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Capitalism's renaissance? The potential of repositioning the financial 'meta-economy'

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ABSTRACT

This paper examines whether the prevailing model of capitalism with its hallmark financial markets is the most productive and stable investment system to underpin the global economy into the future. It returns to the creation of the stock market in 1602 to examine the stock market's origin without the presumption of its respectability. Often considered the genesis of modern corporations and contemporary financial markets, its venerable status is questioned. The instability of the system, established incidental to the Dutch East India Company's solution for financing East Indies voyages and never intended as a model for global capitalism, is found to be insurmountable. Rather than extrapolating the current trajectory of capitalism, an alternative future based on the expansion of productive primary economic activity, is considered. A movement that is evolving spontaneously around innovative lending to expand business enterprises in the primary economy offers the possibility of this alternative future with goals other than amassing capital, more akin to the economic model that originally funded the Renaissance.

1. Introduction

Just as it was being embraced globally, the 2008 Financial Crisis shook faith in contemporary western capitalism and damaged the reputation of its hallmark financial markets, triggering a quest for a more stable structure. Vehement criticism, particularly of stock market volatility and derivatives, has come from a wide spectrum of economists. Their response has overwhelmingly involved regulation, usually favouring elements of the suite of reforms that Bello describes as having 'real teeth': the 'banning of derivatives, a Glass–Steagall provision preventing commercial banks from doubling as investment banks; the imposition of a financial transactions tax or Tobin tax; and a strong lid on executive pay, bonuses, and stock options' (Bello, 2013). Less popularized, more targeted reforms of the stock market include Stiglitz's proposal that there should be only one other trading period after the initial public offering of shares (Stiglitz, 2013, p. 115) and Keen's 'jubilee shares' that expire after 50 years (Keen, 2012).

This paper does not propose the regulation or reform of the stock market nor consider the merits of any such proposals. It takes an entirely different approach. Rather than asking the non sequitur: 'How can we control 'free' markets better?' capitalism is examined more broadly to establish whether the prevailing system is the best model to underpin the global economy. It contests the view, implicit when only regulatory change is prescribed, that secondary markets are essential or

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too important to be allowed to fail and sets out to demonstrate why capitalism requires re-structuring which involves more than re-adjusting regulations. It proposes that marginalising secondary markets is both justified and of greater benefit to capitalism than their protection or reform.

A premise of this paper is that 'investment' should directly relate to productive enterprise, not to unproductive financial transactions. The relationship between primary and secondary markets is its focus. The term 'meta-economy' is coined for the aggregation of secondary markets in order to position them with respect to the primary economy. As Westerhoff notes, this relationship has been studied less than the workings of the secondary markets themselves; the academic focus has been on 'the dynamics of financial markets and (virtually) nothing is said about how the dynamics of financial markets impacts on the real economy and, likewise, how changes in the real economy affect financial markets' (Westerhoff, 2011, p. 21).

The most commonly accessed capital-raising secondary market is the stock market and, as a vital interface between the financial sector and primary economy, it is the focus of this paper. Singh (1993, p. 23, 2010) has recommended bank-based investment rather than the development of stock markets in emerging economies but this paper's proposal is slightly different, recommending the demotion of the stock market, in favour of primary market investment as a different capitalist paradigm. This future for capitalism may even have been instigated already; 'peer-to-peer' investing, an alternative means of raising capital has developed spontaneously and rapidly while the number of companies listed on US stock exchanges peaked in 1997 then fell by 38% until 2013 (World Federation of Exchanges data) and a similar decline occurred in Britain. The proposed paradigm is not entirely new, however, as something similar operated during the Renaissance (Gelderblom, 2010; van Zanden & van Leeuwen, 2011).

It is difficult to position this paper as it does not sit easily within the existing literature but spans across much of it, idiosyncratically linking apparently conflicting ideologies over the 400-year history of the stock market. It accepts both Marx's view of the stock market as a 'paper economy' (Marx, 1894, Chap. 29; Stanford, 1999, 2008) and the aspirations of neo-liberal financiers who seek to operate within unrestricted financial markets. Support for the unfettered operation of the stock market, however, is not given with conventional justifications like 'increased efficiency', 'transparency' or purer 'price discovery' and there is no engagement in the debate which pre-occupies the whole spectrum of financiers and economists from Greenspan (Andrews, 2008) and Bernanke (2014) to Shiller (2012), Krugman (2012) and Stiglitz (Moss & Cisternino, 2009) regarding the optimal nature and level of financial regulation. This paper examines history to argue not only that the very nature of secondary markets makes regulation ineffective in achieving stability, as has been demonstrated throughout their existence, but also that they are not essential to capitalism. Unfettered secondary markets are given a place in capitalism's future simply because they are a means by which investors can retrieve their investment capital and the coincidental speculative activities that are facilitated represent longstanding and entrenched economic freedoms; such individual liberty being a defining principle of capitalism along with private enterprise. This paper seeks to define a capitalist structure that allows secondary markets to be circumscribed via a better understanding of their essential nature rather than imposing a changeable stream of regulations. In broad terms, this paper can be considered as 'pro-capitalist, anti-secondary-market', a vital distinction lost in most 'anti-market' rhetoric. It has no directive regarding state ownership or government intervention and no generalised preference for globalism or localism.

The functioning of the stock market poses many ongoing theoretical challenges: Berle's 1962 call (Ireland, 2001, p. 15) for a new philosophical framework distinguishing share purchases from 'investment' remains unanswered; there is no agreement on the causes of repeated market failure, only a plethora of disputed reasons, unique to each crash; philosophies of market control are contradictory (Shiller, 2004, p. 14); opposing views are taken on the stock market's role as an economic indicator (Bosworth, 1975; Stock & Watson, 1989); research to relate share prices to their company's underlying value has produced inconclusive results (Fama & French, 1995; Djajadikerta & Nartea, 2005); advantages of financing companies by equity rather than debt are equivocal (Parrino & Weisbach, 1999, p. 4); in 'balanced portfolio' pension default settings, shareholdings are acknowledged as 'high risk', the definition of 'market stability' is uncertain(Foot, 2003) and even the stock market's driving forces are disputed. Intelligent investors have been caught out by stock market caprice for centuries: Isaac Newton lost 88% of his South Sea Bubble stake (Levenson, 2009, p. 244), Maynard Keynes dropped 82% of his peak portfolio value in the 1929 Crash (Skidelsky, 1992, p. 342), Long-Term Capital Management lost \$4.5 billion in 1998 (Lowenstein, 2008) applying directors Merton and Scholes' Nobel Prize-winning derivative valuation formula and Warren Buffet lost around \$67 billion in the 2008 Crash (Beales, 2009) For nearly a century the stock market has been denigrated as a 'casino' by eminent economists from Keynes (1936) to Stiglitz (2013, p. 91) and Kay (2008). Nevertheless, it remains a central pillar of contemporary capitalism and its most venerated institution (Stiglitz, 2013, p. 98).

Since its inception, the stock market has been repeatedly subject to shocks. Focusing on historic crashes separately has resulted in their 'causes' typically being identified amongst unique contextual factors. This paper reasons differently, proposing that the market itself is the problem and external contextual factors merely set the scene and act as triggers. All crashes are, therefore, symptoms of an unsound structure, the capricious stock market being easily de-stabilised by myriad external factors. The unpredictability of psychology (and reverse psychology) on the sentiment of diverse traders that drives the endless trading of intangible business arrangements in the stock market creates a pervasive potential instability which can be triggered by many factors from political instability to de-regulation or irrational exuberance. Of all these variables, none are readily governable to provide stability to the whole; so overhauling capitalism requires more than re-setting financial market regulation.

A pre-occupation with financial market dynamics can reduce the future of capitalism to the identification and vilification of various aspects of financial markets with critics railing against 'Wall St', exotic derivatives, the actions of speculators or the