit insurer.

15. Projecting Capital-Ownership Distribution-Based Demand

16 Binary Growth

If members of the poor and middle classes are enabled to compete with existing owners for the acquisition of corporate stock representing the capital requirements of credit-worthy companies,

1. they would bring to the bargaining table a chip not possessed by existing owners: a pent up appetite for the necessities and simple luxuries of life that the rich have long enjoyed from capital income.
2. After the acquisition debt obligations have been satisfied, the earnings of capital acquired by members of the poor and middle class, if fully paid to them, will create more production-based consumer demand than if that capital had been conventionally acquired.
3. If conventionally acquired, most of the capital earnings would seek investment opportunities but in the context of weaker prospective consumer demand.

17. Maintaining Market Share in a Growing Economy

To maintain market share in the projected growing economy, producers will have to increase production and productive capacity (more fully utilize existing capacity and acquire more capacity) before binary income begins to be distributed to its new owners.

18. Some Additional Effects of Broader Capital Acquisition

1. As capital income is more broadly distributed to welfare recipients, government transfer payments can be reduced, and corporations whose shares provide that income can be given a tax deduction.

2. As capital income is more broadly distributed to taxpayers, they will pay more in taxes thereby increasing government revenues and providing a basis for tax deductions for corporations whose shares provide that income and/or general tax rate reductions

3. As poor and working people are provided a more competitive means of acquiring the least risky, most insurable capital acquisition, well-capitalized people will have incentive to move further out on the investment risk curve, thereby providing more financial capital for entrepreneurial activities, the development of new technologies, start-up companies, and smaller companies,

4 The growing capital-based consumer demand generated by binary financing will make more capital investment credit-worthy and profitable and less risky, and therefore more insurable, less expensive, and more profitable.

Over the same period of time, in a traditional economy, with relatively less capital-based consumer demand, capital investment will be riskier, and therefore more expensive, and less capital investment will be credit-worthy and profitable.

5. With a broadening distribution of capital ownership and income so that the supply generated by technological change and increased investment will be increasing balanced by a corresponding increase in demand, the amplitude of the booms and busts of business cycles will be reduced.

6. Thus, binary financing will reduce systemic risk.

19. Ownership-Broadening Growth Without Redistribution

1. Ownership broadening growth does not require anyone to work harder or smarter.
2. It is not caused (although it is accompanied) by an increase in capital investment, advancing technology, or any other traditional basis for growth.
3. It is not the result of a redistribution, because it only materializes from the broader pattern of capital acquisition generated by the voluntary operation of the binary economy that enables all poor and working people to acquire capital with the earnings of capital.

20. Two Additional Steps to Facilitate Ownership-Broadening Capital Acquisition With The Earnings of Capital:

1. A Market-Based Governmwent System Of Capital Credit Reinsurance and
2. Central Bank Monetization of Ownership Broadening Financing.

21. Central Bank Discounting:

Consistent with necessary monetary discipline, the central bank would be authorized to discount the constituency trust's outstanding promissory note at its administrative cost.

22. Cost of Financial Capital

Based on experience with present bank loan-service charges, insurance charges of the USA Federal Housing Administration, and the administrative costs Federal Reserve, the cost of borrowing to the constituency trust has been estimated at approximately at less than 5% per year, consisting of

1. 2% bank service charge,
2. 2% for the capital credit insurance and

   1/4% for the central banks administrative costs.

(See Kelso, Louis O., and Patricia Hetter, pp 70-73, 108. (1986). Democracy and Economic Power: Extending the ESOP Revolution through Binary Economics. Cambridge, MA: Ballinger Publishing Co.)

23. Summary of Proposal

The proposal would offer an entirely voluntary means

1. to enable prime-credit-worthy companies
2. to meet any portion of their capital requirements
3 while simultaneously enabling their employees, customers, neighbors and others to acquire
4. (with non-recourse, insured, monetized credit)
5. full-dividend shares of the participating companies
6. which would pay their full return
7. (net of depreciation, research, and development reserves)
   first to repay the capital acquisition loan obligation
8 and then to provide a capital source of income
   to supplement wages and welfare benefits.

24 Consider effect of this plan based on the binary premise (contrary to the assumption of mainstream economics) (that a broader distribution of capital acquisition with the earnings of capital ***will*** promote growth). Consider its potential

1. Promote more sustainable growth,
2. Enhance the earning capacity of poor and working people
3. Enhance the capacity of national governments to raise revenue
4. Reduce the need for transfer payment nd other government expenditures
5. Enhance the value of equity investments
6. Enhance the credit worthiness of national governments

25 The Time Frame for Beneficial Effects

Though the income benefits of broader capital acquisition begin only after the capital has repaid its acquisition obligations, what would happen in the immediate future
to the value of equities and the credit-worthiness of government bonds
if binary economic principles were widely understood?

IV. Some Socio-Economic-Political Implications
of Focusing on the Right to Acquire Capital with the Earnings of Capital.

1. A Market Right, Not a Welfare Right
2. An Underlying Economic Cause of the Cold War
3. Voluntary Ownership Broadening Growth Without Redistribution.
4. Growth & Distributional Effects Distinct From Keynesian Analysis and "Free-Market" Neoclassical Analysis, and Marxist Analysis..

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V. A Plan for Greece:
What can Greece do now that it has surrendered its monetary sovereignty?

1. If Greece remains in the Euro-Zone,
   1. Greece can advocate the binary solution for all of Europe, championing for poor and working people throughout the Euro-Zone democratizing the right to acquire capital with the earnings of capital.
   2. Greece can negotiate for itself the power to implement a Euro-based, ownership-broadening monetary policy consistent with binary principles..
   3. Greece can issue a second currency to facilitate ownership-broadening capital acquisition that would float against the euro to unleash the untapped productiveness of the Greek people and the nation's wealth.

2. If Greece leaves the Euro-Zone or if the Euro-Zone collapses, Greece can regain its monetary sovereignty and implement the world's first national binary economy.

3. Whether in or out of the Euro-Zone, Greece can initiate an ownership-broadening joint venture program described below to promote sustainable prosperity.
   1. Create joint ventures of indigenously-owned operating corporations and temporary assistance corporations.

   2. The indigenous operating corporation would be privately owned by their employees.

   3. The shares of full-return stock in the indigenous operating corporations would be acquired on behalf of employees and held in constituency trusts with borrowed money supported by capital credit insurance.

   4. All net income earned by the shares of stock would be used first to repay the acquisition loans and then to pay production-based income to employees, thereby providing the market-based consumer demand for additional capital investment.

   5. The temporary assistance corporations would be owned by those foreign and national contributors of technology, capital goods, supplies, and expertise necessary to build and operate the planned enterprise who accept a security interest in one or more temporary assistance corporations in full or partial payment for their contributions.

   6. Those contributors that require immediate payment for part or all of their contributions would be paid by the operating company with some of funds it received by selling binary s`tock to the constituency trust.

7 Foreign and domestic participation in the joint ventures by way of the temporary assistance corporations would be of limited duration. The foreign assistance company would be required to commit itself by private or governmental contract (or both) to maintain its participation in the joint venture not perpetually but for a specified time period to achieve specific objectives in return for a reasonable profit.

8 After start-up and initial operations of the project businesses, the temporary assistance corporation would sell its interest in the project business through secondary re-offering of shares to eligible local households who own little or no capital, again using insured capital credit to finance the acquisition.

9. Within the Greek economy, existing owners will be free to compete for capital acquisition as before.

10 The cumulative net effect of such a development program will be to create the indigenous productive capacity and widespread earning capacity to provide the basis for sustainable growth, distributive justice, and growing affluence, while creating a credit-worthy history of profitable international economic relations which will make future international commerce all the more auspicious.

11 These benefits will be achieved without abridging the private property rights of existing owners within the developing economy or beyond its borders.

VI. CONCLUSION

1. The binary economic paradigm provides an important new way of understanding the current interrelated Greek, European, American, and global financial crisis. Although the projected distributional and growth effects of the binary proposals seemingly take years to realize, they nevertheless exist precisely in the same time frame as the interest rates that market set for ten-year government bonds. Thus, with widespread understanding binary principles, their effect on the credit worthiness of national debt would be immediate.

   Thus, the binary economic paradigm provides an important new way of mitigating financial crises by enhancing the prospects of
   1. the value of equity securities
   2. the solvency of pensions and social programs
   3. the growing earning capacity of poor and working people
   4. the credit-worthiness of nations and their bonds,`
   5. the dependability of government revenue sources
   6. the credit-worthiness of nations and their bonds,
   7. sustainable growth, and
   8. prosperity without austerity.