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Virtual Currencies and Intrapreneurial Coordination

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Virtual Currencies and Intrapreneurial Coordination

Abstract

Managers of conglomerates or companies with multiple business units are, like central planners in socialist countries, unable to perform economic calculation. These units exchange goods and services internally based on transfer prices, not market prices, and it is hard to ascertain the value contributed by management, which is often hired and rewarded based on political considerations. Innovation is also often unwelcome, as it may challenge privileges of executive management. Until 2016, conglomerates lacked the technology to benefit from economic calculation. In this paper, I propose that a blockchain platform supporting an internal virtual currency enables economic calculation inside conglomerates, unlocking productivity and supporting intrapreneurship.

Keywords

Blockchain, intrapreneurship, conglomerates, virtual currency, algorithmic complexity

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1. Introduction

Since the end of the 19th century, the number of companies with multiple business units has grown exponentially. This is a global phenomenon that transcends national borders. In this paper, I shall refer to these companies as conglomerates, going forward. Some of these conglomerates are the property of nobody in particular, if their capital trades publicly and they lack a controlling investor. Some of them even enjoy a legally enforced monopoly. They are managed by employees who are overseen by a board of directors, but in practice, executive management are accountable to nobody. The revenue size of some of these conglomerates is comparable to the GDP of a nation and their management is constantly encouraged to increase it, regardless of profitability, to grow or maintain their power and privileges. Growth is therefore driven by politics.

The executive managers of these conglomerates, like central planners in socialist countries, face the same constraint: They are unable to perform economic calculation.

In the case of the conglomerates, many of their business units exchange goods and services internally, between themselves. These exchanges are accounted for based on transfer prices, not market prices. Transfer prices are the outcome of political decisions, instead of free exchange between two counterparts.

In conglomerates, management is also hired and remunerated on the basis of political considerations (i.e., loyalty) and, given the absence of a market price, it is not possible to ascertain the value contributed by managerial appointments. Just like in any other nation under socialism, the discipline imposed by executive management to enforce loyalty in conglomerates is an obstacle to innovation. Often too, innovation is never welcome, for it represents a tangible challenge to the entitlement of executive management.

There are however conglomerates that are privately owned by a controlling shareholder. This individual is also faced with managerial decisions, usually delegated to executive management. But these decisions are not aimed to maintain or expand power: They seek to maximize profits. As his/her conglomerate is not publicly traded, he/she can execute on a long-term strategy, without public scrutiny. However, until 2016 the world lacked a technological innovation that would allow conglomerates, public or private, to enjoy the benefits of economic calculation.

Until 2016, the best mechanism available to perform economic calculation within a conglomerate was that of transfer pricing.

In the following sections, I propose that a permissioned blockchain platform supporting a fungible or non-fungible token, allows for economic calculation within a conglomerate, unlocking productivity unseen until now and simultaneously supporting intrapreneurs and their innovation.

2. The market process as algorithmic complexity

One of the main tenets of the Austrian School of Economics is that society or the market is a spontaneous and dynamic process of exchange. Entrepreneurship is the force that drives this process and consists in the creation, discovery, and transmission of information, using “the price system”. This information is infinitely diverse and can be transmitted through indirect exchange, thanks to the institution of money. It is hard to ignore the perennial contempt there is by so many, in the academic world, for the market process. This is probably due to the difficulty

of formalizing it. Indeed, its inherent nature makes a general equilibrium approach futile, as Ludwig von Mises proposed, as economic goods are subject to a duality¹.

Based on the work of Kurt Gödel and borrowing concepts from algorithmic algebra, Sibileau (2014) proposed that the impossibility of mathematizing human action can be proved by applying the Church-Turing thesis². In formal, logic terms, Sibileau concluded that human action is not decidable, complete, or consistent. However, the output or the creation of human action, i.e., economic goods, is indeed decidable, complete, and consistent. Under this approach, economic goods are algorithms and social cooperation, also known as “the market process”, can be conceived as the projection of an algorithmic network.

This network has two unique characteristics however: (a) Its nodes, i.e., human beings, not only transmit but also create information. This creative process is a feature of entrepreneurship, and (b) The exchange of information is not done directly between the nodes, but indirectly, using a medium of indirect exchange.

Conceiving the market process or social cooperation as algorithmic complexity and applying concepts of algorithmic algebra, we observe that the operator that bonds algorithms is called money. Money is “compatible” with any algorithm and this compatibility is what is commonly called “barter”. Money is the only economic good that can be bartered against any and all other economic goods. As an algebraic operator, money should not contain information about itself, i.e., money should not be an algorithm. On the other hand, fiat currencies or any other asset with credit risk that is used to settle debts or is centralized will necessarily have information, and therefore, will be less compatible. Fiat currencies are not algebraic operators but algorithms themselves. When the amount of information embedded in fiat currencies grows due to volatile credit history, the asset becomes exponentially less compatible³, negatively impacting the algorithmic complexity of the social network.

If the market process is an undecidable, inconsistent, and incomplete system, central planning is the attempt to make the system decidable at least and consistent and complete at best. Central planning is formally equivalent to introducing axioms in the system that can either prove or negate a sentence (i.e., the value of an economic good), according to the theory of the central planner, looking to make the system decidable, consistent, and complete. Interestingly, when this attempt at decidability, consistency and completeness succeeds (only possible through coercion, always), the system loses complexity⁴. Extrapolating these concepts now to the sphere of conglomerates, a loss of complexity caused by central planning (i.e., management) eventually triggers bankruptcy, if the

¹ This duality was first noted by Eugen von Bohm-Bawerk in “Kapital und Kapitalzins”: “...«...Innerhalb des allgemeinen Kapitalbegriffes sind ferner bekanntlich zwei Nuancen zu unterscheiden: der volkswirtschaftliche Kapitalbegriff, der die Mittel zu volkswirtschaftlichem Erwerbe und nur diese umfasst; und der individual wirtschaftliche Kapitalbegriff, der die Mittel individualwirtschaftlichen Erwerbs, d. i. die Güter umschliesst, durch die ein Individuum Güter für sich erwirbt, gleichviel ob die ersteren im Sinne der ganzen Volkswirtschaft Erwerbs oder Genussmittel, Produktiv-oder Konsumtivgüter sind. So werden z. B. die Bücher einer Leihbibliothek zwar unter den individualwirtschaftlichen, nicht aber unter den volkswirtschaftlichen Kapitalbegriff fallen...» Kapital und Kapitalzins, Innsbruck, Verlag der Wagnerschen Universitätsbuchhandlung, 1884. Ludwig Von Mises would later mention it as well, in chapter IV, Ends and Means, found in “Human Action”.

² This thesis simply states that something is algorithmically computable if it can be computed by some Turing machine. This means that all functions computable on any computing device are computable on a model of computation according to a table of rules.

³ In other words, the demand for money collapses. Keynesians use the term “velocity of money”: velocity spirals upward.

⁴ In the course of human history, this loss of complexity is what is popularly known as the “fall of civilization”. It occurs every time a serious number of axioms are introduced in the system, leading to a complete loss of complexity. Systems that suffer such loss in complexity are commonly called “self-sustained economies”.

conglomerate operates in a competitive market⁵. It should also be easy to intuit at this point the similarity between the algorithmic network referred to here and a blockchain platform.

In the following section, I will proceed to examine the introduction a fungible token in a conglomerate, through a permissioned blockchain.

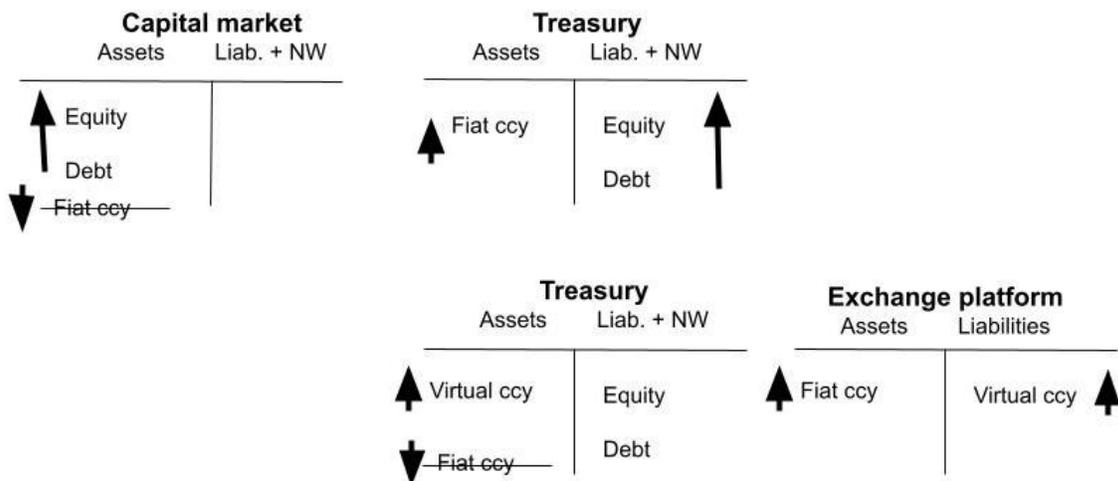
3. The process: Units

By definition, a conglomerate will have different business units. I define a business unit here as the minimum entity that runs a profit & loss account within the conglomerate.

The value of the token to be introduced will have to be measured in relative terms, against an asset. As its circulation is limited within the conglomerate in a permissioned blockchain, this asset will be the fiat currency raised by the conglomerate's Treasury.

The Treasury raises capital in the market and makes payments on behalf of the conglomerate. It has a centralized function. The need for a convertibility board (an exchange platform) between the token and the fiat currency raised by the Treasury can be addressed with a centralized exchange. With the introduction of a corporate token, convertibility with fiat currency can be set at 1:1 in the beginning. All the raised fiat currency needed to settle internal exchange will be converted into the new token. For ease, going forward, we denote fiat currency with "fiat ccy" (i.e., dollars) and token with a virtual currency, "virtual ccy".

Figure 1. The treasury raises capital and converts the raised funds into virtual currency.



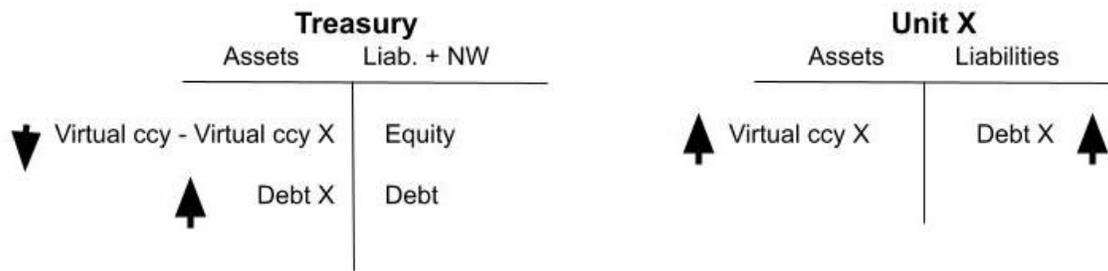
Source: author's own.

⁵ If the market in which the centrally planned conglomerate operates is subject to high inflation, complexity actually is a disadvantage, as changes brought about in relative prices by inflation (i.e., inflation is never neutral), affects coordination. A contemporaneous example of this is the break of global supply chains taking place in 2021.

4. The Process: Raising and Allocating Capital

Once the Treasury has raised capital and converted it into virtual currency, it can proceed to distribute the virtual currency to the business units. At the start, this would be done the way it had been done before, based on central planning. However, the Treasury must consider a hurdle rate of return, under which all use of capital is inefficient. That hurdle rate will be the one they had to pay in the market to raise the initial fiat currency. The different business units may be asked to issue debt to the Treasury, at that rate, in exchange of capital.

Figure 2. Units issue debt in exchange of capital denominated in virtual currency.

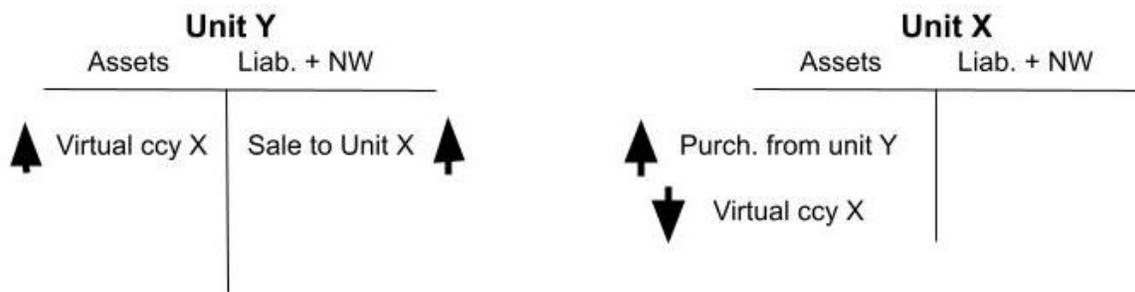


Source: author's own.

5. The Process: Internal Trading

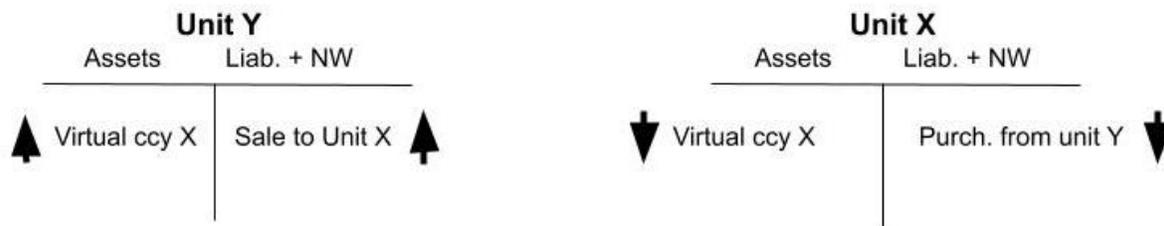
Once every business unit is funded with virtual currency, issuing debt to the Treasury, the units can set up prices in virtual currency, to trade amongst them. It is critical that they can also outsource the same resources externally if they wish to. We will see an example of this later below. The units should be free to set their own prices, in terms of virtual currency. These would probably not be too volatile, as they are set in contracts over a certain period.

Figure 3. Unit Y sells goods to Unit X. Unit Y books a profit, Unit X adds to inventory.



Source: author's own.

Figure 4. Unit Y sells a service to Unit X. Unit Y books a profit, Unit X expenses the service.



Source: author's own.

Why is this more efficient than allocating under transfer prices? Transfer prices are ultimately determined arbitrarily by senior management and the conglomerate cannot have a dynamic, demand-based valuation on the resources transferred. Furthermore, when the business units are atomized (i.e., each unit counts with a profit & loss account) and they can exchange resources among them, their employees are free to develop their intrapreneurial skills. The minimum expected return from these exchanges, ultimately, will be the hurdle rate they commit to with the Treasury.

6. Liquidity in the Conglomerate

In every conglomerate, in every company, there are units with no P&L, that have no interaction with a final customer. In some organizations, these units are commonly called “back office”, while those which do have said interaction are called “front office”. In others, the names “support centres” (vs. P&L centres) or “cost centres” (vs. revenue centres) are applied. In this paper, I will call them non-exporters, whereas “exporters” will be those units which do have interactions with final customers, i.e., those who bring fiat currency into the business unit.

In the conglomerate, there will be two freely floating currencies: fiat currency and virtual currency. This means that whenever any unit or employee wants to exchange fiat currency for virtual currency or vice versa, the rate of exchange will not be fixed, but determined on an internal platform, through a normal bid/ask process. Initially, the use of this innovation will involve the capital allocation only (i.e., funding). This is the scenario first described above, where the units receive the initial capital from the Treasury. However, when the units need to make a payment in fiat currency to their suppliers or employees, they will need to purchase fiat currency, that is, exchange their virtual currency for fiat currency. The supply of fiat currency will come from the exporters or from the Treasury. None of them must be forced to offer fiat currency. But if the exporter (i.e., exporting business unit) has a profitable business model, which means that their profitability is higher than the minimum hurdle rate demanded by the Treasury, it will accumulate fiat currency steadily over time⁶. This accumulation will occur while the stock of virtual currency remains unchanged, ensuring that over time, there will be more fiat currency available than virtual currency. This has important consequences discussed later below.

⁶ This accumulation could be deposited in an internal checking account owned by the unit, with the Treasury.

7. Economics of Capital Allocation

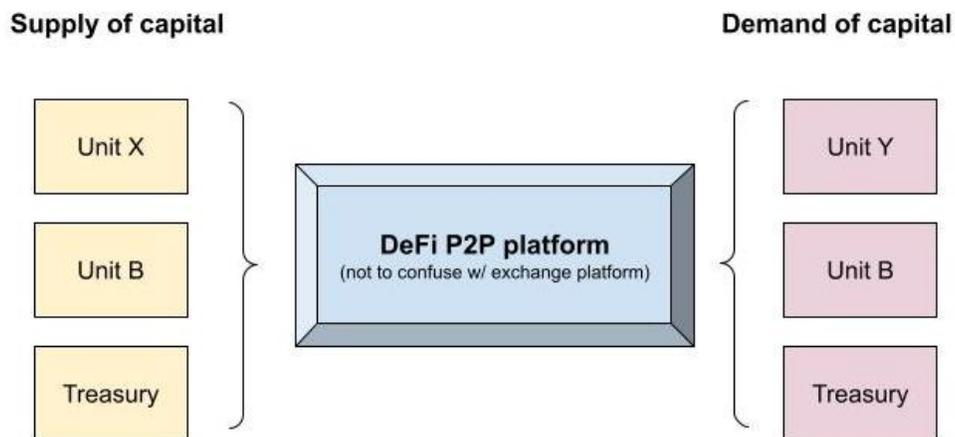
Once virtual currency is established and the initial distribution from the Treasury to the units has occurred, there will be exporting units that will be more successful (i.e., profitable) than others. The more successful will look to expand and will require capital. The less profitable will question their own strategy and may find that the capital initially budgeted to them can be put to better use, without having to wait for an executive committee to come to that same conclusion.

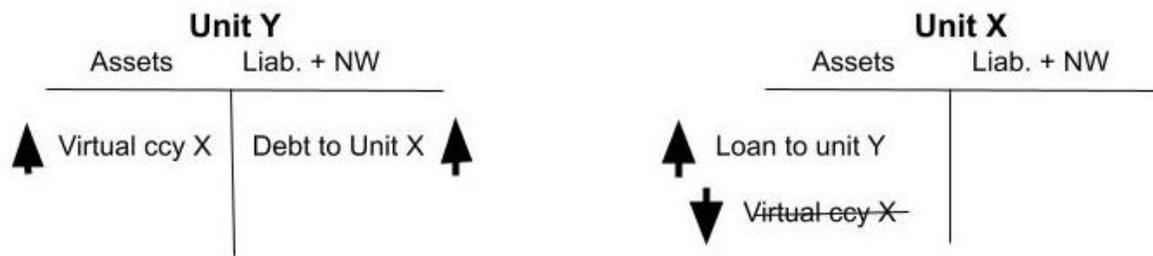
Under the current status quo, units that were over-allocated capital (i.e., at the end of their fiscal year they find out that the capital allocated to them was more than they could find use for), usually spend it, to avoid returning it. With this innovation, units do not need to wait until the end of their fiscal period to either return the capital to the Treasury or transfer it to other units who are more profitable and need it to expand their operations. The existence of a tangible cost on the capital and the ability of profitable exporting units to demand it spontaneously thanks to a centralized exchange trump any budgeting or central planning exercise. This is evident in a capitalistic society as much as in a conglomerate that decides to adopt an internal currency and gives freedom to its units to set prices and to outsource.

The transfer of capital from non-profitable to profitable units can take place on a peer-to-peer basis on an open exchange. Under this arrangement, there is a central clearing unit that puts the capital for auction (i.e., Dutch auction) to any unit that may demand it.

The Treasury, like any other unit, should be allowed to participate in this auction, either to demand or to supply. The auction would result in transfers of capital that take place at a rate no lower than that at which the Treasury pays to raise it. Why? Because if it were lower, the unit that supplies the (surplus) capital would return it to the Treasury and cancel its debt.

Figure 5. Capital is freely exchanged within the conglomerate.





Source: author's own.

In this way, without depending on a central planner or a skillful budgeting team, capital will be allocated within the conglomerate in an efficient and dynamic way (It will be dynamic because it will be independent from pre-scheduled committee meetings: It will happen precisely when the stakeholders need it to happen).

8. Dividend Payments and Share Buybacks

What is a reasonable dividend policy? Is there an objective way to tell? The sincere answer is that to claim knowledge on this is simple pretense. But with this innovation, dividend policy will be the natural outcome of market dynamics and price-based resource allocation. In theory, dividends should be paid out when management of a company cannot offer a better marginal use for the capital invested by shareholders (marginal being the operative word here). But how does the company know what marginal opportunities are out there? How can the CFO of a conglomerate using arbitrary transfer prices, cost factors and hundreds of other non-market-based inputs determine the right payout ratio? With the proposed infrastructure, there are different units bidding and asking for capital in virtual currency constantly. If over time the CFO finds a stable accumulation of virtual currency goes unclaimed, he will undoubtedly have a signal that capital can be returned to investors. If the Treasury must pay interest on capital and the same is uncalled, there is an explicit signal that it can be returned.

The introduction of a permissioned blockchain platform also allows for independent internal capital raising for new projects from intrapreneurs, as discussed further below. These projects will represent new initiatives that can challenge a return of capital to shareholders via dividends, in an informed way, i.e., based on a market process.

9. Dynamic Efficiency

The proposed innovation will generate, inside the conglomerate, the same dynamics that is to be expected in a capitalistic free market, with a fixed stock of money and no fractional reserve banking. This means that with a stable stock of virtual currency, as the company accumulates fiat currency stemming from sales, the exchange rate between virtual currency and fiat currency (i.e., virtual currency/fiat currency) will strengthen in virtual currency's favour, making it more expensive *not* to outsource. The business units that are not exporters, i.e., the cost centres, will be under constant pressure to remain competitive, as their products appreciate vs. similar products sold outside the conglomerate. In an environment of perfect coordination, this pressure, if steady, will continually push the units to become highly specialized.

In this context, good management consists in ensuring and promoting an ever growing frictionless and stable coordination between the units and within the units themselves. Why within the units? Because under this system, employees can have the option to switch to a different regime: From being employees to being lenders.

Labour is another form of debt. When hired, employees actually advance a resource regardless of the outcome of their work. They receive the discounted value of said resource (i.e., they get paid a wage), regardless of the outcome. If the outcome is positive, they have no claim on the profits. Under the new system, if employees could sign their contract in virtual currency and virtual currency/ fiat currency appreciates, employees will benefit from the increase in productivity. In a conglomerate, they could also bid capital to the specific units in which they operate.

Today, the average employee of a conglomerate may receive stock, and that may make her feel a connection between her work and the conglomerate's performance. But if she is given the option of allocating capital to her own unit, the incentive to deliver top quality results will be more tangible. This could obviously dilute shareholders' equity, but the overall effect could be positive⁷, as intrapreneurial attitudes awaken in employees.

Another behavioural outcome is that in an inflationary context (i.e., fiat currency devaluing against virtual currency), the benefits of coordinating and using virtual currency as a unit of value will exponentially increase. It could very well trigger a trend whereby businesses seek to merge into conglomerates if the threat of inflation is perceived real.

10. Bankruptcy

Before we examine the case in which a unit is unable to return capital to another unit, let's remember that we assume that any unit, be it exporting or non-exporting, is allowed to outsource, that is, to procure its inputs outside the conglomerate.

As in any other bankruptcy, the assets of the bankrupt unit would go to creditor units. If the bankruptcy was triggered because the debtor unit, threatened by outsourcing alternatives, could not raise the price(s) of for its service(s) or product(s), said bankruptcy signals that outsourcing was the choice to go for, and the creditor unit should sell the assets and outsource immediately. This is creative destruction at its finest.

11. The Exchange of Goods and Services

So far, we examined the benefits of a dynamic allocation of capital internally, with the use of a virtual currency that is exchanged by units on a centralized platform.

But units also exchange goods and services. For instance, one unit's output can be another's input. If the unit also sells the output in the market, there will at least be a market price to guide economic calculation. But if the unit only sells within the conglomerate, there will be an improvement if the exchange is carried out at a free internal price, using a virtual currency.

As the exchange rate between fiat and virtual currencies determined by all the participants in the conglomerate fluctuates, the price of the input (to the buying unit) will fluctuate too. If the conglomerate makes a steady profit and the supply of virtual currency is not increased, the exchange rate vs. fiat will, making internal inputs more expensive. This price dynamics will create a healthy tension whereby units must become more productive to justify this higher internal price, as the threat of being outsourced becomes more real.

⁷ The overall market value of the shares in the public market could increase more, thanks to this dilution, than without it. This is as counterintuitive as when a government ends up collecting more revenue through lower rather than higher tax rates.

If the conglomerate starts printing losses steadily, the exchange rate vs. fiat will tend to fall and internal inputs will be more profitable if sold outside rather than inside the conglomerate. This will make a case for spinning off the units producing said inputs.

This same dynamic will be experienced with the exchange of services. Every conglomerate has an administrative corporate unit that supports the rest with financial, legal, and marketing services. These are usually spent supporting those business units that are the least profitable, as they require focused work on their strategies (i.e., marketing, budgeting, operations management) or face legal or regulatory issues.

Regardless of the exchange rate between the virtual currency and fiat, if these services are not allocated across the units but independently charge fees in virtual currency to those who actually demand them, the true cost of supporting units in distress will surface, affording management with a clearer picture of the situation. At that time, a more educated decision will be needed on whether to continue subsidizing these units or closing them.

Another advantage of being able to avoid overhead allocations and forcing units to recognize the actual share of corporate expenses is that a decision can be made on whether certain corporate functions deserve to be internalized by specific units, instead of leaving them at a corporate level. When corporate services become in high demand and their prices rise making them unaffordable to other profitable units that have little use for them, it is time to internalize costs to the unit that most demands them and leave the rest to hire their own or recreate a new corporate team for their common use.

12. Permissioned vs. Permissionless Blockchain

At this point, I on the reason I propose a *permissioned* blockchain and what I mean by that. Perhaps the easiest way to illustrate this is by contrast: In a permissionless blockchain, each node would have the freedom to store as much virtual currency for as long as it wishes, and to exchange it for another token, on a compatible blockchain platform. Such decentralized, permissionless blockchain would allow the seamless and instantaneous unwind of a conglomerate by its autonomous units, violating the property rights of the conglomerate's shareholders. In a centralized, permissioned blockchain however, the conglomerate's Treasury reserves the ultimate right to reallocate, unwind exchanges between units, and allow the conversion of virtual currency into fiat money. The Treasury's privilege to exercise these rights is consistent with the legal organization of the conglomerate and fiduciary duty of management to shareholders.

13. Intrapreneurship

In November of 1937, R.H. Coase published "The Nature of the Firm". His task was "...to attempt to discover why a firm emerges at all in a specialized exchange economy...". His main conclusion was that: "...The main reason why it is profitable to establish a firm would seem to be that there is a cost of using the price mechanism..."

This statement would seem to imply that entrepreneurs do not discover or create market relevant information, a feature already established and well discussed by Austrian school economists. Instead, entrepreneurs are assumed to find and interpret information that is already available in the price mechanism, for them to act upon. This latter view is still prevalent in mainstream Economics. It is a sterile view, which fails to see entrepreneurship as the driver of the market process.

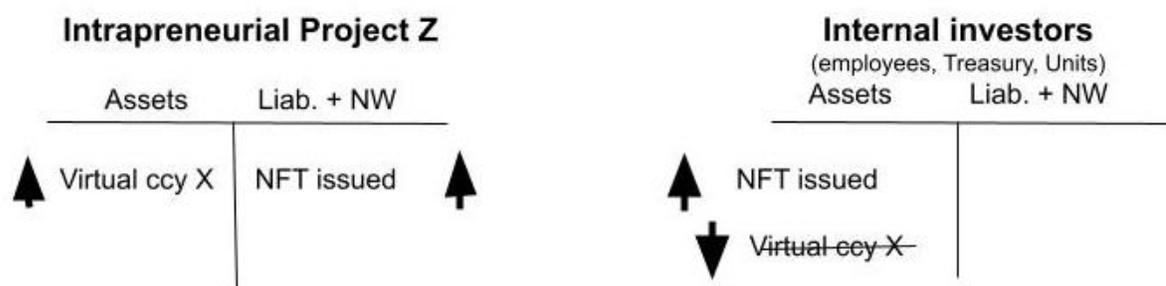
Evidently, if Mr. Coase was correct, the use of blockchain technology described here will contribute significantly to lowering the cost of using the price mechanism, I dare say to a minimum expression. But it is not just a reduction in cost, what the blockchain technology brings. Its ease of use is also a factor that could finally unlock the power of intrapreneurship within a firm, and more so within conglomerates.

If we define intrapreneurship as “...the process used to develop new businesses, products, services or processes inside of an existing organization to create value and generate new revenue growth through entrepreneurial action...” (Foley, 2020), then it is easy to see how intrapreneurs would most profit from blockchain technology. Indeed, we have so far discussed a framework where the Treasury of a conglomerate would exchange fiat currency raised externally (by whichever means: debt, equity, etc.) for an internal virtual currency, and distribute it across the different units of the conglomerate, whereby the management of each one of these, could make payments for the internal sale of goods and services. This platform would be centralized and governed by the Treasury, while the internal virtual currency would be fungible.

But conglomerates could also benefit from this new technology to support intrapreneurs, within a market-based management practice.

Under current technological conditions, an intrapreneur with an initiative presents a business plan to executive management which, if approved, will likely require funding that will be raised in the next relevant (fiscal) period. Additionally, the intrapreneur needs only convince the same management of the potential benefits of her plan. Only after it is approved and funded, will she be required to communicate it to those that will be involved in the new venture. Such involvement will also be executed in vertical fashion, without the approval of other units or colleagues. If the initiative is of relevant size, it will be shared with the board of directors and shareholders of the conglomerate. Otherwise, it will just be a small project under the radar. Most often, the criteria to determine relevance are based on politics, not economics.

Figure 6. Intrapreneurs raise capital internally, by way of a non-fungible token.



Source: author's own.

With the help of blockchain technology however, intrapreneurs can issue non-fungible tokens representing ownership in their proposed initiatives, whereby the tokens instantaneously become assets with liquidity in terms of the virtual currency of the conglomerate. Internal buying and collateralization of any of these initiatives would be available to employees, shareholders (by way of warrants) and management. Their trading on the same central platform that supports the virtual currency would allow the transparent communication of information expressed in terms of the exchange rate of the NFT vs. the virtual currency, in real time. As the initiative proves profitable, the value of the NFT will appreciate relative to the conglomerate's virtual currency, providing the intrapreneur the

necessary resources to expand on her initiative. If, on the contrary, the initiative proves unprofitable, the value of the NFT will dwindle accordingly and at the speed necessary to transform it into an anecdote. This dynamic will be devoid of any political consideration.

Eventually, as the conglomerate supports intrapreneurship, their business model will become a chronology of NFTs issuances living in parallel to whatever original units still survive.

14. Management

What would be the role of executive management in conglomerates that adopt this new technology? Without the need to perform calculations on transfer prices, overhead costs, capital allocation, or product innovation, will their leadership be necessarily diminished? Blockchain technology is run on protocols, which coordinate the actions of the nodes (i.e., units of the conglomerate). Laying it out and supporting it as it grows and develops additional features (i.e., smart contracts) requires vision and leadership. On this basis, without knowing how exactly these new networks would morph, one can anticipate that executives will still have their hands full, albeit on more productive work.

15. Conclusions

The ultimate results of the dynamic efficiency described above, unleashed by the introduction of a virtual currency, depends on the final details of implementation. Just like in any country, complete freedom of movement of capital (and labour), freedom to trade, to set prices, to downsize or to expand are necessary for economic growth to take place, within a conglomerate too, the same degree of freedom must be prevalent, from the very beginning and for all units. Gradualism will fail. The introduction of this framework must be sudden and unrestricted.

Declaration of Interest

The author declares that there are no conflicts interest.

Data Availability

N/A.

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