Leadership is More Than Profit

In the rush to globalization, the United States has tossed aside a crucial principle that guided the economic prosperity of the twentieth century: corporate leaders have a responsibility to their country, their community, and their employees that goes beyond maximizing share value.

Many shareholders will surely wince at this statement, in no small part because financial leaders have argued on this page and elsewhere that the only responsibility of corporate directors is to maximize shareholder wealth. There is even a widely cited, erroneous claim that corporate directors have a legal duty to maximize share value. In fact, there is no such legal requirement in the U.S., and this extreme and sole focus on share value has caused the actions of corporate leaders to veer wildly away from the interests of their employees and the nation as a whole.

Not that long ago, the success of corporations was intertwined with the health of their communities. In the early twentieth century, Henry Ford recognized that not paying his workers enough to buy the cars they produced would hold down the growth of the automobile market. Instead of racing to the lowest common denominator, Ford invested in human capital, productivity, and technological training in Detroit, building a corporate giant that grew in tandem with the local and national economies. As recently as the 1970s, General Electric CEO Reginald Jones argued that corporate leaders must balance shareholder concerns against the interests of employees, American industry, and the nation, a view that was endorsed by the Business Roundtable in 1981.

In the intervening years, this concept of corporate leadership has waned, replaced by the idea that businesses must always choose the path that increases shareholder profit, and that governments must support business in doing so, in order to increase GDP. This mindset implicitly excuses corporations, in the United States and elsewhere, to outsource factories, expertise, jobs, and resources, all on the promise of increased share value. Indeed, the Business Roundtable sadly reversed its position in 2004, asserting that the only obligation of business leaders is to maximize
shareholder profit. As a result we have seen economic growth in the US, but the benefit of that growth is going almost exclusively to the wealthy.

Corporations once had incentives to invest in R&D, education, and the development of technological expertise at home. Now, corporate directors have a greater incentive to make these investments where costs will be cheaper, and the United States is seeing the effects on its economy. It is no longer just low-wage jobs that are being shipped overseas, but also the technology, know-how, and capital that once fueled rapid growth at all levels of the economy.

It is time for western governments to develop sound national strategies that realign the interests of corporations with the country. A start is the British Companies Act of 2006, which explicitly codifies that directors should consider employees, the community, and many other factors in their decisions. Many US states have passed similar statutes in recent years, but they have had little impact on the actions of corporations.

Asian countries such as Singapore and China are beating us to the punch by offering tax and other incentives that lower costs and make it profitable for corporations to locate high value-added jobs in their countries, thus tying corporate growth to their national economic goals. Conversely, record corporate profits and record CEO paychecks in the United States have done little to aid the American economy.

If the United States and other western countries expect to thrive in the new global economy, it is time to admit that the interests of corporations and countries have profoundly diverged. If we continue on our current path of emphasizing corporate profit above all other concerns, and refuse to develop a strategy that strengthens the national economy along with corporate growth, we will continue to see global corporations thrive while local economies dwindle.

While many are already persuaded of the need for such a national strategy, some simply throw up their hands and say there is nothing that can be done. But in fact there is much that can be done. One obvious possibility is to do an American version of what we have already seen in Asia: create incentives for companies. While we do not have a government with a tradition of making individual deals with individual corporations, we do have a long tradition of using income taxes, including the corporate income tax, to provide incentives. We should consider a corporate income tax that rewards companies for having high value jobs in the U.S. This can be done in a revenue-neutral way if it also raises income tax rates for those that don't. This only the beginning of what we can do if we set our minds to it.

We should not continue to drift and leave our corporations with no sense of leadership in the national interest. Let us start now to narrow the gap between corporate and country goals.