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Musings

#50: Defending Capitalism

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It crushes me to have to write about this but in today's world I feel the need. While far from perfect, capitalism is clearly the best model.

Have you ever seen a government service delivered well? I haven't. I dread the trip to the DMV (took me three hours to get my REAL ID driver's license). How about the long line at the post office? How about the work ethic and customer friendliness of the TSA staff? Don't try calling the city office after 5:00, god forbid they would work a couple more minutes.

Government workers are not bad people. This behavior flows from a lack of incentives. Owners who have capital at risk will drive a culture of client attentiveness. They realize that the business won't succeed if the client isn't happy. No one serves that role in a government office. The government staff is inward focused. It is about working the least amount possible. Generally, they can't be fired (don't get me going on public unions – where exactly is Sinclair's Jungle in that context?) and promotions are based on tenure, not meritocracy (see "step and lane" systems in public education.) Why work hard and try to do well if you get the same result as a colleague who does not?

Shareholders also instill fiscal discipline. They want to maximize their returns and not have to invest more money so they ensure that the most is achieved with every expense dollar. No one serves this role in government systems. How many times have you seen handfulls of workers standing idle in a construction zone on the highway? Take today's Covid situation, my understanding is that there have been no layoffs in the city of Chicago or State of Illinois employees. We are paying librarians in Chicago while the library is not open and they don't work (probably can't furlough them under their union contract.) The federal government will describe expense "cuts" when what they are doing is reducing the rate of growth of an expense. Chicago and Cook County will just increase taxes to drive more revenue to cover the lack of expense management.

While non-profits are not as bad as the government, I am struck by the new "idealization" of non-profits. You see it in advertisements as a badge of honor. In many cases, non-profits should really be called "non-tax paying". Nonprofit is a designation under the IRS code which eliminates any need to pay taxes. It does not mean profit is not being made. Many non-profits make money – they just call it surplus and not profits. In the fiscal year ending June 2018, Southern New Hampshire University had revenue of \$807 million with a net surplus of \$133 million after expenses. Do we really think that big hospitals or universities should not pay property taxes at the same time they have million dollar executives and millions on their balance sheets?

The profits (if they exist) of a non-profit just build up on the balance sheet since there are no shareholders to dividend it to. This can lead to extreme waste. Recently, I was interacting with a large non-profit that had accumulated over \$1 billion on its balance sheet. It proceeded to literally waste a

couple hundred million dollars on a failed attempt to enter a new area. There were no shareholders to hold it accountable. Capital is a societal resource that drives economic growth. Money wasted like that hurts society.

I don't think capitalism is perfect and should go unchecked. Those who say the only fiduciary duty of boards is to maximize profits for shareholders (even to the detriment of workers or communities) have it wrong. I support the move by the Business Roundtable in the fall to revise its statement on the purpose of a corporation to be for the benefit of all stakeholders – customers, employees, suppliers, communities and shareholders. There are unethical people who will hide behind the shield of capitalism who might do harm to the environment or otherwise who need to be called out. The growing role of “social impact investing” is great.

Be safe. Work hard. As you drink your Starbucks, remember it wouldn't exist if Howard Schultz didn't put capital at risk and watch every dollar.

jml