Corona, Command and Capitalism

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"Tobacco sales ban is cruel, unworkable and unscientific" (ANA Reporter, 2020)

On 15th March 2020, South Africa's National Coronavirus Command Centre imposed social distancing measures (lockdowns), applied price controls, "asked" data providers to offer free services and banned sales of tobacco and alcohol (vanStaden, 2020). Whilst the constitutions of most liberal democracies provide the legal principles which define the relationship between civil society and emergency state powers, the extent of these powers, invoked not by the horrors of war but by a microscopic virus, have ranged from Hungary's "rule by decree with no end date" (Quinn, 2020) to Sweden's "official advice to citizens" (Klamberg, 2020). In many instances it makes business sense for companies to align themselves with the current mantra (be this "coronavirus", "climate change" or "gender identity"), but at what point should we question the cost to shareholders for the public good?

Shareholder primacy

The stakeholder versus shareholder primacy debate has raged for decades; itself an indication that these issues are not well understood (Smith, 2003).

Milton Friedman has habitually been quoted as the seminal advocate of shareholder primacy:

"There is one and only one social responsibility of business — to use its resources and engage in activities designed to increase its profits so long as it … engages in open and free competition, without deception or fraud." (Friedman, 1962)

Alternatively, promoters of stakeholder primacy have argued that all individuals or entities contributing to the business are stakeholders, whose opinions should be considered in decisions. One essential departure point has been whether, and to what extent, shareholders may need to forgo profits to benefit other parties (Smith, 2003). What differentiates the state from other stakeholders, is its power to command a stake via legislation.

Corona complications

In April 2020 Glencore announced the closure (for three months) of its Mopani mine in Zambia on account of low commodity prices – an indirect consequence of the coronavirus. In a letter to the CEO Nathan Bullock, a furious Zambian mining minister threatened to revoke Glencore's license to operate, endangering the Swiss company's $4bn investment in the country. Mr Bullock was later arrested at Lusaka airport (and subsequently released)

(Hume, 2020). Whilst it seemed obvious that closing the mine was in the best interest of shareholders, it clearly impaired Zambia's ability to service its $11bn offshore loan commitment and, by extension, the public good.

As with Glencore in Zambia, governments and unions have been quick to recognise the hazard the pandemic has presented to jobs (Martin, 2020). South African Airways, a state-owned enterprise, which had previously received more than R20bn of tax-payer support, entered business rescue at the start of the pandemic. SAA was criticised when it offered severance packages to its entire 5000 workforce after failing to secure another bailout (Smith C. , 2020). With billions lost, was it unreasonable for shareholders to insist on retrenchments and assets sales through "restructuring", "right sizing" and "turnarounds"? And, since the shareholder is the government itself, must taxpayers continually foot the bill?

Banks in trouble

If markets were to be believed, in the long-term the Corona crisis was likely to be (economically) worse than the 2008 financial crisis (Chaudhry, 2020). The Bank of England indicated that the UK was facing the worst recession in 300 years (Giles, 2020). In 2008, after Lehman Brothers failed, the Federal Reserve Bank followed conventional economic remedies; firstly, short-term interest rates were rapidly cut from 4.5% to (almost) zero. Secondly, the US government commenced fiscal measures: TARP[1], purchasing assets, bailouts and infra-structure projects. To make these actions less costly the Fed brought into being "quantitative easing" (Chappelow & Scott, 2020). Unfortunately, the COVID-19 crisis has come before banks have recovered, and with little conventional economic ammunition to fight the nascent economic catastrophe, new weapons such as "helicopter money" have been touted (Stevis-Gridneff & Ewing, 2020).

If central banks are in trouble, corporate banks are too (MacKillop, 2020), as evidenced by the ratings downgrades of five South African banks (Mkhabela, 2020). For the decade preceding Corona, commercial banks had been engaged in continuous operational restructuring: axing jobs and selling assets - the main reasons being lower interest rates, cybercrime, increased competition from shadow banks and technology (Carney, 2018). With already high levels of debt in the economy, "kicking the can further down the road" by funding debt problems with more debt, was not a solution:

> *"Nationalising the losses from the corporate sector is one thing. If you go down the route of forcing the banks to take the losses and then have to nationalise the banking system, you have a far bigger problem" (Jenkins, 2020).*

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[1] Troubled Asset Relief Program

Privatising profits and socialising losses (Kenton, 2019)

In the wake of the 2008 global financial crisis, on 1st June 2009, the 101-year old General Motors company, with 240 000 employees, filed for bankruptcy. GM was burning cash at the rate of $3bn per month as buyers shied-away, fearing failed guarantees and low re-sale values. Amazingly, 40 days later the US government, under the Obama administration, injected a record amount of $50bn into GM, accepting a 61% equity stake in the company. Many argued at the time that this was a gross misallocation of tax-payer resources (McTague, 2009). Over the next months, hundreds of properties and plants were liquidated, hundreds of dealerships closed, four (out of eight) brands dropped and eleven of the twelve directors replaced. It was trumpeted as an impressive turnaround, with GM showing $4.7bn profit a year later. But, in the final analysis, the US government had lost $10bn when they exited their stake in November 2013, and over the next few years the remaining shareholders lost a further 15% (Wright, 2013).

Many have argued that such interventions helped save millions of jobs whilst others contend that these well-intentioned actions merely created "zombies", with cashflows sufficient only to service debt (Earle, Park, & Schmedders, 2020). Perhaps the strongest criticism related to the corruption of capitalism, which in September 2011 birthed the Occupy Wall Street movement, made famous by their refrain: "privatising profits and socialising losses!".

Would capitalism survive a system in which shareholders, in the good times, added cheap debt to fund dividends and share buybacks, and taxpayers bailed them out in the bad times (Tierney, 2015)?

Problems and penalties

For most companies, restructuring is inevitable. Leadership that maximises shareholder wealth through cheap debt, failing to recognise the ebb and flow of markets, will face the reality of market power through catastrophic restructuring. Those more cautious, engaged in continuous restructuring, are more likely to survive. But, what are the incentives to encourage the latter? What penalties should apply to serial defaulters like Venezuela? What rates should be levied on borrowers like Zambia and other African countries currently requesting $44bn in debt relief (Bartenstein, 2019) (Pilling, 2020)?

In 1850 Lord Palmerston ordered the Royal Navy to blockade the Greek port of Piraeus to enforce compensation claims - the classic case of "gun-boat diplomacy" (Wright O. , 2018). Prior to their banishment in the UK in 1869, Debtor Prisons housed delinquents until they could pay off their loans. This unlikely solution has been replaced by modern bankruptcy laws. Insolvent individuals, through a court order, are granted relief from their debts (Bankruptcy, n.d.). The lender suffers; the idea being that creditors must pay a price for irresponsible lending.

In a time of crisis, these symmetries of debtor-creditor responsibility are appealing, but who takes responsibility for the coronavirus? Can banks further extend loans? Should retrenched workers in restaurants, banks and airlines suffer the consequences of their unfortunate career choices? Must shareholders (read pensioners) shoulder losses to support the public good? Ought governments bail-out frail industries - using tax-payer money? Or do we allow central banks to reduce interest rates and conjure-up billions of dollars via QE and hope for the best?

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