“The Coercion of Capital:
Inflation, Risk Premium, and the Structural Impossibility of Ethical Rent”

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<u>Preamble</u>

In an inflationary monetary system, the mere holding of money becomes a losing position: while nominal sums remain unchanged, real purchasing power steadily erodes

This transforms capital preservation from a passive act into an active necessity. Individuals are pushed into asset allocation not as a matter of preference, but as a matter of survival

This paper develops a structural position: (i) preserving purchasing power requires inflation absorption, (ii) inflation absorption generally requires participation in asset markets, (iii) asset markets only offer real returns (beyond inflation) in exchange for risk-bearing or extraction, and (iv) consequently, sustained “ethical rent” — defined as rent charged only to absorb inflation and maintain an asset — is structurally unattainable without first engaging in high-yield, private-equity-like accumulation to pre-fund reserves

Inflation therefore operates as a coercive mechanism which forces ordinary actors either to accept capital degradation or to enter roles with rentier or extractive characteristics. Ethical stewardship is not impossible, but under prevailing conditions it is systemically gated

In reading this paper, it is important to understand the stages that we are stepping through

> *It begins with a considerable amount of money being held in a bank account, we then consider moving it into something that we would like to consider owning (for example, a block of apartments)*
>
> *There are many reasons why someone would want to put their capital into something that is not a bank account, or a purchase of government debt : it may be fulfilling, it may be interesting and engaging, and it may be something meaningful where the person would like to exert some control in ensuring that people are treated well*
>
> *We will also discuss what happens when we seek to establish ethical (financial) arrangements, how long it takes to implement, the effect of adding leverage (ie. loans and mortgages) and whether it is even possible to free one’s capital from the limitations of our current monetary system to be able to implement ethically sound investment at the level of the individual wealth holder*

Introduction: The End of Ownership That Never Arrives

A person with a sum of money may reasonably assume that this should represent a preserved resource: a store of value to be deployed later according to need or desire. Under such a conception, a sum held in reserve is complete in itself — a finished act. It should require no further engagement. It should not need to grow. It should not need to "perform."

Yet in modern monetary conditions this conception fails. Inflation disrupts the moral and functional neutrality of saving. To hold money is to lose it, slowly and predictably. Capital preservation becomes a continuous task, not an accomplished state. A reserved resource becomes a deteriorating resource

The system thus converts the saver into a forced participant: either accept erosion, or enter market exposure

Inflation as Structural Coercion

Inflation introduces a permanent wedge between nominal and real value. Nominal capital is preserved in a technical sense, but real capital is not. The consequence is simple:

- if inflation persists, purchasing power falls;
- if purchasing power falls, reserves lose their meaning as reserves

In this environment, capital cannot remain inert. It must seek instruments that absorb inflation over time. "Investment" ceases to be an optional behaviour and becomes a compelled response to monetary decay

This coercion is not merely financial. It reshapes behaviour, identity and social role. The ordinary person holding reserves is pushed into becoming an investor. In inflationary regimes, neutrality is punished

The Two Types of "Protection": Inflation Absorption and Real Yield

At first glance, the solution appears straightforward: invest capital into assets that grow in line with inflation

However, inflation absorption alone is rarely offered cleanly and reliably. Most asset allocations — especially those accessible to non-institutional actors — do not offer guaranteed inflation linkage. Instead, they promise probabilistic appreciation and/or cash yield, both subject to market degradation

Thus an investor often seeks not merely inflation absorption but **inflation + additional return

This “additional return” (the real yield) is commonly justified as compensation for:

- uncertainty and volatility
- liquidity constraints
- operational fragility
- policy and regulatory change
- market drawdown and capital impairment
- counterparty risk

In short: the real yield is structurally a **risk premium**

The Risk Premium and the Myth of Passive Innocence

This is where the ethical conflict emerges

If one believes that capital should not itself be a perpetual source of wealth generation — that its only legitimate task is to preserve its purchasing power — then the risk premium becomes morally unstable. Why should ownership entitle a permanent surplus?

Yet the market insists: without surplus return there is no risk compensation; without risk compensation there is no capital allocation; without allocation there is capital erosion

The saver is thus forced into a contradiction:

- do nothing, and be degraded by inflation;
- act, and become structurally aligned with extraction (or with risk-seeking behaviour that tends toward extraction)

The system makes innocence expensive

A Two-Phase Ethical Model: Principal Neutralisation

A coherent ethical response is possible, but it requires a shift in framing. Under this model, the real yield is interpreted not as perpetual entitlement but as **temporary compensation

Phase 1: Risk Compensation Mode

Capital is allocated into an asset returning:

- inflation absorption, plus

- additional return (real yield)

The additional return is not treated as profit in the ethical sense; it is treated as **reserve-building**, a form of self-insurance. It is the price paid to neutralise the future impact of risk

If inflation is 4%, this phase may require instruments yielding 9%–15% gross — a level rarely accessible without palpable risk, operational complexity, leverage, or extraction

Phase 2: Preservation-Only Stewardship Mode

Once a sufficient reserve exists — i.e., once the investor has generated enough real return to “support” the initial capital allocation against plausible market degradation — the ethical justification for surplus extraction ends

At this point, rents (or yields) can be reconfigured to:

- absorb inflation only
- preserve the asset
- maintain the reserve threshold
- and remove the permanent risk premium from renters

In this arrangement, market degradation may still occur, but it does not transmit into lived harm: the reserve absorbs shocks. Neither the investor nor the renter experiences destabilisation

Risk still exists; its *impact* is neutralised

The Viability Constraint: Why This Resembles Private Equity

The model above is ethically coherent, but practically constrained

To reach Phase 2, Phase 1 requires sustained high returns — returns which are difficult to secure without behaving like an institutional allocator or an active optimiser. In property markets especially, net yields in excess of inflation typically demand:

- leverage
- operational intensity
- distressed acquisition
- rent increases
- cost compression

- market timing
- or regulatory arbitrage

In other words, to create sustainable inflation-only stewardship rent, the investor must first operate structurally like a **private equity fund**: extracting or creating surplus in the early period to build reserves sufficient to later reduce extraction

This reveals the system's deeper mechanism: ethical rent is systemically gated behind accumulation

A person seeking to become a steward must first become a machine

Though : this is where the reality is concerning : even if one is willing to become the machine before becoming the steward, leverage makes the "steward stage" remote — because ethical rent reconfiguration is incompatible with outstanding debt

> For example : assuming leverage has been added to generate higher yields, eventually the mortgage would need to be repaid (a lender is very unlikely to stay in the investment if the rents were reconfigured to inflation-only which would probably only meet the interest payments)
>
> This means (assuming 75% LTV), the capital would need to make 4x itself in additional yield before the capital preservation support reserve was built up and thus phase 2 could commence. Based on the Author's experience, making 4x invested capital in a leveraged structure from a sale event alone is a *huge* result, so making 4x from additional yield alone in order to build the reserve as well as repay all the outstanding debt would take decades

A note to my former colleagues in the industry (for all readers - please refer to the 'About' section at the end of this paper): that is the cost of purchasing responsible, ethical and moral stewardship in our current capital system - anywhere between 2.5-4.0x depending on 60-70% leverage. Assuming of course we are managing capital not hindered by returns-generative fiduciary responsibility to investors

<u>Structural Conclusion: Inflation Produces Rentiers</u>

The system's output is predictable

Inflation forces capital out of neutrality. Neutrality requires losses. To avoid losses one must enter assets. Assets require a risk premium. Risk premium is earned through surplus yield. Surplus yield, especially in rental markets, is typically paid by those with less capital

Thus the inflationary system tends to manufacture rentiers even out of those who do not wish to be rentiers

This is not a psychological failing, nor merely “greed.” It is a system design. The structure coerces:

- either capital degradation for the saver
- or extraction from others for the saver’s preservation

This is the engine of widening inequality: the rich can sit safely; the less rich must hunt yield; yield-hunting puts them into dominance relations

Implications

Several implications follow:

1. Moral condemnation of small rentiers often misses the structural coercion which creates them
2. Ethical stewardship is not a personality trait; it is a market position available mainly to those who already possess sufficient capital
3. A system that forces risk premium extraction to preserve purchasing power cannot claim neutrality.** It embeds dominance into routine behaviour

The solution space is therefore not primarily “better ethics,” but altered conditions under which capital can be preserved without coercion into extraction

Closing Statement

A person with a sum of money should be able to preserve it as a reserve and deploy it later without being coerced into an adversarial posture toward others. The fact that this is not possible is not incidental: it is a core property of the inflationary environment. The system produces extractive roles. If an individual wishes to escape those roles — to become an inflation-only steward rather than a perpetual toll collector — they must first become something closer to private equity, accumulating reserves to neutralise risk. Ethical rent is thus not prohibited by moral weakness; it is prohibited by structure

There is, however, a partial alternative — a safe haven that sits adjacent to the market: the placement of capital into low-risk, secured government instruments, such as government bonds, which may yield returns closer to inflation and may preserve purchasing power without requiring active extraction from others. This alternative depends on a single foundational condition: that the relevant state does not default on its debt, either formally or through stealth mechanisms that degrade the real value of repayment. Government debt is therefore not merely an investment product. It is a trust structure

This matters for the present argument because it reveals a further constraint: while the broader monetary system coerces capital owners into risk-taking and extraction, it simultaneously offers a narrow corridor of preservation through state-backed instruments — a corridor whose existence rests on political stability, institutional credibility, and the enforceability of public obligations. In effect, a portion of society is permitted to preserve capital passively only insofar as the state is capable of acting as guarantor

Accordingly, this paper's central conclusion remains: within the general environment, reaching the stage where a capital owner can preserve wealth through inflation absorption *while shielding others from extraction* requires an initial period of machine behaviour. The capital owner must become the accumulator — the optimiser — the private-equity analogue — before they may become the steward. Seemingly stewardship, under modern conditions, is not born from neutrality. The stewardship must be earned and purchased

About the Author

With regards to relevance to the topics discussed in this paper, the Author learnt the capital management game through fifteen years in private equity and investment banking, managing high risk investment strategies in operating companies and real assets at a number of elite investment funds. The Author notes that his fundamental DNA with regards to the principles and practice of responsible, investor-aligned capital management has been formed by working for some of the brightest minds in the sector, both as a manager and capitalist : the Author's current philosophy moves that alignment towards the public and the state, and pays tribute to its formational DNA by adapting it into a form that may benefit the wider public and the state. As such, credit for The Good State Project's ethical and moral successes must also go to those past managers and colleagues at Marathon Asset Management, Starwood Capital Group, Avington, Advent International and Deutsche Bank