Peter Burgess LinkedIn Blogs

Seven Dimensions of Capitalism (7D-Capitalism)

About a hundred years ago, movies were coming into vogue. They were a technology leap from the previous static picture shows. And then came sound, but they were still black and white. And then there came color … technicolor. And then digital and surround sound … and then 3D. Amazing change and progress in about a hundred years.

Capitalism has changed rather more slowly. Adam Smith set the stage for modern economics and capitalism publishing the 'Wealth of Nations' in 1776 … around 250 years ago. Capitalism has had its fair share of critics over the years and many alternative systems of economics have been proposed, including the communism. The alternatives have not proved to be as effective as capitalism … but that does not mean that capitalism is perfect.

After a hundred years, movies became available in 3D. I argue that after 250 years capitalism needs to be available in 7D.

This will answer the question … how can capitalism be improved?

At its core, capitalism is about increasing capital, and the idea is that free enterprise will optimize the use of resources to achieve this goal. In a complex system, I is most unlikely that centralized decision making will ever get things right, but it is also true that laissez faire market economics will get things wrong if the metrics of everything are wrong as they are now.

For a long time, economists talk about the factors of production: capital, land and labor, and this segmentation of resources is a clue to how capitalism might be rethought to reflect the more complex world that is the 21st century.

Capitalism in the past and up to now is one-dimensional financial capitalism. What we need for the 21st century is a multi-capitalism that includes all the capitals: (1) financial capital, (2) physical capital, (3) human capital, (4) social capital, (5) institutional capital, (6) knowledge capital and (7) natural capital. This is 7D capitalism.

Natural capital is really where all wealth comes from. Natural capital is amazing, and for most of history was taken for granted. It is only in the relatively recent past that people have started to understand the role that natural capital plays in the success of humankind anjd also that there are finite limits to natural capital. Obviously, the environmentalists are interested in natural capital, but in fact natural capital in the form of land has been central to capital since the three factors of production were defined hundreds of years ago. The success of the 'New World' was in large part due to the fact of abundant land, one of the components of natural capital. A huge part of modern financial capital originated from the exploitation of natural capital.

Human capital is being talked about more and more. In many cases the conversation is about people being trained so that they are more useful for the employing organization. Human capital in the context of 7D-Capitalism is about an individual having a better quality of life and standard of living … a function of very many factors including what has happened in the past (like parenting, education, nutrition and health) and what is affecting a person at the present time (like security, for example) and the present value of what are the possibilities for the future. The potential of human capital is only being achieved by a very small part of the total population, and billions of people are realizing just a tiny fraction of what is possible.

Knowledge capital is a key to a world that works. Knowledge has been increasing at an increasingly fast pace over the years, and it is amazing what is now known. I argue that the power of knowledge is maybe a million times more now than it was 50 years ago. As an example, I installed a mainframe computer in the 1960s with 4K of main memory. Now my cellphone has 8G of memory … a million times more. The potential of knowledge is huge. The use of knowledge to make the world a better place is, however, up to this point, quite modest.

Knowledge has been a big enabler of the agricultural revolution and the industrial revolution, both of which resulted in amazing improvements in quality of life, standard of living and longevity. It is knowledge that enabled natural capital to be exploited to provide power that facilitated the production of goods and services that are the foundation of a high standard of living.

But knowledge is interesting in that unlike other capitals, when you give knowledge to one person, it does not need to be taken from another person. Knowledge is also very powerful, but it needs to be used in constructive ways in order for the outcomes to help make the world a better place. Unfortunately, like so many things, knowledge can be used to improve things or be a part of something quite horrendous.

Physical capital and institutional capital are both capitals that have been created by human initiatives and serve to support economic and social activity. Physical capital is all the things that have been built like buildings, factories, machinery and equipment, roads, bridges and ports that are all used in the conduct of economic activities. Institutional capital are all the organizations like government, universities, corporations, churches together with systems of law and regulation that are the framework for economic and social activity.

Social capital has something with a lot in common with human capital. It is the capital that is associated with a community or group of people rather than a unique individual. A strong social capital feeds into an individual's human capital, and vice versa.

Most socio-economic metrics reflect the state of financial capital much more than they reflect the state of any of the other capitals. Worse, there is confusion in the most commonly used metrics about what is state and what is flow. GDP (Gross Domestic Product) is a measure of flow that measures the activity in the economy, yet it is widely used as a proxy for the state of the economy. There is an assumption … terribly wrong … that more and more GDP (flow) is going to results in a better state of the economy.

I use the bathtub metaphor. How full is the bath? The tap is running at 15 gallons per minute. This is good when the bath is nearly empty and needs filling. This is not good when the bath is overfull and about to overflow.

More GDP is going to improve quality of life when people are very poor, but more GDP for people who are already wealthy has little impact on quality of life, but has an important impact of natural capital.

When we start to measure the change in all the capitals over time, then it will be apparent what is good performance and what is not. For most of the agricultural and industrial revolution financial wealth was created by the exploitation of land (natural capital) and labor (human capital). Natural capital was diminished by resource depletion and environmental degradation. People were exploited in ways that resulted in little improvement in quality of life while also putting people's health at risk … human capital was compromised. From the perspective of financial capital the results were good … financial capital increased.

Thinking of the economy through the lens of conventional double entry accounting, over time the balance sheet of the 7 capitals, the values of each of the capitals changed over time with financial capital going up and up, while the other capitals were being diminished, in some cases by very substantial amounts.

I visited a lot of industrial communities around the world while I was still a student. I remember visiting Sudbury, Ontario where nickel was being mined and refined. Resource depletion and environmental degradation were producing financial capital. A few years later I passed through Butte, Idaho where copper had been mined and refined. Disastrous resource depletion and environmental degradation, but copper resulted in business profit and augmented financial capital. The major multinational oil companies operated in many different parts of the world using the same socio-economic business model.

Conventional double entry accounting has worked well for financial capital. Something similar is need so that there can be rigorous accounting for all the flows and the impact on all the capitals. It is possible to expand the double entry logic of conventional accounting so that there is accounting for the state and flows around all the capitals. Each capital should have a unit of measure that simplifies reporting in summary form and fits well with the underlying technical characteristics of the capital. Quantification is not easy, but it is essential … and it can be done.

When we start to have capitalism that measures all the right things, and looks to optimize socio-economic performance with respect to all the capitals, … that is 7D-Capitalism … then we have the potential for amazing change and a far better world.

Peter Burgess – TrueValueMetrics – Multi Dimension Impact Accounting

------------------------------ /// ------------------------------

Contact information for Peter Burgess: Founder / CEO ... TrueValueMetrics

Website: http://truevaluemetrics,org
Email: peterbnyc@gmail.com
Skype: peterburgessnyc
Twitter: @truevaluemetric
LinkedIn for Peter Burgess : www.linkedin.com/in/peterburgess1/
LinkedIn for this blog: https://www.linkedin.com/pulse/article/20140920144334-27861-seven-dimensions-of-capitalism-7d-capitalism

