Christian Virtues and Finance

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This article discusses both anecdotal evidence and the findings of recent research to demonstrate that the biblical virtues of integrity and its close cousins[1], justice and righteousness, are integral to the efficient functioning of financial markets and the efficient financial performance of businesses in our system of democratic capitalism. The article notes that the presuppositions of finance currently ignore these normative considerations, and discusses the possibility of a paradigm shift toward a values-based perspective in finance.

Introduction

Graham Tucker wrote in "Rediscovering Kingdom Values,"

> ". . . many of the values of the kingdom of God, although not recognized as such, are being rediscovered by a pragmatic business community. I believe that an enlightened Christian laity could transform our society and move it from the philosophy of competitive individualism, the Adam Smith approach, to co-operative community, the Jesus approach" (24).

What relevance have Christian virtues to the discipline of finance? Isn't the driving presupposition of the discipline the egoistic paradigm of profit maximization and its more sophisticated offspring, in the corporate[2] context, shareholder wealth maximization? As commonly viewed, participants in this field at best pursue their self interests with a value free, coldly calculating amorality—blithely assuming that the "invisible hand" is harmonizing all of this individualistic activity for the greater good of society. At its worst, the financial community might be viewed as guilty of calloused manipulation—pursuing a gospel of greed as proclaimed by its apostle, Ivan Boesky.

The three major presuppositions of the field, (1) shareholder wealth maximization (SWM), (2) time value of money, and (3) risk-return tradeoff, which form the basis for financial analysis and the development of financial management strategies are seen as forming the basis of a positive discipline "which merely

attempts to explain observed phenomenon, and as such is exempt from the normative value-based considerations of business ethics." (Dobson, *Reconciling* 29). However, there is an emerging awareness in the discipline of the inadequacies of the model of the rational economic man and the need to give serious consideration to normative issues.

Kenneth Arrow, an early voice urging a broader perspective, concluded:

> It can be argued that the presence of what are in a slightly old-fashioned terminology called virtues in fact plays a significant role in the operation of the economic system. . .[T]he process of exchange requires or at least is greatly facilitated by, the presence of several of these virtues (not only truth, but also trust, loyalty, and justice in future dealings (*Gifts* 15)

Thus Tucker is correctly attuned to the shifting of paradigms[3] in business, including the discipline of finance. However, he has an incomplete understanding of the philosophy of Adam Smith who deeply appreciated the critical role of virtue in the functioning of society. In his discourse on the virtues of justice and beneficence in *The Theory of Moral Sentiments*, Smith concluded:

> All members of human society stand in need of each other's assistance, and are likewise exposed to mutual injuries. Where the necessary assistance is reciprocally afforded from love, from gratitude, from friendship, and esteem, the society flourishes and is happy. All the different members of it are bound together by the agreeable bands of love and affection, and are, as it were, drawn to one common centre of mutual good offices (II.ii.3.1).
>
> But though the necessary assistance should not be afforded from such generous and disinterested motives, though among the different members of the society there should be no mutual love and affection, the society, though less happy and agreeable, will not necessarily be dissolved. Society may subsist among different men, as among different merchants, from a sense of its utility, without any mutual love or affection; and though no man in it should owe any obligation, or be bound in gratitude to any other, it may still be upheld by

a mercenary exchange of good offices according to an agreed valuation (II.ii.3.2).

Society, however, cannot subsist among those who are at all times ready to hurt and injure one another. The moment that injury begins, the moment that mutual resentment and animosity take place, all bands of it are broke asunder. . . .Beneficence, therefore, is less essential to the existence of society than justice. Society may subsist, though not in the most comfortable state, without beneficence; but the prevalence of injustice must utterly destroy it" (II.ii.3.3).

Thus, a utilitarian commitment to justice and the welfare of society are the minimal criteria for its survival; however, the biblical virtue of selfless love is capable of taking the society, in the words of Rev. Johnson Oatman, to "Higher Ground." We shall examine the biblical understanding of the virtues of integrity, justice, and righteousness and then go on to examine their crucial importance to the finance discipline.

Integrity, Justice, and Righteousness in Scripture

Let justice roll down like waters
And righteousness like an ever-flowing stream (Amos 5:24).

To do righteousness and justice
Is desired by the Lord rather than sacrifice (Proverbs 21:3).

For the Lord gives wisdom;
From His mouth come knowledge and understanding.
He stores up sound wisdom for the upright;
He is a shield to those who walk in integrity,
Guarding the paths of justice,
And He preserves the way of His Godly ones.
Then you will discern righteousness and justice
And equity and every good course.
For wisdom will enter your heart (Proverbs 2:6-10).

Integrity (from the Hebrew *tāmam*) connotes one who is whole, sound, complete, blameless, honest, and upright. One with integrity will use speech which "is complete, entirely in accord with truth and fact" (Harris 974) unlike Ananias

and Sapphira (Acts 5:1-11). He will demonstrate fidelity and be constant (Hebrews 13:8) like Job (Job 2:3) even in times of stress and adversity, rather than being unstable or double-minded (James 1:6-8), i.e., expedient and unreliable.

One who is just and righteous (from the Hebrew *sadeq*) will conform to ethical or moral standards and vindicate those who are oppressed. There is a redemptive aspect[4] in that "the righteousness of God appears in his God-like dealings with his people, i.e., in redemption and salvation" (Brown 355).

God does not show partiality or take bribes...

Furthermore, righteousness is worked out in the quality of relationships between individuals. "The man who is righteous tries to preserve the peace and prosperity of the community by fulfilling the commands of God in regard to others. In the supreme sense the righteous man is the one who serves God (Malachi 3:18)" (Harris 753) and who "will live by his faith" (Habakkuk 2:4). Hence, since God does not show partiality or take bribes, but rather defends the weak and befriends strangers (Deuteronomy 10:17-21), we are not surprised that the prophets trumpet these themes with regard to the behavior of God's people (Leviticus 19:9-18,33-37).

Amos (2:4,5) decries those who pervert justice, trample the poor and righteous, take bribes and deprive the weak of due process. Micah (2:6,7) indicts: the powerful who defraud the weak of fields and houses evoking the memory of Ahab preying upon Naboth's vineyard (I Kings 21); dishonest, violent businessmen with short measure, dishonest scales and deceptive weights; and the judges and rulers who seek bribes. He, rather, urges them "to do justice, to love kindness, and to walk humbly with your God" (6:8). His contemporary, Isaiah (1:16-28), pleads for a spiritual awakening which would result in social justice for the orphan and widow in place of the violence, corruption, and oppression which characterized Judah in his day. In contrast, we see Job, a righteous man of integrity "delivers the poor and orphan, helps the blind along the way, supports the weak and is a father (provider) to the poor (Job 29:12-15). . . .care[s]

for the traveler (31:31-32), eschew[s] wealth for its own sake (31:24-25), thus not victimizing himself or others in its pursuit. Nor did he squeeze out of his servants the last ounce of effort (31:13) having their limits of strength and comfort in mind" (Harris 753).

The New Covenant continues these themes with James expressing concern about: the care of orphans and widows (1:27); partiality (2:1-13); and the misuse of power and riches in holding back wages, hoarding wealth, ostentatious living, and oppression of the righteous (5:1-6). Jesus, of course, with His law of love (Matt. 22:37-40) takes us to that "Higher Ground" worked out in ethical terms in the Golden Rule (Matt. 7:12). The real struggle comes when Christians are called to make these virtues relevant to the market.

Christian Virtues and Market Efficiency

Words heard in the religious sphere are often also heard in banks and brokerage firms, labor unions, and corporate offices. In both fields one regularly hears such words as trust, fidelity, fiduciary, promissory, confidence, debt, redemption, saving security, futures, bonds and so on. It is as unimaginable to enter into basic economic relationships without these words as it is to speak biblically of God without them (Meeks 29).

The Ideal

The literature strongly endorses the thesis that virtues and virtuous behavior make markets more efficient and that sufficient integrity must exist to engender a critical level of trust or markets will completely collapse. There is less clarity as to how one might incorporate these findings into financial economics (SWM) and how society might encourage such behavior within our system.

> One of the most rigorous yet important theorems (work of Arrow and Debreu) in mathematical neo-classical economics is that ubiquitous perfectly competitive markets can satisfy economic desires efficiently and pareto optimally (Richardson 384).

That is, when consumers maximize utility and firms maximize profits in this environment any departure from the allocation of resources obtained as a result of market transactions would necessarily make someone worse off. So there we have it—the invisible hand. Commitment to SWM is

good for shareholders and society.

Troubling Realities: Concentration, Externalities, and Moral Agency

Unfortunately, real world conditions normally depart from the conditions for perfectly competitive markets in a number of very important regards and these, "together with unconstrained opportunism, can lead to market pathologies" (Noreen 361). For example, concentration of market power can lead to exchanges that are not mediated by the market, giving organizations and individuals in positions of power the opportunity to act against the interests of society—to make moral decisions. Our system has moved to constrain such abuses with anti-trust legislation, and I suspect that the emergence of the global economy mitigates this problem in open societies such as ours. For example, the auto industry has been transformed from a U.S. oligopoly to a highly competitive environment where firms failing to heed consumer preferences face the threat of extinction.

A second exception involves goods such as air, water, public and employee safety,[5] health hazards arising from product use (e.g., guns, tobacco, alcohol, pornography) etc., where property rights are difficult to define and transaction costs are high. Individual production or consumption of public goods tends to give rise to externalities, i.e., the micro exchange does not fully capture the costs or benefits to society. This tends to create inefficient allocation of resources. Society has responded by using taxation to fund government provision of public goods, by regulation of market behavior in these areas, and by artful extension of property rights to capture the efficiency of market mediated exchanges (e.g., air rights in New York City). The SWM model clearly fails to deal adequately with this exception.

Ethical Vacuum or Ethical Values?

Generally the firm's normative intersection with these goods has been left to Business Ethics. As Dobson notes, "An incongruity currently exists between a growing body of business ethics research, which promotes morally restrained behavior and extant Financial Contracting Models[6] (FCMs) that assume agents operate in an ethical vacuum." (*Reconciling* 24) Friedman

attempts to reconcile the two by arguing that "the social responsibility of business is to increase its profits[7] so long as it stays within the rules of the game (i.e., constrained by ethical custom), which is to say, engages in open and free competition without deception or fraud" (244). Weston and Brigham argue this constraint implies compliance rather than proactive initiatives:

> Certainly firms have an ethical responsibility to provide a safe working environment for their employees, to ensure that their production processes are not endangering the environment, to engage in fair hiring practices, and to produce products that are safe for consumers. However, socially responsible acts such as these have costs, and it is questionable whether businesses would incur these costs voluntarily. It is clear, however, that if some firms do act in a socially responsible manner while other firms do not, then the socially responsible firms will be at a disadvantage in attracting capital. To see why this is so, consider first those firms whose profits and rates of return are normal, that is close to the average for all firms and just sufficient to attract capital. If one company attempts to exercise social responsibility, its product prices must increase to cover the cost of those actions. If the other businesses in the industry do not follow suit, their costs and prices will remain constant. The socially responsible firm will not be able to compete, and it will be forced to abandon its efforts. Thus, any voluntary socially responsible acts that raise costs will be difficult, if not impossible, in industries that are subject to keen competition [efficient](17).

Hence, in the language of Novak, the moral cultural system would perceive a problem of justice/welfare in the community and pressure[8] the political system to intervene in the economic system by establishing new/revised rules governing the trade-off between public goods and economic efficiency. Thus the nature of the constraint to SWM is clarified, and moral behavior by the firm is seen to be compliance. Indeed, when firms failed to respond to calls for voluntary action in areas of social responsibility following WWII, society responded with regulation of air and water quality,

employee safety, and equal opportunity in the work place in accordance with this model. The moral cultural system impact on the judicial system forged radically new standards for product liability shifting the onus from buyer beware to provider beware. This approach has the advantages of negating the need for unilateral action by firms, it utilizes the political process to broker the necessary compromises and tradeoffs, and it places minimal moral requirements on the firm. However, the saga of John Mansville and the asbestos litigation which led to its bankruptcy, suggest that society does expect corporations to have a measure of moral agency.

Moral Agency

Mansville was held accountable even though it violated no existing laws or regulations because it knew asbestos could kill and it proceeded with business as usual. In the end, the cost to the firm of avoiding socially responsible behavior was higher than the cost of foregoing this business opportunity—and the cost to society was enormous. Hence, we see that legalistic compliance is inadequate. The understanding of Friedman's constraint must be expanded to embrace behavior in accordance with the broader standard of the ethical norms of society, even though this complicates the SWM model. However, unilateral, proactive acts with material costs are still proscribed as discussed above, because they are not economically efficient[9] and take the corporation beyond its societal mandate.

How does virtuous behavior by firms impact efficiency when they are acting in accordance with this process to deal with goods generating externalities? The process is extremely costly to society. The weight of enforcement and compliance bureaucracies, decision making inertia, and increased incentive for corruption take their due. Enthusiastic cooperation rather than grudging compliance by firms can reduce these costs once regulations are in place.

However, even greater gains are possible when industries[10] practice self-regulation. Individual firms could encourage this process by agitating for action within the industry and by readily disclosing information (including some which might be sensitive or embarrassing) which could lead to optimal decisions regarding these goods.

Enlightened self-interest[11] should dictate this strategy as costs of self-regulation are much lower to the firm as well as to society, and examples of such behavior are numerous.[12] However, too often outrage in the moral cultural system must spark the threat of government regulation before action takes place. For example, in the aftermath of the fiascos in the banking industry and other examples of fraudulent financial reporting in the 1970s and early 1980s, Congressman John Dingell, chairman of the House Subcommittee on Oversight and Investigations, began hearings on the accounting profession. These hearings motivated a consortium of five key organizations in the accounting profession to sponsor formation of the National Commission on Fraudulent Financial Reporting (Treadway Commission) which returned sweeping recommendations for change (Bulloch 61). The favorable response of the profession to these recommendations was clearly influenced by the threat of governmental interference. Jerry Sullivan, chairman, Auditing Standards Board, noted in a panel discussion:

> Congress has referred the Treadway Commission recommendations to Comptroller General Charles Gowsher of the General Accounting Office. He will be monitoring what is happening and will report back to John Dingell in the summer. If the results aren't satisfactory, in terms of implementing the recommendations, it's clearly going to heighten the concern of Congress. And Congress will focus on these concerns, in my judgment, if the private sector hasn't responded to the initiatives in the Treadway report by next fall (Hensey 51)

Perhaps we should not be surprised that government is required to act to promote justice and integrity. Through his grace God has ordained such to prevent chaos in this fallen world. "By me kings reign, and rulers decree justice, By me princes rule, and nobles, all who judge rightly" (Proverbs 8:15-16). The king gives stability to the land by justice, But a man who takes bribes overthrows it" (Proverbs 29:4)

The third exception to the perfectly competitive market "invisible hand" paradigm we shall consider is the condition that each participant must have perfect knowledge of all market

conditions and possibilities. This exception is of critical importance to finance, and it is the focal point of recent literature dealing with a paradigm shift.

Evidence from Recent Scholarship

I am indebted to Dobson for his excellent review of the literature dealing with the development of:

> an increasingly dominant role . . . .[for behavioral models of financial economics (FCMs)] . . . . in the evolution of the theory of the firm . . . . they stem from the contemporary conception of the firm as a nexus for a set of contractual relations among individuals. Thus the firm is no longer viewed as an atomistic unit but as a web of explicit and implicit contracts between stakeholder groups: namely bondholders, stockholders, management, employees, customers, suppliers, and society at large. . . .Unlike the 'classic' models of finance . . . FCMs recognize the pivotal role of market imperfections in driving equilibria. Conflicts of interest between stakeholders who are unable to costlessly enforce all contracts have led to a vast literature on agency theory, while a recognition of the uneven distribution of information among stakeholders has led similarly to an extensive literature on signaling theory (Reconciling 24).

He goes on to point out that the wealth maximization function "of the nonhuman firm . . . has simply been shifted to human agents" (24) in these models, and they "are invariably built on the premise that the only 'reasonable' motivation for agents is unbridled self-interest." This creates a moral dilemma, however, for "the models lead to second-best equilibria in which the cost of opportunistic behavior is borne by the agent.[13] The outcomes are second-best because there is a deadweight loss to the economy resulting from the agency problem. . . .FCMs generally indicate that if agents pursued a goal of trustworthiness, rather than narrowly defined self-interest, first-best outcomes would be possible. . . .Trust would act as a costless contractual enforcement mechanism; agency costs, in particular the residual loss, would not even be incurred. Thus FCMs indicate that honesty really is the best policy "(25).

In his work developing the ethical implications of agency

theory, Noreen uses Akerlof's "Market for 'Lemons'" to demonstrate "that in the presence of asymmetric information and unconstrained opportunism, adverse selection can lead to the collapse of markets and/or to costly investigation" (361). If a car model has a high incidence rate of lemons then initially the used car market would reflect an expected value based upon the overall rate of lemons. However, at this price owners with 'good' cars would be motivated to keep them (price is too low) while those with lemons would be motivated to dump them into the market fast (the market price would represent a windfall gain). The rapidly increasing percentage of lemons in the used car market would eventually drive all potential buyers out and the market would collapse. This outcome could be avoided if all sellers made full disclosure regarding the quality of their cars. Norene goes on to show a similar adverse selection problem can cause the collapse in the market for new stock issues if "opportunities and proclivities for consumption of perquisites [abuse of management's fiduciary responsibilities] differ across firms and these differences are difficult for an outsider to accurately estimate. . . .The central problem is how to enforce truthful reporting" (362), and this brings us back to the significance of the fraudulent reporting discussion above. Noreen's conclusions regarding virtue then are similar to Dobson's:

> It is evident that compliance with certain rules promotes efficiency; that is, the "economic pie" is larger when certain behavioral rules are followed. . . . .altruism economizes on the costs of policing and enforcing agreements. Agency theory suggests some of the rules that could be fruitfully adopted—truthfulness in commercial transactions being the most obvious one (363)

Bowie, in his frontal attack on the egoistic paradigm, reaches conclusions similar to Noreen's:

> Egoistic behavior, if universally practiced, is self defeating.[14] An egoistic world is unstable and participants in such a world do not maximize their interests (10). . . .The conscious pursuit of self-interest by all members of a society has the collective result of undermining the interests of all. As more people believe that others behave egoistically, they will

> respond in a similar fashion. Egoistic behavior must be constrained to keep it from exploding into the kind of destructive force Hobbes described. If individual self-interest is to be maximized, the citizens of society cannot publicly advocate egoism, they must act as if they were altruists. . . .This form of as-if altruism is not sufficient to contain the self-defeating chaos of egoism. Only genuine altruism [agape love?] can do that (12).

Dobson concludes similarly:

> In equilibrium agents do not benefit from opportunistic behavior; wealth maximization is not achieved, either for the individual or the aggregate through pursuing an objective of wealth maximization (*Reconciling* 32).

Perhaps natural law is at work here for the Scriptures affirm these conclusions. "He who walks in integrity walks securely, But he who perverts his ways will be found out" (Proverbs 10:9) "The integrity of the upright will guide them, But the falseness [duplicity] of the treacherous will destroy them" (Proverbs 11:3)

Lundholm uses signaling theory and a laboratory market to conclude that "diversity of informed traders' information and aggregate uncertainty[15] together lead to inefficient markets, but neither treatment by itself causes inefficiency" (487). Hence, the kind of level playing field relative to disclosure of information which seems to be inherently just also promotes market efficiency. Fishman and Hagerty reach similar conclusions in their analysis of insider trading. They show that:

> under certain circumstances, insider trading leads to less efficient stock prices. This is because insider trading has two adverse effects on the competitiveness of the market: it deters other traders from acquiring information and trading, and it skews the distribution of information held by traders towards one trader [asymmetrical information]" (106).

Anecdotal Evidence: Folklore on 'Ethical Practice is Good Business'

While browsing a shelf of books on business ethics I came across one by Armerding which was full of stories of Christian business persons engaged in moral struggle. One chapter with its supporting set of anecdotes was

entitled "Good Ethics Can Make You Rich." I was somewhat inclined to dismiss this anecdotal evidence, but then I came across Roger Smith claiming that "ethical practice is good business," and Gary Brytczuk urging those in the financial planning profession (CLUs) to "cast their bread upon the water" (Ecclesiastes 11:1) because:

> The rewards of doing what is right for the benefit of others is the finest way to build a business and [this approach] will return rewards far greater than you can imagine" (53).

He further elaborates that "successful relationship[s] with our clients . . . must be based on trust" (53). Bowie seems to agree:

> Persons who have personality traits that result in acts of hard core altruism have an advantage. Since they will be more trustworthy in situations where the purely self-interested person would not, these persons will be much sought after in positions that require trust. Note, however, that these persons must be genuine altruists. You wouldn't really trust a reciprocal altruist because they might defect in situations where there is no possibility of a reward (14).

Hence, these authors argue, success will frequently accrue to the individual or firm who puts others first and possesses the Christian virtues of integrity, justice and yes even love. However, the motivation must be the deontological well-spring of faith rather than the expectation of gain.

Integrity in the Commodities Market

Ritchie, an active trader, observes:

> In all fairness to the industry as a whole, it would be completely wrong to end a discussion of dishonesty without placing things in perspective. The average commodities broker does not deserve the negative reputation that results from the behavior of a few. The entire industry works on the honor system. Every trader who steps into the pit is bound only by his honor to live up to every trade he makes. Millions of dollars change hands daily by this method. Nothing is signed; there is not even a handshake. Sometimes there is not even a verbal exchange; merely the wave of a hand or the nod of a head. Any trader can cheat any other trader any time he

chooses and there is nothing that anyone can do to stop him. The amount of integrity required to carry on business is nothing short of phenomenal" (185).

Trust in the Diamond Market

Noreen explains the workings of the wholesale diamond market in New York City as follows:

> In some markets there are seldom formal contracts; there is instead a high degree of trust among the regular participants in the market. If a trader is discovered to have acted unethically, he is excluded from the market and loses his investment in human capital" (364).

The Scarlet Woman of Wall Street

Gordon recounts the saga of Daniel Drew and his cohorts, Fisk and Gould, and their manipulation and plunder of the investing public using the vehicle of the Erie Railroad (Scarlet Woman) during the 1860s to help us understand Wall Street at a time when:

> speculators were bound by no rules beyond the natural ones of the market. They pursued their self-interest by seeking short-term trading profits in the stocks of companies they controlled and without regard to the long-term consequences to the market, to the companies whose securities they manipulated, or to the economic system as a whole (xviii).

Drew, a zealous Methodist lay preacher, abused his insider position by manipulating Erie stock prices for personal gain, watering the stock with no disclosure (no one knew how many shares were outstanding and hence could not accurately value the stock), 'cooking the books,' preventing outside stockholders from voting their shares, issuing new stock to himself and friends without due process to avoid loss of control, betraying friends, breaking contracts, buying judges, attempting to control the political process, and perpetrating violence on competitors. "The Fox of Wall Street was [loose in] the Erie's henhouse" (110). Needless to say, the Erie's infrastructure deteriorated under the weight of this type of stewardship and its business fortunes faltered. As a morality play aside, Cornelius Vanderbilt's stewardship of the New York Central involved improvement of the physical plant and service and

fair treatment of outside stockholders. Drew died having lost the remnants of his fortune while Vanderbilt died the richest man in the world.

But the big story is that Wall Street pulled back from the abyss as the New York Stock Exchange moved to vigorous self-regulation to reign in the chaos, e.g., moving in 1869 to require registration of all listed securities, thus reducing the asymmetric information problem and creating a more level playing field. By 1883, "an investor could rely on the fact that, if a broker was a member of the Exchange, his sales pitch, however glib, was not fraudulent. If a security was listed he knew it represented real assets, however risky, not smoke" (380). Gordon sums up by observing:

> Throughout history free markets have tended to be ephemeral, for once they grew to any considerable size, individuals pursuing their self-interest sought to dominate, and thus destroy them. Indeed, the idea that free markets are a positive good in their own right—for the game is not a zero-sum one—dates only to . . . Adam Smith. That Wall Street (recognized the need for integrity and justice and) succeeded in establishing rules which maintained its free market was no small accomplishment . . . (xvii).

The importance of integrity and justice was further acknowledged in 1933 in the aftermath of the 'crash' when the Securities Exchange Act required registration of new security offerings with the SEC and full disclosure of all relevant information in a prospectus. The 1934 Act extended these disclosure standards to the secondary markets (10K etc.), and moved to control insider activities. In the wake of the 1987 stock market crash a government task force was commissioned to investigate the possibility that new developments such as programmed trading had impaired the integrity, orderliness, and efficiency of the financial markets and to make recommendations in this regard—thus underscoring society's understanding of the connectedness between market integrity and performance.

Lessons from Kenya

With the help of western aid, Kenya's market economy has done well since independence, growing at roughly double the U.S. rate and trouncing

neighboring Tanzania with its experiment in socialism even though both started the period with comparable situations (Barkan). However, during the past several years this performance has faltered, and it is likely that problems with market integrity are at least a partial cause. The centers of economic and political power in Kenya are one and the same with political figures frequently receiving exclusive franchises which are then protected by the political apparatus from aggressive competition. Coughlin argues that this encourages domestic investment and assists development in other ways. However, clearly this lack of competition and the absence of a level playing field erodes efficiency and distorts resource allocation. Significant sectors of the economy are also controlled directly by the government through parastatals, and, lacking bottom line discipline, they badly underperform the private sector. The parastatals are used as sources of political patronage and a source of capital in the form of interest free loans for the well connected. For example, in 1991 we observed coffee plantations lying untended in Kenya with maize growing between the plants, largely because of the low prices paid by the coffee parastatal which monopolizes the export trade. It has diverted substantial funds into the pockets of the powerful, and, being therefore short of cash, it acerbates the havoc caused by its pitiful payments to growers by delaying them for months and even years after shipment. Such abuses by the powerful have strained the social contract to the breaking point and eroded economic efficiency and growth.

Integrity and the Utility of Money

> Justice requires that the value of money be reliably known and stable, thus inflation rep resents poor stewardship and defrauds the nation's citizens. It wastes resources and is particularly harmful to the poor and the powerless" ("The Oxford Declaration" 15).

Ellul ascribes to money a sinister life force which will seduce and destroy man unless he accepts "God's judgment delivering [him] from possession by the [spiritual] power of money" (103), even though he recognizes its "excellence" in the secular sphere. Nevertheless, money is the facilitator of our modern economy and without it

modern society would collapse. It facilitates efficient exchanges and as a store of value it permits the decoupling of production and consumption events (a critical limitation of barter) and also permits the accumulation and flow of productive capital. One only has to recall the horrible implications of Germany's horrible post WWI hyperinflation to appreciate the critical importance of integrity in monetary stewardship. As Rose puts it:

> We can see that there is a moral requirement for the money creators—be they private or government—to maintain the integrity of the monetary unit. If they fail to do this, people will be cheated and duped out of their honestly gained wealth through a debauched currency. The prophet Isaiah spoke strongly against monetary debasement: "How the faithful city has become a harlot, She who was full of justice! Righteousness once lodged in her, But now murderers. Your silver has become dross, Your drink diluted with water (1:21-22) (197).

Likelihood of a Paradigm Shift

Dobson has a certain sense of urgency about the need for a shift. He observes:

> When [financial economics] adopts as its premise that the objective of the firm is to maximize shareholder wealth it implies that this is the right objective. It indoctrinates its audience with a certain moral philosophy. By assuming away other motivations and thus elevating [SWM] to the status of a necessary law of nature . . . theorists may be sanctioning behavior that society at large regards as immoral. In the corporate milieu, by assuming unbridled self-interest, financial economics promotes unbridled self-interest (*Reconciling* 30).

Hawley observes similarly, "SWM may actually encourage unethical and socially irresponsible behavior under some not-too-unlikely circumstances" (717). He also observes that corporate finance textbooks are almost completely silent on the subjects of agency theory, business ethics, and social responsibility, and he concludes that financial educators are abdicating their responsibility in this regard.

Speaking of the role of business school instructors Noreen warns "it would be a

mistake to wittingly or unwittingly inculcate in the next generation of accountants and managers the notion that it is foolish, naive or abnormal for businessmen to feel constrained in their actions by ethical considerations" (368). Finally Bowie warns "the more people believe that psychological egoism is true, the closer it comes to being true. . . .If people believe it's a jungle out there, the world will become a jungle" (9). Hence, the urgent need for a shift before our stock of Judeo-Christian moral capital underpinning our institutions erodes away completely. And defense is not enough. Bowie, reflecting on our international competitiveness says, "the destabilizing effects of egoism being what they are, a business system like Japan's will be competitively superior to ours in the long run. To put the point another way, self-sacrificing behavior is an important factor in competitive success" (18).

In spite of the high stakes, my perception is that the paradigm shift in finance is going to come slowly for the following reasons:

1. In economics, significant theorists like Arrow have put their weight behind the shift and are speeding it along.[16] This has not happened in finance, and until the modern portfolio theory experts weigh in, progress will be slow.
2. Most participants in finance lack an appreciation for the vital importance of the moral foundations of markets or take such foundations for granted as a given. Hence, there is no sense of urgency with regard to a paradigm shift. Perhaps Christians have an opportunity to make a major contribution as prophets in this area.
3. It is not readily apparent how ethical objective functions can be incorporated into the SWM model as other than simple constraints,[17] and the public goods nature of some of the returns (benefits) of virtuous behavior is an enormous complication. Dobson advocates incorporation of 'internal goods'[18], i.e., virtues. "It is what Adam Smith defines as 'perfectly virtuous'; the man who acts according to the rules of perfect prudence, of strict justice, and of proper benevolence, may be said to be perfectly virtuous." (VI,iii,1). He suggests that "as an objective, the internal good could be measured as internal utility. As with utility of

wealth, internal utility may comprise several factors, trustworthiness being prominent among them" (37). Measurement may remain a practical obstacle. Bowie advocates embrace of Robert Frank's commitment model, and certainly it has the potential to generate first-best outcomes like the incorporation of internal goods. However, again, development of practical mathematical expressions applicable to finance may require some time. Furthermore, as Christians we must question the practicality[19] (not desirability) of commitment models in a fallen world.[20]

Conclusion

We have demonstrated that normative considerations, and most especially the role of Christian virtues, are of crucial importance to the efficient functioning of the market in the context of finance. This supports the need for a shift away from the egoistic SWM paradigm to a more comprehensive model incorporating the normative virtues of integrity and justice. Altruistic behavior consistent with the commitment model seems to require 'love'[21] or at least a commitment based upon faith or some other deontological foundation rather than opportunism.[22] Thus, Christians have an opportunity to be socially redemptive in this area. Secondly, Christian educators have the opportunity, yea obligation, to sensitize students to the costs of egoistic behavior and to the gains of commitment. Such knowledge may promote at least a utilitarian-based commitment to others in line with Adam Smith's minimal criteria for the survival of society.

ENDNOTES

[1] See Psalm 15:2; 25:21 & Proverbs 2:1-9; 20:7

[2]The scope of this paper will be restricted to the context of corporate finance including the specialized areas of financial intermediaries and financial markets. Financial professionals working with individuals (personal finance) and in the treasury functions of government face similar issues but the nature of the fiduciary responsibilities are somewhat different. Note also the close kinship of this discipline to accounting which is the language of finance and to economics with its insight into the economic environment for financial analysis and decision making in areas such as the cost of capital, climate for growth, and availability of capital.

[3]Richardson cites movement towards more value oriented, normative paradigms in economics. "[There] is an important presupposition that economists themselves sometimes forget. Markets require ethical . . . foundations to work. . . .Markets don't spring up haphazardly like mutant wildflowers. They are cultivated plants. . . .Modern economics consequently builds on ethics. . . .Ethics and law argue that deceit is wrong and make fraud a criminal offense, allowing markets to work

better. . . .New wines to gladden a believing economist's heart . . . .[are] economics with a bouquet of trust, deceit, reputation, integrity, shirking, conflict resolution, and changing preferences. . . .[it] depends on virtue, vice, character, and relationship (386-389)."

[4]See Meeks for a profound development of this concept in the economic context.

[5]Arising from asymmetric information and a social welfare approach to health care.

[6]Extension of SWM model.

[7]hence responding to consumer preferences and utilizing resources efficiently.

[8]See, e.g., Economic Justice for All, the Catholic Bishops pastoral letter which created such a furor for a time.

[9]Some would contend that the emergence of green marketing, the proliferation of social screens, and the growth of funds under socially responsive management ($700 billion in 1993 [Meeker-Lowry 49]) have led to a positive economic return for socially responsible initiatives by corporations. Poitras, while recognizing a probable negative correlation between stock prices and intentional illegal corporate activity, cites enormous difficulties in empirically testing any positive correlation between stock prices and other types of socially responsible behavior. He concludes that the evidence to date is inconclusive and fails to support a hypothesis of positive correlation. Many are careless about the identity of dependent and independent variables. For example, Kurschner concludes that research showing the "investors in those firms that did more for their workers realized an annual shareholder rate of return that was about 45 percent higher than those firms that did the least for workers" demonstrates that "good work practices enhance financial performance" (21). One could as easily argue the reverse—that affluent firms can afford to do more for their employees. For the present, then, one must conclude that markets do not reward individuals or firms for their contributions to the public good, creating the need for genuine altruism, a binding social contract or imposition by society. We Christians would say that the greatest of these is love.

[10]The industry context avoids problems associated with unilateral action.

[11]i.e., a more altruistic form of self-interest consistent with the treatments of Adam Smith and Rawls where actions are governed by a utilitarian commitment to the welfare of society. This would be consistent with the biblical injunction that "whatever a man sows, this will he also reap" (Galatians 6:7-10), and to the allusion of being in the 'life boat' together. The strong social contract in Japan seems to be based upon this enlightened self interest rather than upon beneficence.

[12]See, e.g., network T.V. and New York Stock Exchange. See Morley for an example of the self regulation of investment professionals and the role which the 'Code of Ethics and Standards of Professional Conduct' plays in this context. See Brytczuk for an example of the role of certification (Financial Planners) in self-regulation.

[13]e.g., in the adverse-selection type of agency problem asymmetry of information can keep the principal (e.g., investor) from discerning whether the agent is inherently lazy or industrious, honorable or a crook, and this can create a pooling equilibrium which will penalize the 'good' agent and lead to non-optimal decisions for principals and society. If signaling (dividends, capital structur , equity issue underpricing, etc.) is employed to enable a separating equilibrium the cost of signaling is borne by the agent. Note also that in the moral hazard type of agency problem "the desire to build or maintain reputation may costlessly dissuade the agent from acting opportunistically. . . .[However,] equilibria based on reputation are quite fragile" (32).

[14]e.g., he argues "if we could not assume that people were committed to telling the truth, liars could not gain the advantage of lying. For liars to succeed, they must free-ride off truth-telling" (2).

[15]i.e., asymmetric information among market participants and a situation where the information available to all participants would, even if pooled, be inadequate, to make the optimal decisions with certainty.

[16]Although most of the work is being carried out at the esoteric, methodological level rather than at the application level at this point.

[17]See Dobson (Role of Ethics 60) for a more extended discussion of the difficulty, and Charalambakis (16) for a description of the new Genuine Progress Indicator (GPI) which seeks to incorporate a wide range of

normative social and environmental factors as a corrective to the GDP at the macro level.

[18]As opposed to external goods which involve property.

[19]The extended family in Kenya illustrates that even altruistic models such as Frank's commitment model can exhibit pathologies in a fallen world. The benefits of family love and support can be offset by the sacrifice of freedom—e.g., the coerced redistribution of income and the greedy, opportunistic behavior and bondage which can result from the bride price.

[20]See Halteman for an excellent development of economic systems in the `two kingdoms.'

[21]See Frank, chap. 10.

[22]Noreen , e.g., discusses religion as an enforcement mechanism (364).

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