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## **College students about temperance**

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### *Introduction of the examined sample*

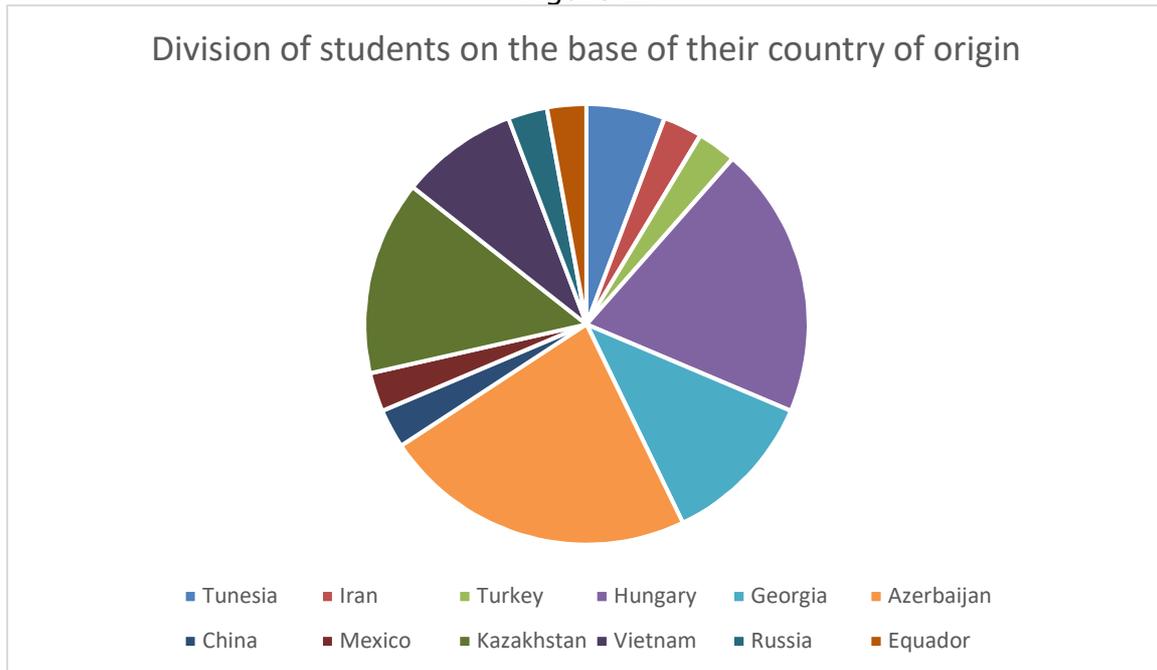
In the previous semester I held a Business Ethics seminar in Budapest for an international group. We talked about the virtues on the base of the Christian catholic categories of moral virtues. At the end of each class we have examined the question where and how the certain virtue can appear nowadays, in the 21<sup>st</sup> century, or it has already become old-fashioned.

Although the opinion of students do not form a real picture of any examined questions from their society of origin, as the size of the group is too small on the base of the scientific statistic rules, and this way the results are not scientifically exact, but make us think the question further. There were 35 students at the course<sup>1</sup>, all of them with economic knowledge and BA degree. They came from countries of the Middle- and Far-East and from Latin America.

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<sup>1</sup> Country of origin of the students: Tunesia 2; Iran 1; Turkey 1; Hungary 7; Georgia 4; Aserbaijan 8; China 1; Mexico 1; Kazahstan 5; Vietnam 3; Russia 1; Equador 1

Figure 1.



### *What is temperance and does it have a meaning today?*

In one of the lessons one of the topics was the virtue of temperance. The students made a good presentation on the base of the professional literature about what we mean under temperance and they even mentioned that it is regarded as a virtue and something to be followed not only in the Christian religion, but in all other big religions, too. After the detailed description I asked not only the students responsible for the topic, but the whole group, if this virtue has a value in our days – how useful it is?

In the previous lessons about other ethical topics there were strong debates between the students at this point about the same question. This time the students agreed that temperance is nowadays an unnecessary thing. They listed several related arguments. At the end they accepted two of them as the best reasons for their opinion. These are following:

- Everything can be bought on the market. Nothing – in some cases not even my own wallet – can limit the fulfillment of my needs.
- Why should I control my needs that can be fulfilled without any problems, because of a saving principle for its own sake and I do not have any advantages of it? This principle was logical and needed earlier but in our days, it is outworn thank to the economical-technological developments.

In the countries of origin of the students the high supply on the market is not common, but they agreed that in case the wished goods can not be bought in traditional stores, with the help of connection capital they can find the channel where they can buy them.

At this point I directed the discussion towards the connection between the term saving known from their studies in economics and the term temperance. All of the students knew the term saving needed in order to reach long term goals. There was a consensus in the group that the own savings are only a minor part of the needed means (the extent was estimated between 20 and 30 % with one opinion of 10% and one of 40%), and the major part of the capital can be financed from sources coming from financial institutes and/or investments.

### *Evocation of the memories of grandparents*

As the explanation of temperance from the traditional economic knowledge seemed to be too long, I have told a story, taking into consideration the division of students on the base of their country of origin. I had the assumption that they have heard stories in their homes about destitution because of war and labour service. The story is the following (Stark, 2008). two neighbours come home after several years of captivity. They are weak and hungry as they have not received enough food. Both families are very happy because of the men who returned and they of course see how thin and hungry the men are. One of the families immediately starts to cook the dishes that were the favourite ones of the men who returned. He is very happy to see and to eat those dishes and eats a lot from them. In the other family there is a conflict between the men who returned and his wife as she cooks only a bit richer soup for him than he received in the captivity. But the soup becomes every day a bit richer. Let us look at the two families after one week. What do we see? The first family, where the men received a lot of delicious food, people are mourning as the men died. The other family is happy, they are sitting around the table, the men is already eating the same food as the others and he is telling stories about his captivity.

At this point one of the students said quietly that he has heard a similar story from his grandparents. What was the difference between the two families and why has one men died and the other one lived longer? Looking for the answer from the point of temperance and referring to medical sciences only shortly we can formulate the following answer: one of the men died because of eating too much food and too suddenly, and the other men could stay alive because the intake was increased slowly, step by step. Nowadays such extreme situations are very rare, but the sudden extra intake overloads the digestive system. This can be so serious that even medical treatment is needed. So as it can be seen from the sample story, in the long term it worth to satisfy the need that is wished for a long time gradually, in small steps, soberly, because if we lose control, our wellbeing can be damaged.

During the discussion about the sample story the students agreed that they should avoid unlimited hedonism for their health's sake. In nutrition

we should keep limits for our health and wellbeing, independent from the reasons of the different gastro tendencies.

### *Is low price really low?*

The next example was about consumer approach, eliminating the terms known from marketing sciences like brand loyalty and many others, and focusing only on price. In the example we suppose that all members of the group live and work in the same small town that is located far from everything. Getting to the closest town takes a day. There are three supermarkets in the town with almost the same price level. One day one of the supermarkets announces with big local advertising campaign that all products are for half price. The first question is about the reaction of consumers. All students agreed that all consumers would go to this supermarket. Some of them added that they would buy bigger quantities of products than their current needs, making a kind of reserve, as it is not known how long prices would be so low. The next question is about the other supermarkets. What will happen with them? At this point the students agreed again and said that they would decrease their prices, too. They step in the price competition or succumb. It depends on the certain market player, how long it is able to survive in the price competition, which probably creates losses in all supermarkets. The one that started the price competition presumably has the capital with which it can finance the continuous loss, but the other two will end its activity and will be closed sooner or later. At this time the supermarket that started the price competition will stay alone in monopolistic situation and can offer its products on much higher price level than originally and the consumers will not have any chance to buy the needed goods anywhere else.

The example comes from competition law, where the prior topic is about competitors, but – as a kind of incremental benefit for the consumers – it also protects consumers. The monopoly knows its own market and can identify the prices, so that they provide satisfactory profit, but – using temperance from the view of the monopoly – at these prices it is not worth for new market payers to enter the market. This method is known in practice under the name predatory pricing (Valentiny, 2004).

There are many ways for a venture to get to power dominance or to monopolistic situation on the market. We can find several examples in economic history and in the company history of certain ventures, too (see not illegal forms of predatory pricing in e.g. Erdélyi, 2006). Law does not prohibit collecting huge property, neither for people, nor for ventures. Law prohibits and sanctions only if the venture abuses with its situation with power dominance. Competition law declares the general prohibition of abusing with economic power dominance, and then gives a list of examples on the base of the cases seen in economic history, keeping the possibility open if a venture abuses with its economic power dominance in

a way not known previously; it can be sanctioned on the base of the general prohibition, too (Hungarian Competition Act 1997. LVII. 21-22.§).

Modifying the end of the example the venture with power dominance incorporates the competitors before they close. In this case there is a fusion between the ventures on the market that is allowed or prohibited by the competition authority<sup>2</sup>.

During the discussion of the example the students agreed that it is disadvantageous for the consumers if there is a venture on the market with power dominance or in monopolistic situation, as the economic interests of the consumers are harmed then. There was a debate among the students if we or someone else can, should or must do something in order to avoid such situation. They agreed that the state has a necessary role, but they could not come to an agreement about the time of intervention and in favour of whom the state should intervene: in the favour of the private person end-user, or in the favour of the venture concerned by predatory pricing. In the given time frame the opinions of the students have not come closer. The reason was that the students collected arguments spontaneously either in the favour of the consumer, or the venture concerned by predatory pricing, or the venture applying predatory pricing. At this point, where there seemed to be no chance to find a compromise, one of the students had an idea out of the box: to ask the state decision maker to intervene in the debate in favour of him. Then the discussion continued about lobbying. The students thought it is a kind of illegal term. The presence of the term lawful lobbying and its practice caused them general surprise<sup>3</sup>. Getting to know to this method that was new for them, the possibility of persuasion stepped into a new dimension, where the parties try to convince not only each other but also the new player who can help the party put across its interests if it is already convinced about them.

As an end conclusion of the example in connection with temperance the students agreed that in case of a huge price discount we have to be careful, because there is a chance that later we have to pay momentary discount more times.

## *Real estate bubble and temperance*

Our last example was the crisis from the near past that affected the whole world. We have examined it from the point of temperance and profit maximizing.

In the first years of the 21<sup>st</sup> century the inflation rate was low all over the world. The reaction of some central banks, also of the American FED

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<sup>2</sup> Depending on the total balance sheet of the ventures in the fusion the authority of the member state or of the European Union decides about the allowance or the prohibition of the fusion.

<sup>3</sup> Some students volunteered to make a presentation in the next lesson about the ethical and legal aspects of lobbying.

was the decreasing of interest rates. In the USA the speed of the growth in consumption increased. The extra consumption was financed by the emerging countries thank to their increasing efficiency of work and their high saving willingness. Practicably the high saving rate of India, China and the oil exporting countries financed the cheap international credit environment and the consumer wellbeing of the developed world, and also helped the integration of the financial markets of the whole world. The huge source surplus of the third world looked for investment possibilities in the integrated international financial system. This soon led to the point where the average risk premiums have not covered the excepted losses any more (see World Bank Fiscal Year Data, 2007).

In this environment the real estate prices started to increase significantly as a self-exciting process: increasing real estate price → increasing credit possibilities → increasing amount of credits → increasing demand → even higher real estate price (Király, Nagy & Szabó, 2008).

Analysing this basic situation post factum, we can come to a conclusion that is a bit like an example from a school book. It is as follows: the self-exciting process will come to an end once, and this will cause the stop or the collapsing of the system that was kept moving till then. Looking at the process calmly it is a logical and experience-based evidence that the self-exciting process collapses quickly after reaching the critical limit. But the date of collapsing can not be forecasted in advance and it is a psychological fact that it is difficult to stop playing when you are in the “winning run”; you prefer to stay in the game.

Here comes the first question from the point of ethics and it is about choosing between temperance and “continuing the winning run”. The students agreed that the advantageous process will come to an end once and we should get out before collapsing, but they also agreed that it is a hazardous question when we should get out, as the date of collapsing is not known. Most of the students considered the question in the frames of willingness to undertake risks, and upon their opinion this belongs to private autonomy, as everyone can use his or her money how he or she wants to. When someone is dealing with handling properties of others, then he or she has strict state regulations that determine the limits, but the losses are born by the constitutor, i.e. the investor.

The outbreak of the crisis started in the secondary mortgage market of USA and thank to the good financial mediator system it could spread quickly. It is important to clarify that the occurrence of the crisis was inevitable in the given circumstances, because of collapsing of the self-exciting process. So, the crisis was not caused by the anomalies of the secondary mortgage market, but this was the market where the self-exciting process collapsed at the first time.

The loan of the customer is granted by the mortgage loan agent, who can refinance the loan by a commercial bank. This bank classifies the customer, executes the judgment and performs the securitization of the

loan<sup>4</sup>. Therethrough the American households' long-term credits were financed by long-term investments of others. The base of the secure operation of the system was the judgment and risk management policy of the bank that performs the securitization and the general trust towards this bank. In the self-exciting process that we detailed earlier, many secondary customers got into the financing cycle, who are more risky upon the traditional bank classification and the loan granted for them can not be securitized. Despite of this banks have securitized these credits, which could have not happen with a traditional bank classification. These securities formed the secondary security market. The extreme quick growth of the secondary security market resulted in the fact that it became very difficult or even not possible to distinguish secure papers and risky papers. During the rush on the market the secondary securities performed well, too.

In 2006 the increase of flat prices slowed and soon turned to a negative spiral. At the same time the non-paying rate of the secondary mortgage loans increased. In the first half of 2007 big financial institutions dealing with mortgage loans announced bankruptcy or significant losses. The crisis appeared on the secondary mortgage market in America. Businessmen and experts expected (trusted? hoped?)<sup>5</sup>, on the base of the data known that time that the crisis will stay on the secondary mortgage market and due to its limited size it will not spread anywhere else (Important opinion influencing the market players, e.g. Bernanke, 2007). But due to securitization a very big volume of securities were created without the security of the state-granted, securely paid versions. The market players dealing with securitization created their structured papers in a way that they consisted of more and more unsecure, secondary securities. Besides it seemed that the financial miracle comes true: – and it received a strong marketing support – you can reach increasing income with decreasing risk. Neither the market players, nor the credit classifiers have taken into consideration that the loss of the secondary securities in the structured papers grows not linearly but exponentially (Fender, Tarashev & Zhu, 2008).

In the beginning of securitization the created securities meant security, liquidity and quality. The related thoughts of the investors could be changed difficultly and slowly by the market that has changed significantly. The obligation to inform investors were performed by the issuer of the security with publishing reports, but not any of the law regulations in the world prescribes that the issuer has to give information in total depth about the risks of the paper for a potential investor and

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<sup>4</sup> The effective Hungarian Civil Code makes it possible that legal entities create a type of security not defined in the law, but indicating the obligatory elements listed in points 6:565. § (5) section a)-f). This gives the possibility of securitization, which is an existing and widespread solution in the old member states of the European Union.

<sup>5</sup> The students accepted the presence of trust and hope in business life, but we have not discussed about the topic deeper.

check if the investor understands the risks well<sup>6</sup>. The new products were not liquid and secure any more, but in the meantime the investors connected the terms liquidity and security with securities in their minds. This investor "illusion", i.e. the misunderstanding of the new products contributed to the crisis, too. Credit classifier companies rated structured securities not according to the real economic value of the securities that meant their base, but performed pure statistical rating which helped maintaining the investor illusion.

As a common result of these theoretical and structural factors the crisis was inevitable. The continuation is already history. Focusing only on temperance in the story there is another question besides the already discussed one, which was about "when should we get out the winning run?". It is as follows: if I knew that a game would collapse sooner or later, but till that time it could make profit, do I get in the game or not? Looking at the question from the point of temperance the students formed three opinions. The first one was that we should not get in such games. The second group of the students thought that they would get in the game but only with their surplus. In case they lose it, no problem would occur. The third group meant that after getting in the game we should pay continuous attention on the market, and get out at the first signs of the coming collapsing. After detailed explanation of the three opinions, there were many students who have changed their minds and chose the second opinion: taking risk only with their surplus.

## *Conclusion*

After analysing and discussing the case studies, the closing question is if there is a sense of temperance in our days or it is something old-fashioned that only blocks us? The common opinion of the group was – with two exceptions – that temperance is still needed in our days as if we leave it away, we can easily get into big troubles. The minor opinion was that temperance is important for a "common man", and using it consciously we can protect ourselves, but the two students said that they loved risk and in order to create something new, and to achieve good results, we have to undertake even big risks, known that there is also a possibility to fail.

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<sup>6</sup> Such investor „exam“ exists at investment providers, where the investment provider accepts the orders of the customer on the base of the filled in risk questionnaire.

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