

# **A SOCIO-ECONOMIC STABILIZATION PLAN FOR PORTUGAL**

**Based on Conditions of Stable Equilibrium**

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## **I. Diagnosis.**

From the socio-economic point of view, Portugal is suffering the ill effects of the following five disturbing factors:

1. A first layer of inflation due to the overissue of paper money and pure bankdeposits through the Central Bank of Portugal, either to cover government deficits or to be used by private banks for speculative purposes in business and finance.
2. A second layer of inflation injected through the private banking system (domestic and foreign) and in form of monetized bankcredit, or pure bankdeposits, issued partly to finance real (productive) investments but for the rest, a larger portion, representing relatively cheap financial means used for purely speculative purposes in business and finance including market strategy for acquiring monopoly positions with extra profits.
3. In the rural areas the Portuguese economy struggles with an invisible deflationary pressure created by the fact that much of the inflated supply of money is concentrated in urban areas where pure speculations in commodities, services and securities are more suitable and more profitable. Thus the Portuguese agriculture, being deprived of sufficient real-capital formation, is forced to remain undeveloped with hidden unemployment of both human and natural resources.
4. A vast and partially unproductive bureaucratic apparatus in government initiated and perpetuated by the old regime is harmful to the Portuguese economy. First, it must be clear that the subject matter here is not the normal, necessary administrative apparatus for regular government business but rather that extra, super-imposed level of bureaucracy associated with controls and regulations which have no justification in a system of stable equilibrium as recommended in this plan. The second layer of superimposed bureaucracy is chewing off a significant portion of the real national income. The same unproductive bureaucracy, through its web of unnecessary controls and regulations, impedes the normal growth of the national economy, i.e., that growth consistent with an optimum level of gross national product and full employment.

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5. Finally, Portugal, like other capitalist countries, is faced with a social problem visible in the significant number of a sort of second class citizens who, partly from their own fault (those lacking any ambition to better their lives) but mostly due to the inherited social conditions and faulty functioning of the present system, cannot fully participate in the economic development of the country. The forces of inflations fostered through the causes mentioned above are automatically eroding the already meager real income of those who are at the bottom of the social scale. Consequently, proverty is perpetuated and a second-class citizenship is created, which inevitably leads to social and political unrest.

## **II. Five Reforms To Be Undertaken.**

Assuming that the above diagnosis is correct, to restore, a free, just, stable and workable economy compatible with a free, democratic form of government, there is need for five basic reforms to be conducted in a systematic way so that no other difficulties may arise.

1. A reform of the monetary system and the Central Bank of Portugal so that the forces of inflation may be cut off at their source;
2. A reform of the private banking system (domestic and foreign banks) so that monetization of bankcredit, as a source of inflation, may also be cut off at its origin.
3. A reform of the financial system so that agriculture, like industry and trade, may also benefit from suitable conditions for real capital formation and accumulation.
4. A reform of the administrative apparatus in the Portuguese Government so that the portion of unnecessary and unproductive bureaucracy be uprooted and after a fair indemnization and due process of law be given a chance to be channeled into the productive sectors of the economy.
5. A social reform of reasonable proportions and without becoming a burden for a normal functioning of the national economy has to be added to the other reforms.

A discussion could be opened about the method to be followed in conducting these five reforms, specifically whether they should be introduced gradually or simultaneously. This plan was conceived with the basic thought that the five reforms in question are so intimately interrelated that it is imperative to have them implemented at the same time. Otherwise other problems may be created as a result of inconsistencies among the different sectors and institutions of the economy, and this, in the end, may foreclose any chance of success.

In conjunction with the five reforms just mentioned, it seems that five concrete steps should be taken simultaneously:

- (1) The Central Bank of Portugal by special law should be declared an independent institution entrusted to conduct the monetary and bankingreform proposed in this plan and should be responsible to a duly elected Parliament. For such time when a Parliament does not exist, the Central Bank should be responsible to the Council of State.

(2) The introduction of a new, heavier Escudo in order to drain off the existing inflation to its bottom.

(3) The establishment of a stable framework for the monetary, banking, financial and economic system, according to conditions of stable equilibrium, so that the inflation may not return in the future.

(4) Once a stable framework has been established, it is the duty of the Government to dismantle that part of the bureaucratic apparatus which is associated with controls and regulations no longer needed.

(5) When old money is exchanged for new money a reasonable social reform can be attached in order to compensate those unfortunate at least partially for social inequities inherited from the past.

### **III. Recommendations.**

All the measures, reforms and policies included in this plan were conceived and have to be judged in conjunction with the realization and maintenance of conditions of stable equilibrium whereby among other things four major goals are to be achieved at the same time:

(1) Price stability, i.e. neither inflation nor deflation; (2) full employment for all Portuguese people capable of and willing to work; (3) maximum social justice in the distribution of national income, and (4) a Balance of Payments in equilibrium, i.e. neither cumulative deficits nor cumulative surpluses.

#### *Part One: The Monetary Reform to Drain Off the Existing Inflation.*

1. The introduction of a new heavier Escudo to clean instantaneously, on a given D-day, the existing inflation to its bottom. There is no other known method to deal more successfully with this issue.
2. How heavy should the new Escudo be in order to eradicate completely the existing inflation? The answer depends upon three factors:
  - (a) The total supply of money in circulation on D-day, composed of banknotes and bankdeposits of the Bank of Portugal outstanding and the aggregate amount of bankdeposits in the private banking system (domestic and foreign) which are not covered in official money but in earning assets (loans and investments);
  - (b) The total amount of gold and convertible-in-gold foreign exchange; and
  - (c) The par value of the new Escudo, which could be equal to 0.0288887 gram of fine gold, as after the change on February 12, 1973 when the U.S. dollar was devalued.
3. By combining 2 (b) and 2 (c) we can calculate the amount of the supply of money expressed in new Escudos which are «Numeraire»- currency (Walras), or 100%-covered real money.
4. By dividing 2 (a) by 3, we arrive at the ratio of the old, inflated Escudos and the new, heavier Escudos. Let us assume that ratio as being 10:1, even though the real figures may be different.

5. Other measures to be taken simultaneously:
- (a) In order to avoid other possible calamities on the same D-day, all current prices, incomes, debts and any other sort of claim including taxes should be reduced in the same proportion of 10:1;
  - (b) If there are any prices or incomes fixed or controlled by the Government, during the week prior to this reform such prices and incomes should be recalculated to correspond to their equilibrium level (as defined in this plan later). On D-day these prices and incomes also will be reduced in the same proportion of 10:1;
  - (c) Foreign claims shall be treated in the same way as domestic claims, i.e. reduced at the same time by 10:1; and
  - (d) Foreign exchange rates shall be adjusted in the same proportion; during the week before this reform is put into practice, all foreign exchange should be allowed to fluctuate freely, with one restraint: pure speculations in the foreign exchange market (nominal transactions speculating on future fluctuations) shall be prohibited as conducive to more disequilibrium.

In one statement, the purpose of the introduction of a new, heavier Escudo is to clean the financial house thoroughly on a given day but accomplished so equitably that nobody will lose or gain anything.

*Part Two: A Monetary, Banking and Financial Reform Consistent With and Conducive to Price Stability and Full Employment.*

In order to restore economic and financial stability both at home and in international markets, Portugal needs a most stable and workable framework of the monetary, banking, financial and economic system so that no inflation or deflation, mass unemployment or other disequilibrium calamities may recur in the future. The new system, for convenience here called «Social Liberalism» to distinguish it from both capitalism and socialism, is constructed in accordance with conditions of stable equilibrium. In the final analysis the new system incorporates a number of self-regulating mechanisms which initially are put in motion by the Government's new reforms.

Immediately thereafter, however, they start to work moved by selfpropelling forces of organized markets. The self-regulating mechanisms are least expensive and in their functioning they can resolve in the best and most economical way our four basic problems: price stability, full employment, maximum social justice in the distribution of the national income and a balance of payments in equilibrium.

### **1. An Independent Central Bank.**

First of all it is necessary that the Central Bank of Portugal receives by law an independent status in the sense that it becomes the public institution entrusted to conduct impartially and skillfully the monetary and banking reform proposed in this

plan, and to be responsible only to a duly elected Parliament, or the Council of State until such a Parliament may come into existence. In practice an independent Central Bank means that the issue of official money is separated from the public budget and/or the financial position of the private bank system. And this is one of the requirements for stable equilibrium of the economy and its finance.

## **2. The Natural Parameter of «Numeraire» Has No Substitute.**

The cardinal condition for the realization and maintenance of equilibrium prices (as demonstrated by Leon Walras) requires first a natural parameter in the form of a 100 per cent «Numeraire» currency for which there is no substitute, plus a system of really free markets where monopoly forces are reduced to zero at the limit. The term «numeraire» means simply commodity-money, that is something with a common denominator between money and all other commodities; a quality needed for any reliable and objective monetary standard used to measure exchange values and claims of any sort.

On D-day old inflated Escudos will be replaced by new, 100%-covered Escudos, and thus the Portuguese monetary system will satisfy the requirement of a natural parameter in form of numeraire. A further question arises on how to make the other sectors of the economy and finances consistent with and workable within the new stable framework based on numeraire and a chain of restructured free markets conducive to equilibrium prices?

## **3. Free Convertibility of the Escudo at Home and Abroad.**

The day after the new reform the Central Bank of Portugal shall declare the new Escudo to be freely convertible in gold (if this is the selected standard) both at home and in international markets. No problems can be expected since on that day all Escudos are covered 100%.

## **4. Any New Issue of Official Money Identified as Numeraire.**

Any new issue of official Escudos after D-day shall be 100% covered in gold and thus no problems can be anticipated with the preservation of free convertibility of the new Escudo.

## **5. The Natural Law of the Equilibrium Supply of Numeraire.**

The supply of new Escudos in circulation will be determined by the real needs of the economy as a whole. Whenever the people will feel that there is relatively too much money in circulation, they have the option to invest new capital exclusively in the production of other commodities and services, leaving the supply of numeraire unchanged. They could even reduce the supply of numeraire, if they find that it is in

their own interest to import more foreign goods and pay for them in numeraire. In both cases the supply of commodities and services is increased, and thus an inflation with too much numeraire in the new system is impossible by definition.

On the other hand, if at another time the people are satisfied with the current supply of goods and services and they feel somehow that the supply of numeraire is not sufficient, then they have the option to invest new capital in the production of gold (the selected standard commodity) or to produce more for export, and import gold. In both cases the supply of numeraire will increase automatically, and thus a deflation with conditions of too little numeraire is again impossible by definition. This may be called the natural law of the equilibrium supply of numeraire consistent with a normally workable system of free markets.

## **6. The Natural Law of Full Employment.**

Since the production of the commodity selected to serve as numeraire implies the mobilization of an equal amount of the factors of production (human and natural resources) exactly as during the process of producing any other goods or services, real income and employment in the economy, in the aggregate, can never shrink but rather will either increase or remain at the same level. We can see here that the natural parameter of numeraire embedded into a system of free markets and an adequate financial structure (as shown below) can create natural conditions for full employment in the short-and the long-run without any government intervention or special monetary or fiscal policies designed for this purpose. This may be called the natural law of full employment that Lord Keynes was looking for but could not be realized because of the lack of the natural parameter of numeraire.

## **7. Answer to the Critics that the Supply of Gold is Insufficient.**

Many contemporary economists fear that should a country select a pure gold standard and other countries follow suit, then in the long run such countries will be squarely faced with the necessity to slow down economic growth and consequently suffer the ill effects of chronic depressions. The cause for this calamity is presumed to be the possibility that the production of new gold might not keep up with the need for more liquidity both at home and in international markets.

There are many reasons which can be offered to contradict such a fear. First, the natural law of the equilibrium supply of numeraire (mentioned under 5.) does not allow the development of a deflation or depression. Second, as far as international transactions are concerned, under conditions of equilibrium with numeraire, a larger volume of trade and capital movements can take place without a need for more liquidity, since under such conditions the value of commodities and capital moving in and out of a country tend to be equal.

Thus numeraire, even under a larger volume of transactions, does not need to move from one country to another unless a position of disequilibrium develops. In internal

transactions a larger volume of trade, up to a certain point, can also be accommodated without a need for more liquidity by a natural increase in the velocity of circulation of numeraire, according to the Fisher equation of exchange.

Third, as long as an equilibrium price for gold is maintained, there is a good chance that in case of a relatively small production of new gold, monetization of previously accumulated gold (natural hoarding in form of bars and other articles) will take place. In this respect natural «hoarding» and «dishoarding» under equilibrium conditions with numeraire not only do not create but on the contrary help to resolve problems.

## **8. The Mechanism to Monetize Other Regional Commodities in Form of «Commercial Commodity Escudos».**

In order to dissipate completely the fear that eventually there may not be enough gold to support a normal, balanced economic development and also to give in fact even more flexibility to the new system of numeraire, this plan recommends that the Central Bank of Portugal initiate a study of how to give to the Portuguese people as soon as possible the right to monetize or de-monetize a certain durable commodity representative for a given district. For this purpose, the whole country must be divided into four or five monetary districts.

The Central Bank of Portugal shall organize the necessary facilities so that upon delivery at certain public warehouses in each district of a standardized commodity an equal value (minus a small discount) in banknotes be issued. A small discount shall be charged in such transactions to defray warehousing and administrative costs. The special issue of banknotes covered in regional commodities is called here «Commercial Commodity Escudos». Commercial Escudos shall be declared freely convertible in their respective commodity.

This novel institution will be of great help to the Portuguese people in rural areas. Whenever the prices of their products seem to be depressed, the people have a chance to monetize a part or the whole production of the special commodity in the district. In addition to increasing the supply of money, the issue of new commercial Escudos represents real capital formation for the district. On the other hand, when the prices seem to be rising, the people are free to convert banknotes denominated in commercial Escudos into the respective commodity.

In addition to producing more real income and employment through any new issue of commercial Escudos, the privilege to monetize and demonetize a regional commodity may exert a favorable impact on stabilization of prices and incomes in the respective district. This will resolve the problem mentioned under *Diagnosis* (point I. 3), namely, that the rural areas will now have their own source of capital formation and will participate with their own decisions on how the supply of money in circulation should change to correspond to the real needs of the economy. In this way the rural sector of the Portuguese economy will no longer be under deflationary pressure, as in the past, resulting from city concentration of banking and finance.

There will be an additional problem for the Central Bank of Portugal, namely, to skillfully manage the discount rate at the public warehouses so that the commercial Escudo is at par or close to the official numéraire-Escudo. This task is not difficult so long as the convertibility of the two forms of money (both 100%-covered) is preserved, each one restricted to its own backing in order to avoid the Gresham law.

All in all, free monetization and demonetization of regional commodities will encourage and support a balanced economic development throughout the country. And this is the best method, and at no cost to the government, to fight hidden unemployment and poverty in rural areas.

### **9. A Banking Reform Consistent with Price Stability.**

(1) Modern banks are useful and productive to the extent that they provide services to the public by being intermediary financial institutions between those who are prudent and save (a natural source of capital formation) and others who ingeniously put available capital to work in productive investments. Unfortunately, modern banks go beyond this intermediary function and monetize credit in form of pure bankdeposits without any direct guidance or restraint with reference to the volume of real income in the economy. The result is that monetization of bankcredit leads inevitably to inflation.

The natural parameter of numeraire as a cornerstone of a stable financial system requires, however, a neutral structure of banking which does not create money. This means that private banks (domestic and foreign) to be in equilibrium should conduct their business within the strict limits of the existing supply of money provided by the Central Bank, which in turn must be consistent with the level of real income in the economy. The goal of price stability requires, therefore, that monetization of bankcredit in form of pure bankdeposits or any other form must be prohibited by law, as otherwise the problem of inflation becomes insoluble. This, by the way, is not something new or unforeseeable. During the 19th century private banks everywhere were prohibited to monetize bankcredit in form of banknotes for the same reason of being inflationary. In fact, the old problem of banknotes issued previously by private banks, in competition and to realize an extra profit, is in principle the same as today's issue of bankdeposits by the same banks and for the same purpose. On this problem, the Government of Portugal and other Western countries are very late in correcting an old evil in a new guise.

(2) How should the private banking in Portugal be restructured in order to become neutral and consistent with the major goal of price stability;

*First*, a new banking law should clearly state that monetization of credit in form of bankdeposits or any other form by private banks (domestic and foreign) and all credit and financial institutions is illegal under heavy penalties, because it is inflationary and creates social problems.

*Second*, the transactions in the money markets, where the funds must be kept immediately available, should be separated from the transactions in the capital markets,

where the funds are committed for a longer period of time. This is the rule of separation between money markets and capital markets derived from the law of general equilibrium which requires a separate equilibrium rate of interest for each of the two markets. If the capital markets, f. i., are not separated from the money market, then in practice it is impossible to have that set of equilibrium rates of capital interest which mediate an equality between new investments and voluntary savings. The same is true for the money market in the sense that if it is not separated from the capital markets, then in practice it is impossible to reach that rate of money interest which is consistent with an equilibrium level of liquidity determined by that part of real income which people have decided to spend for current consumption of finished goods and services.

*Third*, as a result of the rule of separation mentioned in the previous paragraph, the banking business of every unit (domestic or foreign) must be divided into two independent sections:

*Department A* will encompass all transactions dealing in liquid funds which usually appear in form of Demand Deposits or Deposit Trust Accounts, subject to the privilege of being used without notice by drawing a check or drafting a payment order in any form. Since liquid funds tied in such accounts have to be immediately available on call, banks should be required by law to keep these accounts 100%-covered in official money at all times. It is understood that banks offer service in this matter, and therefore they should be free to charge a fee sufficient to cover the cost of opening and maintaining such accounts.

On the other hand, no one would pay a fee for having this sort of account unless there is a need and intention to use those funds by drawing a check or other payment order. Consequently, the aggregate amount of checks or other credit instruments issued under the above arrangement will be equal or close to the volume of liquid funds entrusted to the banks. Thus the supply of money in circulation will not change significantly, and this is consistent with neutral or non-inflationary banking activity. Often there is some apprehension among economists when the system of 100 per cent reserves is mentioned on the ground that those funds blocked were idle. This is not true at all. The liquid funds of the public put into the banking system as demand deposits and covered 100 per cent do not represent idle funds as long as the public can dispose of them freely. On the contrary, the function of such reserves is active since they assure stability of the banking system and an equilibrium level of liquidity in the economy as long as monetization of bank credit is made impossible.

*Department B* Dealing in savings (funds committed for different periods of time) shall be free to look for the best possible form of investment and lending of available capital derived from collected savings or their own funds. The new banking law must specifically indicate that a bank may not grant a loan or engage in an investment transaction unless the bank possesses the whole amount of the capital involved. As far as the use of checks or other credit instruments are concerned, only Department A can deal in such matters.

The earnings of the private banks will come from the service charges related to

any Demand Deposit or Trust Deposit accounts and the differential between the rate of interest charged to loan-customers or acquired from investments and the rate of interest paid to savings and time deposits. The banks may not gain as much profit as today, but they will be able to earn a supporting income according to the services provided to the public just like any other business and, most importantly, without creating inflation and social problems in the economy. With the issue of commercial Escudos the banks may extend their business into rural areas and thus capture a new source of income without creating problems for the rest of the community.

(3) Private banks (domestic and foreign) should not be allowed to join other kinds of businesses in order to create holding companies and thus avoid the provisions of the new banking law. The already existing bank holding companies shall be included in the new law.

The purpose of such a measure is to eliminate the old evil of modern banks financing mergers or market strategy, both leading to undue concentration of economic and financial power including monopoly prices and profits.

(4) Private banks (domestic and foreign) shall be free to participate in any new issue of securities but only so far as they possess the necessary capital from their own resources or from adequate savings, in which case the time element of the commitment is to be decided by the savers' consent. The banks, however, should not be allowed to finance pure speculations in securities and commodities. This refers to those nominal transactions where the seller does not have the respective security or commodity; he makes a pure speculation in the form of what is called a «short-sale». The buyer may also enter into a pure speculation when he has no interest in the respective security or commodity; he buys for the sole purpose of liquidating the transaction in the future with the hope of making a profit. Such pure speculations, depending whether the bullish or the bearish group of speculators is stronger, may easily distort a free market and thus induce or intensify disequilibrium prices.

For these reasons pure speculations should be prohibited by law. On so-called «organized markets» or «bourses» only real transactions shall be conducted in the new system.

(5) The organization of credit for private and public purposes can be developed efficiently with the help of banks and other credit institutions but without its monetization since that is inflationary. This means that the volume of credit used over a period of time must be restricted within the limits of the existing real income in the economy over the same period. In other words, credit granted by individuals or institutions in the new system of stable equilibrium at any time has to be backed by an equal amount of real income. This is real and non-inflationary credit.

## **10. A Reform of Public Budget and Finances Consistent with Stability.**

(1) In the new monetary and financial law a provision shall be included whereby it should be indicated explicitly that the administration of the public budget and finances is separated from the issue of official money in form of numeraire.

(2) A reminder to any present or future Minister of Finance shall be added in the same law-namely, that monetization of credit to cover deficits in the budget or any other public expenditure is illegal and therefore prohibited as being harmful to the national economy because such a practice would produce inflation and other social inequities.

(3) The basic financial rule to conduct government business shall be: First income (from its own resources or from borrowing) and then spending. This rule is derived from the concept of general equilibrium and in application will unify the whole body of finance, private and public.

(4) As long as the new financial system based on numeraire is safe from inflationary or deflationary pressures, it will not be difficult for the Portuguese Government to follow strictly a fiscal policy of balanced budget. In addition, the Government may borrow as much as needed, but in this case government borrowing will not change the supply of money in circulation since monetization of public credit is not allowed.

(5) With a new stable framework of the financial system, it is recommended further that the public budget be programmed and voted upon every five or six years. Government activity can then be planned and conducted in a more rational, effective way, thus increasing efficiency or the social productivity of the taxpayers' money.

(6) The present progressive system of income taxation has not achieved its original goal of reducing the number of rich people and has failed to create conditions for a more equitable distribution of national income. For this reason, it is proposed here that the Portuguese Government initiate an immediate study for the introduction of a unique tax on the annual gross national product, f.i. 15% and no income or other taxes at all for those who have an income below a certain minimum considered legitimate for the Portuguese standard of living. The unique tax shall be paid concurrently with wages and the other sources of private income so that the Government may keep pace in its finances with the rest of the economy.

A unique tax on expenditure, in application, will again help to unify the whole body of private and public finance. In addition, it will simplify the fiscal apparatus. The quest for more equity in paying taxes can be compensated by other means, f.i. by reducing taxes on property or even eliminating it altogether for those who have an income below the minimum level as mentioned above, and by keeping temporarily higher taxes on property for the more affluent.

Also a social reform is attached to this plan which would create more social equity in the distribution of national income.

(7) Once the new system of stable equilibrium conditions has been introduced, the Portuguese Government should proceed with an operation of weeding out of the administrative apparatus any superfluous bureaucracy associated with the many controls and regulations of foreign trade, capital movements and other sections of the domestic economy.

In order to avoid human hardships and possible social unrest, it is recommended that the Government pay all employees laid-off during this cleaning operation at least 6 months' salary without requiring them to perform any counter service. They should

be free to seek new positions, and the Government must help in every way possible to insure their successful resettlement in the private sector of the economy.

### **11. The Mechanism of the Balance of Payments in the New System.**

(1) Under a 100 per cent Numeraire- Currency System and with a stable structure in banking and finances (private and public), Portugal will have no problem with the balance of international payments.

The familiar mechanism of the gold (numeraire) points will secure a balance of payments in equilibrium and stable foreign exchange rates, leaving the possibility of only simple, temporary fluctuations of natural adjustments.

(2) Since no internal inflation or deflation is possible in the new system, the additional mechanism of the price-specie relationship together with the interest rates mechanism will provide conditions for a fast and, in most cases, mild adjustment process so that the internal value of the escudo will be equal or close to its external value. This is the visible sign that the balance of payments of a given country is in genuine equilibrium.

(3) Suppose that the whole free world remains under a regime of paper-money and monetized bankcredit, i.e. under a system of «anti-numeraire»! Would this mean that Portugal cannot proceed with this plan for monetary, financial and economic stabilization?

The answer is, definitely Not! A regime of stable equilibrium conditions in Portugal will not, and cannot, be disturbed by an outside financial system in disequilibrium. Portugal with the new system will enjoy the fruits of price stability and full employment, whereas the rest of the world will be drifting from open to hidden inflation or deflation and all other known economic and social disturbances.

(4) Would the new system bring Portugal in conflict with the International Monetary Fund? The answer is again emphatically, No! Portugal's membership in the I.M.F. will not be weakened but on the contrary strengthened by delivering the proof that stability of a national currency at home and in international markets can be achieved and maintained through a reasonable experiment by adopting a 100 percent numeraire-currency together with other reforms oriented toward conditions of stable equilibrium.

Finally, Portugal, after all her other political troubles, may give the free world a living example of financial and economic stability so that other countries may follow her experiment, and so prompt the International Monetary Fund itself to reorganization in the same direction of establishing conditions of stable equilibrium at the national and international levels.

### **Part Three: The Attachment of a Reasonable Social Reform and the Introduction of A Code of Ethics in Business (Law of OMENIA).**

#### *1. The Problem of Social Inequities inherited from the Past.*

Portugal, like other capitalist countries, has inherited from the past social ine-

quities which have been perpetuated from one generation to another. Similar conditions in the present continue to add new inequities or to increase those inherited. Here reference is made only to those social inequities which are associated with a reduction in the real income of a significantly large number of people who happen to have already a low level of income. That is how social problems are created!

The economic, social and political conditions or vehicles by which social inequities are initiated are known: Inflation with cheap paper-money and monetized bankcredit reduces the real income of the many; so does monopoly of land or other factors of production including business, overtaxation (direct or indirect) and arbitrary manipulation of prices, wages and other incomes by the government or powerful trade unions. The ultimate solution to the problem of social inequities can be divided in two parts: First, to compensate the poor in a reasonable and peaceful way for some of the inherited social inequities which now constitute a heavy burden for the present generation; second, to take all the necessary measures so that the main causes, just mentioned, which produce social inequities be eradicated with no chance of repetition in the future.

## **2. A Reasonable Social Reform for Past Inequities.**

As far as the past is concerned, there is no way to correct completely all social injustices for the obvious reason that it is impossible to calculate economically such inequities for each individual involved. What can be done, and if successful may become a social landmark of human progress in modern times, refers to a social reform of reasonable proportions, which can be attached to the operation of exchange of old, inflated escudos for new, stable escudos.

How can such a social reform be conducted peacefully without creating other disturbances in the economy? It is the task of the Portuguese Government to explain to the people first that a social reform of this type is necessary, and that it is better for the future of the entire nation to take an additional sacrifice now by those who can afford it in order to have social peace tomorrow. This is the best way and the best social investment to exterminate the seeds of social unrest and political agitation for revolution.

Once the Government has made the cause of a limited social reform plausible, then on D-day when old money is exchanged for new money, a certain portion, f.i. a graduated scale of 5 to 20 per cent of any sum in excess of a certain minimum level of cash and savings (obviously not associated with social inequities), shall be temporarily blocked in a «Special Fund for Social Peace and Reform». Meanwhile, during the process of exchange of old money, statistical information should be collected to show, on an individual basis, the exact number of those people who are really poor and possess rather small cash balances and little savings, if at all. Knowing the exact amount of money accumulated in the Fund for Social Peace and Reform and also the exact number of poor people, it is possible to calculate how much financial help could be granted to these diasadvantaged citizens.

To reinforce the constructive character of this social reform, a requirement may

be attached whereby the recipients of such financial aid may use it only for productive purposes, that is, for buying a home or establishing any sort of lucrative business or sending children to professional schools or institutions of higher learning. After this reform, no welfare payments should be given to persons capable of work.

This social reform will require a sacrifice on the part of the more affluent who are able to afford it, but this sacrifice is socially most beneficial and economically very productive, since the money in the Social Peace and Reform Fund will be converted into real capital and used immediately in the economy to increase productivity.

In the final analysis, therefore, this social reform will strengthen the moral fiber of the Portuguese society and the foundation of the Portuguese economy.

### **3. A Code of Ethics in Business (the Law of OMENIA) as a Support of Social and Economic Justice in the Future.**

As far as the future is concerned, and to be sure that the kind of social inequities known in the past and present will not recur, this plan is recommending the introduction of a constitutional law in the form of a permanent «Code of Ethics in Business», here also called the «Law of Omenia». The term «omenia» is an intranslatable expression from the Romanian language, and it means in principle to be humane to the highest degree in all relationships of life and in business, to be fair at all times and under any circumstances so that no social problems are created for one's fellowmen.

The Law of Omenia or the Code of Ethics in Business shall require that all business transactions of any nature and regardless of the amount or size of the firm involved be concluded at equilibrium or faire prices. Equilibrium prices in turn shall be calculated in good faith respecting the spirit of the law to make up for the cost of production or reproduction to which a normal rate of profit (representing the opportunity cost for managerial services) was added. More specifically, equilibrium prices shall be calculated in such a way as to include only the real payments made (or imputed) for the factors of production (labor, land and buildings, capital, management) and government taxation.

The Law of Omenia in business does not mean in any way an arbitrary government interference reminiscent of unnecessary controls and regulations of the past. In the new system of stability business will be free to develop according to the needs of the people but under the basic condition of fairness to all parties involved, i.e. not to produce social problems. Indeed, in a free and stable society of tomorrow as envisioned in this plan, the institution of free enterprise is recognized as an indispensable instrument of economic progress, as long and so far as it satisfies the law of general equilibrium.

And the Walrasian law of general equilibrium says that in a system of free markets with numeraire, the prices for both consumer good and capital goods will be equal to the least cost of production as defined above. In an equilibrium price, therefore, there is no chance for extra profit or surplus value. The Law of Omenia or a Code of

Ethics in business, in the final analysis, supports the realization of equilibrium prices and thus it becomes a legitimate and necessary institution in any free, just and stable society and economy of tomorrow.

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#### **IV. Final Remarks: A New Message.**

**We are living in a time** of confusion and frustration almost everywhere. We have reached a critical point indicating a crossroad in modern history. The whole free world is financially drifting in diverse directions as a result, among other things, of the disequilibrium forces unleashed by the last crisis of the international monetary system after the suspension of the convertibility of the American Dollar in August 1971. The natural parameter of numeraire has been eased out of both national economies and the international financial community, and consequently the dikes of inflation are broken everywhere, with no solution in sight.

The whole free world now at an impasse is impatiently waiting to see somewhere an example of «stabilité sur le vif», as the French say. This comprehensive plan offers Portugal the tools and the reforms with adequate policies to provide such an example of clean and sound stability for the short and the long run.

Portugal was once the window through which Europe looked at the rest of the world, part of which was unknown. Portuguese men like Magellan, Vasco da Gama, Bartolomeu Dias and others with their outstanding skills, courage and devotion to great undertakings, have crossed the oceans of our planet and thus gave the world a new outlook. Here is a program by which the Portuguese people under their present new leadership can participate in another great experiment of our time, to prove that it is possible to have a new, better society of tomorrow based on freedom, social justice, full employment, price stability, social peace and a balance of payments in equilibrium. It is a new road called «Social Liberalism», leaving behind both Capitalism and Socialism as being inadequate and insufficient to resolve the major problems of our time. On this new road an equitable and self-supporting «economic miracle» lies in the realm of the possible. Portugal may become again the window through which the rest of the free world can see its way to regaining confidence in the virtues and blessings of a free and stable society and economy.