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Should Business Schools Peddle Shareholder Value Maximisation?

We should teach our students that there are alternatives to the view that the purpose of business is shareholder value maximisation.

Educational and professional institutions have significant influence in setting norms for legitimate organisational practices. In this sense, business schools play an important normative role when they convey the paradigms through which managers should analyse the corporate environment. If business school students only get taught that shareholder value maximisation (SVM) is the purpose of the firm, then this is the most likely lens through which they will see their future professional roles.

The 2008 financial crisis was by some commentators blamed on business schools perpetuating an excessively profit centric view of the role of corporations and their directors. Such a charge is difficult to evaluate, but it does hold true that most business schools primarily teach SVM as the purpose of business. What is often left out from such a lesson is that profit is not the same as shareholder value and furthermore directors are unlikely to face a legal requirement to maximise shareholder value. Intellectual honesty demands that this be taught.

First then, shareholder value is nothing more than what *shareholders value*. This could be any legal goal or activity. It is certainly fair to say that many if not most investors are seeking financial return, though this need not be their sole concern. This is clearly portrayed by the increasing amount of financial resources being invested in ethical funds that have normative goals beyond the mere financial. Current corporate governance practices are not perfectly suited for determining shareholders' normative preferences, but this could be addressed through shifts towards greater shareholder democracy. The point is that shareholder value does not necessarily imply maximising shareholders' *financial* returns.

Secondly, directors are unlikely to face any legal requirement to maximise shareholder value even if the stated value desired by shareholders is financial return. Directors have a fiduciary duty to further the interests of shareholders, but this duty does not preclude attention to other stakeholder interests. In the U.S., for example, most states have non-shareholder constituency statutes that explicitly *allow* directors to consider the interests of other stakeholders. In the U.K., under the 2006 Companies Act, directors are further *required* to take into account the interests of other stakeholders such as employees, suppliers, customers, the community, and the environment.

While SVM is not a *legal* norm it is certainly evident as a *social* norm among directors. This is largely due to shareholders' sole voting rights for the board of directors which puts shareholders in the privileged position of being able to impose their interests on

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the board. Quite simply if shareholders are not pleased with the direction of the firm they have the power to dismiss the board of directors (although this rarely happens in practice). Business schools also play an important role in perpetuating the SVM as a social norm. Most teach as part of the "Theory of the Firm" that profit maximisation is the purpose of the corporation in society and that it is the duty of managers to pursue this end on behalf of shareholders as their agents. If no broader conceptions of corporate purpose are taught elsewhere in the curriculum then this is the paradigm that students are left with—and often this is taught without attention to the now widely-documented flaws of the theory and the misconception of the role of company directors and managers as agents for shareholders more specifically.

Given that "shareholder value" is open-ended and directors have goal-setting discretion, business schools should surely—if only for reasons of scholarly integrity—teach that there are alternative conceptions of corporate value creation to profit maximisation. It can potentially be whatever shareholders or directors want it to be.

When it comes to alternative theories to SVM, the most prominent contender is Stakeholder Theory, which says that the corporation is a vehicle for creating value for all stakeholders. This involves managers balancing the interests of various constituencies or even having board representation for stakeholders.

Viewing the notion of shareholder value as open-ended is not only significant for business students' future role as executives and possibly company directors but also their future role as shareholders. When shareholders are aware that a corporation's purpose can be other than SVM, then more may demand normative along with financial goals. Shareholders will then be exercising not only their rights but also their responsibilities.

*This editorial is based on Smith & Rönnegard's newly published paper **Shareholder primacy, corporate social responsibility , and the role of business schools** in the Journal of Business Ethics.*

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