

Dismantling Shareholder Primacy: Seizing the COVID-19 Moment



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Can, and should, the COVID-19 crisis signify an inflection point in dismantling shareholder primacy?

Decades after Milton Friedman invoked profits as the *raison d'être* of a corporation, debates over corporate purpose continue unabated.

Friedman's credo has proved remarkably durable. It lay the groundwork for both shareholder primacy and its allies, financial economics and principal-agent theory. The deregulation, free market ethos of the 1980s further enshrined the concept as foundational to corporate purpose.

Nonetheless, a new chapter of purpose debates unfolded in the 1990s, driven in part by the Bhopal (India) chemical spill and Exxon Valdez oil spill tragedies. These seminal events, coupled with rising concern over supply chains, labor standards and human rights, stoked new debates centered on corporate transparency and, more broadly, global capitalism and the financial system upon which it depends.

A new vocabulary began to emerge. "Team production," "redesign" and "multi-capitalism" laid the groundwork for rethinking the architecture of corporations amidst early 21st century exigencies. Concurrently, the "dot-com bubble," the Enron collapse and the Great Recession exposed the structural flaws in a system dominated by the demands – and metrics – of finance capital.

Since 2000, increasingly contentious debates spawned a wave of challenges to the legal underpinnings of shareholder primacy which Lynn Stout, a leading academic dissident, famously termed a "myth." Initiatives such as the U.S.-based "Corporation 20/20" and the European-based "Purpose of the Corporation Project" assembled multi-stakeholder processes to challenge the hegemony of shareholderism.

Enter COVID-19. Amidst the insurgent pandemic, corporations have been scrutinized and rated relative to their role in the escalation and mitigation of the public health crisis: pharmaceutical companies for raising prices of drugs related to COVID-19 treatment, meat-packing plants for unsafe working conditions, and the hospitality industry for unfair treatment of full- and part-time workers. At the same time, critics point to companies' stock buybacks and out-sized executive compensation in tandem with layoffs and downsizing.

As the economy has contracted, the disconnect between stock performance and the lived experience of the unemployed and food insecure has widened. This gulf between the financial economy and real economy was summarized in a recent *New York Times* headline: "Stocks are soaring. So is misery." While this divergence is not new, COVID-19 has brought it to a historic extreme.



Through the [lens of corporate purpose](#), COVID-19 shone a laser light on the consequences of financialization and the skewed interpretation of prosperity it fosters. When purpose is equated to share price, finance capital rules at the expense of human, social and natural capital. In the aggregate, across thousands of firms, shareholder primacy drives wealth disparities as capital owners claim a disproportionate share of the surplus. In fact, it is the collectivity and interdependence of all capitals that lies at the heart of long-term value creation. The deification of share price is a recipe for undermining both strategy and operations, distorting executive compensation, undermining worker compensation and benefits and diverting expenditures on R&D indispensable to a firm's long-term competitiveness.

The COVID-19 crisis is a crucible for the corporate character. Research findings in the [Test of Corporate Purpose \(TCP\) report](#) are revelatory. Companies that historically have demonstrated a commitment to multi-stakeholder capitalism have excelled in their response to the pandemic. Further, those that responded earlier responded better. These findings suggest a virtuous circle is in play. Firms with a more holistic, anticipatory approach to value creation are outperforming those lacking such approach. This, in turn, lays the groundwork for greater resilience in a turbulent, uncertain world.

By some indications, investors are seeing these dynamics at work acting accordingly. While ESG integration in investment strategies has steadily increased in both the U.S. and globally, recent data suggest superior returns of actively managed ESG funds that have outperformed traditional funds by 15 percent. Taken together, these trends suggest further unraveling of the misplaced and discredited assumption that for investors, doing good and doing well are inherently at odds.

The economic and social havoc wrought by the pandemic should serve as a moment of reckoning for corporate purpose. COVID-19 is forcing challenges to conventional assumptions about essential workers, work at home, living wages, paid and sick leave, the efficacy of online vs. in-person convenings and a host of other work/life practices. In the same vein, it should prompt soul-searching among corporations, encouraging boards, executives and workers alike to reconsider purpose in ways that confront the deleterious effects of shareholder primacy in favor of a more nuanced, holistic view of the enterprise.

Professor Colin Mayer of Oxford University, the Chair of the British Academy's FUTURE OF THE CORPORATION Project, argues that "Corporations ...do not and should not revolve around their shareholders any more than the planets revolve around the earth..." COVID-19 is a once-in-a-generation opportunity to make good on this maxim.