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8 April 2013

Mr John Cupples
Director
Read Along Publishing

by Email

Dear John,

As requested, please find below a "Letter to the Reader" for Book 3 in the series, entitled *A Path to Social & Economic Equilibrium.*

Best regards,

Denis Kilroy
Managing Director

A Path to Social & Economic Equilibrium

A Wealth Creation Paradigm for the Third Millennium

Shaping a regulatory environment that encourages the business community to create customer value, build shareholder wealth and enhance community wellbeing

by Denis Kilroy with Marvin Schneider

A Letter to the Reader

*In **Book 1: The Legacy of Good Leadership**, the reader was given a destination and a roadmap. In **Book 2: The Choice to Serve or Exploit**, the reader was given the opportunity to illuminate both the journey and the destination by lighting the beacon of noble intent.*

*The purpose of this book, **A Path to Social & Economic Equilibrium**, is to define the regulatory conditions and mindset required in order to both encourage and sustain nobler or more virtuous business practices.*

The destination mirrored the belief that is not only possible, but also highly desirable, to build an enduring institution that that could create value for customers and wealth for shareholders on an ongoing basis – and do so in a way that at minimum preserved and in many cases enhanced community wellbeing. The roadmap provided a clear way to get there.

But the reality is we need more than a destination, a roadmap and a conscious intent to serve. It is important to also have supportive conditions in which to operate – including the regulatory environment.

Why do some companies exploit their customers? Why do some employers exploit their employees? In the first instance, they do it because they choose to do so. It is their intention. But they also do it because in some respects the current paradigm tends to encourage them to do so – or at the very least it fails to dissuade them from doing so.

If the intention is to create wealth, and most of the key players with whom a company interacts, including government appointed regulators, believe that the only way to do so is at the expense of others, then exploitation is likely to follow just as night follows day.

Here are some examples of beliefs held by law-makers and regulators that underpin the current paradigm. None of these beliefs is intrinsically true or necessary for economic success as an individual, a business or a nation.

- *In relation to shareholder primacy… A CEO's first responsibility is to shareholders [even though this is not in fact true in law]*
- *In relation to some fast food, soft drink and OTC pharmaceutical segments… Market integrity and a consumer's right to choose must be preserved at all costs [even if consumers lack the information to make wise choices and none of the options available to them if consumed really serve their long-term best interest].*
- *In relation to taxation… Companies should be taxed on the profit they generate [even if they must meet the tax payment from cash flow, which for a growing company is always less than profit, which in turn creates an incentive to look for ways to minimise taxation].*
- *In relation to advertising… A successful advertising campaign is one that creates significant demand for the client's product [regardless of whether or not consumption of the product serves the long-term best interest of the consumer, or whether the campaign itself consciously set out to manipulate the behaviour of consumers, rather than just inform them].*

- *In relation to electricity distribution… The best way provide value for consumers is to ensure they get the lowest price [even if it leads to underinvestment in network infrastructure and an increased risk of outages and a lower level of safety].*
- *In relation to capital markets… Market efficiency demands that short-selling be permitted [even if it means selling something you don't own in the hope you can force down prices such that you can buy what you have sold at a lower price than you sold it]*
- *In relation to most fast moving consumer goods markets… Competition is the best protection for consumers [regardless of the fact that consumers are only exploited when someone chooses to exploit them]*
- *In relation to business philosophy, (to quote Milton Friedman, the father of economic rationalism) … The social responsibility of business is to increase its profits [regardless of the fact that this mindset leads to many casualties among the stakeholders in almost any listed company].*

We have created an economic structure that gives primacy to three things: the interests of shareholders over and above the interests of other stakeholders; the right of an individual or a company to act as they see fit so as to enhance their own wealth, so long as it is within the law; and the maintenance of market efficiency almost regardless of the cost. In doing so we have created a significant problem.

Our narrow definition of economic benefit excludes large economic and social costs that arise either directly or indirectly from the activities of many industries. Examples include obesity and its link to the fast food industry, attention deficit and hyperactivity disorder (ADHD) and its link to common preservatives used in factory-made bread, and of course the multitude of health consequences arising from tobacco use.

All of these industries are from time to time able to create wealth for their shareholders. But this can be a distorted reality, since many of the costs they generate are not captured in the economic framework that we employ. These costs, which economists refer to as externalities, are borne by individuals (often in the form of a negative impact on their health), or by the wider community through the taxation system.

Perhaps the greatest problem arises when a government itself becomes dependent upon taxation revenues from industries with high social costs. The gaming industry is a particularly interesting example of this phenomenon.

Ultimately, we need a different mindset at the level of our legislators and the regulators whom they appoint. And we must be prepared to let go of some of the ideas about free markets that have become articles of faith since the 1980s. Only then can we establish an economy that creates wealth by making the best use of available resources to generate products and services that serve the long-term best interests if individuals, the wider community and the environment.