CAPITALISM AS AN ECONOMIC SYSTEM. AN EMPIRICAL ANALYSIS OF THE CAPITALIST FINANCIAL STABILITY DURING CRISIS

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Abstract

Capitalism is a very powerful regime nowadays. Capitalism regards capital as a main factor of production. It supports the capitalist to benefit from wealth accumulation without putting this capital at risk. The mechanism to do so is called interest. This results in the following consequence; Weak competitors who are not able to provide a capital compared to that of a big capitalist are excluded from the competition and put aside. So, the capital is of nature to influence the basic economic decisions like what and whom to produce.

At the state level, governments depend on the capital of capitalists to expend on development. The capital also influences policy making and election campaigns. In other words, the political and social life depends on the market which is in the hands of capitalists.

This article empathizes the problems that accompany the capitalism by conducting an analysis of the financial stability. To achieve this, there are used the profitability ratios for 20 financial institutions in times of different crises that have affected the financial market. This article concludes that; in the todays' economic environment, which is ever changing, the capitalist system might be at risk. It needs either restructuring or reconceptualization in order for the economic system to perform accurately.

Keywords: *Capitalism, Economic System, Financial Stability, Profitability Ratios*

1. Introduction

Capitalism is thought to last no longer anymore. Given all the problems arose nowadays it has turned into a threat for the whole globe. A brief introduction would help understanding it and trying to identify the elements of a SWOT analysis for providing a better alternative to this "old fashion" system.

The essence of capitalism as an economic system is the capital accumulation. The accumulation of capital means to gather as much capital as possible by different means which derive from the use of the ownership. These sources of additional capital, otherwise called as financial return, might be:

- Profit - It comes from the differences in prices
- Rent – It comes from the transfer of the right to use the property, from the owner to the user.
- Interest – It comes from the transfer of the right to use the money.
- Royalty – It comes from the transfer of the right to use the asset for generating profits.
- Capital gain – It is a result of the changes of the value of the asset in the market.

All of these elements are of great importance and need special attention for a deep analysis. This paper aims to analyze the use of the interest as the main element of the capitalism, by emphasizing the problems that it might bring.

What could be an alternative of the interest? Is it possible to totally avoid it without putting the economic system in risk? Can we afford a system which skips the interest and promotes the share of risk, mobilizes people savings and enhances the total welfare? Moreover, how much possible is its implementation in order to increase the financial stability?

To address these questions, the paper will start with a broad overview of the capitalism by emphasizing its advantages and drawbacks.

1.1. An overview to capitalism

Capitalism, as an economic system, is characterized by the private ownership of the production means, and the use of them in generating profit. The basic components composing capitalism there are: accumulation of capital, market competition, a system of prices, rights to private property, salary labor and freewill exchange.

According to Fulcher, James (2004), Capitalism A Very Short Introduction, Capitalism is the decision to invest your own money in return for a profit. In generating this required profit, the capitalist should undertake a considerable amount of risk. Generally, the higher the desired/required return, the higher the risk you should undertake. In this presumable situation it is very simple to calculate the profit. It is the difference in prices between the country of production where there were used all the production means, and the country of exportation which is willing to pay for something of real value. If there was only one producer providing this good, the buyer would only rely on him, resulting in a very huge difference between these prices, so huge profits for the provider. It is the market which diminishes the power of this producer by accepting alternative producers. This way the market gets saturated and the profit for each of the producers is determined by the equilibrium. This results in a fairer price for the buyer. This example refers to the merchant capitalism.

If we talk about the financial capitalism, it generally refers financial markets. Instead of the underlying assets there is used other instruments, called derivatives, to represent the transactions on these assets. Such kind of instruments might be, Future and Forward Contracts, Call and Put Options, Caps, Floors, Collars and SWAPS. These instruments are used for arbitrage or hedging purposes and they rely on the expectations of the customers/ investors. The parties use these contracts in order to avoid the risk related to the underlying assets, based on their expectations regarding the possible movements on the prices and returns of these assets. Such transactions between different parties make up the financial market. The arbitrage technique uses the small differences that result in the prices due to some technical issues between different markets. A smart investor might take advantages by exploiting these opportunities. It is also the stock exchange market which might provide room for such differences to be profitable for the engaged investors who carefully study the market movements. All in all, behind this global structure, it is the consumer expectations which make able the chance to take advantage from the investment opportunities. Sometimes it might cause a non-representative of the real value, price, which is hidden behind the "Good will" or "Mark" terms, and traded for as an added value to the customer, who is the one which will bear this artificial fictional price.

In the light of the recent crisis, we can see the capitalism as modern economic system which is still adapting to the ever-changing world. In the Oxford English Dictionary, capitalism is referred to as "accumulated wealth reproductively employed". The capitalist system stresses the importance of the private property, the economy based on the market, the importance of the contracts, the innovation driven by the entrepreneurship, the pay for the work provided, in financial terms and for sure the available free credit for investment purpose. That way the modern capitalism is far different in definition, but in functioning as well by the explanation on the dictionary.

It is the credit which stands in the roots of capitalist economies. As McCraw Thomas K said in his book "The Current Crisis and the Essence of Capitalism" (reference here), it is crucially related to the believe in the future. Simply said, only because the capitalist expects a bright future, he is willing to use his wealth today for a higher return in the future. Moreover, it goes eve beyond that. The entrepreneur might be willing to invest even the unreal accumulated wealth for this purpose. Every financial transaction is based on a fake, illusionary accumulation of wealth which is now in the hands of nobody. Banks enter into lending activities with customers by using sources they do not own, and allow themselves to lend more than their available reserves. They do that only because they expect that they will generate interest revenues in the future. Corporations issue bond and stocks to finance their activities and every calculation on the due payment is done by considering the expectations for future income which might arrive from their assets. Customers engage in trading activities for assets that do not really exist. This is done in the frame of their belief for the better future. They expect the asset to be ready on the due date specified in the contract and with the required predetermined features. In these terms, everything which is traded for today, is based on the future forecast and expectations. This is how does the modern capitalism look like.

Probably, with the missing backing asset it might be the rider of many economic problems, why not even crisis. It might also be an enormous opportunity to take advantages of any good economic opportunities, even with a credit absence. This dilemma will be explained in the continuing sessions by arguing on the advantages of capitalism as an economic system as well as its drawbacks. Moreover, a comparison between capitalism and other economic systems will show up the benefits and weak points.

1.2. Advantages of Capitalism as an Economic system

Tejvan Pettinger (5 October 2019), in his article "Advantages of Capitalism" tells that the capitalism has five advantages. Firstly, he says, there is no better alternative than the Capitalism. According to his explanation capitalism, likewise the Democracy is the best alternative the economists and philosophers might have ever found. Regardless of all its possible disadvantages, there is no any other system that might perform better than capitalism so far. By this attitude towards Capitalism, it is clearly understood that everything else is just the explanation how a good system Capitalism is.

The second advantage according to Pettinger is that Capitalism promotes efficiency. This efficiency lies in both directions, either in the resource's allocation, or in the production efficiency. When we talk about the allocation of the resources, the Capitalism, by the introduction of the free markets and the concept of the invisible hand of the market conditions, makes it easy for any producer or provider of goods and services to freely allocate its resources for such a production anyway in the world. The efficiency here is fulfilled by the competition on these resources. On a free market, the manufacturer is free to choose the best sources and due to the competition, he can achieve that with a low cost.

The production sources, especially when we refer to a manufacturing business, might be classified as direct materials, direct labor and factory overhead. The primary source of production, the direct materials can be easily allocated all over the world and the capitalism makes it easy to provide them in the most efficient way possible. When it comes to direct labor, to which Capitalism allocates the payment in the form of wage, even this source can be easily located in the market with the highest quality for a low price. This makes the use of labor efficient. The last element of the production, the factory overhead might be the easiest sources to be allocated efficiently in the market. The competition for them is even higher and their distribution is wide.

When we talk about the production phase, the transfer of these primary sources in what is called the "Work in process" is then achieved with a high efficiency. The automatization of the processes, the possibility to outsource the operation means, and the phases of operations themselves, makes the production effective and efficient. I would like to go even beyond that. The just in time processes are those who can increase even more the efficiency of production. Everything is allocated, produced and distributed in the most efficient way. Even the feedback comes back immediately and when required. This makes it possible the change and the continuing improvement to happen not only efficiently, but just in time as well. Given that, the practice over time makes it even easier to implement an added efficiency in the future. This can be achieved when the manufacturer gets familiar with these rapidly changing preferences, driven by the ever-changing world. The Capitalism makes it possible for the provider of the goods and services to predict the preferences and the behavior of the customer in the long run, thus being able to even dictate their needs and preferences. At this point in time there are other ethical issues that might rise. If we go beyond that the legitimacy of capitalism might even diminish.

Another advantage of Capitalism according to Pettinger is the freedom to choose. Even though it might be seen as a political and social issue it

is indeed all inclusive. According to Friedman "There is one and only one social responsibility of business — to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game". It means that in a free economy, everyone is free to choose whatever he wants. The producer firstly has the total freedom to choose the sources of production, the way of organizing his operations, and the type of the products/services he will be delivering. Moreover, he is free to distinguish between different suppliers of his row materials, in order to deal with the best price and quality. He is also free to choose the customers he would like to serve too. He can decide whether to expand on the entire market, to choose a segment or even a niche. The price he will put on his product is also his choice. Beyond that, he is free to choose the information and promotion channel to achieve his customers.
On the other hand, the counterparties have their freedom too. The supplier is free to choose the design, the price and the quantity of the row material he will be selling to the manufacturers. He is also free to choose which partner to work with.
The employees have a total freedom to choose the company he would like to work too. He is the one who puts the requirements on the wage he will accept, as well as the work conditions he would like to work on.

The customer on the other hand is free to choose between multiple sellers. He is free to require for the best price and the best quality.

In this entire scheme there is a tradeoff between costs and revenues, only if the net revenues exceed the total cost, each party will be willing to collaborate with the other. The profit margin is also an issue which should be taken into consideration. Again, there is needed an analysis of the tradeoffs between costs and profits about the margin that everybody would be willing to accept. In this viewpoint, the only limit to the freedom of each party is the entering in the freedom zone of the counterparty. The government would in this case only interfere as a regulator. This is because, due to the economic freedom, there will not be a need for political enforcement. The economic freedom would be able to provide political freedom as well. Furthermore, the greed to have as many deals as possible, put in place by the equilibrium of the market, and would enforce each party to give the best of him. The result will be a win-win game for all the parties and the effect would be transmitted on the economic progress as a whole.

The financial incentives have been seen by Pettingeras as another advantage of the capitalism. As the father of capitalism, Adam Smith stressed the thrift and savings from individuals, families or even businesses are a very important element which contributes to the development of the entire economy. That takes place especially when these savings are not kept in a bank account but rather when they are invested in the economy. This investment would make it possible for the industry to buy more machinery which might save the labor and improve the innovation. The technological improvement might then be used to increase the total return on the capital invested, which would mean money circulation in the economy. This is translated in higher living standard. The question is: Is the today's capitalism using the savings and thrifts as Adam Smith intended years ago?

Milton Friedman says "The great virtue of a free market system is that it does not care what color people are; it does not care what their religion is; it only cares whether they can produce something you want to buy. It is the most effective system we have discovered to enable people who hate one another to deal with one another and help one another." In this sense, another advantage of the capitalism is the lack of the discrimination. The employer would seek for the best worker who would do his job properly, without thinking of which color, race, culture gender or religion he belongs too. As far as the market is which puts the rules, the only objective would have been to accomplish these rules. Even if the employer would think twice while hiring this worker or not, it would be the market constraining him not to think for longer. This is because the competition is too harsh. There is no time to think twice for one choice, because your competitor might have done it far before than you. At that point you would be constrained to restart the hiring process by scratch, because the employee just flew to the counterparty. However, everyone is aware that this process is too costly and time consuming.

That is why, in the continuous changing world, the winner is the one who thinks and acts the first. Given this, all the possible workers in the market will be equal in the eyes of the employers. The only characteristics differentiating them would be their skills and abilities, something that seems to be fair enough.

The producer on the other hand is in a continuous search for the best provider of the production resources. Neither would he/she see for the color, ethnicity, and gender and so on. His/her only concern would be to find the most appropriate supplier for his/her business. So, all the suppliers in a competitive market are the same. The qualifying element for them will be their quality and price. In this sense the discrimination is died even in this aspect.

Moreover, the final customer has got no race, gender, ethnicity, or religion. The producer is always eager to serve to the highest number of customer possible. His/her only objective is to maximize the profits and he/she can only achieve this objective by reaching the highest number of purchasers. Additionally, he/she will be continuously seeking to keep this customer satisfied for as long as possible, in order for the competition not to take him/her away. In this sense, the discrimination on the customers is extinguished.

It is discussed so far that the employees have got no “color”. Indeed, they have all possible colors of the world, but this is not a threat for them. This is neither a source of discrimination. In the light of free market, it is seen as a source of intangible assets that adds value to the company. The differences between them are those which enhance the organizational culture, open new horizons and put the business forward.

The same happens with the suppliers. Their richness in the “colors” is an opportunity for the manufacturers to be exploited. They can offer miscellaneous choices to the business by differentiating it in the competitive market.
The last but most important one is the customer. His multicolor is the source for innovation. There are these differences which might add value to the operation of the companies. The marketing strategies can best be constructed by exploiting these differences. They are the source of deep thinking, innovation and continuous improvement, because in a long battle to fulfill all different needs coming from these different customers, the producers will be facing their opportunity to express their power.

Given that the market dictates equal opportunities for employees, suppliers and even customers, the colors belonging to each party make a whole beautiful picture of the future. The employees can only compete on merit basis, the suppliers can only compete on quality and cost basis, the producers can only compete on quality and cost basis. In a harsh competitive market, the survivors will be the ones who will provide the best. This is the incentive for innovation and continuous improvement. All in all it is the customer who will gain, it is the system, and it is the entire society who will benefit. I still wonder, is really Capitalism being implemented as it was thought?

1.3. Disadvantages of Capitalism as an economic system

“Capitalism is the astounding belief that the wickedest of men will do the wickedest of things for the greatest good of everyone.”– John Maynard Keynes
Based on this, Tejvan Pettinger wrote in his article, “Pros and cons of capitalism”, published in Economics Help, that Capitalism presents some disadvantages, such as:
the possibility of the firms to exploit the customers by gaining a monopoly power;
these firms can use this power even for the lowering of the wages to the employees;
the possibility to damage the environment by the externalities, especially when they are not controlled, the inequality that comes as a consequence of inheritance and the possibility to cause booms and busts to the economy.
As Branko Horvat wrote "It is now well known that capitalist development leads to the concentration of capital, employment and power. It is somewhat less known that it leads to the almost complete destruction of economic freedom"

The capital concentration in the hands of the richest ones will let the rest of the population in a huge poverty. The rich people are becoming richer and the poor people are becoming poorer. This will create a huge gap between the rich and the poor as far as the middle class might even disappear. This picture will not last for too much to appear in the new economic and global system. It will merely come because of the concentration of wealth in the hands of some people that might think that they deserve everything. Nowadays more and more entrepreneurs are merging with or even acquiring others. The greed to become even bigger does never end. This will probably lead to a general monopolization of most of the sectors of the economy.

The concentration of the vast amount of money in the hands of very few people will lead to a political power loss as well as a loss of the democracy and economic power for the majority of the population. The economic system will be directed by some greedy corporations with an unlimited power as to influence the government and the syndicates as well. They will become a kind of government where the hierarchies and bureaucracies will kill the free entrepreneurship. Their only driver will be the profit maximization and nothing else will have higher value than this. In this sense they will be the promoters of the degradation of the social welfare. David Schweickart says: "Ordinary people [in capitalist societies] are deemed competent enough to select their political leaders-but not their bosses. Contemporary capitalism celebrates democracy, yet denies us our democratic rights at precisely the point where they might be utilized most immediately and concretely: at the place where we spend most of the active and alert hours of our adult lives"

Franklin D. Roosevelt says that "the liberty of a democracy is not safe if the people tolerate the growth of private power to a point where it becomes stronger than their democratic state itself. That, in its essence, is fascism—ownership of government by an individual, by a group, or by any other controlling private power." In this sense the democratic liberty is put on question as we always see the increasing power of the capitalists which might even not promote any real development even because some of them might have inherited it.

The monopolization is the worst thing that might happen to an economy. Firstly, monopoles will make the exploitation of their employees. Given that the number of the businesses will be very low; these employees will have low alternatives to choose. This is of nature give the existing ones the freedom to lower the wages of the employees to the minimum possible. Not only that but, in an attempt to decrease the costs as much as possible they might also justify the lack of good work conditions. The employees might be constrained to work in poor conditions and with low wages and none of the competitors will be willing to offer something more. This is the worst exploitation ever done to the workers by any form of political or economic system.

Diseconomies of scales are also another threat related to the development of the monopoly. As it is known, the increase of the amount of production can result in economies of scales. This is due to the decrease of the cost per unit as the total amount of production units increases. But on a monopoly situation, the total quantity is believed to increase as much as the production cannot be managed and controlled any more. The average cost would then increase in such dimensions as well. This would cause the inability to control the average cost of this production. That way, the increase of production, driven by the monopoly would cause totally the contrary. The cost per unit would start to increase even more.

The lack of choice is another drawback assigned to the monopoly. Nowadays, consumers do not only buy to fulfill their basic needs. That would be the case of many years ago, when it was more than enough one variety of products to satisfy the consumers' needs. In the hierarchy of needs of Maslow, there are other needs beyond the basic surviving needs of the human beings. Now, consumers are more and more looking on self-actualization and self-esteem, given that the lower levels of needs have been already fulfilled. The lack of choice will be the killer of those needs and wishes for the customers, let alone any psychological problem that they might cause to them.

Inequality is another drawback of capitalism. This is related to the unfair distribution of wealth and power. The wealth is concentrated on the hands of very little people who rose from the monopolistic system. As Ravi Batra calls it "share of wealth held by richest 1%", it is explicitly shown that the most of global wealth is concentrated on the hands of an almost invisible part of the society. To concentrate that enormous wealth and power only on that little share means to drive the whole economic, political and social system toward destruction. The biggest and most powerful ones will always exploit the rest of small and week people which constitute the majority of the society. It seems like all are living to make this minority satisfied and happy, when it should be the contrary happening. That situation cannot last for longer as far as the people understand their rights and start dictating their power through unions and other types of organizations.

Capitalism promotes market instability as well. As Marx believed, the production in the capitalist system occurs in an irregular way. Any time that a recession occurs, this relates to overproduction, which is a waste in the entire system. This way of production has several contradictions within. On one hand, the capital sphere is on anarchy represented by the free market and on the other hand, it is the industrialism which promotes socialized production in the labor viewpoint. As Marx and Engels said "Society suddenly finds itself put back into a state of momentary barbarism, and why? Because there is too much civilization, too much means of subsistence, too much industry, too much commerce"

2. Methodology

Two methods are used to prepare this research paper. The first part uses a theoretical approach by collecting secondary data from multiple sources of scholars' researches. All this information is condensed in a reflection essay which explains the advantages and the drawbacks of capitalism as an economic system. Moreover, the analysis of the weaknesses shows out the possible areas of improvement. It is also discussed of how to manage the drawbacks in order to convert them into strengths.

The second part of the research is an empirical analysis of the elements that better represent the financial system in the framework of the capitalism. As it is derived by the term itself, the most important element that the capitalism uses is the capital. In order to evaluate the performance in the use of capital different types of ratios are used as they are explained below. Given that the financial services sector is one of the most important and influential sectors of the economy, the analysis of the ratios is done by data gathered from this sector.

There is chosen a sample of top 20 financial institutions to be evaluated for their financial performance. The first sampling technique used is the purposive sample. As this research takes into consideration the analysis of the interest, as a means which is thought to be the major problem of capitalism, the comparison between these institutions' performance better explains the problematic raised by this component.

Then, the number of the variables in the sample is determined by convenience. It is not feasible for this research to use more than 20 institutions from each group. The ranking within the groups is determined by organisms that engage in the ranking of the institutions worldwide. For the conventional sector it used the report of Forbes for "The largest financial services companies by revenue"

The period chosen includes a range of 15 years, starting by 2006 to 2021. This range is chosen in order to highlight the fluctuations on the profitability during and after the financial crisis of 2008 and also during the COVID pandemic.

3. Empirical research

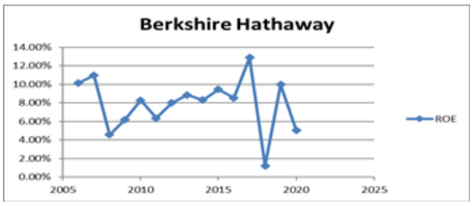
Based on the data gathered from the annual reports of each of the top 20 financial institutions, the analysis consist on an explanation of the profitability ratios as follows.

3.1. ROE

Return on equity is a ratio which expresses the efficiency of the use of equity in generating returns/income. In the sample of conventional financial institutions, what is obvious, is the fluctuations shown in this ratio during the time. These fluctuations tell about unsustainability in the financial performance of these financial institutions. The only conventional financial institutions with an almost stable return on equity are those of China. Given that in China, the government has an important role in the overall financial conditions, the rules and regulations, as well as the control and support toward private financial institutions helped them to keep the sustainability

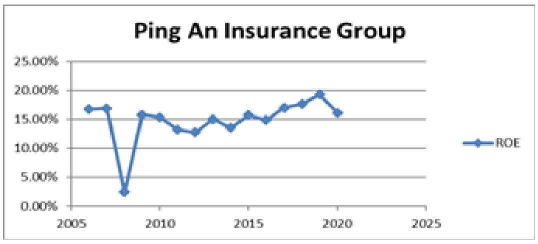
The graphs below show the fluctuations of profitability ratios for the most representative conventional financial institutions.

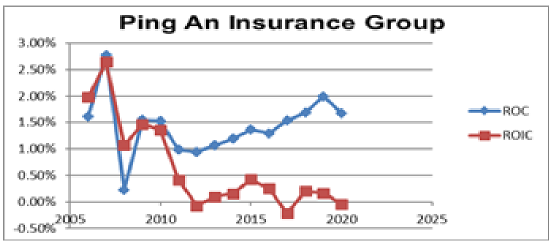
Berkshire Hathaway is a conglomerate located in the USA. Given that it operates in different industries, the consolidated returns of this multinational company rely on



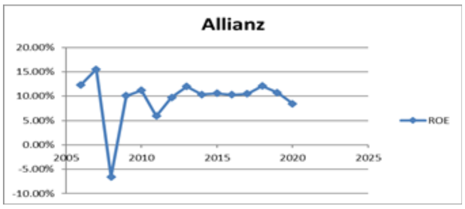
the returns of each of these industries. Its declines are mostly obvious on the crisis of 2008 on 2016 and on the pandemic of Covid 19. Since the crisis have been global and affected almost every industry, it couldn't take advantage of a well-diversified portfolio.

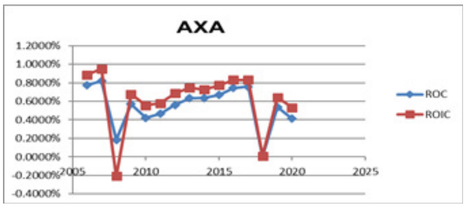
Ping An Insurance Group is an insurance company located in China.

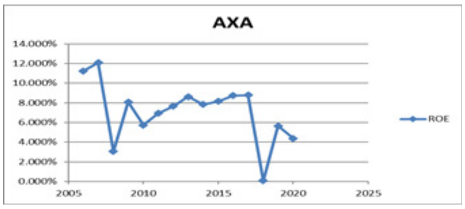




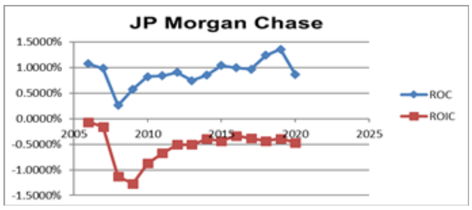
As previously explained the ROE in this company is more stable. A huge decline is present on the years of the financial crisis. It is also shown a decrease in the time of pandemic but this not to huge. In general, the insurance companies did not suffer high loses during the pandemic due to the increase of the number of entities which required to get insured in order to prevent possible future losses imposed by the crisis.





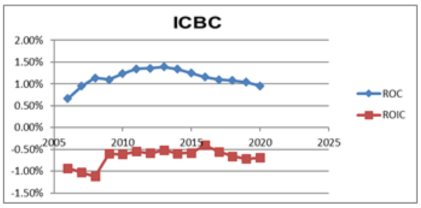


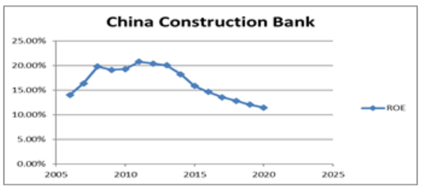
Allianz and AXA are also insurance companies. They operate in the European market, where the influence of the government is not too extended. That is why we observe fluctuations in the return on equity. The behavior during the financial crisis of 2008 and the pandemic are quite the same with other insurance companies.

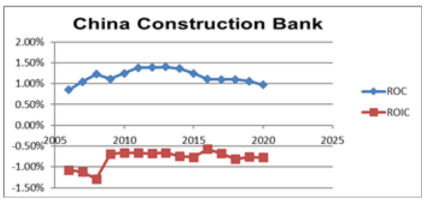


JP Morgan Chase is a bank located in the USA. The financial institutions with higher fluctuations in the return on equity are the banks. This is due to the use of the interest. The interest is the main element which provides revenues as well as imposes expenses to these banks. As such, the net income calculated after all types of revenues and expenses, including net interest income are too fluctuating. It should be mentioned that the main source of operational return in banks is the interests. Given that it is strongly related to the ability of the customers to pay, the behavior of net income is also fluctuating. It is obvious a huge decline on net income and also on ROE during the financial crisis of 2008, for which the main cause was the high interest rate.

It is also obvious a decrease on the time of pandemic. Like in insurance companies, there has been present an increase in the willingness of the people to make their money as safe as possible due to the fear brought by the pandemic. But, unlike insurance companies, the banking activity was mostly concentrated on saving accounts rather that operations which include interest, which imposes on the other hand a high risk. That is why, the decline of the return on equity is higher in banks compared to the insurance companies.

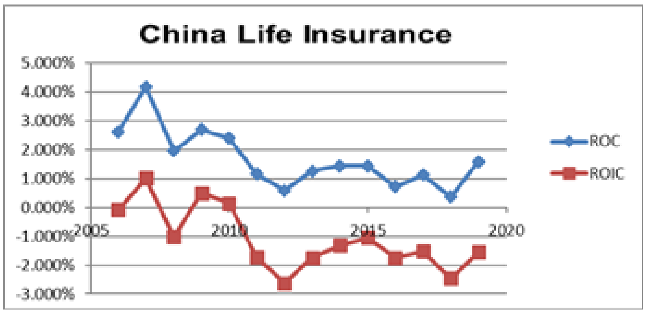






ICBC and China Construction Bank are also banks, but given that they operate in China the role of the government has helped in their smooth transition. The behavior of the return on equity for these financial institutions shows a characteristic shape of the product or business life cycle with no fluctuations.

The life insurance companies have special features,

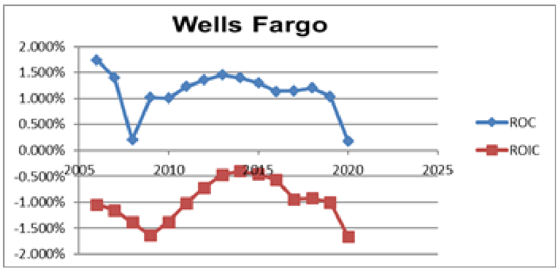


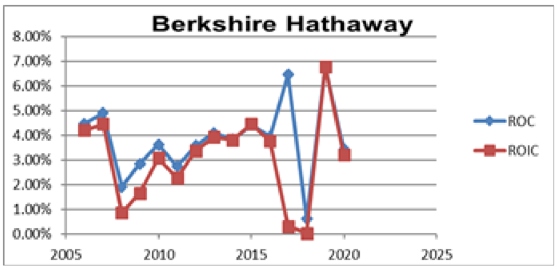
different from other insurance companies. In China, the life insurance companies operate on individual and group basis. Generally, the insurance is done by people for the people, sometimes even from the businesses for their employees. Given that, the returns on this kind of business rely on the peoples' expectations and evaluations of the risk of death. These risks and evaluations defer based on each one living conditions, rather than on macroeconomic conditions. This might be the reason on the fluctuations of the returns on this type of financial institution. What is obvious is the decrease on the return during the financial crisis of 2008, as in all the other businesses. What is more obvious is the huge increase on these returns during and after the pandemic of 2019. This is because of the increased fear of the population for the consequences of the pandemic and for the predicted expenses that the pandemic might cause. Another reason might have been the increase on the number of insured ones to take advantage of the death occurrence of their elderly family members. Given that for most of them the event might have taken place, it is expected for these financial institutions to experience declines in their returns, since they will be obliged to cover the expenses of the insured ones.

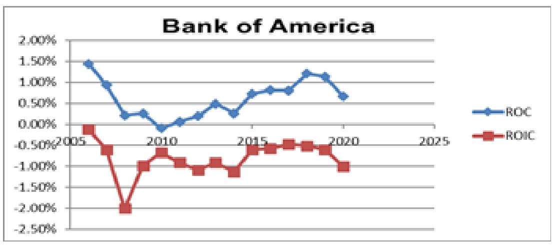
2.2. ROC and ROIC

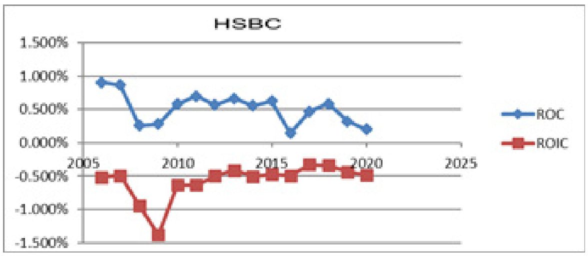
The Return on Capital and the Return on Invested Capital ratios express the efficiency in the use of capital to generate profits. Differently from the return on equity, it doesn't only take into consideration the use of the stockholders' equity but also the use of outside money generated by the third parties. It is referred to as debt. Given that, the return on capital tells about the profits generated by the total capital of a business, not only what belongs to the owners but also what is taken by the others.

The conventional financial institutions take loans or issue debt instruments for financing the operations or their investments. Given that they pay interest in these debt instruments, they face a higher risk related to their investments. That is why we observe fluctuations in the return of capital of conventional financial institutions.









As it can be seen from this sample, the behavior of the return on capital is very similar to that of return on equity. The higher declines are shown during the times of financial crises and the pandemic of COVID-19. What is too important is that the values defer too much. Given that in return on capital, except from the owners' equity is also used the financing from the third parties, this ratio is far low from the return on capital. This occurs mainly because of the cost of the debt. Since the business should pay for the debt that it takes, these expenses decrease the net income for it.

When it comes to the return on invested capital, its behavior is very special for the conventional financial institutions. As it is calculated as EBIT (earnings before interest and taxes) * (1-t), divided by (debt + equity) – (Cash + equivalents) there are some elements that should be taken into consideration in this analysis.

First of all, it only considers the invested capital, so the capital which is used for investment, except from cash and equivalents which are kept for security. Given that, we should be waiting for an increase in the values of the ratio comparable with the return on capital. There is another element, more important that the reserves which has caused a lower value for this ratio, and even negative. Given that the main operations of the conventional financial institutions, and especially banks, rely on the use of interest. As such, we observe that the EBIT in most of the conventional financial institutions is negative. The EBIT is calculated as net income – net interest income because these financial institutions, while computing the net income do take into consideration all the sources of income, one of which is the interest. It is indeed the most important one. All in all, these financial institutions result in negative values on the returns from general operations, because their focus is mainly the hedge and the speculation in the interest rates. Given that the interest rates on the market are too fluctuating, and especially in times of crisis, the ROIC is fluctuating as well. This tells about the instability of the returns on the conventional financial institutions.

Moreover, the values of the Return on Capital and the Return of Invested Capital for the conventional financial institutions are far different from each other, even though the behavior most of the times is the same. That is why the values of the ROIC lie on the negative plane of the graph mostly, while those of ROC lie on the positive one.

Conclusions

Capitalism is a system, the function of which is put on question nowadays. Many scholars argue that it will destroy itself, it will no longer survive to the changes on global range, it will go against the ones who invented it or it will even destroy the global order.

• Capitalism has had many advantages for which it become too important in the whole economic system. These advantages started with the freedom to offer and take everything on a fair exchange experience. This freedom was extended in all the spheres of the global interchange, starting from the acquirement of the raw to the distribution of the goods and services to the customers. Another advantage was the equality and the fairness. No discrimination could prevent the parties willing to participate in an exchange. All the involved actors of the global market could only compete with their comparable advantages. More over this system used to promote efficiency and effectiveness as far as it was used to achieve the required returns. It was for longer believed to not have a better alternative than capitalism

• The worst feature of this system is the capital concentration on the hands of few people. The rich get richer and the poor poorer. The incentives for efficiency and effectiveness have passed all the limits by sacrificing the added value and the quality. Nothing is traded anymore for the real value; it is traded indeed for a fake goodwill. There are no more incentives for common prosperity. The equality and fairness is compromised and the social prosperity is bypassed. The environmental sustainability is compromised as well.

• One of the main elements bringing the problems of the capitalism is the interest. The speculation on this element has caused financial instability. The crisis times reflect the problems arose by the use of the interest. The deepest declines in profitability are shown during these times. More over there is needed too much time and effort to recover from the recession.

• Due to the use of the interest the profitability ratios show huge fluctuations. This tells about the unsustainability of the financial system in a capitalist regime.

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