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CAPITALISM'S TOUGH SKIN

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Chief Richard Akinjide, CON, SAN, FCI Arb (U.K), FCE is a **Member** of the **Bar** of **England** and **Wales** with **Chambers** at **9 Lincoln's Inn Fields, London WC2A 3BP.** He practises also at **The Gambian Bar.** He specialises in **Oil and Gas, Companies and Banking Matters, Mergers and Acquisitions, Shipping, International Commercial Arbitration and International Law.** He is a **Fellow of the Chartered Institute of Arbitrators, United Kingdom (UK).** He took **Silk** in **Nigeria as a Senior Advocate on January 12, 1978** and was **Called** to the **Nigerian Bar** in **March 1956. Member of Nigerian Federal Parliament 1959- 1966,** Member of the **International Law Commission of the United Nations in Geneva from 1981 – 1986, Federal Minister of Education 1965 -1966. Attorney-General and Minister of Justice of Nigeria 1979-1983.** He is the author of the **2nd Edition** of **"Africa** and **The Development of International Law"** published by **Martinus Nijhoff** at **The Hague, The Netherlands (1988)** and selling worldwide. **Pro-Chancellor and Chairman of Council of the University of Jos 1976-79.**

He is an **active** member of the **Association of International Petroleum Negotiators (AIPN)** in **TEXAS, United States of America (USA).** Cases he handled are reported in various **Law Reports in Nigeria, England, The Gambia** and in **International Law Reports.**

He represented **Nigeria** as the **Co-Agent** and a **Counsel** in the case **Cameroon v Nigeria** at **The World Court, The Hague** for **about 8 (eight)** years involving **International Boundary Dispute from Lake Chad to The Atlantic Ocean.** He was a member for **four (4) years** of the team of **International Jurists** that drafted **The Law of The Sea-Convention** otherwise known as **"The Constitution of The Sea"** which is the **biggest Convention** ever sponsored by the **United Nations (UN).**

Chief Richard Akinjide signed that **Convention** and **The Final Act** on behalf of **Nigeria at Montego-Bay, Jamaica. Publications** of **AKINJIDE & CO series** which started with **"Advocacy, Ethics and The Bar"** have now reached **41 (forty-one)** issues and circulates world-wide. **Chief Richard Akinjide** established trusts in the **Universities of Ibadan, Jos and Cambridge (England) and the Nigerian Law School for Annual Prizes** in **Law. Five (5) of his children read law. Chief Richard Akinjide** was the **President** of the **Nigeria Bar Association (NBA) 1970-1973** and past

Chairman of the **Nigerian Body of Benchers** and **a** past **Member of the Council of Legal Education. Was a visiting Lecturer** for the **LL.M Programme** in the **Alternative Dispute Resolution, International Commercial Arbitration etc at the University of Ibadan. Awarded Commander of the Order of the Niger (CON) in 2002. Distinguished Fellow of the Nigerian Law School.** Honoured as **Fellow** of the **Babcock University Circle of Eminence (FCE) in 2007. He travelled extensively in all the continents of the world. He reads widely outside law.** He is **a collector** of **Works and Arts in Nigeria, Europe** and **USA.**

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CAPITALISM'S TOUGH SKIN

By: Chief Richard Akinjide, CON, SAN, FCI Arb. (U.K), FCE.

The most prominent ideological conflict of the twentieth century was undoubtedly the political battle between capitalism and socialism. **Socialism, the powerful doctrine of Marx and Engel which predicts capitalism's self destruction by lack of outlets, became a mode of government at the beginning of the 20th century when Lenin notoriously prophesized "we shall give them the rope they'll hang themselves with", meaning that greed would ultimately be the cause of capitalism's death.**

Although the prediction made some sense, it is socialism which did not survive the 20th century. As early as the late 1960s, it became clear that Soviet Union was on the road to collapse, the only unknown being then. The late 1980s and the 1990s finally proved all doomsday prophecies about the inexorable extinction of capitalism wrong: it is Soviet Union which collapsed, the Berlin wall which fell, the Russian economy when frantically liberalized and the doctrine of economic laissez-faire which triumphed. At the dawn of the 21st Century, capitalism was the only king left.

Then 2008 came.

When at the end of last year it became clear that a severe crisis which had started as a result of increasingly risky speculations originating from the American banking sector, would not only spread the world over but will also prove very costly, voices were heard at the highest level of governments sentencing capitalism to death. This excess in speculative activities, it was forcefully said, was intolerable and should be stopped; never again such speculative utterances should be permitted. Societies must get rid of speculation and speculators. **Would the end of speculation also mean the end of capitalism?**

Because there was no other way out, world governments came reluctantly, but frantically and massively to the rescue first of ailing banks then of collapsing businesses, thereby revisiting the methods of interventionism and burying the corpse of economic liberalism. General Motors became Federal Motors – a development yet unseen in the economic history of the US. Traders were jailed. Strong political statements were proffered against the inhumanity of capitalism. People rebelled against capitalism's fallen angels: golden parachutes, performance – related bonuses and stock options. Even the Financial Times, the bible of capitalists, published stories promoting moral values reminded us that before he wrote **"The Wealth of Nations" the great economist Adam Smith – the founder**

of economic liberalism – published "The Theory of Moral Sentiments" which extensively investigates the powerful role of non-profit values. Due to unexpectedly large demand, Adam Smith's book, as well as Karl Mark's "Das Kapital", was being reprinted. It was planned to sell more copies of them both than had been the case in the past twenty years.

Perhaps the most fundamental criticism that was then proffered against capitalism was that the financial sector of national economies was not only prospering to the detriment of their real sector (agriculture, industry and non-financial services) but was also, when financial crises occurred, the direct cause of real sectors' depression.

The outlook was unequivocally grim: added to a background of environmental degradation, communism had collapsed and capitalism did no longer work. **That left observers of economic matters wondering: was there any yet unknown politico-economic system that could prevent crises once and for all; that could make everyone better of; that could eradicate poverty; that could establish social justice; that could give a job to everyone willing to work; that could keep our environment safe and clean?**

Nobody had an answer, simply because there is no answer.

In the meantime, the strongest among ailing banks quietly went to work to put their affairs in order. Others died: survival of the fittest. The strongest among ailing businesses adjusted as they always do: by cutting less profitable activities and suppressing jobs. Others died: survival of the fittest. Those who lost most as a result of the prevailing crises were, as always, those who having been caught short, proved unable to avoid the collapse as well as job seekers and the salary earners made redundant.

Today, **a year after the collapse of Lehman Brothers,** while in most countries the real sector remains depressed, while in most countries economic growth remains in the red (there are some notable exceptions), while everywhere unemployment continues to grow, banks which have survived are bigger and stronger (they swallowed the failed ones), their profits are back, the money they borrowed from governments has been or is being refunded, traders are actively sought after and provisions are again made to distribute large performance bonuses to the most deserving among them. The so much publicized regulation of financial markets which threatened to be unforgiving now looks milder – to say the least – than was planned a year ago. As always, pragmatism and real politics prevail.

Speculation, the great evil of yesterday, has regained nobility. Why? Because it is no longer through their traditional activity, savings and loans that banks are making money and are getting out of the red: these are yesterday's top profit makers. It is rather through speculation on a diversity of markets that banks are generating profit again. And because it is from profits drawn from market speculation that banks will eventually derive surplus funds to fuel the recovery of the real sector, governments are no longer that vocal against the utterances of capitalism.

As in all matters of human activity, history is a great teacher.

In 1944, 700 representatives of 44 nations met at the Mount Washington Hotel in New Hampshire to map out a new economic order for the post war world. Bretton Woods, the international monetary system and the conferees agreed upon, basically established a fixed relationship between currencies and recognized the leading role that the US dollar would play in the scheme as it was then undisputable that the United States had become the world's foremost economic power, holding two-third of the world's gold reserves and being the only country whose production capacity had been untouched by the war.

The Bretton Woods system did not make currency trading a very exciting activity. Banks bought and sold currencies on behalf of customers at official rates with little room for creativity. Occasional crises here and there presented profitable trading opportunities but they were not frequent enough to support a permanent business. **In 1976, J.P. Morgan hired fifty new staff from its training programme and only one chose to go into trading. Then young bankers with good prospects and valuable connections aimed at commercial lending jobs, the royal road to upper management functions.** Was not real banking a matter of arranging loans for important corporations?

But the world of finance had already begun its in-depth transformation. Because of its excessive rigidity in a context of rapidly growing world economies, Bretton Woods, after many hiccups, had finally collapsed resulting in inflation, volatile interest rates and currency turmoil. Banks were now finding it more difficult not only to source lendable money but also to arrange corporate loans: loan seekers could borrow directly from investors in the new commercial paper markets and depositors were offered higher returns elsewhere. As banks' traditional activities became less profitable, it was also becoming clear that taking risks in the financial markets could replace corporate lending as a major source of revenue.

It is from this time – the mid 1970s – that the impact of the financial sector's transformation on world economies is said to have been as deep and strong as that of the discovery of nuclear energy in physics. It is from this time that the revolution in finance turned banks into organizations for disbursing no longer funds but risks: the risks of interest rate movements, currency shifts, stock market booms or busts. When markets are stable and predictable, as it was mostly the case under Bretton woods, bank prosperity depends upon the availability of funds. When markets become uncertain and volatile, as it has been mostly the case in the past three decades, bank prosperity depends upon taking and managing risks. **The keyword here is volatility, a measure of the variability of the price of anything over time.**

The Philadelphia exchange, the oldest organized stock exchange in the United States, was moribund in the late 1970s when a staffer invented a new product: the currency option. An option is the right to choose whether or not to buy or sell something for a specified price at a specified time. Options exist on a variety of products – currency, equity, future contracts, swaps, etc. As such, options are traded on exchanges and in the inter-bank market. Options are a key product in the international network of financial power.
They have over time, made many billions of dollars. It was said that not since the invention of paper money had financial history seen an innovation with such an impact. Unquestionably, options were the most powerful and versatile of the financial tools then developed by private markets to face increasing economic uncertainties.

Yet the concept of options is as old as the civilized world. Peter L. Berstein's Capital Ideas: the Improbable Origins of Modern Wall Street (New York, Free Press, 1992) explains that the first option was invented by the Greek Philosopher, Thales of Miletus. Mocked for his poverty, Thales decided to show scorners that he was poor by preference, not by inability. He read the stars, analyzed the weather and concluded that a copious crop of olives should be expected for the year. Before the fruits began to form, he offered all owners of olive presses to pay them in advance for the right to rent their presses at harvest time if he should need them. He did not have to pay the rent immediately. He just paid a one-time fee for the right to rent. Also negotiated in advance was the rent he would pay should he decide to rent. Thales was lucky that he negotiated the rent well in advance of the crop at a time when no one else foresaw the great demand for presses that would result from an abundant crop at harvest time. As harvest proceeded, Thales paid the rent he had promised to pay but, because he controlled all the presses, he charges the olive growers whatever he pleased for the ability to use the presses and produce olive oil, hereby making a handsome profit.

If Thales had been unlucky and the crop had failed, he did not have to rent the presses. He would just have lost the one–time payment he made to purchase a right. Thales acquired the right to speculate on the renting cost of presses without having to pay the rent.

Speculation is not the only reason why people bet about the future. **Another reason is to hedge, that is, to make a financial commitment that protects against adverse changes in the cash flow from an operation.** This is the job of futures. Economists have long known that the engine of growth is trade and particularly, international trade. The development of international trade heightens the need for international investors and business people to buy and sell currencies which they often do for future delivery. And American company selling a large consignment to a customer in Germany is likely to be paid in euros. In order to turn the euros into dollars, the American Company, knowing when the euro payment will be effected, makes an agreement with its bank to buy euros forward. This agreement obliges both the bank and the company to exchange dollars for euros at a given price and a given date.

From these older investment tools – options and futures – traders have in the past twenty years, developed new derivatives markets with the astounding power to generate huge profits from small investments (and great risk taking) while also revealing the vast damages that such risk taking can cause. **In 1987, Andy Krieger, who alone reportedly created panic at New Zealand's central bank when he sold the money of that country short, earned US$300 (Three Hundred United States Dollars) for Bankers Trust Company. In 1988 the same Krieger, betting that Britain would register a huge trade deficit, began to borrow pounds and sell them for another currency.**

If his intuition was correct he would buy pounds back at a lesser price (he would get more pounds for the same amount of the other currency he had initially exchanged for pounds) repay his loan and pocket the profit. He has sold 900 million pounds when it was announced that Britain's trade performance had in fact been much better than expected. This caused the pound to appreciate. **But Krieger did not cut his losses. He doubled his bet continuing to borrow and sell until he had sold almost 2 billion pounds. It is reported that some of Krieger's colleagues fell sick when they saw the amount of risk he had taken.** In the meantime the pounds kept appreciating. Then, the Bank of England, fearing that the pound was moving too far too fast, began to sell pound. As a result the pound fell. When it reached a level that made Krieger pocket a healthy profit, he bought a billion pounds back (the story does not say what profit he made). This caused panic and chaos in trading rooms. The pound rose sharply as a result of such a massive demand from one trader. The bank of England fought the surge pushing more and more pounds on the market to keep the currency stable. But Krieger had done his trade, pocketed his profit and could not care less about the chaos he had caused.

Andy Krieger is not the only trader to have written the tale of the golden boys. George Soros in 1992, drew international press attention to hedge funds by making a billion dollars in a few days when Britain withdrew from the European Monetary System (EMS). Nick Leeson in the 1980s led Barings, Britain's oldest merchant bank, first to riches – Leeson's bets in Japanese bonds and Nikkei futures provided almost a third of the bank's total revenue – then to collapse when he bought enough future contracts to cause over 1.5 billion pounds in losses to a bank who could never recover and was later acquired by Holland's ING for one pound or US$1.6 at the then current exchange rate. In a strikingly similar context, in 2008, a young French trader led Societe Generale to a loss of some 5 billion euros later resulting in the resignation of the bank's president. In both cases, alarm had been earlier raised and warning proffered about the absence of control on traders' activities; to no avail.

Every institution which populates the private world of capitalism is driven by profit optimization. Trading and investment only require a small proportion of banks' staff force, perhaps 10 or 20 percent, but make as much money as the balance of it. At that level of reward, the risk is worth taking.

Capitalism has a tough skin. Once more, the rope that was supposed to hang it broke before any lethal damage has been done to victim. Many of the most vocal critics of the latest crises of capitalism have disregarded history. They have forgotten that crises of capitalism are not a new historical event but have repeatedly occurred since the 17th century. They have always unraveled, with more or less damages the way they did in this most recent occurrence and they have never so far sentenced capitalism to death.

Why is capitalism so resilient? The answer is in all economics textbooks. The one behavioral standard that is constantly found behind the entire theoretical edifice economists have constructed over the years to explain human economic activity is not moral; neither is it virtue or kindness. It is self interest and its inseparable companion - greed. No matter how regrettable such a down-to-earth reality may appear to some, **greed is here to stay because it is a much greater driving force of human endeavor than spirituality, selflessness or generosity.**

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October 2009