The Sovereign Economic Model© (SEM) : some ideas

A White Paper

by

SOVECOMO Consulting (http://www.sovecomo.com)

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In memory of Jon Hellevig (RIP 2020).

Abstract

This white paper - manifesto lays out ideas for the Sovereign Economic Model©, a way for countries to run their national economies. It is a step back from globalization, partially back into 20th century economies, where most countries had state led economies and many – France, South Korea, China became strongly advanced nations, and in part a step forward to create a strong, resilient and sovereign economy. As an economic model, it is influenced by Georgism, Rhine (social capitalism) theories and the East Asian development model.

What is economic sovereignty?

In a business context sovereignty is the concept that a state/country is full in charge of its largest businesses and business policy, without resistance or interference from external (or externally controlled) actors - for ideological/geopolitical reasons or "pure greed" -.

Therefore, a country must firmly control its largest companies, infrastructure and main economic driving mechanisms.

That said, often the participation of several market actors and external minority shareholders are useful for governance, as a counterweight to the bureaucratic and political nature of state companies and as benchmark for quality and product innovation.

Sovereign natural resources for the sovereign nation

To preserve economic sovereignty the largest slice possible of the revenues created by exploiting natural resources (including land, forestry, water, fishing) should be redirected to state coffers. To achieve it, control of oil & gas, mining firms should belong to the state or highly taxed. Ownership itself can be diluted to 51% if external shareholders are not hostile and/or bring significant expertise in technology/processes that improve the efficiency/productivity of the company. Else, schemes such as non-voting shares could be introduced to keep control of a company.

In these matters, the Russian president Putin structured this perfectly: state control, a clever (export) tax regime, but external shareholders and -often- foreign managers to counterbalance local lobbying interests, so that state owned enterprises don't become a playing field (and fiefdom) of local political parties and businessmen. Lately, both policy, incentives and disincentives (taxes) have been introduced to favor processing of natural resources over export of raw unprocessed resources.

Value creation from natural resources in a sovereign economy

Many countries produce millions of tons of a variety of natural resources, ranging from minerals to food. These resources are often exported in raw form. A sovereign country should have a framework in place to process the largest percentage possible locally. The processing should include all steps necessary to transform a natural resource to an end product, used or consumed by business or individual end users. State support should be directed to those companies which add the most value to the natural resource.

Sovereign strategic business infrastructure

Utilities are most often monopolies, as building different sets of infrastructure is almost impossible from a financial point of view. So, the base infrastructure like electric grid, gas, water networks should belong to the state. Market actors can provide a variety of connectivity services, and last mile sales to end consumers.

The concept for the telecom sector should be identical, at least 51% of the physical infrastructure network should belong to the state, with market actors owning the rest. In the telecom context state ownership can guarantee a tighter national security and consumer privacy compared to private companies. Also, procurement decisions of equipment and suppliers can be taken centrally to better manage costs and integration.

Sovereign Business - De-financialization

Macro-economic and financial hocus pocus are just a panacea, but prudent financial housekeeping and long-term strategic policies are better suited for the well-being of an economy. Granted, some financial tools are absolutely necessary and are helpful to finance new business ventures or expand current business. IPOs are helpful in raising money for further development, Dividends are an equitable payout that share profit and reward investors for the investment and risks taken. Other tools like bonds are also useful for raising additional money, as long it is strictly for furthering the business, and not providing short term profits for shareholders. Hedging is a way to reduce risks in production and can act as a business insurance.

Just before the Euro appeared, many European countries sold government backed "people mini bonds" in local currencies and with good interest rates, where everyone could invest their savings in the short or medium period. This was probably the most stable and sovereign way for a state to raise money in local currency while giving its citizens an easy and safe financial investment with decent returns and keeping the debt locally in local currency.

Sovereign Business - Import substitution

Import substitution as policy is absolutely needed for every nation. It allows a country to industrialize the economy by producing local products and therefore reduce imports. This is an absolutely must for developing nations, also to reduce geopolitical and economic risks and currency volatility.

Import substitution has many positive aspects: industrialization, advances in technical capabilities, R&D, investments, economic diversification, STEM education, upskilling of workers, local employment and many more indirect benefits.

Not every nation can develop every technology, especially the more complex industrial manufacturing like space/aviation, advanced military weapons and nuclear reactors, but can develop a good set in such segments as agri-food, FMCG, pharma(generics), generic industrial items like cars, tools, machines, devices and software.

Financially, it allows a nation to retain the wealth created, by increased tax payments, and creation of local supply chains, thus further retaining the wealth.

Sovereign Business - Technology Acquisition – Build vs buy

Not every country has a heritage of strong technical abilities, a very strong STEM driven education system or economic models geared towards technology. And all nations besides a few, have gaps in many technology areas.

Therefore, sometimes it is convenient to acquire technological capabilities via IP acquisition or even whole businesses to plug gaps in the economic fabric of a country. Sometimes hiring specialists suffices to start up a new technologically advanced business.

Any acquisition should close gaps in production capabilities both as technology and knowledge of business processes, but also act as a template to create a national ecosystem in a strategic industry, and perhaps a national champion to pull it forward.

Now in 2020, for example it would be quite smart and profitable to buy automotive firms, as these are in midst of a sales and innovation crisis and a paradigm shift (to hybrid/electric with a very adversarial legislation for thermal engines) at the same time, so many famous brands could be acquired cheaply by a country to create a national industry.

Sovereign Economy – Mittelstand SMEs are the solution for diversification

We believe that an economy is more sustainable if it is made up of a large share of Mittelstand, i.e., small and medium businesses like in many Central European countries (Germany, Italy, Austria). Many SME companies provide innovation, extreme diversification and variety of choice, competition on quality and price. They also process and add value to locally extracted/grown resources given by geography and climate of the area using their locally rooted, traditional and historic skills.

At the same time, they and also their supply chains are spread over the local territory providing vast employment and tax money to budgets of local and national government.

From a financial perspective, the earnings of the company are distributed between many small shareholders or extended families and decently paid employees.

With such distribution the wealth is spread(deservedly) in a more uniform way too many more companies instead of a few large corporations.

Another positive aspect of the Mittelstand SMEs is that it both requires and also creates a very strong technical/scientific skill set in a variety of fields, and the competition forces the businesses to increase the research of new products, tools, processes to remain competitive furthering even more the skills set of the employees.

Generally, these small businesses are hyper specialized, produce high quality products and have good profit margins, thus grow organically in time and start exporting to neighboring countries, further increasing the wealth of all stakeholders.

Sovereign Economy - De-monopolization (market share scattering) and De-aggregation

One of the problems of many economies is that too many relatively simple products and services are controlled by very few companies owned by even fewer financial banks and funds. That means a maximization of profits by market control: ownership of brands and distributions channels. This limits choice, quality, diversification, innovation, free market dynamics. Therefore, it is necessary to limit strong concentrations in market segments, especially for low tech consumer products by limiting market share for any one company to -ideally- less than 10%, or even less for huge markets. Similar restrictions should apply also to states/regions of a country. FMCG should be the first candidates. Exemptions could be made for state companies, associations of independent producers, unique inventors/innovators, and perhaps businesses with high capital upfront expenses.

Aggregators of services should also be restricted, if they do not belong to their main services providers, e.g., hotels and accommodation business should "own" their national booking platforms. This should also apply to very large distribution networks for medicines and food.

These policies would allow smaller players to enter the market and produce better, cheaper and more differentiated products, increasing competition to make the economic ecosystem more dynamic, innovative and resilient.

Sovereign Business - De-Taxation of "primary wealth creators"

Taxation is a necessary evil to allow the state to provide basic services, infrastructure and (sometimes) a safety net for the unlucky. We believe the current regimes of taxation are not optimized for most economies.

In many countries in the West (EU, US, UK) new business is now hindered by bureaucracy and high taxes. In the aftermath of WW2, and before, business taxes were almost non-existent or extremely low, and in that period most of the known historic companies were started. Now, the system is rigged in favor of those who seek comfortable and zero risk government jobs, and social welfare checks rather than enterprising people starting a new business. To rebalance this system, we must redefine the paradigm.

First, we must distinguish essentially 2 sides of an economy: "producers" and "servicers".

"Producers" include low tech - Agri-food, middle tech - FMCG such as personal care, generic manufacturing and high tech - complex manufacturing and R&D such as aviation, electronics, pharma, software, oil & gas).

The "producers" create innovation - new products, variety, competition - different quality/price points - and ultimately wealth.

The "servicers" piggyback on the availability of this wealth to provide services to the citizens. They trade (re-sell) other companies' products, service them (e.g., cars, machines, electronics), augment the original product with services (e.g., insurance), or manage wealth(banking). And much more, but without the original wealth creators most would not be able to exist.

So, a tax regime is needed to help the "wealth producers" to be created, nurtured into stability to allow them to flourish.

As with plants and even human beings the most difficult period is at birth and first period of existence, they have a need to be protected, so also new businesses should be nursed at startup.

So, taxation should be exempted for a small business that manufactures tangible goods to help stabilize the startup period to allow the business to gain continuity.

An example would be tax exemption up to 5 million USD revenues, the first few years without dividends or similar payouts, depending on level of technologic and scientific innovation and a set of priorities/parameters of national strategies.

Also, lower taxation (50% of standard rate) should be provided for exporters of manufactured goods, as in most cases their product needs to be "first class" to be competitive on a foreign (global) market, and often have necessary authorizations and standards of quality, and compliance to laws, regulations of other countries. This applies specially to emerging economies which have to adapt to "First World" nations' invented and imposed standards to be able to sell into those markets.

Sovereign Agri-food

Any country should be as self-sufficient in food as possible. Not every nation has the right geography to be able to grow all types of plants to support people and feedstock. But most nations should strive to be as self-reliant as possible, and use their geography for growing the local plant variants, livestock and fishing. Excess production can be sold or exchanged in barter for other types of food or resources.

A good approach - in line with the Mittelstand - would ideally be a large number of small-midsized sustainable agro businesses, perhaps aggregated into local/regional unions/cooperatives/consortiums. The farmers concentrate on working the land, but are also members and shareholders of the cooperative, which provides the storage, logistics, food processing, marketing, and all other possible services to the farmer. Ideally such business aggregations would also be connected to academic and research institutions for technical collaboration on a varied set of topics, such as pest control, veterinary medicines, genetic development of plants and animals.

There are successful examples of such setups worldwide in dairy, meat, wine, fruit production, many aggregating thousands of small farmers sharing the profits in an equitable way.

This would cut off many middlemen in the industry, provide many advanced services, add value to raw agricultural goods, shielding farmers from volatility of prices, and give farmers a cut in the profit of the value added.

Sovereign (Mittelstand) Internet Commerce

One of the difficult tasks for a new business selling "physical items" is to place their products on the market both directly or through resellers. In case of food, a new supplier to a supermarket needs to get certified on all sorts of aspects (quality, financials) and accept the re-seller conditions on quantity/prices into a market dominated by established businesses with long term - probably preferential - contracts.

Direct sales are a way, either through direct stores (very expensive) or through own site but with impact on minimal target audience and expensive at startup.

For a consumer, buying though a small site is often not very convenient, payment to unknown sites can be slow, unreliable, might feel untrustworthy and delivery expensive.

To encourage and enable small companies to enter the market with ease, a solution needs to be found.

Therefore, access to

1) a common low-cost e-commerce platform must be simplified, either as a national e-commerce site of all small "producers" or very cheap access to main third-party marketplaces.

2) a unified internet delivery platform where all small producers can use the logistics and delivery points of the unified platform.

By using a cheap, effective e-commerce platform, small businesses can enter the market with less effort, competing equally with much larger companies. Therefore, the competition would increase drastically.

Sovereign Internet

The Internet is a telecoms-based fabric on which core infrastructure (routers, DNS, domain registrars) is based on and governed by a select few countries, despite the promised openness.

On the Internet depend most companies and businesses, from e-commerce, to banking, apps, sites and all other IoT dependent services and facilities.

So, having a national sovereign back-up infrastructure in place would be a good idea for "just in case ... " scenarios, especially if a country is subject to sanctions from the "owners" of the core infrastructure.

Russia is the first country to implement such a system, declaring it a necessity as a "business continuity" scenario. The parallel system duplicates the key infrastructure pieces, so that, in case of disruption, the Russian internet (RUNET) continues to work.

Another possible advantage would be the filtering and management of bandwidth. One such case could be restricting bandwidth to certain sites (adult, streaming, and other foreign services), which can be inappropriate or consume extremely large bandwidth. An additional possibility could be to restrict things like advertising or transactions of unlicensed or non-tax registered/paying businesses.

Additionally, the security aspect could be better safeguarded, as most of traffic would flow within the country's electronic border.

Conclusion

The Sovereign Economic Model© (SEM) is both top-down government managed, for all the natural monopoly and strategic businesses, but at the same time should be a bottom-up fiercely competitive free market. Only highly organized and motivated countries are able to pursue this road.