

**“Economics for Everyone:  
How to Cut Through the Jargon**

Later Life Learning, Innis College  
Instructor: Dr. Jim Stanford  
Fall 2021

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**Session 4**

**Bosses, Owners,  
and Companies**

**Readings:  
Chapters 7-8**

*Illustrations © by  
Tony Biddle*

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**Key Topics Covered**

- What is capital
- How companies are organized
- The ownership of companies
- How companies behave
- The logic of profit
- Business investment performance

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## Key Terms Introduced

- corporation
- capitalist class
- top managers
- major owners
- surplus
- profit
- interest
- investment
- private costs and benefits
- social costs and benefits
- retained earnings
- capital gain
- stock market
- return on equity
- depreciation

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## The Economy is Work



- We use our capacity to work (brains & brawn) to transform what we harvest from nature (hopefully sustainably!) into useful goods & services.

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## Working With Tools

- Nobody works only with their bare hands.
- Humans learned very early that working with tools makes us more productive.
  - Even many animals know this!
- Tools allow us to:
  - Produce more output.
  - Produce higher quality output (goods and services that we couldn't produce without the right tools).
- Humans "learn by doing":
  - The more we work, the more we find better ways to work (including new tools).

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### Where Do Tools Come From?

- Like any other product, tools are produced by work.
  - "Intermediate good": Something that is produced to then produce something else (rather than consumed).

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## Where Do Tools Come From?

- Like any other product, tools are produced by work.
  - "Intermediate good": Something that is produced to then produce something else (rather than consumed).
- Think of working with tools as a two-stage, "indirect" way of working:
  1. First we work to produce the tool.
  2. Then we use the tool to perform our end task.
- But remember: Humans did all the work.
  - The tools themselves are not productive.
  - Knowing how to make & use tools is productive.
- Merely owning a tool is not a productive act.

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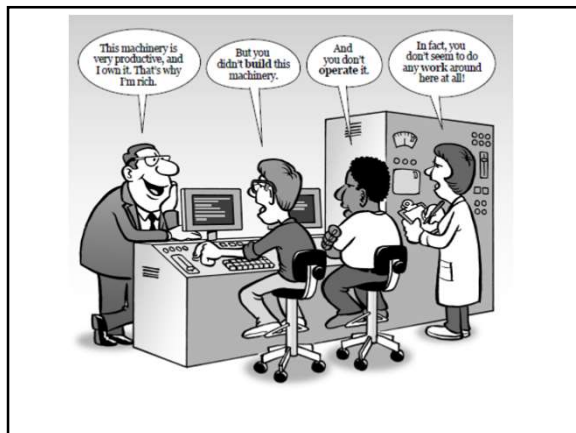
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## Demystifying "Capital"

- "Capital" is just the economic term for "tools."
- Physical capital: real, tangible products used to produce other products.
  - Distinct from "financial capital," which is just money.
- Fixed capital: long-lived, used in a workplace.
  - **Structures:** buildings, offices, stores.
  - **Machinery and equipment:** computers, assembly lines, hand tools, transportation equipment.
  - **Infrastructure:** roads, bridges, utilities.
- Working capital: the value of raw materials, inventories, and other items used up in production.

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## The Private Company

- One of the defining features of capitalism: most production is undertaken for private profit
- The private company is the entity through which that profit-seeking activity is organized
- Private companies come in all shapes and sizes:
  - Large corporations, with global reach
  - Medium-sized firms (most work done by paid workers)
  - Very small firms (most work done by owner & family)
- All companies have two key features:
  1. Somebody owns them and its profits
  2. The owner directs the firm in their interests

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## Types of Companies

- Individual proprietorships
  - Individual owner owns & controls it directly
- Partnerships
  - Joint owners share the investment & profit
- Corporations
  - Separate legal entity which limits the liability and potential losses of the owners
  - Large corporations are usually owned through joint-stock (issuing equity shares)
  - The biggest global corporations are economically larger than many countries, and operate through tight central plans

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## The Biggest of the Big

(p.90)

Category	Large Company	Equivalent Country
<b>Value-Added</b>	<i>ExxonMobil</i> (\$195 billion)	<i>Finland</i> (\$195 billion)
<b>Employment</b>	<i>Wal-Mart</i> (2.3 million)	<i>New Zealand</i> (2.3 million)
<b>Cash</b>	<i>Apple Inc.</i> (\$147 billion) (Cash & securities)	<i>U.S. Fed Govt</i> (\$110 billion) (official reserves)
2013 data, \$US.		

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## Who Owns Corporations?

- Ownership of joint stock companies is dispersed
  - Shares are bought & sold on the stock market
- Problem: how to ensure company acts in owners' interests
  - Problem solved through major share ownership and executive compensation
  - Top managers of the firms are major owners, with huge personal stake in share price
- Ownership of business wealth as a whole is concentrated among a small elite
  - It's a myth that the stock market, mutual funds, etc., have allowed everyone to become "owners"

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## Meet The Modern Capitalist



- Less than 2% of advanced capitalist population owns enough wealth to not have to work
  - Many do work anyway, but they are not compelled to work for survival
- This small group owns a controlling interest in the private business sector
- Large overlap between this group and top executives of large and medium companies
- "Major owners and top managers" = the modern capitalist class

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## The Shocking Concentration of Business Wealth

Distribution of Financial Wealth				
	Top 10%	Top 1%	Billionaires	Bottom 50%
Canada	58%	~30%	5% (54)	3%
U.S.	71%	34%	6% (~500)	2%
Australia	53%	~25%	7% (37)	6%
U.K.	71%	34%	10% (169)	1%
World	57%	32%	n.a.	4%

- Most financial wealth is owned by the top 10%.
- The bottom 50% own almost no financial wealth.
- A handful of billionaires own more than the majority.

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## The Logic of Profit

- Competition forces companies to meet the "going rate" of profit or go out of business
  - This imposes a logic & discipline on the system
  - This logic (not the personal views and actions of CEOs) explains why capitalism does so much harm
- Under capitalism ("production for profit") something is done if it is profitable
  - Not necessarily if it is *useful*
- We cannot assume that profitability is a measure of an activity's value
  - "Production for profit" does not guarantee that human needs are being met

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## The Logic of Profit

- Think of something that is profitable but not useful.
- Mention it in the Q&A.
- One example:



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### What is Profit?

- In both economic and accounting terms, it is a "surplus."
  - Economic: Something left over after the costs of reproduction (human and capital) are paid.
  - Accounting: What remains after production costs are deducted from revenue.

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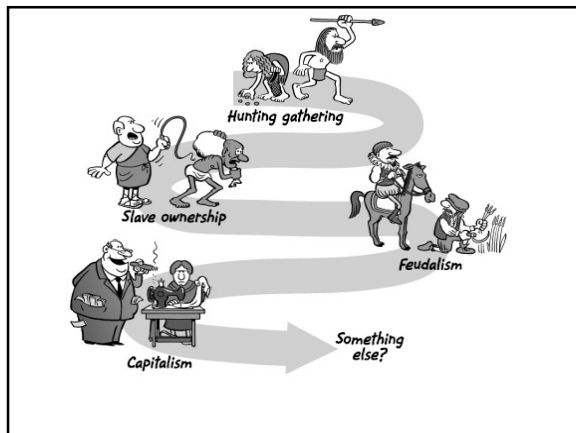
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### Measuring Profit

- Operating revenues
  - Operating expenses
  - = Operating profit
  - Depreciation (wear & tear on capital)
  - Interest costs
  - Other overhead
  - = Income before tax
  - Corporate income tax
  - = Net income

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### Evaluating Profit

Operating margin =  
Operating profit ÷ Revenue

EBITDA = Earnings before interest tax  
depreciation & amortization

Return on capital =  
Net income ÷ All invested capital

Return on equity =  
Net income ÷ Shareholder equity

Total surplus =  
(Profit + Interest) ÷ Invested capital

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### Capturing Profit

- There are many ways for owners to access the profits of their businesses.
  - Direct income (proprietorships).
  - Dividends.
  - Interest in various forms.
  - Capital gains.
- Big irony: Tax system offers huge advantages to capital income.

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## Business Investment Today

- We are told that economic policy must cater to business, so we get “jobs and growth.”
  - Can you list examples? (Use the Q&A!)
- Problem: Under neoliberalism, the economy has become more business-friendly (and profits have improved).
- But business investment spending has slowed down, not picked up.

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## Less Effort (p. 156)

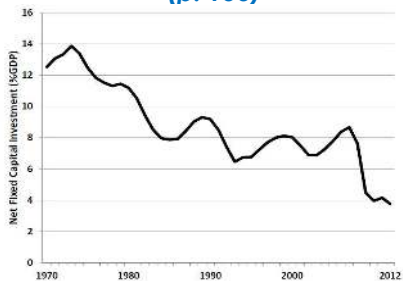


Figure 12.1 Falling Investment Rate, OECD

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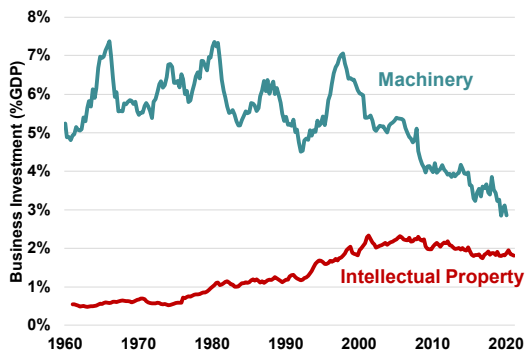
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## Lazy Canadian Capitalists



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## Determinants of Business Investment

- AMOUNT:
  - Profit (current & expected)
  - Capacity utilization
  - Economic growth (current & expected)
  - Interest rates
  - Political / legal environment
- LOCATION:
  - Unit labour costs
  - Infrastructure
  - Taxes
  - Transport costs
  - Supply chain
  - Local market
  - Trade policy
  - Political / legal environment

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## Have Capitalists Lost the Will to Work???

- Neoliberalism has boosted profitability.
- But investment spending has weakened.
- Uninvested profits are a source of ongoing stagnation:
  - Excess corporate savings.
  - Increased payouts to owners.
  - Financial speculation & other schemes.
- Stock markets remove capital, not raise it.
- Does the economy need a new engine?

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## Thank You!

*Let's take 5 minutes...*

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