FALLACIES OF GLOBOPHOBIA

by Jean-Jacques Rosa

Globalization and international financial markets are not a threat to French society,

but rather tools to create new prosperity

The tone of public discussions over the last few weeks suggests that the French are approaching the year 2000 with mixed feelings of fear and powerlessness. Fear of losing their identity in various ways, of being melted down into a kind of homogenized global culture covering up for an American capitalist dictatorship and concealing the helplessness of their elected officials to oppose it.

Indeed, in these columns, Jean-Pierre Vesperini touched upon the inadequate government response to the stock exchange confrontation between the BNP and the Société Générale, expressing the view that the state should have actively intervened to impose a purely "French" solution and protect our banking system from the future meddling from international companies. Clearly their interests do not concord with those of our economy or of French citizen-consumers. Investments in capital markets are seen as a form of short-term profit seeking which is diametrically opposed to a company's long-term prosperity. The profit motive alone is therefore considered to be contrary to the interests of the French people.

"Short-termism"

This idea is widely held in political circles and in the media. It is however completely incorrect. Profits realized on the stock market and the capital gains sought by all investors, great and small, are directly linked to an increase in share prices. But equity only represents the right -- and a negotiable one -- to a share in company profits, present and future and for the entire life of the company. By purchasing a PSA or IBM share, the investor acquires the right to receive a corresponding share of the company's profits in the form of dividends for as long as the company continues its activity. This means that all forecasted profits, even at the more distant horizons of 2003, 2010, or even 2012, contribute to defining its share price today.

A share price can only rise in the short term to the extent that the current value of all forecasted future profits is on the increase. It follows that even if investors or pension funds that manage capital seek short-term capital gains, they can only achieve them if the firm they choose prospers in the middle and long-term. Shareholder pressure on managers to achieve stock market gains in the short term thus has a positive effect on long-term investment policy.

If this were not the case, no company listed on the stock market would invest, since any investment would result in additional costs over the short-term and thus a reduction in current profits. But in reality, companies that announce additional investments, and often investments with a very distant return, such as research and development financing, do benefit from share price increases.

Long-term considerations are no longer the enemy of share capital gains, but rather their driving force, with capitalization as the tool that allows the perspective of profit in a distant future to translate directly into current share prices. And we are not talking about a blind confidence in the virtues of the market or a theoretical vision divorced from the facts, but rather of an observable reality that has been repeatedly confirmed in a plethora of studies.

Competition, mistakes, and corrective action

The very natural interest in long-term benefits that drives stock market confrontations and the expectations of high profits held by both individual and group shareholders is a decisive factor in increasing wealth for a company. Shareholders encourage companies by purchasing shares in those firms that create the most wealth in the middle or long-term. And they sell shares from other companies whose strategy appears less promising.

Naturally, markets can be mistaken in their forecasts, just like any other economic player and each one of us, because the future is uncertain. But they continually correct these errors day by day depending on the new information that becomes available. The price corrections evolve through a process of trial and error where the probable value of each company is constantly re-estimated.

Bureaucrats in the ministry of finance or a central bank cannot do any better than the thousands of professionals all over the world who are looking moment by moment for the best information on a given company. This is why it is important to allow financial markets to set share prices and decide upon allocation of capital to company financing and re-organization.

The social role of shareholders

Is this merely a question of defending the interests of capitalists? Absolutely not. Creation of wealth on a domestic level is the only way to enrich the French people as a whole, directly, by developing production and paying salaries and dividends, and indirectly through taxes that companies active in France pay to the state. This fiscal revenue is used to provide residents with public services that contribute to a higher standard of living.

A firm that loses money does not create wealth, but rather impoverishes the nation as a whole, even if it produces a great deal and employs many people. The value of goods and services it injects into the market are by definition less than the company's consumption of resources such as manpower, intermediate products and the capital bound up in production. It thus destroys more value than it creates. Strong production and strong employment in unprofitable companies thus contribute to a reduction in the overall standard of living.

It is therefore in the national interest to maintain as many companies as possible in the territory, that is, companies which are profitable on a middle and long-term basis, as shown by higher share prices, and to eliminate the others.

The social role played by investors seeking capital gains is to spot the companies which create the most wealth for the community and encourage them to do even better, a process whose results go well beyond their private interests. Investors must seek out these capital gains if we want financing to go to the most productive companies and our standard of living to increase.

Effective sovereignty

Do we need to fear uncontrolled competition in capital markets and possible control by various foreign investors of French companies? On the contrary. It is good for the French economy to attract capital from all over the world, providing a guarantee of financial stability by number. Just like a private French investor, an American or Japanese investor's main objective is capital gains and dividend payments. Thus he will choose companies on the basis of exactly the same criteria, that is, long-term creation of wealth. It follows that the pressure on managers will be exactly the same whatever the nationality of the investor. American or Japanese citizens do not invest in European companies to achieve some mysterious strategic objective. They have other fish to fry and other uses for public funds. It is the private investor looking at companies all over the world that is likely to create the most wealth.

And in fact, when Axa purchased Equitable in the United States, or when Allianz purchased RAS in Italy, their objective was the same: improve management quality and increase profits while respecting the laws of the country. Thus, there is no difference in actual behavior between investors of different nationalities. It is of little importance that the purchaser of a given company be French, American, Russian, Japanese, or Chinese. What counts is that competition between shareholders remain as open and lively as possible to ensure that share prices accurately reflect the reality of the company, and that the pressure on managers to increase wealth remains at a maximum.

Governments that have wisely abandoned ownership and management of for-profit companies over the last few years can in no way improve the process by intervening. Indeed, they are faced with many other priority tasks that only they can handle, such as safety of goods and persons and infrastructure development in addition to social, monetary, exchange and fiscal policies, along with other tasks that have been handled with dwindling success over the last few years.

For a government, sovereignty implies the independent choice of basic policies which meet the expectations of the citizens. And the role of a sovereign state on an economic level cannot be evaluated by the degree of interference in the affairs of businesses through a type of state control inspired by the past but no longer viable today. It means implementation of adequate policies covering safety, infrastructures, basic education, social protection, currency and exchange that will attract the most creative companies to our territory. No one is dictating these policies to us. They are chosen by the community. And they are a determining factor in encouraging creation of wealth by businesses in our national territory.

In social areas as in all the others, specialization is an advantage. Each to their own business, each to their own specialty. Let shareholders judge managers and reorganize companies to create wealth. And let the state concentrate on its own specific tasks. A nation's prosperity is a direct result of this vital, unscheduled cooperation.

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