

Your Turn

by Richard R. Ellsworth

I The Corrosion of Corporate Purpose

What has led seemingly moral business leaders to conduct unethical, and even criminal, acts? In many cases, the seeds were planted by the country's most prestigious business schools. When these leaders were students, many of them were indoctrinated with a near-religious ideology: the belief that maximizing shareholder wealth is a corporation's reason for existing. Today, this dogma continues to be the unofficial religion of business education, even though it's at the expense of moral courage and inspirational purpose.

The high-profile corporate scandals of the past three years may have tempered the strident rhetoric of some who doggedly put shareholder wealth first. Yes, corporate governance has received greater attention and some ethics and governance courses have been developed. But many of those courses, such as those on Enron or WorldCom, promise to have limited shelf life. Furthermore, they haven't eroded the pervasive influence of this ideology within business schools. The shareholder-driven ideology remains unchanged.

Consider the results of a recent Aspen Institute survey. When incoming MBA students were asked about the primary responsibility of a corporation, the most frequent answer was to satisfy customer needs. However, by graduation, their responses had changed—most answered that the highest ideal was to maximize shareholder value.

Business schools' emphasis on shareholder wealth—and its surrogates, ROI and the discounted net present value of investments—has its



roots in the business school war of reputations and rankings that began in the 1960s. Many leading schools found that nothing had greater impact on their standing than increasing the quality and visibility of their finance faculty, since the finance field was becoming more aligned with theoretical economics than with the practice of management. Certainly the increased rigor of financial theory has benefited students, corporations, markets, and individuals alike; but it has also had critical unintended consequences.

In many schools, intense, yet subtle, struggles ensued between “tough-minded” finance professors and “soft,” managerially oriented faculty. As finance faculties grew increasingly powerful and their theories became widely lauded, an intellectual arrogance arose that chilled opposing points of view regarding the purpose of corporations. Other courses like strategy, management, organizational behavior, and marketing, which should have challenged this orthodoxy, did not. Consequently, the shareholder-first ideology became the dominant business school doctrine.

This new religion—the maximization of the firm's current share price—effectively supplanted the long-standing belief that serving customers' needs was the prime function of the enterprise. One unfortunate result of the emergence of the stockholder-first faith has been a bifurcation between people and economic issues. People are increasingly seen as a means to financial ends.

As a result, MBA students are graduating indoctrinated in a narrow, largely unchallenged set of beliefs about the basic purpose of the enterprise. Professors who ground their theories and teaching in an alternative set of beliefs are widely marginalized. Debate on true corporate purpose has slowly disappeared from the mainstream curriculum, except in courses on business ethics. Even those courses often are appendages to the curriculum and on the periphery of faculty interest.

These business-school phenomena, which work to silence dissent, have clear parallels in today's corporate scandals. Those who had the courage to speak up internally about their organizations' misdeeds—such as Enron's Sherron Watkins and WorldCom's Cynthia Cooper—were silenced or pushed aside. Their bosses chose ideology over good judgment and felt these people did not grasp the ideology's first imperative. Maximize shareholder wealth!

Like many seductive “solutions” to complex problems, the doctrine of shareholder wealth is beguilingly simple, clear, and quantifiable. It allows students to ignore the real-world complexities and responsibilities that many find difficult to comprehend, much less appreciate. They never need to confront the messy necessity of pitting one corporate

EXEMPLARY CORPORATIONS ARE ENHANCING THEIR COMPETITIVENESS BY DEVELOPING A CUSTOMER-FOCUSED SENSE OF PURPOSE THAT EMPLOYEES VALUE AND FIND PERSONALLY MEANINGFUL.

responsibility against another. There is always one answer: Act in the shareholders' interest. For faculty, this belief simplifies the world sufficiently to allow them to develop elegant, tightly reasoned theories, uncluttered by business realities.

The tenacious power of this faith extends well beyond business school indoctrination. It provides a simplistic rationale for many of management's questionable actions. Its moral justification is, in essence, that "greed is good." It promotes the outdated assumption that financial capital, not human capital, is the primary source of any organization's competitive advantage. At its foundation is the belief that the pursuit of shareholder wealth (which many equate to "personal happiness") will put financial capital to its best use and thus create the greatest happiness in society. Undoubtedly, some corporate managers have used this argument to pressure outside auditors into approving questionable accounting practices.

After arguing that their overriding allegiance is, legally and morally, to the shareholder, senior managers often establish boards dominated by management-approved directors. They align themselves with the most docile major stakeholders, often composed primarily of financial institutions more willing to sell their shares than to invest energy in influencing management's actions. These factors set managers free to use their presumably inviolable responsibilities to shareholders to deflect any criticism of their actions and increase their autonomy from more troublesome constituencies.

Business schools and corporations must reverse this trend by exorcising the destructive cult of shareholder

wealth maximization and return to a venerable, central truth—that providing value to customers is an organization's *raison d'être*. This is a guiding philosophy that leads a company to lasting competitive success, as leaders of great companies know.

Fortunately, the time is ripe for change. Corporate governance has been strengthened and transparency increased by recent legislation, more strict enforcement, and public outrage. Today, students and managers alike more readily question the efficacy of a shareholder-focused purpose. Strategic pressures are forcing a shift to knowledge-based competitive advantages and away from capital, to customer interest and away from all-encompassing shareholder interest.

Exemplary corporations are enhancing their competitiveness by developing a customer-focused sense of purpose that employees value and find personally meaningful. Consequently, these companies are realizing the considerable power that lies within their own employees' commitment, imagination, and aspirations. More managers are recognizing that in a knowledge-based, increasingly competitive, global economy, the shareholder-wealth ideology is unlikely to win in the long term. It neither promotes competitive advantage, nor unleashes human creative potential.

To respond effectively to these realities, what is required of business schools is not marginal change in curriculum, but a transformation. Business schools should begin with the recognition that, while they cannot teach moral courage, they can provide students a coherent path to developing their own well-grounded philosophies of management. They

can do so by broadening and deepening students' understanding of the world, human aspirations, managers' responsibilities, and the true sources of competitive advantage.

Fundamental to this transformation is the recognition that management is as much an art as a science—a liberal art that encompasses the humanities and the social sciences. Management education needs to overcome its insularity. Its faculty need to reassess the philosophy of management underlying their research and teaching—beginning with a corporation's primary purpose. In the end, some professors might not advocate a customer-focused corporate purpose, but their teaching still should be open to other options. Only then can they help students appreciate the social, economic, and practical implications of the alternatives.

The prevailing view of corporate purpose in America is under competitive attack. The stakes are high. The outcome will determine the nature of 21st-century capitalism and which companies will survive. The question for business schools and corporate leaders is, how can they influence that outcome? One answer lies in how they influence their students' and employees' beliefs about the corporation's primary purpose. Those beliefs will determine not just the moral quality of their actions as managers, but the very future of their organizations and their nations. **Z**

Richard R. Ellsworth is professor of management and co-director of the Institute for Advanced Studies in Leadership at the Peter F. Drucker Graduate School of Management at Claremont Graduate University in California.