

December 2019

VOLUME X, ISSUE XII

PEGASUS

A NEWSLETTER FOR THE CAUX ROUND TABLE FOR MORAL CAPITALISM
NETWORK LOOKING AT BUSINESS ABOVE THE CLUTTER AND CONFETTI



Pegasus

Introduction by Stephen B. Young

Page 2

Proceedings of 2019 Global Dialogue

Page 4

Introduction

This issue of Pegasus brings you a report summarizing the discussions at our 2019 Global Dialogue.

A reflection on dialogue and its contribution to ethics might be timely, given the rise in protests from Hong Kong and Iraq to Chile and Paris and the breaking apart of community solidarities – say, Brexit or the intense passion to impeach Donald Trump, driving 48% of American voters offset by an equal determination to defend him at all costs directing the emotions and politics of a different 48% of the voters.

The Caux Round Table for Moral Capitalism (CRT) began in 1986 with a dialogue among Japanese, European and American business executives on the then (and now again today) divisive dynamic of populist nationalist trade protectionism.

Dialogue – words between two or more persons – is ethics in practice. It is the surrender of the right to impose or dictate beliefs to others. It requires some humility in being willing to listen. Dialogue does not presume that one party will be the winner. Rather, I think, the presumption is that the exchange of words will lead to changes in thinking, values and understanding on several sides with the hope of reaching agreement.

We also know the phrase “dialogue of the deaf,” where no real dialogue takes place and where positions are taken and firmly held without regret or apologies.

We might say that dialogue encourages win/win outcomes and seeks to prevent win/lose, zero/sum, antagonisms.

Dialogue does not require the surrender of our own narratives or our convictions as to higher values or the truth itself, but as a process, it insinuates that our personal narratives and our perceptions of the truth may be only contextual with limited validity for others because the dialogue may change our understanding of the relevant context.

Dialogue works because the human mind can learn and because goodwill is a human capability reinforced by reciprocity which opens minds to trusting others and learning from them.

The CRT's Principles for Government adopts much of what German philosopher Jurgen Habermas called "discourse ethics" – the reaching of decisions and the building of community through engagement with others, not through violence or other compulsion.

Evidence of the power of dialogue to do good has marked the work of the CRT over the years. Those who have gathered at our round tables and global dialogues have changed the minds of others and changed their own minds. Their observations and reflections after discussions and debates and sometimes just conversation have led to important insights and recommendations not forthcoming from individual minds alone.

Dialogue is a best practice in making ethics practical and effective.

Stephen B. Young
Global Executive Director
Caux Round Table for Moral Capitalism



Caux Round Table for Moral Capitalism 2019 Global Dialogue
"Three Paradigms for the Global Economy:
Nationalized Socialism, Brute Capitalism or Moral Capitalism?"

November 22 and 23
Minneapolis, Minnesota

Proceedings

Introduction

The Business Roundtable provided in August 2019 a compelling case for a moral capitalism. The Roundtable affirmed that the purpose of a business is to take due care of its stakeholders: customers, employees, owners, creditors, suppliers, the environment and the community. In capitalism, the purpose of stakeholders is to sustain business profitability in return for goods, services, incomes and wealth creation.

As Adam Smith insightfully wrote, the moral basis of capitalism is reciprocity. The most important reciprocity is between the company and its customers. Every business fails which does not provide what customers will pay for. Business success - pricing power - comes from benefiting others.

From the exchange of goods or services for money, wealth is created and a firm's dependent constituencies can prosper - employees, owners and suppliers.

But there must be reciprocity between the firm and the community, including the environment. A business needs a supportive community - contract law, property rights and community approval of its goods and services. A business-driven capitalism which degrades our planet cannot survive.

The best companies prosper thanks to inspired employees. As a leader, you have a limited

number of tools to reward your employees for great work. In my experience, being proud of their work on a daily basis is, for most people, the most powerful spiritual force at work in our economy.

Competition with a company with an inspired work force when your employees are lackluster is a formula for failure. It is, therefore, the responsibility of leaders to make choices that allow their employees to be proud of what they do and help the employees see their contribution to their community.

If a business executive limits the purpose of the enterprise to providing cash returns to owners, he or she off-loads responsibility to passive third parties and so subjects the company, its customers, employees and even its owners, to moral hazard. Future threats and opportunities are not managed well because immediate pressures are given full attention.

Focusing on the wrong ends leads, as well, to spiritual emptiness, wherein there is no will to care, no commitment to run risks and no conviction that life is good. The wrong ends engender mediocrity which metastasizes its downside risk throughout an organization or a culture.

Capitalism is worth improving. Capitalism has given us modern civilization – per capita incomes stratospherically above those of our ancestors; better health and longer lives; opportunities for self-actualization unheard of in human history; middle classes which support constitutional democracies, value human rights and prefer social norms of tolerance and pluralism.

But capitalism is vulnerable to imbalances where reciprocity declines and some do so well they can turn their backs on others. We are now experiencing such a period of imbalance, as finance has become the driver of much higher returns to money than to labor and other forms of human capital.

At the Caux Round Table for Moral Capitalism (CRT), we refer to this as “moral capitalism” and we are committed to its deployment in the communities we serve. We also believe it can be harnessed to take on challenges more effectively than any other social system.

Brad Anderson
Co-Chairman
Caux Round Table for Moral Capitalism
Former Chairman and CEO of Best Buy Inc.

Overview of Global Dialogue Sessions

Last year, participants at our 2018 Global Dialogue gathered at a time of uncertainty and discontent in our global order. The various modes and instances of dissension and divergence were many. The Dialogue advanced a statement of ethical principles which should guide reciprocally those who seek new homelands as refugees and migrants and those who open their nations to them.

In 2017, the CRT convened its Global Dialogue in Wittenberg, Germany. Five hundred years earlier, that small German city was host to a revolution in vision and spirit responding to humanity's deepest needs for clarity of purpose. This is not to say that Martin Luther solved our problems in finding happiness and well-being, but to note that principles enunciated there in 1517 shaped humanity's evolution into today's global civilization.

In terms of fair and principled politics and governments, necessary for the rule of law and a moral capitalism, our current moment, again, gives cause for concern.



Herman Wijffels, former Chairman of Rabobank in The Netherlands, former Chairman of the Dutch Social and Economic Council and member of our World Advisory Council, has insightfully suggested that human history is at an inflection point – an era is ending and few know what is coming next.

Commentators have noted in regard to the rise of populist nationalism that the order established after World War II to prevent such wars seems to be under stress and is, therefore, succumbing to fragmentation. The premise of the CRT from its first meeting in 1986 holds that business enterprise creates the wealth which optimizes human well-being. How, then, should business enterprise respond to the current trends shaping our global community?

Others have summarized the options for humanity as: nationalized socialisms, a “devil takes the hindmost” kind of capitalism or a moral capitalism.

The first session of the 2019 Global Dialogue invited consideration of the highest and best purpose of the business firm. A movement seems to be underway to integrate moral considerations into business models and risk management modalities. The Business Roundtable has adopted the stakeholder model of corporate governance which has been advocated by the CRT since 1994. The U.N. has adopted 17 Sustainable Development Goals which cannot be achieved without actions by business and finance. Investors, more and more, are allocating investment capital to firms which integrate ESG variables (environment, society and governance) into their operations.

The second session then turned to consideration of finance as the necessary substance for enterprise. Though unavoidable in any market capitalism, finance has its dysfunctional dynamics. Since the tulip mania of 1637, debt incurred to buy ownership of financial contracts can bring about misleading valuations of those contracts which result in the collapse of trading markets and much loss of wealth. The pertinent question for financial markets today is how will they sustainably support stakeholder capitalism?

The third session of the Global Dialogue sought clarification as to the contributions of intangible forms of capital – social and human – in post-industrial global capitalism. If such capitals contribute to firm success, then investors should invest in them, as assets and owners should measure them and manage them for long-term value appreciation.

Session four put on the table for innovative consideration the best method to be used for finding the value of a company.

Session five directed our attention to whether there are moral fundamentals governing the relationships which support or limit the accumulation of social and human capitals which can become full partners with self-interested economic incentives in shaping the outcomes of capitalism.



Session six responded to the robust opposition to capitalism now shaping the 2020 election. Demands by Bernie Sanders and Elizabeth Warren for a “Green New Deal” proposes to socialize most of the American economy under administrative regulation and transfer payments from the rich to the poor.

Session seven posed the question of whether the current rise in populist/nationalist leaders and political movements based on identity politics of race, ethnicity or religion will create the structure for the coming era of global civilization. Nationalist socialisms in various forms would seem to be the most suitable form of economic organization for such a fragmented world order.

It is up to us now not just to walk along with our heads down, just accepting whatever comes, but to assert anew, in our time, values and ideals which lead to courage and constructive action among good people everywhere.

We welcome you and look forward to your contributions towards an enlightened analysis of where we are and where we should seek to go.

Stephen B. Young
Global Executive Director
Caux Round Table for Moral Capitalism

Session 1 The Purpose of the Corporation: Stakeholders or Shareholders?

Participants reviewed the Business Roundtable’s Statement on the Purpose of a Corporation, really of any business entity operating in market economies. There was little disagreement that a business entity has to be much more than an exclusive contract between selected private parties only for their mutual benefit. A business enterprise, it was said, must be more inclusive, given its reliance on an ecosystem and its impacts on strangers to the organizational contract. At a minimum, a business enterprise depends on the state for enforcement of contracts and for the continuous maintenance of market reliability.

The corporate form requires a guarantee from the state that investors in the business entity will not be liable for the debts of the business. Thus, a corporation is very much a creature of the state and not a self-sufficient, ruggedly autonomous actor which can be imperiously heedless of its circumstances. But from this same perspective of dependence on others, a corporation must reconcile its business purpose with the interests of its shareholders.

But one question is: what interest of shareholders is most material to the corporation profits or capital value?

That non-shareholders have vested interests in the business is a reality. There is tension between those various interests, requiring the firm to balance what it delivers to different stakeholders in a balancing of the equities, as lawyers would say. A business succeeds or fails in an ecosystem, a complex, interactive network reaching out beyond the formal legal structure of positions, roles and responsibilities which form the internal social system of the company.

Session 2 Financial Intermediation: Capitalism's Dr. Jekyll or Mr. Hyde?

There is a growing belief that something in capitalism is broken and it is most likely finance. On the other hand, it is financial intermediation which provides funds for risk-based business undertakings. What protections are needed to ensure the continuous willingness of investors to entrust their money to others for a promised future return? When money is matched with production, everyone is better off.

But any system can lose equilibrium if it tilts too much to one side or the other. President Theodore Roosevelt spoke of the "swollen fortunes of the few." The global economy now has produced great inequality where 1% of the population has vast wealth and the top 10% controls more wealth than most of the rest combined.

In 2019, Credit Suisse estimated that the top 1% held 43.9% of the world's wealth, the top 10% of adults held 82.8%, while the bottom 90% held the remaining 17.3% of the world's total wealth.

In the U.S., the top 1% controls more than half the equity in public companies. Of all the assets and liabilities of the financial sector, only 10% are loans to production.

A comment was made making reference to the physical laws of thermodynamics that finance is the natural flow which sustains economic activity. Many tributaries combine to contribute flow to the main channel which provide nourishing energy to wealth creation. Contracts channel the flows and move flows towards a common enterprise - production. The flows overcome obstacles to keep moving forward, just as water always wants to flow downhill. The channels open and close, move right or left, as they must to keep the flows moving. The main channel then divides and branches out, as a river does when forming a delta to distribute the flow into smaller channels.

The proper function of finance is to get the flows into the delta where they are absorbed and turned to good use. Thus, the value of finance is to fund growth in production of goods and services.

The analogy to the flow metaphor is that stewardship in finance – knowing through face-to-face relationships who benefits from the flow – is needed to optimize the value contributed by the flow.

With the rise of proprietary traders in finance, stewardship relationships in finance were abandoned. Those directing the flow were no longer concerned for feeding the distributing channels of the delta. There was a cultural shift in financial firms where value was just associated with cash returns.

It was noted that, among humans, flows follow trust. Where there is no trust, nothing flows and stagnation sets in. Growth declines. The Edelman Trust Barometer has documented declining levels of trust among Americans.

One participant noted the emergence of SRI funds and funds investing where companies demonstrate commitment to ESG values – having regard for the environment and society and using good governance. These two modes of investing contribute to enhance trust in business.

But additional measures of addressing stakeholder interests are needed.

Session 3 – Social and Human Capitals

It was noted that there is a predilection for the centralization of bureaucratic power in corporations which in turn facilitates a concentration of money, but that the most empowering entrepreneurial environment is one of shared trust.

In most industries, three firms share most of the market, creating barriers to entry for innovators. Concentration of market power permits more rewards to shareholders than to employees and lowers demand for investing in a trusting corporate culture.

The most predictive indicator of business success is employee engagement. Employees, therefore, are an asset which like financial assets, earns profits for the firm. There is often in firms a disconnect between leaders and employees. There are dynamics which incentivize toxic personalities, not trust. Trust augments social and human capitals.

Start-ups survive on their social capital, while they seek market penetration. Their most valuable asset is a sense of purpose, leading to dedication in work habits. Companies should invest in emotional connections.

Session 4 Valuation

Some preliminary comments were to note the importance to firm success of supply chain integrity. What happens beyond the firm can dictate outcomes for the firm.

Paul Polman, Chairman of the International Chamber of Commerce and former CEO of Unilever, in his luncheon remarks tied long-term value of a company to: 1) its efforts to deal with carbon; 2) its ability to move towards a circle economy minimizing waste; 3) its inclusiveness and providing hope for employees; and 4) its ability to serve financial markets.

Knowing the ecosystem in which the firm seeks profitability permits prediction of its future expectations of success or failure. The discounted future cash flows of a firm is the best method to gauge the quality of its interactions with its ecosystem. The margin it can charge reflects its value to customers. The merits of its goods and services attract or create customers. Perceived value which is a freely chosen social good adds to a company's margin on sales. Responding to perceived value with a business model is a social process and so what is thereby created by the firm – brand - is a form of social capital with value to the firm in that it creates profit flow.

The winning formula for a firm is: acquire the value of trust; create value for customers; accept that responsibility is financially valuable. Then, the result is value to the ecosystem, external to the firm.

But some customers are unwilling to pay for intangibles; low cost is of more value to them. This reflects Maslow's hierarchy of needs where first-order priorities are more tangible. From a utility point of view, where the marginal utility of money is high, lower cost is important and substantive value is preferable.

It was noted that “unicorns” – start-ups with remarkable high capitalizations – are presumed to have exponential growth prospects and “stickiness” in their customer value propositions. The justification for their high valuations is the assumption that with enough volume, the fixed costs per unit will drop, so margins, will at some time, rise to profitability.

Valuation needs sensitivity to the innovator's dilemma – decay setting in at the height of

success. How to spot in advance the tipping point when the benefits that came with innovation have lower and lower marginal utility and the firm becomes ossified.

Valuation also needs sensitivity to the herd dynamic in financial markets where irrational exuberance takes over pricing and asset bubbles form. Value in such cases is found outside the bubble in non-financial market realities.

How could leadership – seeing what is coming with unicorns with innovations living on past their prime and with bubbles – be valued?

Session 5 The Predicates for Moral Capitalism: Moral Sense Theory and Reality; an exercise in design thinking

Design thinking is simple: first, find a problem and reframe it. Design thinking generates innovations. It is a flow dynamic keeping up with realities, as history moves through time from past to present to future. Secondly, resolve conflicts, move towards win/win outcomes among stakeholders, avoid bi-polarity and find the third way or plan B.

Adam Smith, in his conceptualization of the early phase of the Industrial Revolution, was a design thinker. His proposal that an invisible hand was at work in trade so that multiple parties would benefit was a win/win insight.

Today, the win/win solution is to put moral sentiment into global capitalism.

Jonathan Haidt writes of moral foundations universal to all people. The human brain has its set ways.

This would argue for a shift in economic thinking away from the absolute of ownership to multiple points of access to goods and services. Consider the circle economy where a chain of owners each has only for a limited time control over the good or service and its consequences. What, then, is a property right? For how long does it personal dominion over something of value?

What is scarcity today with data capable of being stored and used by AI? Where sunlight is a limitless source of energy for our civilization? With the sharing economy where under-utilized assets are made available outside of the buying and selling of exclusive ownership rights?

The question was raised as to who does design work – systems or individuals? Who delivers the design and who the implementation? At what level of hierarchy and with what requirements for collective assent? Plato wrote in praise of a philosopher king who should have authority over society’s design process.

Technology is largely for private sector design.

The jobs that will be resistant to automation are those which demand human-to-human interaction – care of others; communications.

Parenting is the basis of every person’s moral sense, so parents are vital designers for society.

We do not have much design in our food system where sugars, salt and fat are plentiful, but lead to diabetes with great long-term cost to society and hardship for individuals.

Also, the current design system around debt using “other people’s money” seems unsophisticated, as it creates moral hazard, time and again, in financial intermediation.

Session 6 – The Green New Deal and Responsible Sustainability

Do we have, to any degree, a shared interest in the future? What principles do we have which can be put into practice? A middle way among conflicting approaches suggests itself. Such convergence would result from good design thinking. Local community actions networked into wider structures of behavior are preferable.

It was commented that as a global system, we would then have many tributaries contributing flow to a larger river which would end up circling back to refresh the tributaries.

One kink in our system is too much choice in the selection of facts used to argue for policies. The RAND Corporation has written about “fact decay” where curiosity to learn facts has diminished and presuppositions as to the facts have gained sway. No one owns the truth in what should be an open-ended and open-sourced process of decision-making. For example, with respect to energy, the facts about batteries – storage and disposal – are ignored.

If sustainability is to be an outcome for humanity, then good governance must become a driver of decisions. How organizations run themselves is of paramount importance.

Lack of sustainability takes the most toll on those who live in poor economies. They are the most subject to the harms coming with climate change.

Session 7 Populist/Nationalism and Ethics: A Challenge for the Global Community?

Populist/nationalism responds to elite failures. Populism and nationalism also respond to the conditions, the imbalances, of late stage capitalism. These cultural movements seeking protection and security for middle and lower classes erode the margin of truth; the veneer of civility thins; holes appear in the social fabric which expose humanity's lingering primal nature, which is rather Hobbesian.

The primary question then becomes is the economy serving people in their daily lives? Another factor is the impact of economics on one's sense of dignity and worth. Capitalism may be undermining that reassurance for many people in the world today.

Governments manage the dynamics of who gets what to guide the flow of benefits to all. Ethics is caring about others and is a cultural discipline, but governments are elite structures and do they drink deeply at the well of ethics?

Ethics is caring about others and is a cultural discipline, but governments are elite structures and do they drink deeply at the well of ethics?

It was noted that the Basel Accords for banks defined certain investment contracts of governments as "risk free" which introduced more moral hazard into global finance. There was a declining perception that certain investors had "skin in the game" and so were favored with the opportunity to spend money foolishly.

Abuse of power is not limited to government officials, but follows power of whatever nature to all manner of circumstances. Both populism and nationalism are protests against abuses of power in our world. Since elites hold power, they subject themselves to opposition and disrepute.

Stephen B. Young

Rapporteur

December 2019



www.cauxroundtable.org | Twitter: @cauxroundtable | Facebook: Caux.Round.Table

“If I say that it is the greatest good for a man to discuss virtue every day and those other things about which you hear me conversing and testing myself and others, for the unexamined life is not worth living for men, you will believe me even less.”

— Socrates

