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The Stock Exchange and the growth of Capialism

La Bolsa de Valores y el crecimiento del Capitalismo

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Abstract

The essay performs a theoretical and historical review of the foundations of capitalism, the stock market, and its functionality in capitalism, seen within the context of business development, economic development, and international economic crises. Through a bibliographic, historical-analytical and descriptive review, we have reached the conclusion that, despite the risks that may come from flexible limits on stock exchanges, as in the cases of the Great Depression of 1929 or in the Great Recession of 2008, the benefits of the existence of an stock market are greater because they it helps to generate increases in savings, capital investments, job creation and, in general, in the well-being of society. This role of the stock exchanges allows capitalism to strengthen and evolve over time.

Keywords

Stock market, capitalism, economic development, economic crisis, business development

Resumen

El ensayo realiza una revisión teórica e histórica de los fundamentos del capitalismo, de la bolsa de valores, y de la funcionalidad de las bolsas en el capitalismo, vistas dentro del contexto del desarrollo empresarial, del desarrollo económico, y de las crisis económicas internacionales. A través de una revisión bibliográfica, histórico-analítica y descriptiva, se ha llegado a la conclusión de que, a pesar de los riesgos que pueden provenir de límites flexibles en las bolsas de valores, como en los casos de la Gran Depresión de 1929 o de la Gran Recesión de 2008, los beneficios son más grandes porque generan incrementos en los ahorros, en las inversiones, en la generación de empleos y, en general, en el bienestar de la sociedad. Este rol de las bolsas de valores permite que el capitalismo se fortalezca y evolucione en el tiempo.

Palabras clave

Bolsa de valores, capitalismo, desarrollo económico, crisis económica, desarrollo empresarial

Introduction

On the one hand, capitalism has a long tradition in economic literature as the system that has become widespread in the West. For Aurelian-Petrus Plopeanu (2016), capitalism has a very clear starting point, that is, the Protestant Reformation, through which political and scientific ties with the church were broken while, at the same time, a space of freedom that is reflected in various visible areas of science such as the Scientific Revolution, the Renaissance, and, later, the Enlightenment. These historical events influence modernity and the West as a whole, shaping capitalism with the system of economic freedoms that propose a substantial improvement in the economic development of nations.

For other scholars such as Maxine Berg (1993), ideas about capital and its influence on societies appear from the 18th century, when international trade grows from the European colonies, and when it begins, the pragmatic bases for the generation of the first theorists of capital such as the mercantilists, the Physiocrats and, later, with the influence of the writings of Adam Smith, Thomas Malthus and David Ricardo. These writings come hand in hand with the development of liberalism as a political theory that serves as the cradle for the generation of liberal democracies, which have their bases in freedom, in the protection of life, in the defense of human rights, in the rule of law, and in free elections.

On the other hand, in the 16th century, the use of bonds, in the form of checks, and their exchange as a form of payments, grew as a practice in commerce, especially in the Netherlands, France and Great Britain. This use was spreading in Europe to form the foundations for the generation of central banks in the seventeenth century and for the generation of the stock market.

At the beginning of the seventeenth century, the Dutch East India Company was created in Amsterdam (Clulow & Mostert, 2018) which was dedicated to the organization of various commercial activities in Asia, designating the creation of certain monopolies. Then, at the beginning of the seventeenth century, several of the Buttonwood Agreement were generated by which several business people were engaged in trading stocks and bonds, which is considered as the principles of the New York Stock Exchange. At the end of the 18th century, the Philadelphia Stock Exchange was created, its function being the expansion of the US financial sector.

The 1929 crisis, known as the Great Depression, would lead to questioning the functionality of the stock exchanges within capitalism, and as an element that can, on the contrary, generate weaknesses within the economic strengths of nations. In recent decades, these arguments emerged strongly after the crisis in the real estate market in 2008, a depression that affected other elements of the economy such as the financial sector and the foreign trade sector.

Thus, the relationship between stock exchanges as an element of capitalism has developed historically for four centuries, a relationship that opens the space for the proposal of an evident, functional and efficient use within capitalism, on the one hand, and, on the one hand, on the other hand, the accusation of being seen as an appendage that damages the capitalist system and that creates weak systems within the economies of nations.

It is clear that, for most economists, stock markets are important to the capitalist system because it is a means of acquiring new investments that companies can obtain to increase their capital. In addition, the use that these companies owe to the new investments generates new returns that can be used as reinvestment or as consumer spending, in any case, the multiplication of money makes it possible for economies to grow. Thus, stock exchanges have a central utility sense within capitalism, although, in some cases it can also be the cause of various economic crises if you do not find restrictions and limits to market speculation.

The present essay has the purpose of carrying out a quick bibliographic review on the functionality of the stock exchanges in the economy and in the development of the company, so that its usefulness and possible risks or damages can be clearly seen. Based on this purpose, the essay takes as its starting point an analytical-descriptive review system from which the most common arguments for and against the usefulness of stock exchanges are examined. The proposed revision leads to the conclusion that the usefulness of the securities markets is more important than the possible risks that they involve, taking into account the nature of a capitalist economy, that is, it is natural to observe that these economic systems go through spiral cycles of increase.

Nature of Capitalism

According to Jahan and Mahmud (2015, p. 44), the principles of capitalism are: private property; own interest; competition and freedom of enterprise; free determination of prices; consumer freedom; limited role of government. These principles have been built over time, debated, some have evolved since their initial presentation, and others have been strengthened. Capitalism is a long-standing theoretical and dialectical construction, some authors find it from the Protestant Reform (Cavalcanti, Parente & Zhao, 2007; Jones, 2019), other authors find it from the Enlightenment and Modernity (Vargas, 2019; Chamorro, 2021).

On private property, it is a principle developed from natural law by thinkers such as Francisco de Vitoria and Luis de Molina, whose advances were used by John Locke or Adam Smith, to establish legal elements for the protection of some of the basic principles of capitalism, the protection of the property of the work, that is, the product of the work has the ownership of the actor of the work. Therefore, legal protections allow producers, be they: farmers, artisans, entrepreneurs or any natural person. Producers or consumers who possess assets that cannot be arbitrarily disposed of.

Regarding self-interest, based on the theoretical advances of Adam Smith (1776) in his famous book The Wealth of Nations, self-interest generates the search for profit by the entrepreneur or the search for better services or products by the entrepreneurs. buyers. It is this same search for personal benefit that includes the benefit of those closest to you, that is, family or friends. Thus, self-benefit ends up being based on the individual, but it spreads to the nucleus of society, that is to say, to the family, and therefore it spreads to the entire society. Therefore, self-interest benefits society as a whole.

On competition, capitalism is based on the idea of free competition and freedom in the acquisition or purchase of goods and services. Freedom in competition allows products to improve their quality and improve their prices because profitability is essential for the existence of companies. On the buyers' side, the freedom to purchase products is based on the rational idea of better quality at lower prices, so when competition on the supply side is high, consumers can exercise their freedom more widely. Thus, market freedom maximizes social welfare.

Market freedom serves as a mechanism for determining prices autonomously, through interactions between buyers and sellers. This freedom also allows customers to buy different products, investors can start more lucrative ventures, and workers can leave their jobs for better pay. Thus, both buyers, sellers, and workers are benefited by competition and freedom, which allow exchanges spontaneously.

The last essential characteristic of capitalism is the government role, considered as limited in nature, and responsible for few functions, namely: the internal and external defense of the nation through the police forces and the military forces; public works; and the administration of justice (Botticelli, 2018). Due to the limitations that the government has, various forms of capitalism can emerge and make room for rapid market deregulation. However, at the same time, the dangers inherent to capitalism also increase in risk such as the formation of monopolies, the violation of human rights or the little attention to the less favored.

In conclusive terms, capitalism is the resource allocation mechanism through individual decisions made by producers and consumers, producers and consumers respond to public signals, such as prices, that work automatically, since they are the result of purchasing decisions. and individual sales added. Hence, in the market anyone plans or governs; the coordination mechanism is decentralized and voluntary. Prices provide incentives that lead individuals to choose behaviors that are advantageous to them and, with some other condition, efficient. The assumption is that society, despite evident frictions, imbalances and inequalities, can be interpreted as an egalitarian system in which each subject is rewarded according to their merits (Bellanca, 2013, p. 59).

Stock Market and its Functionality in Companies

In principle, the stock market of a nation serves as a means of inflow of new resources to companies that are publicly traded, increasing capital. In other words, the sale of new shares in an industry means the increase of investments that help in productivity, in reducing costs, and in increasing sales. All this means that companies' profits will increase steadily and systematically. This way of thinking about the stock market is a recurring way to maintain the financial stability of the largest companies, and with greater risks, but at the same time it is a way that helps the growth of jobs, as well as the job stability and increased sustainable wages.

When large companies manage to sell shares on the stock market, they increase their income considerably, in a short period of time. These new inputs are designed for the increase in infrastructure, to improve the technological bases of a company, for the acquisition of more inputs, or to solve unexpected expenses. In most cases, this increase in income helps productivity because it requires as a result of the investment a reduction in production costs through new technology or through economies of scale. At the same time, those bond buyers expect a sustainable rate of return over time. This risk involves a rational decision on the effectiveness of an investment in the stock market.

According to Rafal Wolski (2017, pp. 15-17), investments in the stock market have less risk than investments in real estate. However, the rates of return also vary, while in the stock market there is a lower rate, in real estate the rates are higher. This shows us that investing in the stock market has considerable risk, however; the rates of return are not as high as one would like. Despite this, investments in the stock market correspond to two fundamental purposes: first, to increase the capital of the company; second, the rate of return of investors.

Furthermore, there is no doubt that investments in the stock market behave as a functional structure to support increased productivity, be it through an increase in capital for the purchase of inputs at better prices, through improvements in productivity. infrastructure, or through technological improvements. In the case of the purchase of inputs, prices are reduced when investment increases, that is, if an industry increases its capital for the purchase of inputs, it is most likely that it will obtain a reduction in prices. In the case of infrastructure improvements and technological improvements, industries tend to buy new machinery or new software that allows them to improve productivity through the replacement of their old machinery or outdated computer equipment.

For a company to improve its economic situation in investments, the prices of its shares must be competitive in the stock market, that is, if its price is higher than the market's expectation, it is possible that the result is a fiasco in the increase of the capital, and therefore in increasing investments. According to Gilchrist and Zakrajsek (2007), increasing the cost of bonds or stocks can significantly reduce investments and the total amount of capital. According to your projections, a one point increase in the cost of the shares may represent a reduction in the investment rate of 50 points.

Finally, economies of scale work in the long term through increased capital, without an increase in investments, economies of scale work only in the short term. This means that if companies fail to increase capital, they will reach a production limit point beyond which they will not be able to pass, and if they try to do so without increasing investments, their productivity will systematically reduce. Therefore, it is essential to increase capital through attracting more investments, which can happen with individual investors or with the opening to small investments but multiplied in thousands.

Stock Market and its Functionality in the Economy

The functionality of the stock exchanges in the economy is observed in the growth of job sources, as well as in job stability and the increase in sustainable wages. These elements contribute to increased consumption and savings: on the one hand, consumption because job stability, as well as sources of work and increased wages, allow workers to spend not only on their basic needs but also on desires. personal; On the other hand, the increase in savings opens the space for the creation of micro-enterprises that allow the labor independence of people, in addition, saving allows to solve family crises, be they health, debt, studies, or calamities in general.

According to Boubakari (2010, p. 15), an efficient stock market contributes to attracting more investment by financing productive projects that lead to economic growth, mobilizing domestic savings, allocating capital competition, reducing risk through diversification and facilitate the exchange of goods and services. All these elements are made up of a solid foundation for the economic development of any nation, taking as a framework of understanding the increase in productivity and financial efficiency.

Many of the buyers of government bonds or company stocks use them as forms of savings for an unexpected future, sometimes this future can be short-term or sometimes long-term. In the case of government bonds, these tend to be medium and long-term, over a period of five, 10, or even 25 or 30 years, with an interest rate that depends on the country risk. The profitability will depend on how risky the investment is in a given country: countries with higher risk tend to present bonds with a higher interest rate, while countries with lower risk place bonds on the market with a lower interest rate.

Government bonds are a transaction that benefits both parties. On the one hand, governments can make money quickly that can be used as capital in productive investments; however, this money can also be used for spending and consumption, in which case prosperity is very short-term and not sustainable. Consumer spending helps sponsor populist governments that require immediate electoral support, while productive investment spending generally takes time to return, which is seen consistently and consistently, but is not seen as immediate prosperity.

On the other hand, bond buyers benefit from the transaction because, whether in the short, medium or long term, they will receive their money back plus the remuneration that is presented in the form of interest, this remuneration can be very high in the case of countries with high risk, or it can be low in case of stable countries. In high returns, the risk can turn into a debt default because normally authoritarian and populist countries tend to accuse the external sector of internal structural problems.

In the case of high-risk investments, when countries decide not to make their national bond payments, the two parties to the transaction lose because, although country X has already received the monies from a certain bond, any new transaction will come with a greater interest in being a riskier country or, even, the sources of debt will be reduced or disappear. On the other hand, the bondholders will not receive the money they expected, in the time they expected, but they will be forced to negotiate them at lower prices in the market. In this scenario, although populist governments receive immediate, medium and long-term support, their debts are more expensive and their development even slower.

In the case of transactions in shares of a certain company, they can also be seen as savings because buyers wait the exact time to be able to trade the shares again and generate profit through this new negotiation. Seeing the purchase of shares as a form of savings currently works only in the short term because the instability and risks of the social and political environment do not allow to foresee the evolution of the prices of the shares of the companies. Therefore, share transactions are immediate and in very few cases long-term transactions can be viewed.

In any of the cases, through government bonds, that is, through the commercialization of shares of a company, the stock exchanges generate mutual gains that can be distributed in the economy and that can benefit society in its set. In the case of government bonds, governments receive money that can be used in investment expenses, this investment expense will allow to increase the sources of work, and will open the door to obtain an improvement in job stability, all this It depends on the type of investment.

If a government's investment is short-term, with high profitability, such as investments in construction or infrastructure, earnings are high, wages are also high and the growth of job sources is evident in the short term, but, when construction ends, worker benefits also disappear momentarily. In this type of investment, governments maintain constant construction programs that allow the termination of benefits to be only momentary.

In the case of long-term investments, the money that the states receive through the bonds allows the generation of stable business systems because they can be used to support the industrialization of a certain sector or they can, or because they can be used as financial credits for the generation of new markets or business niche. In this case, state bonds serve the economic development of a nation because they improve job stability, as well as increase the sources of work and allow wages to also grow in the medium term.

On the other hand, company shares provide at least four sources of profit: the first, for the company; the second, for the buyers of the shares; third, for the company's workers; room for the company's clients. In the case of companies, because it provides immediate money that can be used as investment capital seen in the improvement of infrastructure, technology, or the business model.

Buyers of the shares benefit from the transaction they carry out in the short term, when prices favor a new purchase or sale. This model opens a way for share buyers to improve their economic situation and, therefore, improve the situation of their dependents. However, these types of transactions also have a high risk because prices fluctuate depending on current events, political decisions or social problems.

Company workers benefit from the sale of shares because the investment in capital can generate new jobs, or it can generate an improvement in productivity, with greater profitability and, therefore, with the possibility of an increase in salaries . Yes, better company performance means a better employment situation. On the other hand, a company that does not improve its productivity translates into a stagnant or damaged employment situation over time.

Finally, a company's customers benefit from its improvements because they get a better quality in their products and because the increase in capital, which has led to better technology and better infrastructure, opens the space for the prices of the a company's assets are competitive. Thus, customers obtain their benefits through the purchase of products with better quality and competitive prices.

The functionality of the stock market in economic development is transcendental when it is seen as a means of bond or stock transactions. In both cases, society as a whole benefits, always bearing in mind that there are inherent risks such as political instability, as well as price changes and fluctuations in a market whose social context is unstable. When the potential benefits and risks are taken into account, it is clear that the benefits are greater and more sustainable than the risks of the existence of stock exchanges. Thus, its functionality of the economy is based on fluidity in transactions, and legal limitations to avoid the greatest amount of risks.

Nurudeen (2009, p. 15) believes that this paper investigates whether the development of the stock market increases economic growth in Nigeria, using the error correction approach. The econometric results indicate that the development of the stock market (market capitalization-GDP ratio) increases economic growth. The recommendations therein include: elimination of impediments to the development of the securities market that include fiscal, legal and regulatory barriers; developing the nation's infrastructure to create an enabling environment in which businesses can strive; the use of policies that increase the productivity and efficiency of companies and encourage them to access capital in the stock market; enhancing the ability of the Nigerian Securities and Exchange Commission to facilitate the growth of the securities market, restore the confidence of securities market participants, and safeguard the interest of shareholders by monitoring the rigorous practices of securities traders market (in particular, speculators)

Finally, according to Levine and Zervos (1996, p. 323), economic theory offers several perspectives to see the functionality and usefulness of stock exchanges in the economy. On the one hand, there are lines that attack the financial system, and the stock markets, because several international crises have emerged from them and have cooperated in questioning the benefits of a capitalist system and, therefore, of the stock market, and even financial systems. On the other hand, there are academics who are in favor of the existence of the stock market because they consider them important in the mobility of resources, in the creation of savings, in the generation of capital that helps productivity and corporate management. After examining data from various regions, the authors state that there is indeed a strong empirical association between stock market development and long-term economic growth. Cross-country growth regressions suggest equity market activities are highly related to long-term economic growth.

Stock Market and its relationship with Economic Crises

The functionality and possible relationship of the stock exchanges with economic development, or with business development, has long been criticized as a result of several economic crises that have arisen from the very heart of the stock market. These economic crises have been used as political and ideological speeches to propose new development paths that include the control or even elimination of the stock markets, or that completely eliminate the capitalist system. These discourses are evident in the case of Latin America in the promulgation of communism in Cuba through the Cuban revolution and its influence on other Latin American revolutions, or as for example in the case of Venezuela through the Bolivarian revolution, the which places Commander Hugo Chávez as its main political leader.

On the one hand, we find the criticisms that arose from the Great Depression of 1929, which resulted in various political attempts at the independence of countries and regions, such as the ideas from Raúl Prébisch (1986) and Hans Singer. (1950) on new processes of industrialization and import substitution that try to grow from within and that avoid the impacts of the international economy. On the other hand, already in the 21st century, we find ourselves with the real estate crisis of 2008, which especially affected countries such as the United States and Spain, but which, nevertheless, its impact spread throughout various regions of the world such as Latin America.

The Great Depression of 1929 arose from the overvaluation of the shares of companies that, in a relatively short time, and through multiple transactions that seemed successful because they generated high incomes, significantly bankrupted the financial system of the United States and, from there, the breakdown of the American economy. This crisis spread to the rest of the world through the external sector, as the great consumer of the world had economic problems, the exports of the countries, especially those of developing countries, suddenly stopped.

The Great Depression caused the entire planet to enter a crisis that would last for about a decade. The United States represented around half of the exports of the Latin American region, then, the understandable that Latin America enters a crisis process which broke the monetary system based on the gold standard, and allowed the advancement of other development models such as that of industrialization and import substitution (Naranjo Navas, 2018). In the case of Latin America, the problems of the export sector would lead nations to think of new development models that exclude the center, embodied in developed countries, and focus on the periphery, represented by developing countries. These new models would try to go through an industrialization process that is strengthened through import substitution, to say: while import tariffs rose to protect national industry, the government would increase its spending to generate growth in aggregate demand.

According to John Maynard Keynes (1965 [1936]), the growth of aggregate demand would allow producers to earn more money, its effects would translate into increased jobs, and increased capital investments. This model, however, also brought several problems for those countries that implemented it. In the case of Latin America, the main problems were observed in the increase in public debt, and in the disequilibrium of the balance of payments (Bulmer-Thomas, 2007, p. 271-273). The strengthening of the role of the state has meant that the government requires greater economic inputs that allow higher spending and promote the growth of aggregate demand. With this objective, taxes were initially increased, then public debt was contracted, which grew for several decades, and finally exploded and what we know as the debt crisis of the eighties.

The imbalance in the balance of payments was caused by the need for inputs that were not produced within local economies. The increase in aggregate demand strengthened the industrialization system in countries such as Mexico, Colombia and Argentina, but, at the same time, the new industry was putting pressure on the upward evolution of input imports. This caused that in a few decades the countries that had entered this development system faced imbalances in the balance of payments (Naranjo Navas, 2020). At the end of the process, a large part of the countries were involved in high rates of growth in external debt, and in a development that was increasingly stagnant due to the imbalance in international trade.

On the other hand, the biggest financial crisis to have occurred in the 21st century occurred in 2008 when the real estate market exploded due to the overvaluation of the shares of these companies, and because of the tight limits and controls of the transactions that are performed within this market. Before the Great Recession, this market did not have a tradition of highs and lows in its prices, but instead, its profits always seemed strong and reliable. As a result, many of the limits and controls that could have prevented the crisis were avoided. Similar patterns were observed in other countries as in the case of Spain, whose assets from real estate transactions increased without having uses a real basis for this increase.

Although the Great Recession did not have the same impact as the Great Depression, it nevertheless kept the planet in a veil of uncertainty for a couple of years. This event became the discursive platform for new socialist movements that appeared in countries such as Venezuela, Argentina, Ecuador, Bolivia, Paraguay, Brazil and Nicaragua. The socialism of the 21st century tried to recreate the development models of the 1950s and 1960s, but with a more authoritarian tone and with a much clearer socialist veil. The case of Venezuela is the most obvious, President Hugo Chávez expropriated a large part of the private sector and persecuted thousands of political and social leaders. Millions of Venezuelan citizens have been forced to migrate because of the persecution and because of the economic crisis that the socialist governments brought with them.

In general terms, two clear conclusions can be observed. First, the crises that arise in the stock exchanges, or in the real estate markets, come from the hand of the overvaluation of the price of shares, speculation, and the lack of limits that governments can establish. Therefore, it is clear that these risks, inherent to the functionality of the stock exchanges, can be supported with public policies and legal penalties that avoid the problems listed. Second, the economic crises that emerged within the stock exchanges have provided a discursive support that has allowed socialist policies, harmful to the liberal environment and the protection of human rights, to adhere to democracy as electorally acceptable avenues.

Despite the risks that may arise, the interaction between the stock market and the economy, and its impact on the development of nations is real and, in many cases, it is crucial because, through the various channels in which financial markets work, economic growth is boosted. Several studies such as the one carried out by Pan and Mishra (2018, p. 661), show that, in the case of China, the effects of the relationship between the stock market and economic development show that the global financial crisis from 2007 to 2012 had a significant impact on both the real and financial sectors.

Conclusions

This essay has allowed us to observe the foundations of capitalism and the stock markets in a relationship of necessity for development. Despite the risks that stock market activity can generate in companies and in the development of national economies, their functionality and usefulness has a greater probability of impact on the development of capitalism, seen as a system that allows the evolution of business, but also seen as a foundation for the welfare state of society, and, in general, seen as necessary for the common good.

As has been seen, the stock exchanges provide a means to increase the capital of companies so that they can invest in productivity improvements and, on the other hand, the stock markets also allow managing ways to increase financing to governments that have investment plans or even consumption plans. In both cases, the role of the stock exchanges in capitalism is visualized in means that allow the rapid generation of resources that are used within the company, to improve productivity, or are used in governments to promote specific development plans.

Weber believed that the individual desire for wealth as part of the spirit of capitalism, this spirit appears to be a driving force behind stock market volatility and economic growth (Bakshi & Chen, 1996, p. 133). In other words, while the impulse towards saving and investment grows, the stock markets, as well as economic development, will experience rates that will increase over time, making the role of the stock exchanges in capitalism very useful and fundamental. seen as business development, as economic development, and as strengthening the common good.

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