17 JULY 2023

Monday Briefing

EDITION #4

A DOSE OF ALL THINGS ENTERPRISE, LEADERSHIP AND GOVERNANCE.

Economic Thought of the week.. Erdoganomics

"Erdoganomics" is a term coined to describe the economic policies pursued by Recep Tayyip Erdogan, the President of Turkey since 2014. Erdoganomics refers to a set of economic principles and strategies that were implemented during Erdogan's tenure as both Prime Minister and President of Turkey.

The impact of "Erdoganomics" on Turkey is a subject of debate and varies depending on the perspective. Considering it was an economic principle, Erdogan's leadership allowed Turkey to experience a period of significant economic growth, with GDP rates exceeding 5% on a yearly basis. This growth was partly driven by increased domestic consumption, infrastructure development, and a construction boom. Erdogan focused a lot on infrastructure development - this resulted in the construction of many major projects such as new airports, bridges and highways, with the aim of enhancing connectivity and modernising the country's infrastructure. Although these projects raised concerns for 'long-term sustainability,' the effects are still relevant today. Turkey is now one of the world's main holiday destinations, contributing to the economy and creating job opportunities.

On the other hand, critics argue that Erdogan's preference for a loose monetary policy, including keeping interest rates low, contributed to inflationary pressures in the economy. Turkey has faced periods of high inflation, eroding the purchasing power of the Turkish Lira and raising concerns about the overall stability of the economy. Another concern is the significant increase in Turkey's external and private sector debt. Besides the significant economic growth,income inequality is still prevalent, as the benefits of economic growth have not been evenly distributed. This has raised social and economic disparities in the country which could have a larger impact on the economy, as the state of the people is crucial to an economy.

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The Economic Edition

Faith Gundani
Head of Knowledge

*The 2023 **NATO summit** took place in Vilnius, Lithuania last week where the Heads of State and Government of NATO member countries to discuss important issues facing the Alliance and provide strategic direction for its activities.*

*NATO - the **North Atlantic Treaty Organization** - was formed in 1949 and currently has 31 countries across Europe and North America who agree to help one another if they are attacked.*

*During the summit, **Recep Tayyip Erdogan**, newly re-elected president of Turkey took a big step this week to mend diplomatic relations with the West to look for solutions to a long and worsening economic crisis including foreign investors who have ditched Turkey in recent years because of its economic woes.*

*In today's Economic edition, we explore President Erdogan's economic policies and the evolution of **the banking system** through **community banking** and **technology.***

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Economic Thought of the week.. (continued)
Erdoganomics

It is important to note that the impact of Erdoganomics is complex and subject to different interpretations. Some argue that the policies pursued under Erdogan's leadership have contributed to short-term economic growth and infrastructure development, while others express concerns about long-term sustainability, economic imbalances, and political factors affecting the economy.

Erdoganomics included increased government spending on infrastructure projects and social programs, which contributed to a growing fiscal deficit and rising debt levels. In the UK - one of the biggest economies - the fiscal policy is guided by the principles of fiscal responsibility, with a focus on maintaining a sustainable budget and reducing the deficit. The UK has a diverse and developed economy withinnovation, technological advancements and a strong financial services sector. Turkey, under Erdoganomics, experienced periods of robust economic growth but also faced challenges such as high inflation, currency depreciation, and external debt burdens, lacking the ability to develop and adapt.

Erdoganomics was implemented in a democratic system, albeit with concerns about the erosion of institutional independence and the rule of law. China, a significantly larger and more diverse economy, operates under a one-party system with a centrally planned political structure that influences economic decision-making. While Erdoganomics included policies to support small and medium-sized enterprises, it was accompanied by concerns about restrictions on foreign investment and an inconsistent approach to market liberalisation. China, on the other hand, has pursued gradual market-oriented reforms, opening up sectors to foreign investment and establishing special economic zones to attract foreign businesses.

In conclusion, the impact of the policy is a subject of debate and analysis, with critics expressing concerns about the sustainability of the policies pursued and their impact on democratic institutions, rule of law, and investor confidence in Turkey.

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COMMUNITY BANKING
BY ABA ANDERSON

Banking has transformed significantly from its origins, dating back to the 12th and 13th centuries. It was originally used as a safekeeping for wealthy individuals' funds. An example of this is the first major banking system established by the Medici Family in the 14th Century. In modern times, disruptive finance solutions propelled by technology have brought about emerging concepts such as FinTech. These concepts are currently acting as a catapult for the thriving of digital banks such as Starling and Revolut, to name a few.
However, there is still more revolution to be done in the banking sector. As individuals are constantly learning, developing and evolving themselves, subsequently, the by-product of evolution in banking is inevitable.The revolutions seen in banking can be visibly represented by the changing of organisational structures and the introduction of new products. At the root of any change is a new way of thinking and a new ideology. Therefore, if we are to question what will form the future of banking, this will be based on the new way of thinking about how banking can evolve.

Banking is widely beneficial to many and acts as a source of credit, guarantee and safety, however, it is not accessible to all. Such resources are often easily available to the largest contributors to society - the middle class - who offer high taxes. Furthermore, the ultra-rich have millions to store in savings schemes. Unfortunately, some 1.7 billion adults worldwide do not have access to a bank account, according to data from the World Bank.Battling with the day-to-day difficulties of being financially excluded from the traditional banking system, the questions posed to low socio-economic communities are: How do they progress financially? How do they get assets without sufficient credit? How do they raise much-needed capital for their businesses?

On an individual level, providing a solution to these problems seems nearly impossible, as children born into low-income families have less chance of moving up in the world and improving their professional status. These facts were highlighted by recent data from the OECD. However, hidden in these problems is the possibility for such communities to find a compelling alternative to create financial prosperity – a sharing economy based on the power of the many.
Low socio-economic communities traditionally are bound together by the need to survive. Where resources may be scarce, individuals within such communities are reliant upon immediate and extended family members to fulfill basic needs such as childcare, food and shelter. In such communities, multiple generations living within the same household is not uncommon. As such, family culture is prominent, focusing on the ability to pull resources together to achieve a common aim or goal. This culture is what forms the basis not just in everyday functionality, but can also be applicable in their method of banking – a unique concept named: **Community Banking.**
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In Community Banking, financial resources are shared and distributed between many. If individuals are blocked out of traditional banking systems, they can depend on a relative to provide a loan to buy stock needed for their business to service clients. Whereas this ideology can be likened to communism, this ethos has Capitalist touch points; individuals are mentored to be progressive, build businesses and aim for high positions in industries and meritocracy is celebrated, but they are aided by the community that stands strong behind them and acts as a support system. Thus, its origins cannot be likened to any ideology that has come before it, the thought of it alone can therefore be coined as revolutionary.

Worldwide, a staggering 700 million people are tagged as living in extreme poverty and 1.7 billion are financially excluded from traditional banking systems. That means that there are billions of people who are currently exempt from a country's GDP, taxes and productivity. However, they do have the potential to contribute.

This new kind of banking can do what no other system has done before, which is capture a missed demographic, and those termed as at the 'bottom of the food chain'. The focus then needs to be tilted towards providing conducive environments for such communities. This included people who do not ask for a handout as they can thrive no matter what circumstance they are put in. They merely require exposure and access to opportunities. These scenarios have to constantly be proposed to create an environment in which once members prosper, they will come back to pour resources into that same community. This eventually forms a continuous cycle of prosperity, belief and job creation.

In such communities, the undertone of theories of ancient banking is evident, individuals belonging to such communities trust that their assets can be kept safe and generate a return on them, but that return isn't to build their monetary wealth, but instead the overall progression of their community.

So, what happens if we take the collective participation of everyone combined, and together build a much more wealthy and prosperous community? There lies the ethos behind the hidden economy in low socio-economic communities that could revolutionise banking.

THE EVOLUTION OF THE WORLD ORDER

Govcoins

Formally known as Central Bank Digital Currencies (CBDCs), Govcoins are a legal tender in electronic form. At first glance, they allow the creation of faster, safer payment systems, but raise major concerns about data privacy.

The question now is, who runs the world? Those over the age of 45 have experienced the world to be dominated by two giants, the US and the Soviet Union. However, those under the age of 45 experience a world not dominated by the Soviet Union, leaving the US with a full exertion of raw power. Many changes cause society to think we live in a 'leaderless' world such as Russia not becoming integrated with the Western institutions though being related to a high level of power or China being integrated into US-led institutions based on the idea that they would get wealthier and more powerful to then become 'American'. Lastly, tens of millions of US citizens and other wealthy democracies had felt left behind by globalisation.

A world order to expect within the next 10 years

The first one being our security order which is a uni-polar order that will overlap and influence the way we live, how we think and what we do. Whilst doing this, our security order will also run as our global economic order, generating a lot of power.

Both the US and China are economically interdependent, meaning one cannot control the other;however, in contrast to this the US-China trading relations are at their highest level so far. It is also expected of the Chinese market to be the largest market in the world by 2030, as seen through society's desire to have access to the market now. The European Union has the largest common market and they set rules which society must follow if they want to have profitable business there. Despite the rise and fall in economies, the Global Economic order will remain a multi-polar order. As for the US, it uses its power in national security as an attempt to bring the world's economies towards it.

Now introducing the Third Order, the Digital Order which is not run by the government but instead by tech! It is the use of technology that allows Ukraine to defend themselves, with tools from the Russian cyber attack. If some tech companies didn't exist, Ukraine would be fully out of line within weeks of the Cold war. Some presidents won't be able to stand without tech, as social media alone promotes them and any conspiracies around them.

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THE EVOLUTION OF THE WORLD ORDER

Technology companies determine our identities. Identity no longer remains to be determined by nature and nurture but instead through algorithms. The chances of challenging an algorithm is very low and a lot of power is held within such a system. If China and the US exert more power over the digital world and tech companies align themselves with the governments within these countries, we will find ourselves in a technological Cold War. This therefore splits the digital order into two.

"If tech companies resist competition with the physical world and persist with global business models, it creates a new globalisation"
- Digital Global Order

However, a techno-global order will be formed if the digital order becomes the most dominant and the government erodes in their capacity to govern the world. The result of this will determine if we produce a world of limitless opportunities or a world without freedom.

Now onto the digital currencies that matter...

With technological change, we see that Bitcoin has gone from being an obsession of anarchists to a 1 trillion dollar asset class that many fund managers insist belongs in any balanced portfolio. We can also identify with PayPal's 392 million users, a sign that America is catching up with China's digital-payments giants.

The most revolutionary link between tech and finance remains to be the creation of government digital currencies, which typically aims to let people deposit funds directly with a central bank, bypassing your everyday lenders. These govcoins are to be treated with humility.

However, the rise in such digital currencies does raise a sense of worry for banks as they think if banks' deposits were reduced, the financial system would be greatly changed: banks would have less to invest in mortgages and the economy.

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UNDERSTANDING THE COST OF LIVING: SACRIFICE RATIO

Economic principles are a set of rules or concepts that govern how people satisfy their unlimited wants with their limited resources. The sacrifice ratio is an economic concept that measures the short-term costs of reducing inflation. It represents the percentage decrease in output (Gross Domestic Product, or GDP) that an economy must endure in order to reduce inflation by one percentage point. Inflation is the rate of increase in prices over a given period of time and typically a broad measure, such as the overall increase in prices or the increase in the cost of living in a country.

The idea behind the sacrifice ratio is that implementing contractionary monetary or fiscal policies, such as raising interest rates or reducing government spending, can lead to a temporary decrease in economic output. This decrease in output is considered a "sacrifice" that the economy must make to achieve lower inflation rates. The specific value of the sacrifice ratio varies depending on the characteristics of an economy, its institutional framework, and the effectiveness of policy measures. Different studies and estimates have yielded a wide range of values for the sacrifice ratio, ranging from as low as 0.5 to as high as 5. This means that in some cases, a reduction of 1% in inflation could result in a decrease in GDP of 0.5% to 5%.

The concept of the sacrifice ratio has been used by policymakers and central banks to assess the trade-off between inflation and output in the short term. By understanding the potential costs of reducing inflation, policymakers can make more informed decisions about the appropriate level of contractionary measures to achieve their inflation targets without causing excessive economic slowdown or recession. It's worth noting that the sacrifice ratio is a simplification of the complex relationship between inflation and output, and it has its limitations. It assumes a linear trade-off between inflation and output, which may not hold true in all circumstances. Additionally, the sacrifice ratio may vary over time and across different economic conditions.

According to the field of monetary policies and macroeconomic analysis, the concept offers several benefits. For example, it can facilitate coordination between monetary and fiscal policymakers. It allows for a better understanding of the potential impact of contractionary measures on the overall economy, encouraging policymakers to work together to mitigate any adverse effects on output and employment. Policymakers can gauge the level of output loss associated with different inflation reduction goals, helping them set achievable and sustainable targets. They can also evaluate the effectiveness of their chosen contractionary measures reassessing their policies and considering alternatives.

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While the concept of the sacrifice ratio provides useful insights, it also has several limitations. It can be time-dependent, meaning that its value may change over different periods or economic conditions. The relationship between inflation and output can vary due to factors such as changes in economic structure, technological advancements, or shifts in consumer behavior. Failing to account for these variations can lead to misleading policy conclusions. Estimating the precise value of the sacrifice ratio is also challenging. It relies on historical data and statistical analysis, which are subject to data limitations, measurement errors, and changing economic circumstances. The sacrifice ratio primarily focuses on the short-term costs of reducing inflation. It may not adequately capture the long-term consequences of contractionary policies.

In conclusion, despite its limitations, the sacrifice ratio remains a valuable tool for policymakers. It helps quantify the short-term costs of reducing inflation, enabling informed decision-making. By considering the sacrifice ratio, policymakers can strike a balance between price stability and economic output. Although it varies across economies and time periods, the ratio guides the development of more effective policies and contributes to ongoing refinements in monetary frameworks. While acknowledging its limitations, the sacrifice ratio remains a useful benchmark for assessing the costs of disinflationary measures and informing policy strategies.

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