

## Economic incentives for optimal sustainability

This note is prepared as a response to Pär Granstedt's article "Vägar till en hållbar ekonomi". Our strategies and actions for sustainability are formulated based on our understanding and vision about the society we want to create. Pär's view on sustainability covers social, environmental and economic aspects of sustainability: "Min slutsats är att det som behövs inte är något drastiskt monetärt och finansiellt systemskifte utan ett politiskt paradigmskifte från målet "tillväxt till varje pris" till "ekologisk, social och ekonomisk hållbarhet." Concrete pragmatic measures are needed for attaining global sustainability.

The first concept I would discuss here is economic incentives to attain economic efficiency and ecological sustainability. Pär's response to an ongoing debate for monetary reform is as follows: "Genom banklagstiftningen har staten stora möjligheter att sätta spelreglerna för kreditmarknaden utan att detaljstyra. Basel III kan vid behov kompletteras med ytterligare regelverk. Men frågan är om det viktigaste är att ytterligare reglera hur bankerna finansierar sin långivning. Jag vill hävda att de viktiga är att skapa incitament för att gynna hållbara investeringar och motverka slöseri". Economic incentives figured as an important tool for sustainable investments. We can look economic incentives bit closer below.

Oxford dictionary defines incentive as: "A thing that motivates or encourages someone to do something." Economic incentives become relevant here because it motivates the society to take actions to attain desired goals. There are economic systems that incorporate both public and private sectors to attain the desired goals. Economic inefficiency of public sector is not a secret while private sector is known for efficient use of resources. Incentives are the driving force behind the private sector interventions in an economy. Engaging private sector to attain development goals would save a lot of scarce resource for public sector as well as ensure efficient and optimal use of resources. However we cannot forget the fact that economic incentives are unable to solve a bunch of social problems. Economic incentives are a double-edged weapon. One example is the failure of Swedish government's unemployment tackling strategy using economic incentives. The government's legitimate expectation is that through economic incentives, unemployment problem can be solved. Private employment firms (bemanningsföretag) are given the task to educate, train and coach the jobless people to get suitable jobs in the employment market. Theoretically those private firms should train the jobless people who have the extreme difficulty to get a job and help them to find a job at the earliest. In return the private employment companies can gain a profit (economic incentive) from state financing. But in reality firms will easily gain more profit, if they select jobless people who are very close or easy to get job immediately without putting much effort to train people who have extreme difficulty to get jobs. This means that firms will always prefer unemployed people who can easily find the job in the market than those who have extreme difficulty to find the job if the scheme is driven by economic incentive principle. But state's legitimate expectation is the other way round. This reveals the inability of economic incentives to solve social problems like unemployment through such market economic solution.

Yet another example is introducing incentives in private health care services. If all people have a sound health then private medical companies, private medical practitioners and hospitals will have to disappear from the market. Medical practitioners and companies can gain incentives if there are health problems. The awareness and knowledge among the private medical practitioners about the danger of life style diseases due to the consumption of poisonous industrialised food contains preservatives and chemical are dangerous to our health would not lead to any health improvement of people if there is no economic incentives. On the contrary existence of such lifestyle diseases will ensure a profit gaining market for them to gain economic incentives. Likewise excess exploitation of natural resources, reduction of

emissions, attaining sustainability and intervention in welfare activities are other areas where market failure may occur similar to that of unemployment reduction through economic incentives. In a market failure an optimal allocation of resources is not attained. In other words, the social costs of producing the good or service (all of the opportunity costs of the input resources used in its creation) are not minimized, and this results in a waste of some resources. Gaining social benefit and social equity through economic incentives (private profit motive) is a perverted concept though private sector.

The reasons are: 1. the very notion of economic incentives belongs to a social paradigm that knowingly promotes the greed of human being for gaining more profit. According to Adam Smith 'it is not because of baker's love towards humanity, but because of mere his selfishness for gaining more profit that motivates him to makes bread'. ("It is not from the benevolence of the butcher, the brewer, or the baker, that we expect our dinner, but from their regard to their own self-interest"). It implies that selfish profit motive is the only driving force of the economic incentives. This perverted concept will invariably lead to an excess exploitation of all resources for maximum profit and never lead to sustainable society. 2. Market economic principles with private profit motive are not compatible or fit or suitable to the character of public sector. Private and public sectors have diverse and conflicting objectives. Public sector has a wider social objective of attaining maximum social benefit. Private sector needed a investors maximization of profit. In other words both in ends and means private sector and public sector are lying in two extreme poles.

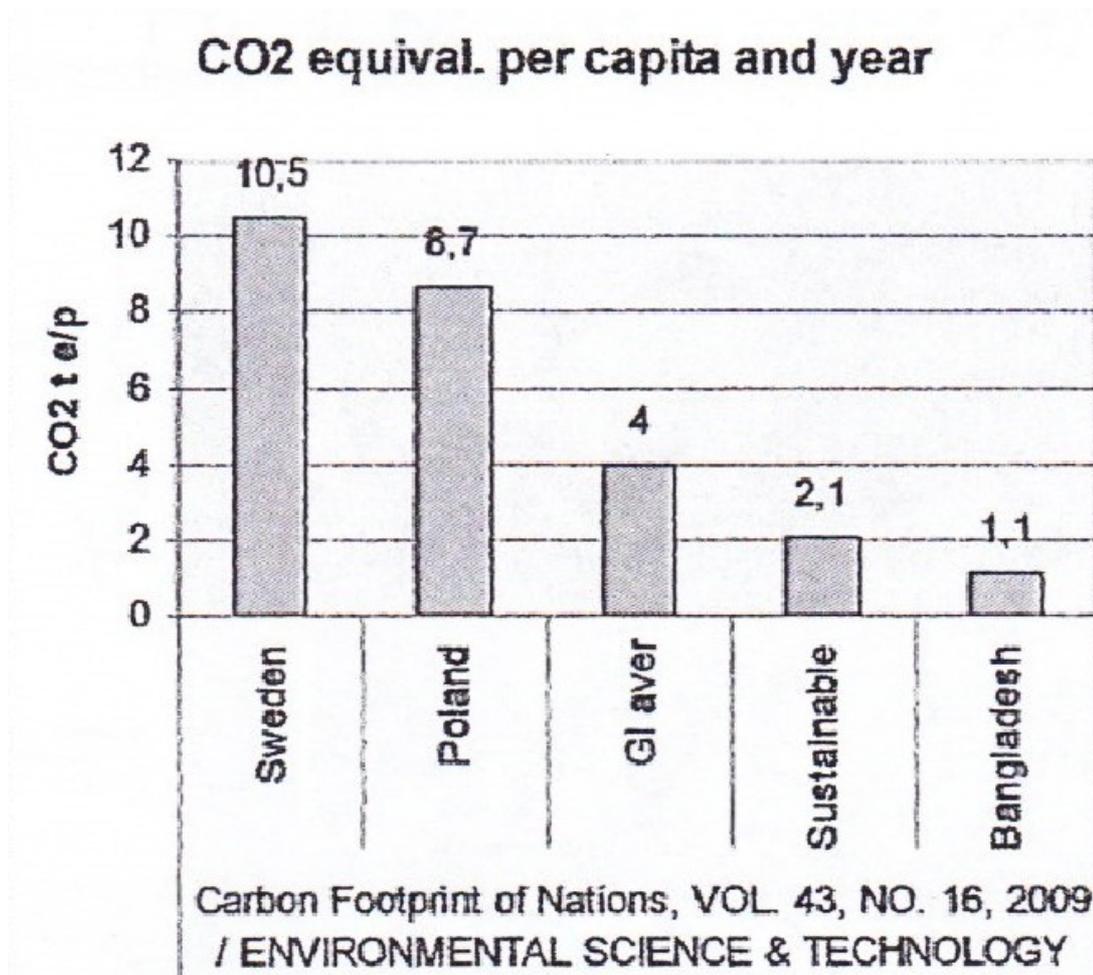
It is very difficult to gain these double (conflicting) objectives of maximum social benefit and economic efficiency through profit driven market mechanisms. Public sector can attain social equity however it is known for its inefficient use of resources. Private sector is well known for its efficient use of resources, but lead to social inequality. Combinations of both these economic systems have tried in mixed economies. A mix of both private and public sectors may function up to a certain extent. As said before market economic values do not suite very well for public sector. Public sector belongs to a social paradigm or realm where maximization of social equity and social benefit to citizens are the ultimate goal. Market economy belongs to a realm where cut-throat competition for profit maximization existing. The role of the state is not doing any profitable businesses. Hence efficient use of resources for higher profit is hardly expected or seen among the State run services. But economic efficiency is a very desirable value in an economy because it saves scarce resources for spending on other needy areas. Bringing the market economic principles without proper controls in the state architecture for attaining economic efficiency will lead to economic inequality in the society. To make efficiency among public sector investments, one must have to place compatible characteristics of both these sectors in a perfect blending. Hence it is very important to place right economic tools to curb the economic inequality while ensuring optimal use of resources.

Why a mere merging of both sectors for best results is not easy to materialise? There are very many contradictions in the very basic character of these sectors. Motivation of the private sector is not use of resources efficiently to attain social benefit, rather use of resources efficiently to maximize private profit. Public sector can attain social benefit and equity, but it is very inefficient in resource usage and can contain other problems like corruption, bureaucratic controls, nepotism etc. There are few important preconditions needed to attain both social equity and efficiency through economic incentives. We have to distinguish the difference between private and public sectors as well as its conflicting objectives. For the public sector, a social problem like unemployment, pollution, health hazards are something to be removed totally from the society for everybody's benefit. But for a market, it can be a

golden opportunity for starting a business and gaining profit. In such markets, a social problem will become a business opportunity for gaining profit while for public sector it can be a burden that incurs costs for eradicating it. Moreover, private sector is not legally obliged to deal with any social problems unless the firm/company has entered into that market with a legally binding contract to deal with it. Once any business is unprofitable, private sector can quit the market and explore profit search in any other areas of business opportunities as they wish. This is possible irrespective of the problems they dealt with remains or removed from the society, because the underlying principle is gaining profit not attaining the social benefit. However public sector (departments like health care or education) has to continue their activities irrespective of its profitability as long as the social need remains in the society. In other words, public sector is responsible to the society, while private sector is only responsible to their investors who are interested in the economic incentives alone. (There are some exceptions like social marketing (fair trade), social investments through alternative banking (Ekobanken). In such exceptional cases the awareness of the people is the motivation rather than the role of economic incentives). However it is not impossible to merge both of these sectors in a subtle way to attain the conflicting double objectives of efficiency and social equity simultaneously. It needs radical change in the resource distribution, pricing rules and incidence of taxation so that net result will be optimal use of resources, social equity and ecological sustainability.

Pär has touches the above topic in his article as follows: “Precis som den totalitära planekonomin och den Keynesianska blandekonomin till en början genererade imponerande ekonomisk tillväxt gjorde den marknadsliberala modellen det också. Men nu, efter ett par årtionden, står vi med ett nytt dystert facit i hand. Vi befinner oss åter i en djup och varaktig global ekonomisk kris. Vi närmar oss alltmer ett globalt ekologiskt sammanbrott, de ekonomiska klyftorna ökar, liksom de sociala och politiska spänningarna. Så hur går vi vidare? Centralistisk planekonomi fungerar inte. Nyliberal marknadsekonomi fungerar inte heller. Kan det trots allt vara så att den bästa vägen är att balansera mellan ytterligheterna? Någon slags blandekonomi, men med en annan blandning är den som var aktuell för Keynes?” A suggestion for creating a sustainable and equitable society is discussed below.

Pär has pointed out the most important aspects including higher tax on consumption needed for sustainable society: “Det är viktigt att en finanspolitik för hållbarhet kombineras med motsvarande åtgärder på andra politikområden. Dit hör skatteväxling med minskad skatt på arbete och höjd skatt på konsumtion och verksamhet som belastar miljö och naturresurser. Dit hör också en fördelningspolitik som minskar de ekonomiska klyftorna och ger alla en ekonomisk grundtrygghet. Det finns också anledning att återuppta debatten om maktförhållandena i näringslivet”. Pär has also mentioned about the global inequalities in his article. “1820, före kolonialismens stora genombrott, uppskattade man att sydgruppen tillsammans svarade för 50 % av världsproduktionen och nordgruppen för 20 %. År 1950, vid kolonialismens vändpunkt, var sydgruppen nere i 10 % medan nordgruppen nått sin höjdpunkt på 50 %. År 2013 bedöms de två kurvorna ha korsat varandra på ca 30 % var. Prognosen för 2030 är att sydgruppen då svarar för 40 % av världsproduktionen medan nordgruppens andel är nere på 20 %.” Many vital aspects for sustainable society like choice of economic systems for equitable distribution of resources, democratic consensus on the power structures of social institutions (power concentration in the corporate) and global economic inequalities are also mentioned above. Since the problem has this multifaceted nature the solution must have also focus on all those vital aspects. We are facing both economic and ecological crises now. In my personal view, in the western world we have to reduce 80% of our consumption level to come to a sustainable level of consumption (See Artur Granstedt's, chart on global emissions per capita as shown in figure below).



The global average consumption must be reduced by half (47.5%) of the present consumption pattern to attain sustainable level. From the above chart it is clear that Sweden consumes 5 times more than sustainable level, while global average consumption is twice more than sustainable level. However there are huge number of people in the world who live at present much below these sustainable levels. Bangladesh consumption is just 50% of sustainable levels. The people who consume less gain nothing in the present systems. In spite of their “savings” to global sustainability they are continuing to be the poor countries. There must be an equitable distribution of resources or a due compensation to attain social justice when poor people are deprived of enjoying the benefits given by the nature. People who consume excessively cause for more depletion of natural resources as well as increased emissions. They must have compensated for their excessive use of resources which actually belong to all people. They have to compensate for the damage they cause for others due to their excess consumption. Since national boundaries cannot stop problems like emissions, climate change, and environmental consequence, we have to follow a holistic view to solve this issue. So we have two major problems here to address: an ecological sustainability problem as well as a social equity problem. How can we attain both ecological and economic sustainability at the same time without compromising the optimal use of resources? Fixing right price rules would solve this puzzle.

Every production that uses extraction or exploitation of natural resource at any part of the globe must incur a cost that should cover the following three types of costs besides the present pricing system. (Present pricing only counts production cost and profits) 1. The cost for keeping that natural resource base to a sustainable level. This means that resource base will replenish and continue to exist for the future uses after this particular extraction or use of

natural resource for production in question. 2. Cost for rectifying the emissions/pollutions just because of this particular production. 3. A cost for this particular natural resource is being taken from the access of rest of the world. (All natural resources belong to all of us collectively including human beings as well as other fellow species. Any usage of natural resources invariably means that the consumer has borrowed it or taken it from others. This has to be duly compensated. Easiest way is to fix a cost on it). These three types of cost will be adding on top of its production cost (more or less the present price level). The amounts of each type have to spend back to respective area to compensate or bridge the gap created due to the particular production process. The third type of prices must be distributed as universal basic income.

To execute this pricing right way, all stakeholders have to get proper voice in the pricing process. Consumers, producers, and authorities (including state, environmentalists and scientists) together can come to a consensus on the price of every type of production. It does not need to fix every single product, instead general categories of products that are using similar production methods resulting similar environmental impacts. The whole exercise should be transparent so that any member of the society can monitor the process. With the support of modern technology all this can be done rather simply and easily.

Once this measure has taken up, the state can privatise almost all its services including welfare measures. Irrespective of which sector provides the goods or services, who consumes it, an automatic rectifying mechanism is inbuilt in the pricing rules. The respective part of the price will automatically replenish the natural resource and ensure an equitable distribution. Private sector gets complete freedom to enter any market they wanted without any entrance control. Consumers are free to consume whatever they prefer from the market. The state can compete with private sector in which an incentive will function as an effective tool for ensuring economic efficiency. Public sector can make profit by selling their products and services in competition with private sector. If public sector services are affected by corruption and excessive bureaucratic control then people will resort to private sector services. If private sector services are expensive (through making a cartel for example), people may go to cheaper alternatives provided by public sector. Whichever sector provides the best services will be opt by the consumers. In theory all the state services can be brought to the open competition with private sector services. However Police, Defence, Judiciary, Health care services beyond a certain monetary limit must be provided by the state in an impartial way irrespective of the citizens' ability to pay for such services for ensuring social injustice.

Economic incentives can work perfectly to attain social equity, economic efficiency and sustainability if there is a perfect competition, people can able to take part in the game and prices covers the actual sustainability costs. The most important precondition is that every member of the society must have the ability to take part in this game fully, through a guaranteed basic economic means financed through resource usage tax. It has to be generated through the realising the real cost of production on a global basis as mentioned before. Why it should be global? The sustainability questions are universal in nature and connected with the whole globe. The right to survive decently on earth is also universal in nature. This applies not only the existence of human beings, but also of all fellow species. People will be taking very active participation if their actions have a direct consequence in economic terms. At present developing countries are exploited for catering the needs of the developed nations and this has high adverse environmental consequences. There are pollution exports going on from rich part of the world to poor parts which have serious environmental hazards. Resource usages at the present pricing patters causes for global inequality as well as a threat to global sustainability. These global problems can be addressed properly only if remedies are also executed with global implications.

The real environmental cost on all production has to be collected and distributed among the whole stakeholders so that consumers can take the most judicious decision on what is sustainable consumption for them. Those who consume less will gain always an economic incentive, and those who consume more will pay extra cost which is an economic disincentive. This extra payment will go back to replenish the natural resources or as a basic income to the people. This flow will lead to a situation where people who consume will have more disposable income which will be used only for sustainable purposes. Such a system will ensure an ecologically and economically sustainable world.

Related with the present global inequality, it is not desirable or fair that any specific group of nations or people gain at the cost of others for a sustainable society. This is a very important reason for arguing for a global basic income. Pär's article identifies this need for mitigating economic inequalities: "Det är viktigt att en finanspolitik för hållbarhet kombineras med motsvarande åtgärder på andra politikområden. Dit hör skatteväxling med minskad skatt på arbete och höjd skatt på konsumtion och verksamhet som belastar miljö och naturresurser. Dit hör också en fördelningspolitik som minskar de ekonomiska klyftorna och ger alla en ekonomisk grundtrygghet."

Moreover, a dividend in the form of Basic Income will ensure all downtrodden and destitute communities to attain the minimum means for their existence with a basic social security. This will help them to get an opportunity to contribute to the society more constructively. This may not solve the whole range of problems we have now, but a considerable part of the present problems.

Pär has mentioned about transparency as a tool to ensure sustainability. "En ökad transparens och möjlighet för insättarna att påverka hur deras pengar används kan också bidra till en mer ansvarsfull långivning". Transparency alone may not add any additional value to sustainability; if the consumer's level of understanding is not correctly corresponding with it. It implies that transparency will work as a tool to monitor what is going on, but people's priority will be depending on their consciousness about where they want to go. This is relevant as Pär refers in his article itself "Politikerna skyller på väljarna, näringslivet på konsumenterna och vanligt folk tycker det är meningslöst att avstå från sin konsumtiska livsstil om inte alla gör det." So it is finally people's understanding and willingness that is a precondition for ensuring sustainability through transparency. In a society where the majority will think that technical solutions will solve sustainability problems in the future, people may not react very positively even if banks will show that their investments are only on unsustainable business. They believe in other types of solutions which may arise in the future to solve sustainability problems. The level of awareness and willingness to accept sustainable solutions of people is the key. Transparency will be very useful to generate this awareness. Transparency alone may not create much positive results to sustainability. If transparency and awareness can work together then it will definitely result in sustainability. On the other hand, transparency will be a good solution to know if banks are creating money out of nothing.

On the ongoing debate on banks creating money out of nothing, Pär's article refers as follows: "Ett annat vanligt sätt att försöka förklara hur bankerna skulle kunna låna ut pengar som man inte har (i form av eget kapital, inlåning eller upplåning på kapitalmarknaden) är följande: När banken har beviljat ett lån, sätter man i pengarna på ett konto i låntagarens namn. Detta ökar bankens inlånade kapital, och kan på så sätt finansiera den utlåning som skett. Detta kan delvis stämma, fram till dess låntagaren tar ut pengarna för att använda dem för sitt låneändamål. Då måste banken i alla fall ha annan finansiering. Eftersom ränteskillnaden gör det till en rejäl förlustaffär för låntagaren att ha de lånade pengarna inestående på banken är det naturligt att den tiden brukar vara mycket kort. Att detta ganska marginella förfarande skulle förklara tillkomsten av 97 % av alla pengar, som påstås, är

uppenbart orimligt.” It also reads: Det är därför bankerna under ett par årtionden haft i princip obegränsad tillgång till pengar att låna ut. Något magiskt ”skapande av pengar ur ingenting” har inte behövts även om det hade varit möjligt.

Something we usually miss here (according to my opinion) is that money is nothing other than a representative value of all goods and services we have in the whole world. For example if there is 80 trillion dollar as money we have now, and if some banks/state creates 20 trillion additional money out of nothing. (Then total money supply becomes 100 trillion dollars). This means that the value of all goods and services will lose its value by 20%. This is the reason no governments just minding new money to meet their requirements like developmental needs, repaying domestic and international debts, and allocate for additional welfare expenditure. If it was as easy to create new money out of nothing, then Lehman brothers would not have collapsed, neither JP Morgan denied the loan request of Lehman Brothers which lead to crisis in the western economies. On the other way, it is the real value and the demand for the money among the customers that decide the supply of money. If someone produces more money than their real ability to pay back when demanded, all those who create such money irrespective of banks or states they will end up in bankruptcy and disappear from the market. Usually no clever banker dares to takes such an extreme deadly risk. This is the way money works in the liberalised financial markets. QE and other measure are mere financial measures to make the economy work smoothly. But the liberalised financial market has one severe danger to depositors. Depositors may be at high risk if their bank is happen to be one which are ready to take a deadly risk by issuing more money than their real ability to pay back. It is Similar to that of Lehman Brothers’ case.

High level of transparency in the banking sector is needed to know what is really going on there, especially to avoid misunderstanding on the creation of money out of nothing. A proper public audit, and publication of audit report verifiable by the public and media, would solve this controversy. We don’t need to propose an extreme step of total reform in the monetary system, just because a suspected impropriety at the banks part, which in my opinion is only a misunderstanding. But on the other hand, in democracy people has the authority to monitor the proper functioning of our public systems. So a proper audit, verification and public accountability among banks can be the first response towards the argument that banks are making money out of nothing. A false way of arguing will cause for losing the legitimacy and validity of voice of alternative movements who wanted progressive reforms.