Value, Kinetic Safety Fund for Corporate: Lessons Learnt From Economic Crisis All Time Answer To the Bailout

Sapovadia, Vrajlal

Shanti Business School, Ahmedabad, India

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Value, Kinetic & Safety Fund for Corporate: Lessons Learnt From Economic Crisis & All Time Answer To the Bailout

Prof. Vrajlal K. Sapovadia
Associate Dean, American University of Nigeria

Economic Crisis:

The economic crisis that surfaced in July 2008 has taken a big toll and invariably no one is spared whether in business or not. Entrepreneurs, Legislators, Executives, Regulators & Experts are busy in finding out the reasons of such catastrophic economic failure. Liquidity crunch, over estimation, over expansion, over valuation, over expenditure, sentiments and what not! There is a consensus that it is man made!! A number of commentators have suggested that if the liquidity crisis continues, there could be an extended recession or worse.[1] The continuing development of the crisis prompted fears of a global economic collapse.[2] The financial crisis is likely to yield the biggest banking shakeout since the savings-and-loan meltdown.[3] Investment bank UBS stated on October 6 that 2008 would see a clear global recession, with recovery unlikely for at least two years.[4]

Bailout packages:

Several country including USA, UK, China and India has injected various liquidity dose through policy measures and offered bailout packages to the industries in general or offered specific industry relief. The officials are finding difficulties in designing bailout packages. The £500 billion banking bailout trumps the US rescue package in both size and scope and means every British taxpayer is potentially liable for up to £19,230 to pay for its cost.[5] Government officials overseeing a $700 billion bailout have acknowledged difficulties tracking the money and assessing the program's effectiveness. The information was contained in a document, released Wednesday, of a Dec. 10 meeting of the Financial Stability Oversight Board. The panel, headed by Federal Reserve Chairman Ben Bernanke, includes Treasury Secretary Henry Paulson and Securities and Exchange Commission chief Christopher Cox. While offering no details, the document also mentioned that officials at that meeting discussed "potential methods" of using the bailout program to help curb home foreclosures and ease problems in the housing market.

More broadly, the officials discussed "the difficulty of isolating the effects" of the bailout program "given the variety of policy actions taken by the U.S. government to support financial stability and promote economic growth." [6]

Big 3 (Auto manufacturers in USA) are facing threat for the survival. General Motors and Chrysler plead to Congress for a bailout. [7] This is the position of many so-called big firms worldwide from developed & developing economies. It is practically difficult to offer bailout packages to all, ultimately offering bailout to corporate means passing off loss done by a company to citizens. Many intellectuals argue that it is back door socialism in action. “Ignoring the free marketplace and empowering intellectual planners to control the economy with a cocoon of regulations and directives characterize socialism. This flows from socialist governments' belief that full employment can be maintained only by massive deficit spending. J. M. Keynes, the economics guru of the the New Deal era, opined that it would be suitable government policy to hire men to dig holes one day, fill them up the next day, then re-dig them and refill them ad infinitum. By contrast, in a free marketplace economy, consumers, not government planners, are the final arbiters of which products and which companies survive and prosper. Despite the endlessly repeated liberal-progressive-socialist dogma, no corporation is able to trick consumers, let alone to force them, to buy its products by use of advertising. If that were possible, GM, Ford, and Chrysler would not be in trouble. They would simply increase their advertising budgets and compel consumers to buy their vehicles.” [8]

There is a wide spread protest over bailout theories. "It would be a travesty for the irresponsible, reckless behavior of Wall Street to result in the sweeping away of the American automobile industry," said Mike Jackson, CEO of Autonation, the nation's largest auto dealership group. "If indeed it came to bankruptcy, it's going to make what happened with Lehman Brothers and all the consequences of that a nice day." On the other side are those who feel just as strongly that the automakers' problems are their own doing, born of bad business decisions, uncompetitive labor agreements and vehicles that Americans have decided are second-rate. They say a bailout will only postpone the inevitable, and that the failure of one or more of the companies is necessary if the economy is to work properly. "The Big Three's financial straits are not the product of our current economic downturn, but instead are the legacy of the uncompetitive structure of their manufacturing and labor force," said Sen. Richard Shelby, R-Ala., the ranking member of the

Senate Banking Committee. "I do not support the use of U.S taxpayer dollars to reward the mismanagement of Detroit-based auto manufacturers." [8A]

Security Transaction Charge/Value Kinetic Safety Fund:

The author proposes security transaction charge on secondary market and the charge so collected should be deposited in special fund for the corporate under the “Value Kinetic Safety Fund”. The fund so collected in form of Security Transaction Charge (STC) should be maintained, supervised & used by the government under supervision of high power committee comprised of Central Government nominees from Revenue/Finance ministry, Central Bank, Security Exchanges, Bankers, Industry representatives & other experts. The fund may be released in the time of industrial crisis of general or particular industry. The fund should be released only in the circumstances of crisis to restore industry in normal position.

The VKS Fund will serve more than one purpose. The fund so collected may be used by the particular industry; hence there is no point of passing off responsibility of loss makers on citizens. It serves equity therefore, as fund is created from its own security transaction that is used in crisis. Ultimately passing off personal loss over public causes distortion in economy and increase inflation. This will reduce probable distortion and check inflation on release of the fund.

The underlying logic of Securities Transaction Charge (STC) may slow down the flow of speculative money, as it would be charged each time a transaction takes place. The STC will curb purely short-term speculation by day traders, “noise traders,” arbitrageurs and big operators without significantly affecting the long-term investors. The STC may be a significant deterrent to speculators and day traders trying to make a quick profit on a huge sum by just trading, without taking any deliveries of stocks. The proposed charge would keep such players away, as they would have to factor in the security cost. It may help in reducing the speculation in security markets. Short-term trading is one of the major factors responsible for increased market volatility. The financial literature suggests that transaction charges increase asset price efficiency by curbing excessive volatility. STC would contribute towards restraining short-term trading, thereby making financial markets less volatile and more efficient.

The volume of Value Kinetic Safety Fund:

Value Kinetic Safety Fund (VKS Fund) over a period of time may be sufficiently large for an active company in the security market. If only 0.10 percent is charged for a transaction, the amount collected for VKS Fund will be huge, and over a period of time it will grow. If an example of Indian stock market is taken as a sample to justify the volume of VKS Fund, it indicates that in future if any bailout package is required, it will be sufficient booster dose for shrinking industry. On an average, the daily trading in the Indian stock markets is about INR 100000 million. By imposing a 0.10 per cent STC on this volume, the Indian tax authorities can collect INR 100 million every day. Assuming financial markets operate on an average 300 days a year, STC could generate revenue of INR 30000 million every year. This is a substantial amount in the crisis times when a country is finding it difficult to raise revenues for bailout packages sinking industries. Several countries like USA, UK, Japan, Sweden, Belgium, France, Finland, Malaysia, Singapore, New Zealand and Hong Kong have imposed similar charge on security transactions at some point of time. [9] If this charge is streamlined and used for the future bailout packages, it would be advantageous to both: Industries & Nation.

India introduced Security Transaction Tax (STT) in year 2004. There was a fear that the market volume will be reduced and there may be market distortion due to STT. But the results of research indicate that the introduction of securities transaction tax (STT) has had no impact on market volatility and also it does not distort the liquidity in Indian stock market. Further, the result also implies an interesting fact that the informational efficiency of the market is not affected by the introduction of STT. [10] Garber points out on transaction tax on Foreign Exchange @ 6/1000 basis points is a realistic maximum magnitude, no reduction of trading volume (being small volume of tax?) and would yield $ 4.3 billion per year. [11]

Other source for VKS Fund:

Other than security transactions, a corporate pays millions & billions of Rupees during its life to various groups, e.g. employees get salary, and banks & lending institute get interest and so on. Ford, General Motor & Chrysler might have paid billions of dollars during it life. If a fraction of those payments were charged from the receiver to deposit in perpetual VKS fund, it would be in payees' interest as employees & creditors to continue business operation. The government may think to levy small charge on such payments to transfer to VKS Fund of a company. If stakeholders (like employees & creditors) are expecting return from the corporation in sustainable manner, then it is equitable to make them pay from the gain they receive when corporation is healthy. These savings result into contingency fund of a business that may be used in sickness of the company. That will help company to carry on business and hence employees, creditors, exchequers & society at large benefit. By these mechanisms, a company may create huge fund as a saving during healthy period of its operation. This also supports theory that life of the company is growing to an optimum and then declines. In time of ascent the company is source of revenue, which may be saved to use in its declining stage after gaining optimum height.

Nomenclature:

The name Value Kinetic Safety Fund has following significance. Theoretically, the stock is traded on the basis of demand & supply, while the prices are determined on the basis of value. The customer satisfaction, as measured by the American Customer Satisfaction Index (ACSI), is significantly related to market value of equity. [12] Stock price is also changed based on the forecast for the company and whether their profits are expected to increase or decrease. There is a value perceived in mind of the trader (buyer or seller) and the company whose stocks are traded is a partner in value. A trader estimates value for the particular security at particular point of time on the basis of current prices, historical & current profitability, management, assets and future growth of company & economy as whole. He determines value on estimates and he pay or receive consideration optimizing risk & return. Therefore, the VKS Fund created is due to created & perceived value, which is stored for some future use in the contingencies or crisis by the company, for the benefit of its all stakeholders. The fund is created of the value (STC based on price), by the value (Trader), for the value (To use in contingency).

VKS Fund is providing booster dose in the time of crisis. Using fund in crisis serves as positive energy; fund is 'Kinetic' as it is created through its own security transaction and without any explicit burden on the exchequer or public. Using the fund in crisis does not distort healthy competition per se. The fund serves as source to put business operation in normal condition. It saves millions of job, it keeps unemployment on hold and hence it is kinetic for industry, society & economy. In absence of any bailout in financial crisis, the

options are limited with the company. Either it goes to liquidation and closes the operation or acquire fund on arduous financing terms. The mechanism to store value in normal business time and to release value in time of crisis may be truly kinetic for the company in trouble. Economic cycles are natural, no one knows what shall be the timing of frequency of ups & down, but there is always a maturity of an organization. The VKS Fund may perpetual in nature and hence it is constant source of energy.

The VKS Fund is intrinsic bailout; provide 'safety' to the company automatically. Without depending on external agencies, the company uses this oxygen mask in emergency. It provides safety to the company independent and without losing market image, does not require submission to the political will of the government. Hence it saves company from collapse of the image & business activity. The fund can be used in any eventualities, whether natural, technological, political or market. Using this fund may mitigate social or economic disturbances. To keep fund safe, fund should be in the control of some independent agencies created by legislation.

A mechanism to collect, store, maintain, use and dispose fund may be a big challenge for the experts. There cannot be a unique model to implement the whole system, but depending upon circumstances, the government may design a system to operationalize the mechanism appropriately. Only the time can shape and reshape the system of VKS Fund, but I am sure on basis of experience, the model may be highly useful and valuable. The model I am proposing is in its infant stage, and hence input from researcher will help shaping the workable model more efficiently & effectively.

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