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# Free Markets with *Caritas*: A Transformational Concept of Efficiency

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“The *principle of gratuitousness* and the logic of gift as an expression of fraternity can and must *find their place within normal economic activity*.”

—Pope Benedict XVI, *Caritas in veritate*<sup>1</sup>

How can we put this *principle of gratuitousness* to effect in the function of the free market?

In this paper I suggest that the principle of gratuitousness can transform prevalent notions of economic efficiency by removing the ethical blind spots which linger in the popular idea of a free market guided by an invisible hand. I aim to show that the principle of gratuitousness, as an expression of *caritas*, can help to distinguish healthy and unhealthy dynamics within economic transactions, and furthermore, this notion of health pertains to the sustainability of a free market. This transforms the conventional concept of efficiency by recognizing and exposing the erroneous presumption that efficiency *per se* is a foundational good. It is not. The concept of efficiency cannot bear the weight of moral scrutiny, unless and until it is transformed by interpretation within the context of *caritas*, which is an authentic foundational good. This transformational concept of efficiency provides a useful framework within which to evaluate the contribution of economic activities to the overall sustainability of the free market.

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<sup>1</sup> Benedict XVI, *Caritas in veritate* [Charity in truth], papal encyclical (San Francisco: Ignatius Press, 2009), sec. 36, emphasis original.

In short, my method here will be to analyze and elucidate by example the differences between economic pursuits that add strength and vitality to the market, and those that detract from it. We shall see that *caritas*—revealed in the principle of gratuitousness and in witness to the value of solidarity—is present in those economic activities that contribute to and enhance the sustainability of the free market.

We may therefore characterize different sorts of economic activities on the basis of whether they are either *additive* or *extractive*. By “additive” we mean the sort of economic activities that create wealth (or at a minimum, create such opportunities with intentionality) beyond the immediate profit a party may derive from the mere transaction. Additive activities are akin to creation *ex nihilo*, in the sense that the outcome realizes a greater benefit than had existed before the creative act. Such wealth-creating effects display *caritas*, by virtue of bestowing gifts that would not otherwise have existed apart from the intentional creative act. These activities demonstrate an inherent component of generosity, charity or *caritas*, in that they distribute benefits into the larger community represented by the free market.

“Extractive” economic activities, on the other hand, are those which seek to gain a profit, yet *without* intentional concern for solidarity, or for the sake of beneficent outcomes motivated by *caritas*. Our method here will be to examine a few types of business and financial activity, in order to assess the role of *caritas* in economic transactions. Our thesis is that additive transactions convey an element of *caritas*, which leads to economic sustainability; whereas, negative transactions do not.

If we think of the free market metaphorically as a living body, we may say that additive transactions contribute to the overall metabolic health of the body: they nourish sustainable wealth creation. Extractive activities, on the other hand, feed off the energy of the

body without adding to its overall strength. Economic activity which bears witness to the spirit and logic of gratuitousness will build solidarity and contribute to sustainability.<sup>2</sup>

## **Demythologizing the Invisible Hand**

To make distinctions between additive and extractive activities is no simple matter. The conventional wisdom argues that such distinctions are simply impossible *prima facie*. Hayek has argued famously that no amount of administrative acumen is sufficient for such matters.<sup>3</sup> The questions are too complex, it is argued, and the valuations too subjective. The suggestion that the logic of *caritas* might be essential for the health of the free market would seem to fly in the face of the conventional wisdom regarding the efficiency of markets. In light of the seeming intractability of questions related to worth and goodness, it is argued, the efficiency of prices in a free market is the only suitable arbiter of value. It is here that the idea of an “invisible hand” is invoked: the market is trusted to blindly make practical, beneficial tradeoffs, “as though guided by an invisible hand,” in the famous words of Adam Smith.

This invocation presumes a lot. First, it presumes that a calculus of prices and other quantifiable market forces offers the only rational means to evaluate the merits and comparative desirability of outcomes. Furthermore, it presumes to provide a rationale unencumbered by the irreducible values and complexities of spiritual faith or overarching

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<sup>2</sup> We might view such activity as “socially useful”, as opposed to other “socially useless” sorts of activities which do not contribute to solidarity, to borrow the phrasing of Lord Adair Turner, chairman of the UK Financial Services Authority, who has called “socially useless” the sort of hyper-speculative, self-serving activities which led to the subprime mortgage scandal. Rowan Williams and Larry Elliott, *Crisis and Recovery: Ethics, Economics and Justice* (Basingstoke, NY: Palgrave Macmillan, 2010), 12.

<sup>3</sup> F. A. Hayek, *The Constitution of Liberty* (Chicago: University of Chicago Press, 1960).

value statements. In essence, it presumes to subjugate all values to the dominion of the profit-driven efficiency of the free market.

The conventional idea of efficient markets trusts the price-setting function of a mythical invisible hand to set prices which will lead naturally to the optimum outcome. This is a severely reductionist approach, of course, and its reductionism is most pronounced and most problematic with respect to the significance of human nature, human dignity, relationship and spirituality.

Anatole Kaletsky, in his critical assessment of the events leading up to the recent collapse of financial markets, points to the flaws in such mythical thinking. He says this conventional wisdom regarding market efficiency leads to

the imaginary world of market fundamentalist ideology, in which financial stability is automatic, involuntary unemployment is impossible, and efficient, omniscient markets can solve all economic problems, if only the government will stand aside.<sup>4</sup>

This imaginary world is built upon the premise that economics may be practiced in a spirit of “scientific asceticism” devoid of moral questions and detached from moral consequences.<sup>5</sup> This premise trusts in the mythical idea of an “invisible hand” which

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<sup>4</sup> Anatole Kaletsky, *Capitalism 4.0: The Birth of a New Economy in the Aftermath of Crisis* (New York: PublicAffairs, 2010), 156. Kaletsky elaborates on the fundamental problems within this “imaginary world” by pointing out that the presumption, common in the practice of modern economics, that human nature can be modeled in mathematical formulas is “an act of hubris”,168.

<sup>5</sup> Luigino Bruni and Stefano Zamagni, *Civil Economy: Efficiency, Equity, Public Happiness* (Oxford: Peter Lang, 2007), 15.

somehow weaves the chaotic movements of human choice into a tapestry of meritorious and beneficial outcomes. The mythological aspect of this premise has recently been critiqued by several observers,<sup>6</sup> including Samuels, who disparages the idea of the invisible hand as “an ambiguous and inconclusive . . . feature of a striking theme in which a belief is offered in the absence of truth.”<sup>7</sup> Adam Smith, the seminal source of this concept, employs the phrase “invisible hand” only rarely and gingerly to fill a gap in the explanation of political economy. Based upon his finely tuned reading of Smith, Samuels concludes that Smith is well aware of the semantic risk in such an elliptical expression, knowing that “people settle for propositions that suit the imagination, or set minds at rest, when truth is unattainable.”<sup>8</sup> Ironically, the vague or even tautological idea of the invisible hand is sometimes cited in support of analytical explanations for the functioning of a market economy. Such explanations accept the explanatory power of the notion on faith.

Sedláček describes well this “historic irony” in the development of economics, and notices how it has been born via the split between ethics and economics:

The idea of the invisible hand of the market is, in reality, born of moral inquiry, but another hundred years later the issue of morality is lost and economics is completely emancipated from ethics. An unusual reversal has taken place. Adam Smith, Thomas Malthus, John S. Mill, John Locke—the great fathers of classical liberal economics—were foremost moral philosophers. A century later, economics has become a

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<sup>6</sup> Sedláček (2011); Basu (2011); Robinson (2012); Brock (2012); Stiglitz (2012).

<sup>7</sup> Warren J. Samuels, Marianne F. Johnson, and William H. Perry, *Erasing the Invisible Hand: Essays on an Elusive and Misused Concept in Economics* (Cambridge: Cambridge University Press, 2011), xvi.

<sup>8</sup> *Ibid.*, xx.

mathematized and allocative science, full of graphs, equations, and tables, with no room for ethics.<sup>9</sup>

In the pursuit of mathematical methods and scientific asceticism, economics has been cut loose from its roots in moral philosophy. This has profound implications for the concept of market efficiency, because it leads into the expectation that quantitative methods are the best tool for determining the common good, and similarly that the pursuit of profits, under the mysterious control of the invisible hand, becomes presumptively the *de facto* means of making optimal tradeoffs among individuals and within society as a whole.

The problem however, is that the profit motive does not distinguish between sustainable and unsustainable activity. The invisible hand does not discriminate between additive and extractive transactions. It can operate with equal force and efficiency in either direction. It is ambidextrous and ambivalent in this regard.

My thesis is that the logic of *caritas* provides the corrective needed to recognize where and how the forces of free-market efficiency are conducive to sustainability, and where they are not. I shall argue that the beneficent power of the market to serve human flourishing is based not in a morally tacit understanding of economic efficiency as a foundational good or cardinal value, but rather in the notion of *caritas* as a necessary component of economic transactions.<sup>10</sup> This transformed notion of efficiency generates and enhances sustainability in the free market.

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<sup>9</sup> Sedláček, *Economics of Good and Evil*, 177.

<sup>10</sup> John Paul II draws the connection between human dignity and market freedom: “No free economy can function for long and respond to the conditions of a life . . . unless it is supported and ‘enlivened’ by a strong ethical and religious conscience.” (*Gaudium et Spes*, n.

## Relationships vs. transactions

The logic of *caritas* is paradoxical. It requires to be understood from within the context of faith in the greater reality of human dignity which transcends the logic of prices and preference relations. The principle of gratuitousness flies in the face of conventional thinking about the efficiency of the market. The problem is not that conventional thinking about efficiency is wrong *per se*; but rather, it is incomplete. It does not countenance the greater reality of the relationships that enable the market to live and prosper. The conventional idea of market efficiency does not allow room for the logic of gift/charity. The conventional wisdom strains to rule out charity, the same way a bilge pump works to rid a boat of unwanted water that seeps into the vessel. The conventional wisdom says that if there is any charity in the market system it must have gotten there through flaws in the market, just as bilge water got there through leaks in the hull. According to the conventional wisdom, therefore, the logic of gift is a contradiction in terms, *prima facie*.

The underlying problem, of course, is that the logic of market efficiency is incapable of bearing witness to any greater reality. It is constrained to the mundane. It can never rise above the rudimentary level of mathematical approximations. It reduces human behavior to something entirely inhuman.

Richard Sennett points to the quest for ever-greater efficiency, as measured by corporate profits, as the impetus for the unsavory changes in corporate bureaucracies.<sup>11</sup>

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24). Cf. 'A Civilization of Solidarity and Love': An Invitation to *Centesimus Annus*, section 5.

<sup>11</sup> Richard Sennett, *The Culture of the New Capitalism* (New Haven: Yale University Press, 2006), 22–25.



Relationships between worker and employee, producer and consumer, seller and buyer, have become more transient and depersonalized. These trends are the consequence of the quest for more predictability and efficiency in profit-engines of business. George Soros sums it up by saying that transactions have replaced relationships.<sup>12</sup>

The quest for amoral efficiency in transactions drives the human element of *caritas* out of the equation. With the moral aspects of relationship cut off from the metrics of efficiency, there is a ratchet effect which leads in the direction of the total commoditization of every good and service. Ultimately, commoditization becomes the arbiter of morality. Prices are everything and Pareto optimization rules. In this sense of market efficiency, there is no room for the transcendent nature of human relationships to provide realism with respect to justice and the moral discernment of good and evil.

Economists are quick to defend the separation of morality from economics, on the basis that moral issues deserve attention in another realm of thought, but the troubling aspect of this position is that moral concerns are soon forgotten as our attention shifts to the econometric analysis of market functions. This econometric focus reduces justice to the lowest common denominator—namely, the quintessential ideal of efficiency in free, open and perfect competition. Justice then becomes categorically defined in the sense of *commutative* justice; that is, justice defined as equal and fair exchange. When all things of value can be bought and sold, justice will be done when the price is fair. Benedict refers to this sense of commutative justice as “the principle of equivalence” and points out its inability to sustain market health:

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<sup>12</sup> George Soros, *The Crisis of Global Capitalism: Open Society Endangered* (London: Little, Brown, 1998),.

If the market is governed solely by the principle of the equivalence in value of exchanged goods, it cannot produce the social cohesion that it requires in order to function well. *Without internal forms of solidarity and mutual trust, the market cannot completely fulfil its proper economic function.*<sup>13</sup>

This is the result of the logic of efficiency: justice becomes a mechanism of efficiency while morality is reduced to a question of pragmatism: How can we ensure that market forces work to price things fairly? This is the variety of justice to which we subscribe when commit to the spurious belief that everything of value can be priced appropriately by market efficiency.

In his treatment of commutative justice Duns Scotus recognizes that there is an indeterminate, yet real, component of gift (*donatio*) necessary in order for a transaction to be free and beneficial, and therefore sustainable in a market economy:

For among men it is hard for contracts to exist where the contracting parties do not intend to set aside something of that exact or indivisible justice owed to one another, so that to some extent a donation accompanies every contract.<sup>14</sup>

This donation or gift is not an unintended accident of the economic trade, but rather is an intentional gifting of one to the other, in recognition of the cardinal value inherent in the

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<sup>13</sup> Benedict XVI, *Caritas in veritate*, sec. 35, emphasis original.

<sup>14</sup> John Duns Scotus, *Political and Economic Philosophy*, trans. by Allan B. Wolter (St. Bonaventure, New York: The Franciscan Institute, 2001), p. 47.

relationship, and in witness to the command, “*do unto another as you would wish done to you*”.<sup>15</sup>

## Circular Logic

In the absence of the redeeming context for the evaluation of economic outcomes as provided by the theological understanding of *caritas*, efficiency in the sense of Pareto optimization stands in for theology as the sense-making context. Pareto optimality seems to provide a coherent logic: Justice demands fairness. Fairness results from efficiency. Efficiency therefore leads to justice. The problem is that this is circular logic built upon spurious presumptions.

M. Douglas Meeks has a keen eye for what has happened to our concept of morality within the modern market economy:

Market forces, then, are said to be automatic, unconscious, mechanistic, and unintended. As such, the market can take the place of state and church and even the family . . . . Naturally, the God concepts that provided these institutions with authority systems could also be replaced. The coherence of the system is derived not from tradition or command but from the unintended outcome of self-interested, self-guided activities of individuals. Taking on the character of necessity and inevitability, economic law could seemingly fulfill all public functions that “God” had previously performed. The market, were its law obeyed, promises a free and harmonious way of integrating and coordinating society without authority and coercion.<sup>16</sup>

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<sup>15</sup> Ibid.

<sup>16</sup> M. Douglas Meeks, *God the Economist: The Doctrine of God and Political Economy* (Minneapolis: Fortress Press, 1989), 51ff. Harvey Cox makes the same point with biting and

The fair and efficient operation of the market thus becomes the new theology of capitalism. It becomes the ground and being of not merely the power of production, but of justice and morality as well. Pragmatism overcomes transcendence. That is the unfortunate and self-contradictory conclusion of the quest for efficiency. It is also the fatal undoing which makes markets unsustainable and brings them to the brink of collapse. This is why free markets require a healthy dose of *caritas* if they are to survive.

The logic of *caritas* (that is, the principle of gratuitousness) transforms the econometric concept of efficiency in the marketplace and makes the market sustainable. The logic of *caritas* restores the crucial element of humanity which is otherwise washed away by the quintessential ideal efficiency. By incorporating the logic of *caritas* into the fundamentals of exchange, human relationships are sustained and restored.

This is the decidedly different concept of human dignity, which flies in the face of conventional wisdom regarding *Homo economicus*. In *Caritas*, Benedict XVI reminds us that human dignity is ultimately grounded in a transcendent vision of the person, and not in a pragmatic view of the person as contributor to economic transactions:

[I]ntegral human development is primarily a vocation, and therefore it involves a free assumption of responsibility in solidarity on the part of everyone. Moreover, such development requires a transcendent vision of the person, it needs God: without him, development is either denied, or entrusted exclusively to man, who falls into the trap

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convincing satire, pointing out that “the religion of The Market has become the most formidable rival [to traditional religions], the more so because it is rarely recognized as a religion.” Harvey Cox, “Market as God: Living in the New Dispensation,” *The Atlantic Monthly*, March 1999.

of thinking he can bring about his own salvation, and ends up promoting a dehumanized form of development.<sup>17</sup>

The idea of *Homo economicus* upon which econometric models are built leaves out the essential aspect of relationship in which human dignity is found. The essence of human dignity derives from the mystery of relationship with God. The transcendent vision of the person as one in relationship with God is also the foundation of relationship with one's neighbors. The transcendent vision of relationship therefore is also the basis for proper understanding of the role of the person in economic activity, as well as the purpose of the market. To arrive at a coherent description of society, whether in politics, economics or any other realm, requires a transcendent vision of the human person as being created for, and existing within, relationship with God. This requires a doctrine of the whole person, the integrated self, as existing in relationship with God.<sup>18</sup>

The mystery of relationships, between persons and in communion with the Triune God, is an essential foundational good which permits the market to operate in the first place. A market which exists only to serve itself will eventually collapse under its own weight because the relationships which support it will wither and die. We can see the warning signals of this dire cycle in the growing inequality of economic opportunities and wealth. The wealth-producing capacity of capitalism is, of course, a boon to human flourishing. Wealth can bear fruit in the form of a virtuous cycle that generates more economic opportunity and creates more customers to be served. But if that wealth is applied only to the goal of self-

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<sup>17</sup> Benedict XVI, *Caritas in veritate*, sec. 11.

<sup>18</sup> John D. Zizioulas surveys the theological development of this insight: Zizioulas, *Being as Communion* (London: Darton, Longman & Todd, 1985), 18.

preservation and self-magnification, in a winner-take-all game of efficiency, the winner will eventually be the only one left standing, and the market will cease to exist.

*Caritas* offers the antidote to this dire prospect, by offering a transcendent view of human dignity as the *telos* of economics.<sup>19</sup>

Economics rested upon a foundation of concern for the greater *telos* of human society for millennia. It is only in the modern era when the practice of economics began to claim status as an academic discipline severed from questions of morality, that these false presumptions have become problematic. The rubric of “political economy” lasted into the twentieth century, consistent with the attempts of philosophers from Aristotle to J.S. Mill (1848) to work out the ethics of good government.<sup>20</sup> Dirksen (1946) grasps the nettle when he calls out the inescapable need for any and all economists to build their theories of economic behavior upon some underlying ideas that presume to know something of human nature:

...every economist accepts certain basic characteristics of human nature which is nothing else than accepting a certain philosophy of man. Whether he accepts one set

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<sup>19</sup> I have addressed this theme elsewhere in: Baker, “Human Dignity and the Logic of *Caritas*: the Source and Direction of Economic Justice”, *Verbum Incarnatum : An Academic Journal of Social Justice*. Issue Theme: Economics and Social Justice. Volume 5, #1, 2012, pp. 1-22.

<sup>20</sup> Turn-of-the-century treatises on “political economy” include: Wicksteed, P.H. (1933[1910]), *Common Sense of Political Economy*, London: Macmillan; and Marshall, A. (1946[1890]), *Principles of Economics*, London: Macmillan.

of characteristics or another doesn't matter; he is dependent upon some kind of philosophy of man.<sup>21</sup>

When the deeper significance of human relationships is removed from consideration, economic transactions become amoral; that is, devoid of moral content. This has sad consequences for the modern moral imagination. The bond is broken between economics and higher order understanding of morality based in spiritual goods. This leads to a loss of consideration for personal, I-thou relationships in the study of economic transactions. Bruni and Zamagni have diagnosed the situation accurately in their call for reform, to help reinstate appreciation of civic-minded responsibility as an explicit virtue of political economy:

Economics became a science relegated strictly to the economic sphere in accordance with the *homo oeconomicus* paradigm to explain human action, while sociology as a science was confined to the social sphere and the *homo sociologicus* paradigm.<sup>22</sup>

Deprived of its psychological and social complexities, the definition of human nature was transformed into a caricature that lent credibility to a double error.<sup>23</sup>

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<sup>21</sup> Cletus F. Dirksen, "The Catholic Philosopher and the Catholic Economist", *Review of Social Economy* 4, no. 1:14-20 (1946), 15. I am indebted to O'Boyle (2007) for this pertinent reference to Dirksen. Cf. Sedláček's (2011, p. 231) comment on this modern state of affairs: "Economics in general has been surprisingly uncommunicative with the ethical sciences it originated from."

<sup>22</sup> Bruni and Zamagni, *Civil Economy*, pp. 130-31

<sup>23</sup> *Ibid.*, p. 132.

The logic of *caritas* is an essential ingredient to bring about this reform. *Caritas* is, after all, a foundational good which pertains to I-Thou relationships. *Caritas* is a spiritual reality which imbues transactions with moral significance by recognizing the transcendent value of the other person. The logic of *caritas* is the cathartic antidote to reductionist utilitarian thinking.

### **A Transformational Concept of Efficiency**

The logic of *caritas* is the catalyst that transforms the conventional wisdom about efficiency. *Caritas* rescues economics from the tyranny of efficiency construed as *summum bonum*. When *caritas* is recognized as a foundational good in the free market, efficiency can no longer be discussed mere in the language of econometrics; instead, it comes to be viewed within the more holistic realm of relationships of transcendent value.

Of course this flies in the face of conventional wisdom, and will be rejected as *prima facie* foolishness whenever and wherever the presumptions of the conventional wisdom are permitted to linger silently beneath the surface of economic discourse. The conventional wisdom presumes to have an answer to this foolishness: by insisting upon value-free concepts, the hypothetical ideal of a perfectly efficient market becomes the embodiment and final arbiter of value. This insistence is grounded in the belief that value-free market transactions are the only way to make progress. But what is “value-free” about such a market system? Value has been tacitly imputed to efficiency as the definitive arbiter of “good”. The logic of *caritas* transforms this concept of efficiency by offering a more robust and more realistic understanding—albeit messier and trickier to analyze—that good and evil exist, and that political economics can both help and harm humanity in ways that elude the antiseptic



presumptions of “scientific asceticism” claimed by proponents of the conventional wisdom.<sup>24</sup>

Bruni and Zamagni see the issue clearly:

We do not identify ourselves with this type of scientific asceticism because, ... we feel that scientific reason can serve a function in the foundation of values, and that values and scientific knowledge are not necessarily mutually opposed.<sup>25</sup>

How then shall we proceed toward the transformation necessary for a more robust understanding of efficiency? How shall we act so as to embody and nurture the logic of *caritas*? The first step is to realize that this will remain forever an ongoing challenge, and that there are no definitive prescriptions. The struggle against the power of Mammon will go on and on until the new heaven and new earth are come. Our present struggle is to recognize the transforming power of *caritas* and to devise ways to build it into our political economy. Benedict identifies this as the fundamental issue with the transformation of economic power and sustainability of global markets:

The great challenge before us, accentuated by the problems of development in this global era and made even more urgent by the economic and financial crisis, is to demonstrate, in thinking and behaviour, not only that traditional principles of social ethics like transparency, honesty and responsibility cannot be ignored or attenuated, but also that in *commercial relationships* the *principle of gratuitousness* and the logic of gift as an expression of fraternity can and must *find their place within normal*

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<sup>24</sup> Hans Jonas, *Il principio di responsabilità: un'etica per la civiltà tecnologica*, trans. By Pier Paolo Portinaro (Torino: Einaudi, 1990), 142.

<sup>25</sup> Bruni and Zamagni, *Civil Economy*, p.15.

*economic activity*. This is a human demand at the present time, but it is also demanded by economic logic. It is a demand both of charity and of truth.<sup>26</sup>

To the extent that economic market power is deployed in the spirit of *caritas*—that is, in the spirit of contributing to the common wealth—then macroeconomic theory has much to gain by relying upon the transformational concept of efficiency in view. When the spirit of *caritas* is absent, however, or the logic of *caritas* becomes broken, then efficiency no longer serves as a trustworthy guide toward the aims of society. The invisible hand can become a harmful and illegitimate taskmaster if cut loose from the moral wisdom of the society which seeks to benefit from it.

To illustrate these concepts and propose constructive steps forward I will examine three specific emerging business developments: (1) patents related to pharmaceutical drug design and marketing; (2) “monetization” strategies in recent internet-based business models; and (3) synthetic financial instruments, such as derivatives. In each of these three test cases, I will apply the logic of gratuitousness (*caritas*) to distinguish between potentially additive and extractive economic activities, and then propose systemic mechanisms to enhance the solidarity-enhancing aspects of these businesses.

## **Pharmaceuticals and Patent Cliff Avoidance**

Patents are a two-edged sword. The rationale is for them is simple enough—to encourage beneficial innovations by granting monopoly power to inventors who might otherwise decide not to risk the time, effort and resources required to develop new products. Patents work by imposing artificial constraints upon an otherwise free market. The whole rationale for them is based in the belief that the efficiency of the market is not capable of

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<sup>26</sup> Benedict XVI, *Caritas in veritate*, sec. 36, emphasis original.

bringing about the greatest common good for society. The upside is to bring about helpful innovations. When patents work as intended, the logic of *caritas* is fulfilled because the economic engine is harnessed to bring a boon to society. This is the proper, “additive” function of trade in patented products.

The downside of patents occurs when their power is abused by using them as a means of extortion through artificially inflated pricing and profits. This would be an “extractive” use of patent power. To the extent that patent power is used as a means of artificially shifting any social surplus to the supply side, transactions for the products in question will suffer from lack of consideration for the betterment of customers and society at large, which will be the outcome of transactions devoid of *caritas*.

To illustrate the extractive effects which can ensue from this misapplication of market power, we look to the example of Pfizer and their business strategy regarding Lipitor, the best-selling drug of all time and the cash cow which helped to make Pfizer the world’s largest pharmaceutical company. Pfizer is estimated to have sold over \$100 billion worth of Lipitor. The drug has accounted for a quarter of the company’s profits during most of the past 15 years. Pfizer’s successful business strategy of creating and sustaining a dominant position in a highly profitable market is admirable and has brought real benefits to society through innovation and successful marketing. These outcomes are not the focus of my critique. My concern regards Pfizer’s efforts to construct additional barriers to entry in search of cartel power exceeding the scope of the seminal patents on Lipitor. These actions beg the question of whether the corporate strategy has drifted into extractive transactions.

Pfizer faced what is known in the industry as a “patent cliff”, meaning that when its patent expired in 2010, Pfizer’s profit margin would dive as generics rushed in to sell cheaper versions of the identical chemical compound, *atorvastatin*.

The entry of generic versions into the free market would presumably be a benefit to society, and certainly to the patients taking the drug, as the price would be expected to fall from \$3 per dose to less than \$1 as competitors established themselves. This restoration of a market-driven price for a hugely valuable product would serve to bring an additive component of *caritas* back into the transaction, in that the customers and society at large would be receiving a greater benefit with every dose.

However, this was not quite how this story played out. Pfizer adopted aggressive strategies to extend the patent protection on Lipitor by filing hundreds of additional patent applications in an attempt to concoct new claims on the drug's usage, and thereby to continue to reap the extortive prices they were receiving by locking the generics out of the market. Since 1998, these applications have yielded 171 new patents for Pfizer mentioning Lipitor and and/or *atorvastatin*.<sup>27</sup> The huge investment in patent filings was financially justified by the even greater profit potential for the drug—but at what cost to society?

Pfizer did not stop with the flood of patent applications. They also negotiated private deals with generic drug manufacturers to secure their agreement to stay out of the market for several months. In addition, during the year leading up to the patent cliff, Pfizer was aggressively “forging deals with insurers, pharmacy benefit managers and patients to meet or beat the price of its generic replacements.”<sup>28</sup> This was in effect an attempt to establish a cartel. These marketing tactics were investigated by the Federal Trade Commission, but to date the FTC has taken no legal action.

On the patent front however, Pfizer was successfully able to extend their monopoly on Lipitor for several months beyond being the originally expected expiration date by appealing

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<sup>27</sup> Based on my research of the U.S. Patent Office database, conducted during July 2012.

<sup>28</sup> Duff Wilson, “Facing Generic Lipitor Rivals, Pfizer Battles to Protect Its Cash Cow,” *New York Times*, November 29, 2011.

previous decisions of the Patent Office, and by negotiating settlements with competitors. The company delayed the introduction of a generic version of Lipitor by Ranbaxy Laboratories of India by up to 20 months later than many analysts had been expecting, according to the *New York Times*.<sup>29</sup> A key factor in Pfizer's strategy was to threaten patent enforcement of their monopoly into 2017.<sup>30</sup>

The ability to extract profits through patents has created an economic incentive for the practice of "patent trolling", in which businesses are created for the sole purpose of acquiring patents that can be then be used to threaten other companies and extract profits from the sales of other companies' revenues:

Rogue patent trolls (law firms) can buy sleeping patents (patents that have not yet been used to bring products to the market) at a low price, and then when a firm is successful in the same field, claim trespass, and threaten to shut it down as a form of extortion.<sup>31</sup>

Patent trolling might be seen to be a business strategy motivated by the desire to benefit from extractive transactions. The logic of *caritas* might transform these methods if there were a way to evaluate the justice issues on the basis of the impact on the persons affected most directly, rather than on the basis of the income statement of the patent owners.

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<sup>29</sup> Stephanie Saul, "Release of Generic Lipitor is Delayed", *New York Times*, June 19, 2008.

<sup>30</sup> *Ibid.*

<sup>31</sup> Joseph E. Stiglitz, *The Price of Inequality* (W.W. Norton & Co., 2012), 203.

## Monetization of Internet-Based Technologies

Due to the rising tide of Internet-based business opportunities, the monetization of personal data has become a driving force. In order to attract users, Internet-based services are frequently offered *gratis*, at no cost to users. Google of course has been the bellwether, the first company to earn large, continual profits by monetizing their access to consumers in the mass-market. At first glance, the “free” price of Internet offerings might seem to be aligned with the principle of *caritas*, gift or grace. Indeed, it is true that the free access to these services conveys a gift to society at large. There is a positive additive effect here, because access to information, goods and services contributes to the overall stability and sustainability of markets. The lesser-known and potentially extractive nature of these transactions however also deserves to be noticed. After all, “there is no such thing as a free lunch.”

In order to make a profit and create a sustainable business model, these companies must devise a scheme to “monetize” their access to users. In simple terms, this amounts to manipulating and selling access to the people who have taken advantage of the free services. As Google, Facebook and countless others have discovered, monetization typically takes the form of targeted advertising, based in data-mining technology.

This new industry of data-mining exists for the purpose of digitizing, analyzing and manipulating the human behavior represented by data gleaned from users’ interactions. Some of the most powerful companies in this field value their obscurity, and operate with as much anonymity as possible. These include Acxiom, eBureau, Epsilon, ChoicePoint and TargusInfo—all names that remain generally unknown by the people whose personal data they harvest. While these purveyors of Big Data might prefer to remain invisible and avoid public scrutiny, their customer set includes almost every brand name in the consumer, financial and industrial markets. The whole purpose of these data-miners is to glean profitable predictions of human behavior based on the accumulation of vast amounts of data

on individuals. Axiom is one of the biggest, with over 23,000 computer servers harvesting data on half a billion people, and processing some 50 trillion data transactions per year.<sup>32</sup> The company has revenues of more than \$1 billion per year, and is poised for rapid growth.

The question at hand is whether this sort of monetization tends to develop in generally additive or extractive directions. This is not a critique of advertising; rather, the issue is whether monetization leads potentially into extractive transactions. My conjecture is that this can be the case. The reason for concern is that the drive to monetize relationships leads to tactics that treat users as data rather than as persons. This can lead to business strategies based in the premise that the personal data of users is an asset to be mined for value, without concern for the human dignity of the individuals represented.

The drive to monetize users' data replaces relationships with transactions. From a business point of view, this means that value resides in the power to monetize a relationship. Persons can thus be treated as commodities. We see this in such rubrics as "net promoter score", a measure of the potential profit a business may expect to glean from any given customer's buying habits and socioeconomic metrics. Since datasets do not carry the same ethical responsibilities as real persons, the logic and spirit of *caritas* is easily neglected.

The financial pressure to take advantage of access to personal data is not a trifling matter. Nonetheless, ethical businesses can strive to protect the individual freedom of their customers by avoiding manipulative tactics that seek to monetize customers without their consent in the bargain.

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<sup>32</sup> Singer, N. (2012). "A Data Giant is Mapping, and Sharing, the Consumer Genome", *New York Times*, 17 June 2012.

## Synthetic Financial Instruments

Business models based in synthetic financial instruments, such as credit default swaps, derivatives and mortgage-backed securities carry a similar risk of replacing relationships with transactions and data analysis. The individuals whose finances are being put at risk end up being treated as commodities rather than as real persons.<sup>33</sup> We have recently experienced the dire and destructive down-side of extractive transactions such as these in the “near-death experience” of our global economy.<sup>34</sup> When moral commitment is eroded, and profit maximization trumps solidarity, the market will eventually suffer the consequences, as Joseph Stiglitz observes:

We have gone far down an alternate path—creating a society in which materialism dominates moral commitment, in which the rapid growth that we have achieved is not sustainable environmentally or socially, in which we do not act together as a community to address our common needs, partly because rugged individualism and market fundamentalism have eroded any sense of community and have led to rampant exploitation of unwary and unprotected individuals and to an increasing social divide.<sup>35</sup>

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<sup>33</sup> Some of the following remarks come from my essay, “Human Dignity and the Logic of *Caritas*: the Source and Direction of Economic Justice”, in *Verbum Incarnatum : An Academic Journal of Social Justice*. Issue Theme: Economics and Social Justice. Volume 5, #1, 2012, pp. 1-22

<sup>34</sup> Joseph E. Stiglitz, *Freefall: America, Free Markets, and the Sinking of the World Economy* (New York: W. W. Norton & Co., 2010) 275.

<sup>35</sup> *Ibid.*, 275f. Cf. M. Kelly, “Not Just for Profit”, *Strategy+Business*, Booz & Co., Inc., Feb. 6, 2009—“The financial meltdown of 2008 was a direct result of the pursuit of immediate



Stiglitz diagnoses the problem with insight, noting how the extractive transactions erode sustainability and contribute to inequality.<sup>36</sup>

The logic of gratuitousness (*caritas*) was missing in the market forces which led to the near-death experience of the global economy. The system was unsustainable, yet bankers kept extracting profits so long as the music kept playing, as one put it infamously. These business models led the global economy down the slippery slope of profit maximization, because the logic of *caritas* was absent. *Caritas* would place a value on the human dignity of borrowers, but those considerations did not enter into the calculations of risk and profit. The invention and deployment of new derivative instruments removed human relationships from the business models of lending, and focused instead on the merely mathematical equations of arbitrage. To use the biblical example of gleaning, it was as if every last scrap of grain was harvested, and the dust of broken husks also was swept up from the threshing floor and packaged for sale wherever the slightest profit could be earned. Bonuses for the winners of the game were similarly maximized. All profits were sucked out of the system, and nothing was given back. It's easy to see in hindsight, of course, but how do we prevent these excesses in the future? Solutions to these problems can be found on a case-by-case basis, and they will invariably embody the logic of gift, to whatever extent possible, and will thereby bear witness to human dignity.

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profit by investment bankers and mortgage brokers who disregarded the impact of their actions on customers, on the larger economy, and indeed on stockholders and the company itself in the long term.”

<sup>36</sup> Joseph Stiglitz, quoted by Thomas B. Edsall, “Separate and Unequal”, *New York Times*, August 5, 2012.

## Conclusion

The logic of *caritas* provides the corrective needed to recognize where and how the forces of economic efficiency are conducive to the health and sustainability of a market system, and where they are not. The beneficent power of the market to serve human flourishing is based not in a morally tacit economic efficiency as a cardinal good, but rather in a gift-bearing efficiency aligned with *caritas*.<sup>37</sup> This latter is the only type of efficiency which generates and enhances sustainability in the free market.

To the extent that economic market power is deployed in the spirit of *caritas*—that is, in the spirit of contributing to the common wealth—then macroeconomic theory has much to gain by relying upon the transformational concept of efficiency in view. Conversely, when the spirit of *caritas* is absent or the logic of *caritas* becomes broken, then efficiency no longer serves as a trustworthy guide toward the aims of society. The invisible hand can become a harmful and illegitimate taskmaster if cut loose from the moral wisdom of the society which seeks to benefit from it.

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<sup>37</sup> John Paul II draws the connection between human dignity and market freedom: “No free economy can function for long and respond to the conditions of a life... unless it is supported and “enlivened” by a strong ethical and religious conscience...” (*Gaudium et Spes*, n. 24). Cf. ‘A Civilization of Solidarity and Love’: An Invitation to *Centesimus Annus*, section 5.

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