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## Christian Social Ethics and Capitalism: A Contradiction?

The history of Catholic social ethics, which over time developed to a corpus of the Church's social teachings, starts with the Fathers of the Church and the philosophers and theologians of the High Middle Ages, who often commented in detail on economic questions. Among them, especially Petrus Olivi, Saint Bernardine of Siena and Nicholas Oresme are important – all three members of the Franciscan Order.

In fact, the Franciscans were the first ones to not only understand and defend the connection between capital and interest, but also to found banks with the support of charitable donations, the so-called *montes pietatis* („Mountains of Mercy“), in order to lend poor people money – for interest, of course, or else the business would not have been sustainable. The Christian Middle Ages were able to distinguish between unproductive financial transactions only directed at acquiring money and those having general beneficial effects, and did not demonize the pursuit of profit. At the beginning of the fourteenth century, Flemish merchant agreements were opened with the formula “For God and Profit”, a formula that was already found in Florentine banking books in the year 1253.

On the threshold to modern times and the peak of moral theological dealing with issues on economic ethics, one can find the late Spanish Scholasticism of the 16th Century with the School of Salamanca and its surprisingly modern and correct understanding of the nature of commercial activities and the theory of money, function of private property, pricing, the question of the just price and the just wage, adequate government spending and fair taxes. Most of these moral theologians were Jesuits – today almost unknown but influential and still relevant pioneers of economic expertise, all the way to Adam Smith. The Catholic social ethics have largely forgotten them.

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When centuries later capital and credit took on new dimensions with the industrial revolution, new questions arose in the field of Church thinking, especially the so-called social question. At the time, many intellectuals, but also the catholic clergy gradually developed an anti-capitalistic mentality.

The clerical anti-capitalism had specifically modern origins. Its causes included the social uprooting of a growing number of people due to the liberation of peasants and the introduction of freedom of trade; as well as the often shocking poverty of the working classes, which could not be eradicated by any political means, and especially became a point of contention because of frequent hard-heartedness and inconsideration of factory owners.

Added to this was growing anti-Semitism, a reaction by those damaged by structural change, in particular members of the crafts and trade industries, but also lower civil servants. The anti-capitalism motivated by anti-Semitism also left its mark on the Catholic social ethics of the 20<sup>th</sup> century, for instance with Gustav Gundlach S.J. or Johannes Messner, who in 1938 under the influence of Werner Sombart described capitalism as the product of Jewish spirit and criticized its immoral acquisitiveness and pursuit of profit in the fifth edition of his work “*Die soziale Frage*”, or “The Social Question”.

In the 19<sup>th</sup> century, following a rise in nationalism, especially Germany experienced a strengthening of the faith in the state and reliance on authorities as well as the conviction that the free markets, cross-border competition and the entrepreneurial desire to make profits only exploited workers and prevented the improvement of their situation. The economy thus required guidance by a bureaucratically organized state. This belief also had an impact on Catholic social doctrine, in particular by the influence of the idea developed by the Jesuit Heinrich Pesch of so-called solidarity as a “third way” between socialism and individualistic capitalism.

Among wide sections of the clergy, an increasing scepticism towards engineering and even technology became apparent, of which traces can also be found in the most recent social encyclical “*Laudato si*”. But modern capitalism is characterized by the connection between the accumulation of capital and technological innovation – and this combination creates increasing wealth also for the lowest class, it is the winning formula of capitalism and will surely remain so. It will also enable us to get to grips with the ecological side effects of progress. However, this capitalistic development, as Joseph Schumpeter said, constitutes a procedure of “creative destruction,” which always creates losers as well, but eventually leads to increasing wealth and improved living standards for the masses. Today, we have become witnesses to how this procedure is repeating itself quickly. By successively introducing capitalistic production methods and market-based principles, the distance between rich and poor countries has been continually and drastically reduced in the last decades, and the number of people living in absolute poverty has been cut in half.

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The positive developments that should fill us with hope are frequently overlooked today, or they are not mentioned. Church statements on issues of worldwide poverty often present themselves as almost apocalyptic and show an image of decline and breakdown. Of course, the Church should act as advocate of the weak, and condemn human rights violations. But in my opinion, it should mainly encourage the forces that effected prosperity for countless people, and will continue to do so. And these are the forces of capitalism, of entrepreneurship, free and open markets, international trade. In the countries where freedom and individual responsibility were given to these forces, and where they were supported, millions of people could free themselves from poverty. Where they are not given any room, also due to a lack of prerequisites such as rule of law and protection of property rights, people still often live in poverty, or at least haven't gained anything.

Even today, a widespread anti-capitalistic mentality and resulting ideologies block the view to reality and the prosperity-inducing force of capitalism and market economy. They diminish the trust in their ability to master the big social and ecological challenges of the future. In fact, I

am sure that capitalism and Christian social ethics are not contradictory concepts. There are many reasons, however, why many people find it difficult to accept that.

I would like to provide some of these reasons in the following.

The *first reason* is the common view of history and still predominant narrative of an allegedly noxious, unbridled laissez-faire capitalism of the past, which caused crises and social misery until the state finally intervened and by social policy and prevention of monopolies and cartels adjusted the market forces in line with the common good. This narrative does not correspond to historic facts, and has repeatedly been refuted by research.

The *second reason* is a widespread lack of understanding of the process of economic value creation, and thus for what capitalism actually is and how it works. Let me provide a brief explanation: Over thousands of years, the majority of people remained on a more or less secured subsistence level. Prosperity gains were destroyed by population growth, but also by epidemics and wars. There is only one way to escape the vicious cycle of poverty and subsistence economy *over generations*: the growth of labor productivity, i.e. economic growth on the basis of innovation. This is what capitalism has achieved in conjunction with the Industrial Revolution, and still achieves today.

Why is this the case? In capitalism, private wealth is neither redistributed nor just consumed by the rich, but profitably invested at one's own risk. Private wealth thus becomes capital, i.e. a production factor for new goods. Capital in combination with entrepreneurial vision and innovative ideas creates labor and therefore wages; this creates buying power and consumption, which in turn makes further investments profitable. This results in an upward spiral of capital accumulation, technological innovation and increase in productivity. As a result, real wages grow continually, which also increase buying power and thus consumption and standard of living.

This is what happened in the 19<sup>th</sup> century. In the year 1964, the – above mentioned – Austrian social ethicist Johannes Messner, at first a critic of capitalism, wrote about England in the 8<sup>th</sup> edition of his work “Die soziale Frage“ (taking as basis data by Joseph Schumpeter) as follows: “From 1800 to 1913 the population increased fivefold, aggregate income increased tenfold, prices dropped by one half, the average individual real income increased fourfold; at the same time, working time for the individual dropped almost by one half, child labor was abolished and work for women was limited.” The situation was similar in Germany, said Messner, even more: in the 19<sup>th</sup> century Germany's population grew by 44 million, real wages at least doubled and working time was reduced by one third.

This process was without historical precedent. It was not a result of social policy or union and labor disputes. It was a result of industrial capitalism of the 19<sup>th</sup> century, effecting the opposite of Marx's predictions: it generated increasing prosperity and not only for the upper class, but for everyone – despite unprecedented population growth, to which capitalism had contributed by the improvement of the hygienic and medical situation. The two main prerequisites for this success were the existence of a state under the rule of law, securing property rights and the enforcement of contracts, as well as a continually improving infrastructure.

Capitalism is the “economic system of giving”. Capital – the investment of wealth – precedes returns. Even if the returns – or the profit – have not yet materialized, and even if it is uncertain whether it will ever materialize, the worker already receives his contractually stipulated wages. The worker’s wages are always an advance payment. The capitalist gives without knowing whether he will receive his share, and even risks losing it. It is therefore not against justice if the returns or the entrepreneur’s profits – depending on the success and the added value – is correspondingly high. With today’s corporations acting on a global market, such profits can be many times higher than in previous times. Increasing inequality within economically sophisticated and technologically especially innovative societies is no more than the flip side of the increase of global prosperity caused by such businesses.

The capitalistic economy is thus both structurally and systemically social. While it is an economy based on giving, socialism is the economy based on taking – in socialism, distribution goes on until everyone is equally poor. Where capitalism and market economy are able to flourish they eliminate the most fundamental social problem of humanity: mass poverty. Capitalism does not create equality, but mass prosperity. Socialism in turn creates equality – and mass poverty. Current example: Venezuela.

At the same time, capitalism has proven to be the most efficient way to serve the social responsibility of private property: i.e. it is the best way to use private property for the common good, thus to procure that the goods of this earth, but above all private wealth benefits everyone. It would be foolish to tax it for redistribution purposes. The church doctrine of the “social function” of property, thus that private property must always be used for the benefit of fellow human beings or the common good, originates from a time in which the rich were called on to hand out alms to the poor and needy, even if on a voluntary basis. This still has its significance, but has by far been surpassed by the possibility to use it in a profitable manner in a capitalist economy, and thus create self-created prosperity for others.

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A *third reason* for anti-capitalistic mentality and why capitalism and Christian social ethics are regarded as contradiction is closely connected to the previous reason. It consists in the widespread understanding that capitalists of the 19<sup>th</sup> century exploited workers by depriving them of the greater part of the loan to which they were entitled, and thus enriched themselves. This is in short the Marxist theory of exploitation of the working classes. Wealth and “capital” are thus subject to general suspicion, because according to this understanding, they were created at the expense and by the unfair exploitation of the working class. Only by government interventions and union pressure was social justice created, and eventually, more adequate wages were paid.

This momentous misjudgment, by which many Catholic social ethicist and unfortunately also Church documents have been influenced, is based on the erroneous opposition of “work” and “capital”. Hereby the “work of capital” or that of the capitalist or entrepreneur is overlooked. In reality, the value of the product made by the worker does not depend on the work of the worker, but from the actual or expected market value of a product; this in turn is measured according to whether it meets the actual needs, preferences, wishes of the consumers. The creation of this value is not the achievement of the worker, but exclusively – I say: exclusively –

that of the entrepreneur, investor, capitalist. The entrepreneurial achievement – or work – consists of discovering the wishes of consumers, even anticipating them, and developing products that are then actually bought and which generate revenue that finally allows the payment of wages. Entrepreneurs have to have visions, be creative, take risks, their achievements are of an intellectual and organizational nature that enable the worker to be productive and have his wages paid to him, for wages do not fall like manna from heaven, but have to be generated by the sale of the products. In short: without capitalist pursuit of profit and the entrepreneurial accomplishments motivated thereby, the masses of people in the 19<sup>th</sup> century would have starved to death, or not even been born.

The problem with starting industrial capitalism was the extremely low labor productivity, and correspondingly low wages. Added to this was the constant excess of workers caused by the rapid population growth, which depressed wages. The alternative – capital-intensive production and higher wages – would have led to mass unemployment and worse misery for many. Only productivity increase by significant investments and the connected technological innovation, i.e. capitalist economic growth, were able to solve this problem. Higher social standards could only be afforded with higher productivity, they couldn't just be ordered. They are essentially the result of developing capitalism, not its containment or correction by social policy. Regarding today, it may be said that social policy can also prevent growth and thus higher prosperity for everyone, and this is very much the case today. The great barriers to higher prosperity today are a flood of legislation and bureaucracy, regulations of all kinds and the constantly increasing public debt, by which our out-of-control social systems are kept alive.

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A *fourth reason* for widespread anti-capitalistic mentality is the experience of the last financial crisis and the ensuing debt and economic crisis, or rather the wrong interpretation of its causes. What caused the crisis were not markets that were too free, not regulated enough and therefore instable, but public policy and government interventions, a politically-driven real estate bubble, government-backed mortgage banks that securitized bad loans, thereby obscuring risks and distributing these toxic but government-certified financial products world-wide with the help of regulated rating agencies. A free mortgage market independent of politics and legal disincentives and risk-aware entrepreneurial conduct and the appropriate bank lending, thus real capitalism and a free market economy, would never have led to an environment in which thanks to government backing, greed and criminal energies run free enough to bring the entire financial system to the brink of collapse.

A *fifth reason* for widespread resentment against capitalism and free market economy is our monetary and financial system. This is unjustified. Our monetary and financial system should not be called capitalist or market-based, but – if anything – rather socialist. For socialism means nationalization of production resources. In today's world, the state holds the monopoly for the production of money by its central banks, and thus controls the creation of money by the banks. It dictates its own money as legal tender, forcing us to accept it as means of payment, even though for decades, it has continually lost value. Since US President Nixon in 1971 terminated the gold standard for the dollar and subsequently all currencies linked to the US dollar under

the Bretton-Woods system, and thus lifted the braking effect, the amount of money in circulation has continually increased. This inflationary development (and not any allegedly detrimental deregulation), by which politicians could finance their continuously new promises, caused the frequently lamented growth in the financial industry, which is partly detached from the real economy. As we have discovered, this is associated with high risks. This “financial capitalism” does not have much to do with capitalist entrepreneurship, but today is regarded as the embodiment of capitalism.

Inflationary monetary policy like it has been practiced over the last decades is in fact contrary to all principles of a liberal market economy, which depends on a scarcity of money in order to keep up its value, and investments in long-term profitable, innovative and growth-stimulating capital goods are promoted all the more.

The inflationary policy of cheap money – and this cannot be emphasized enough – was an essential prerequisite for and contributing factor to the last financial crisis. Today, we are in a situation in which the toxins that led to the financial crisis are used as alleged antidote to overcome the crisis. Instead of applying painful but healing structural adaptations, monetary policy is attempting to postpone them, thus causing an ongoing inflation in property prices (i.e. shares and real estate). This in turn benefits the wealthy, who are more able to invest in shares and real estate, and – at least statistically – makes them richer and richer. At the same time, savers and thus the ordinary people lose out. The low interest rates further secure the survival of unprofitable businesses – at the expense of the common good – which inhibits or even prevents innovation and growth.

The policy of cheap money also favors consumerism, which has been rightly criticized by the church, but is most likely misinterpreted. And this leads us to a *sixth reason* for distrust of the market economy and capitalism. Harmful consumerism is not a result of market economy, but a consequence of public policy that does everything it can to encourage people to consume on loan instead of saving money. This policy of constant “living above one’s means” obviously uses market procedures, but follows the recommendations of Keynesian economic theory, which claims that this could stimulate the economy and control unemployment. This, however, is a fallacy. A society cannot grow richer by its citizens’ increased consumption. A society can only grow richer by savings and investments in long-term profitable capital goods. The counterbalance that is required is the interest, the price of money, which however can only develop on a free money market. But the money market is de facto nationalized, it is manipulated by the government and its price system is suspended. People no longer know what things and even money is worth now. For this reason, there is no incentive to save – the time horizon is the present, not the future.

Nobody knows when this magic of cheap money will end. It has nothing to do with capitalism and free market economy, but a lot with the idea that the state has to control the economy and the primacy of public policy, as glorified by the competent European politicians. What seems certain is that the end of this public policy could get very uncomfortable. Once more, Capitalism will surely bear the brunt of this. And it is just as sure that even more government regulation will be demanded, and in view of the social upheavals to be expected, even more determined primacy of public policy.

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My conclusion is as follows: from a Christian viewpoint I believe that capitalism as the “economy of giving” is the economy that most closely corresponds to the basic principles of Catholic social ethics. I would even say: true capitalism and a Christian entrepreneurship form a natural symbiosis. The mediaeval slogan “For God and Profits” still applies for Christians today, and in no way constitutes a contradiction.

Entrepreneurs who are aware of their responsibility as Christians often seem to have a bad conscience when they act entrepreneurially, i.e. when they defend a profitable business model and want to run a profitable business, even regard profits as the yardstick for their business success and therefore, in order to reach their goals, sometimes are forced to make job cuts. I would tell these entrepreneurs that they need not have a bad conscience. If as entrepreneurs, investors, but even employed managers, they act entrepreneurially, meaning they act in accordance with the logics of capitalism and market economy, and try to sell a good product to their customers in order to make money, this is not unchristian but the best way to use their mind, their knowledge, their work and their property for the benefit of the common good. They need not be ashamed of their salaries and other compensations, provided they correspond to the provided value.

The common good is mainly created by successful, which always means profitable, entrepreneurial activities – even if this is not intended, but serves the purpose of supporting oneself and one’s family and providing an adequate standard of living, or even if one just wants to become rich and pursue one’s dream. In capitalism, this can be effected without harming others, unlike in socialism; one rather contributes to an improvement of the situation of others. The entrepreneur is not responsible for the well-being of an entire country or a region; this falls into the competence of government institutions and politics. The entrepreneur is responsible for the well-being of his business, those directly affected or dependent, and of course those for whom he primarily works: normally himself and his family, or other members of his personal social environment.

In my opinion it would be wrong to believe that an entrepreneur, in order to justify his actions in social or even Christian respect, would have to pursue any social or charitable purposes in addition to his entrepreneurial activities. Depending on the circumstances and opportunities, an entrepreneur would be obligated to do this *as a human being and as a Christian*. But not with his own enterprise, but with the income he is paid or pays himself as owner of his enterprise.

Today, everyone is talking about so-called “corporate social responsibility”, whatever the intentions may be. Experience shows, however, that entrepreneurs only successfully take social responsibility beyond the immediate business purpose if they do it for *strategic* reasons, i.e. because they reckon that it will be worth it for business and the enterprise. This is smart, because long-term entrepreneurial thinking is ultimately the best business model. Milton Friedmann’s saying *the business of business is business* still applies here. Only if it is a “deal” does a business fulfill its specific social function, which is fundamentally an economic function.

But is this enough, from a moral perspective? Doesn’t this show that the logics of the market are morally subversive, or at least not conducive to moral conduct, but purely utilitarian? I

believe the opposite is the case. Unlike the state-organized forms of business activities such as socialism, the logics of capitalist market economy call for the best qualities and instincts in people, such as initiative, responsibility for one's own actions, willingness to take risks and to bear the consequences, contract compliance, but above all: building trust, the most precious resource of businesspeople. The more the state interferes, the more lobbyism, chase after subsidies and corruption will arise – entrepreneurs and politicians then attempt to get hold of advantages at taxpayers' expense, thus in an unproductive manner. I would not claim that profit-pursuing capitalists and entrepreneurs are better people, but they do something that serves them as incentive to act more or less morally, provided they really act in accordance with the logics of capitalism and in an entrepreneurial manner.

The world of capitalist economy is not an ideal world. It is infested with losers, fraudsters, crooks, and cutthroats. Sooner or later, however, the market will sanction incompetent and immoral conduct, especially if it is embedded in a functioning legal system with clear rules. It is wrong to expect more from an economic system that to provide the right moral incentives – its purpose is not to make us all saints. This falls into the responsibility of other authorities – but that is another story.

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