

The *Real* Purpose Of A Corporation

Among the many questions about corporations that I have pondered on over the last few years, none is more intriguing than the one on the fundamental objective of the joint stock company: What is the *real* purpose of a corporation? The brightest minds, all over the World, have written in lucid detail on this, yet none of their arguments are fundamentally compelling, as, for instance, assertions in biology or physics, which are the documentations or extrapolation of observed or deduced factual behaviour. Arguments about the real purpose of a corporation always speak of founder behaviour, the corporation's influence on Governmental policy, improvement in quality of goods and services and in their availability and about the merit of competition and the free market. Are these arguments convincing?

My contention is that the objective of a corporation is not, as is popularly imagined in management academia, the creation of wealth for its shareholders. History reflects on the quality of shareholders with some derision - most, indeed the vast majority of, shareholders aren't investors but speculators. They will buy the stock of a company essentially because others are doing the same thing (the 'others' have the same argument) and will prefer to buy at high prices, in anticipation of immediate higher prices, the 'inevitable' result, they suggest, of aggregate demand and supply, helped in some measure by the odd market tip. Oddly enough, the same investor, in a subsequent depressed market, will not buy the same stock at a significantly lower price, even if the performance and the growth of the company has been stellar over this entire cycle.

Organisations aren't the exception to this irrational behaviour either. The maturation of a market is meant to imply that individuals participate less and less and 'professional' money managers - pension funds, mutual funds, institutional investors and fund managers, managing the corpus of high-net worth individuals - operate more. The underlying motive is however the same everytime - greed and the desire to display 'performance' quickly, even when the corporations that they invest in can seldom do the same thing. Hence, they exercise just about the same discretion as their less-informed clients do.

These fund managers have, however, one critical advantage, that of financial power and visibility. The Board of a Company can comfortably ignore the pleas of a discontented small investor. It must however pay the closest attention to the rumblings of disenchantment from any Mutual Fund, if it wishes to see its stock price stable. The founder of a Company or the dominant shareholder needs the help of these Funds to support his own net worth and future issues of equity by his Company. This scenario is now wonderfully set to focus the objective of the corporation on short term operations and speculation.

Shareholder wealth creation can be quite different from the business and financial fundamentals of the Company. An existing shareholder in a company will benefit from an increase in the price of the company's shares - this is commonsense. However, such an increase need not accrue from the implementation of long term business strategy - on the contrary it could be due to :

- The Stock Market's *expectations* of future growth, real or imagined and a 're-rating' of the Price - Earnings Multiple, either of the company in question or of the industry it is in. As an example, companies that have been in renewable energy have seen a 're-rating', as the climate change issue moved to the front pages of newspapers.
- Eschewing long term growth for short term profitability. For instance, not investing in advertising would increase the short term profitability of a well-established cash-cow brand. This would deplete its brand value for the future though.
- The 'noise' around a Company's share: the tips whispered, the gossip exchanged, the 'emerging new story' believed in.

History, that sagacious teacher, tells us that only a fraction of the Companies listed on the Stock Exchanges actually witness a *consistent* correlation between the long term growth of the Company and its immediate share price. The stock market is often efficient, and often terribly inept at judging long term prospects. The result: frequent ups-and-downs in share prices driven by irrational behaviour of speculators who expect corporate managements to cater to their silly behaviour. Indeed, they are not alone; a substantial number of companies, unfortunately, see the vicissitudes in their stock prices as perfect opportunities for manipulation and personal gain for those owner-managers who value their bottom line over the company's future.

Isn't it therefore quite asinine that the purpose of the Corporation should be the continued growth of that one number, the Share Price, to the exclusion of all others? Isn't this a simplistic way to judge a complex network of human relationships that interact to perform numerous commercial and emotional transactions? Isn't it equally silly, that a sensible person, should accept this argument as valid and justified? It all began, of course, with Wall Street, when money creation and dissipation, along with outrageous displays of the wealth acquired through 'honest sweat' (as opposed to the accumulation by the mafia or a dictator or indeed even by the Royalty in a natural resource rich region) was the cornerstone, the example, the very foundation for Capitalism, long touted by the West as *the* panacea for humankind. A few decades later, while the wheel has not yet turned the cycle, there is substantial disenchantment with Capitalism, which has now been the New World Order for a couple of decades.

What has gone so horribly wrong with the Western order of Economic Thought is that it assumes disparities in its economic calculations and often *encourages* it in the name of 'Markets' and efficiency, while pontificating, within its own geographies, of gender equality, democracy and freedom. Economics, it seems, has its own principles (as opposed to laws), even if these principles are contrary to what is just and right in a civilised society. The Principle of Profit Maximisation is the first such principle. Under this, it is deemed perfectly alright for a developed nation with excess milk production to pour it down the drain rather than transport it in suitable form to those who need it most, because supply must be kept within limits to manage price. It is equally acceptable in the pharmaceutical industry to test new drugs on people who live on the margins of sheer existence, since, in economic terms, their lives are 'cheap' and hence easily purchase-able. The same industry justifies prohibitive costs of a new and important drug by pricing it for the economic elite, when they may not need it the most. Their argument - high research costs must be recovered as soon as possible,

else the stock markets would beat the Corporation value down. Interestingly, the team of scientists who develop these drugs often differ in opinion from their Board. They are driven to research by the passion for finding solutions that will improve the human condition. Yet, when they succeed, the Corporation will listen more to the speculators in the stock market, than to the ideological inclinations of its finest minds. This obsession with maximising profit and hence the market capitalisation of a Corporation is a phobia, a malady, no less.

Another key example of an economic principle - the principle of efficient allocation of land, a resource - gone awry is the Special Economic Zone program in India that encourages corporations to become business infrastructure providers. Across the country, farmer movements have emerged to emphasise the criticality of their livelihood, as corporations flexed their sinews to purchase land at low costs and 'value add' to the status of an industrial park; the divide between industry and agriculture, urban and rural, 'developed' and 'under-developed' is now complete. These farmer movements are not the product of political instigation alone. On the contrary, they are the last resort of an economic community on the margins, who have no alternative but to fight back.

Even a corporate group with a carefully cultivated image of munificence as the Tatas has been on the wrong side on many occasions: two instances being the displacement of the largely tribal population in the district of Kalinga Nagar in Orissa for a Tata Steel plant and farmer displacements at Singur in West Bengal for the factory that will produce Nano, a small car by Tata motors. In the first instance, it is now known that the company acquired a large tract of land from the State Government at a subsidised price to set up an enormous project, which would cause substantial displacement of the local people. This was done after the Government had acquired this land from the tribals at a further discount, playing the role of a realty broker with elan, backing its acquisition with its colossal power.

In June 2008, a small news item in *The Hindu* was telling. It stated that participants in a public hearing conducted by the Andhra Pradesh Pollution Control Board in a Rachapalli village in Vishakhapatnam district had overwhelmingly rejected a Rs. 8,000 crore alumina refinery plant, to be set up by a company called Anrak Alumina Limited. The reaction from the participants came as a shock to the ruling party as it took a lot of pains to get the villagers' consent and deployed a large police contingent as a means of deterring potential dissenters from voicing their views. Many villagers, who had earlier accepted monetary compensation for their lands, rejected the project at the public hearing, while three women from the village were in tears while expressing their anguish over parting with their lands. Such complete rejection is now the norm across the country, as rural India sees the divide between them and the city dwellers growing, as their education gives them the tools to be belligerent and as non-profit organisations working to alleviate their plight take cudgels up on their behalf or mobilise them to resist the decimation of their livelihoods.

A variation of the same argument of economic efficiency dominates vendor selection - the focus here is on price and the lowest-cost-alternative. An excellent example is the business of apparels, illustrated in the State of the World 2004 by Juliet Schor, Professor of Sociology, Boston College.

The Global Sweatshop

In the United States, clothing has become so cheap that it's even hard to donate. About eighty years ago, the average US household spent 17% of its total expenditure on clothing. In 2001, the figure was just 4.4%, despite the fact that consumers were buying far more apparels.

The reason: exploitation of female labour in apparel factories throughout Asia and Central America. Vendor factories supplying Nike, Disney and others routinely require employees to toil over 100 hours per week in dismal working conditions, often subjected to serious supervisory abuse. The New World Order has only exacerbated this condition. Factories in Bangladesh, India, China and Indonesia compete with each other to *retain* vendor status to the large American brands, the focus of their competition being just one factor: price. The industry being labour intensive by nature, the outcome is that workers are continuously repressed by management on the truly credible threat that their customers would take their orders elsewhere. Wal-mart, which controls 15% of the US apparel market and is the World's largest clothing retailer, relentlessly squeezes labour costs in Chinese factories - they can be as low as Rs. 5 per hour and rarely go beyond Rs. 10. Yet, the mark-up at Wal-mart stores can be enormous, possibly 10 times the cost of the imported apparel.

The result of this trade equation: apparel prices *fell* by 10% over the last decade. Demand, concomitantly, sky rocketed, increasing a stunning 73% between 1996 and 2001. By 2001, the average US consumer purchased 48 new pieces of apparel a year, about once a week: ready made apparels are now considered a disposable commodity.

In a truly ironic turn of events, some international NGOs have attempted to ship large quantities of used clothing to disaster areas, including Bangladesh.

A third economic principle, always unstated, is to view production and sales as units of economic value, quite independent of the societal implications of such output. An excellent example of such a principle gone wrong is the tobacco industry. Surely, there is no sane person on Earth who does not believe in the ill-effects of tobacco, no one who hasn't viewed the increasing flood of evidence against tobacco with rising alarm. Yet, the tobacco industry, it must be acknowledged, is a financial's analyst's delight. The addiction that tobacco induces means sustained and increasing profitability; the earlier children are inducted into the habit, the longer the cycle of cash flows. However, this goes against the basic definition of human progress, if it means an increase in the quality of human existence. We may have eliminated small pox, but have, in turn, replaced it with lung cancer, driven by the inestimable greed of giant corporations. Indeed, so defensive is the tobacco industry about its 'cause' that in 1993, Philip Morris and its public relations firm created a non-profit group called the Advancement of Sound Science Coalition, to fight regulation against tobacco. Their logic : there is no *concrete* evidence against tobacco, only circumstantial. In other words, before you ban something, prove beyond all reasonable doubt that it is harmful (an argument now being advanced by the proponents of genetically modified food technology). Excuse me, shouldn't it be the other way around? Shouldn't something be introduced, only after it has been proved to be harmless, beyond all reasonable doubt. Smoking surely has no benefits. If the argument is that it provides pleasure and hence connotes a standard of living, there is no refuting an acceptance of cannabis or opium or, indeed, any of the multiple forms of human depravity.

This approach of asking for 'Science' to be the impartial judge is shrewd. It appeals to the intellect of the common man and the judge on one hand, and seeks, on the other, to brand the alternate brigade - the environmentalists, the NGOs, the Conscious Community - as a motley group of career protestors, who need an issue to ensure their own survival, driven by emotional decibels and passionate language, rather than cold logic. But asking for 'Science' is deceitful and self-serving. To prove something beyond all reasonable doubt, takes years, if not generations during which time the Corporation can use its own lobbying power to influence policy or look to build credible financial alternatives to its existing cash cow. Corporations have used this logic with stunning success as evidenced by the persistent bleatings of the pesticide industry on the safety of its extraordinarily toxic formulations. Indeed, since the word 'pesticide' sounds dirty and toxic, the ingenious alternative in use is 'crop protection compounds'. The 'Science' argument was most notably used recently in 2003 by US Vice President, Dick Cheney, when he argued in favour of opening Alaska up for oil drilling. In doing so, he batted with elegance for the Corporations he represents in the American Government. That these Corporations control American policy is now accepted. That they can be prepared to damage the environment that our future generations will inherit is, thankfully, still being fought by courageous, yet solitary, warriors around the globe, none more notable than Nigeria's Ken Saro-Wiwa, whose ethical stand against Shell's depredation cost him his life.

The consolidated and sustained assault of the Corporate Sector on society has given it a sullied image. If you are not in the Sector, you are clearly outside it - termed a 'have-not' - and often at the receiving end of its abuses, sponsored in ready terms by the State. These 'have-nots', as can be readily imagined, are the poor, the tribals, the landless, the rural emaciated labour, the millions in the villages of India's heartland, where development in any form is an alien concept, where the hour-hand

of the clock moves because it must, where the purpose of existence today is to seek the purpose of existence tomorrow. When a Corporation moves into the neighbourhood of a village caught in this time-warp, the opportunities that it brings with it to create meaningful, grassroot change are truly immense. Yet it chooses, with a few rare exceptions, to exploit the natural resources and labour of the village and to create only a few enduring job opportunities for them, to acquire agricultural land at dismal prices negotiated directly with senior ministers or bureaucrats of State Governments who have no emotional linkage or livelihood dependence on the land to be sold, to create dependency on the Corporation, rather than foster inter-dependency. The power remains only with the giant. Corporations, of course, choose to 'give back', by setting up a clinic, building a water tank or sponsoring a school, but the cost of this effort is but a mere fraction of the sacrifice made by the village, as evidenced by the story of Coca Cola in the village of Plachimada in Kerala (story in a box below)

Thanda Matlab Coca Cola : a story in 2004

This is the tale of two lives.

One is the World's best known brand. Actors and cricketers endorse it. The World drinks it. Warren Buffett invested in it. It represents the idea of mass market. Of global uniformity, even far more than McDonald's. It is said that its original formula, codenamed X, is probably the World's best kept secret. Thanda matlab Coca Cola.

The other is a little hamlet, subsisting on agriculture called Plachimada, in Chittoor taluk in the Palakkad district of Kerala, close to the Tamil Nadu-Kerala border. The local residents have survived on their land for yeons, in Kerala's agricultural bowl, largely at peace - tribals from the very backward Eravalar and Malasar communities.

Two years ago, Coca Cola's bottling plant began operations in this village. Today, this plant uses over half a million litres of water *per day* for its operations. The villagers have no water for their land.

As a token of munificence and mercy, the Coca Cola bottling plant supplies drinking water to its victims, the residents of Plachimada.

This is not a capitalism vs socialism debate; that would be ideology and banter. This is a simple example of a question that you and I must ask ourselves: just what is development?

Consider the facts: the bottling plant uses 600,000 litres of water to produce about 150,000 litres of aerated drinks. City dwellers, like you and I, use about 200 litres every day for our needs. Poor people use much less - in all probability the inhabitants of Plachimada use about 50 litres every day and therefore, the bottling plant's daily utilisation of water represents the life line of *twelve thousand local people*.

Did you ever realise that for every bottle of Coca Cola that you drink, three bottles of water are wasted, ie, converted into effluent?. A good part of this is used to wash the bottles, with chemicals and detergents. And while the company claims that this spent water is treated and then released outside the plant, residents say that the waste is a foul-smelling semi-liquid and sedimented slurry. Initially, the bottling plant attempted to pass it off as "good fertiliser". The residents of the village found that the waste did not decompose at all and its foul odour persisted; they then refused to accept the "fertiliser" anymore, but the lands of many had, by then, turned unproductive and barren . Today, the company dumps it along the bank canals and within the factory premises.

Where does the bottling plant get its water? That's the genesis of the problem. It has dug an estimated six borewells, *within a two year period*. This has depleted the water levels in open wells and borewells over a large area around the plant and the village. In fact, the level of water depletion can be gauged by the fact that three irrigation reservoirs in the area, at Meenkara, Kambalathara and Venkalakayam, *have dried up completely*. Due to poor rainfall in 2001-02, the region went dry for seven months, which has led to an acute water scarcity.

What do you think the Coca Cola bottling plant will do when its water sources dry out completely? Move to a new site, of course, its move facilitated by Government "backward area subsidies" and other sops such as sales tax deferment and the like.

But what about the local people? Are they doomed to move from subsistence to starvation as a result of our daily fix of Coke? Will they get the backward area benefit when they migrate from Plachimada to Palakkad and other towns in Kerala to live on the edge in overcrowded slums as the marginalised, ignored section of a rapidly "developing" economy?

Surely, we have a problem. Inequalities have existed, and will exist, in all societies, but any activity that widens the gap this way surely cannot be "development". Is this Coca Cola bottling plant symptomatic of our national investment and economic decisions that seek to project an image of India as a open and rapidly evolving economy - an image that the rest of the World and our own urban and semi-urban constituency seek shelter in?

Then, are the poor doomed?

So, if this is the way of the Corporation, can there be a change? Can the World move towards a more equitable system? Is there, essentially, a panacea? If so, what is it?

I believe that Corporations must re-think their objective on two parameters.

The first.

The real purpose of a Corporation is the creation of Social Wealth, not shareholder Wealth. Shareholders are but one interest group in the Social cauldron. If a Corporation accepts this tenet that I put forward, it will walk away from strategic directions that, while maximising profitability, place the objectives of the shareholder at loggerheads with those of society. For instance, if the shareholder imperative is to shift an existing polluting factory in a developed nation to a less developed country that needs employment and is prepared to live with toxic waste in return, the Responsible Corporation will choose to focus instead on the far greater challenge of improving its own production process and meeting stringent emission norms or developing alternatives that are environmentally compatible, in relentless pursuit of sustainability. This will mean short term losses, negotiation with the aware Governments in the host country of the Corporation, much larger costs of effluent treatment and the pain of dealing with an incensed community of irascible speculators. It will mean, however, that the planet, *our Planet*, will become a healthier place to live in and the respect for the Corporation that has the courage to address real issues will grow.

Again, a Responsible Corporation will mercilessly monitor vendors from countries with cheap and ill-treated labour and shift its business, not on the basis of costs alone, but on the basis of humaneness and vendor responsibility. This approach will directly contradict the view of the Speculator, who is the dominant sub-species of the shareholder class, yet, I am convinced, such responsibility will directly benefit the long-term responsible shareholder.

The finest epitome of this standard would be an Annual Report that speaks to the Community and not to the Shareholder alone. Such a firm would present its various Statements of Performance and Responsibility, audited not by a firm of Accountants alone, but by experts in Fair Trade, Environmental Standards, Labour laws and customer satisfaction. Among organisations that have set standards in defining the scope and objective of their societal responsibility are Ben and Jerry's, Patagonia and The Body Shop, and in India, Thermax, a mid-sized corporation in the business of energy and environmental engineering solutions.

Business must now be told, and repeatedly reminded, that it is the most significant force in Society, just as the Monarchy was in ancient times and the Government was for most of the twentieth century. In a world that increasingly values economic power, over all else, as a source of dominance, 51 of the top 100 economies in the World are Corporations. A Corporation like Mitsubishi alone is the size of Indonesia in economic value, with only a minute fraction of its population and with no moral responsibility other than the declared profit maximisation goal towards its fickle shareholders. This economic power is, further, heavily concentrated - the combined

sales of the top 200 Corporations in the World is equal to 28% of the World's GDP, while about 70% of the World's trade is managed by 500 Corporations. With such polarisation, the realisation of the Real Purpose of the Corporation is now not an option - it is an imperative.

The second.

Far too much is said of efficiency - doing the thing right, as it were - and the Global Corporation is second to none here. The focus must change to effectiveness - **doing the right thing**. Efficiency dictates continued exploitation of apparel factory workers. Effectiveness demands responsibility, customer education and viewing the vendor's labour as an extended work force. Efficiency demands a strategic positioning of the tobacco business as a 'cash cow'. Effectiveness demands focus on rapid replacement of this business with a sustainable and forgiving product, that bolsters the standards of living and upholds human dignity rather than demeaning addiction. Efficiency is driven by the dogmatic views of a Cost Controller. Effectiveness is driven by the Visionary, the Financial Strategist, the Thinker-Doers of a Corporation.

It isn't easy, of course, to be effective - indeed all metrics of measurement in today's Corporation oppose it in thought and deed - which is why a fundamental and paradigm shift in consciousness is needed. Primarily, I believe the focus must move to the long term, as it used to be many years before the Market-isation of the Economic Order, as well as the eschewing instant gratification. Since no Corporation will voluntarily make such a change, arguing that the competition will then wipe it out, the consumer, through her wallet, can drive the Corporation's conscience to do the right thing. This change in focus must necessarily be accompanied by the enlightenment of the academics who teach Management and espouse new theories, whose own excessive analytical short term reasoning is, in part, responsible for the dimensions of the problem. Take, the theory of the bottom of the pyramid, an apparent opportunity in market creation, first espoused by Prof CK Prahalad. In this model, he exhorts companies to create products and services that are so designed and so priced as to seek to convert the lowest ranks of the social income structure into productive, self-respecting consumers. On the face of it, the logic underlying this is cogent. In practice, however, this *could* mean a variety of things, many of them most undesirable in rapidly evolving societies such as India's. An example: when consumer product companies began to market sachets of shampoos and detergents in India's remotest villages, they offered consumers access to two 'developed' market products created using a basket of chemicals, at a highly affordable price of Re 1 per sachet. Many other products, including the highly addictive and noxious gutka, are now offered in sachets.

Two important effects observed are:

- The countryside is now littered with used sachets, which when burnt, as is usually the case, cause a health hazard to the local population. The solution of one problem has created another, of a more toxic nature. Similarly, the local lakes and ponds in village communities now carry unsafe levels of detergent phosphate and their water is unsuitable for filtration.
- Traditional forms of personal hygiene have now been relegated to the bins of history, with only a superficial understanding of their efficacy.

This is a classic example of being enormously efficient (as judged by the penetration of these products over a fifteen year period), yet ineffective in the larger societal context. This arises because, in the opinion of the Managers of these Corporations, their responsibility is to their shareholders and to themselves principally and, if time and profits permit, to their employees. They have no obligation to design ecologically sustainable products or take back used packaging since Society does not pay them to be responsible to it (though there are rare exceptions - organisations such as The Seventh Generation, Tom of Maine's and Body Shop head this list). Any problem their operations create will be addressed by the Government to whom they are obliged to pay taxes. This is a comfortable and evasive agreement of sorts, couched in layers of public relations around corporate social responsibility. If, as a result of negligence, there is a crisis, as happened with Union Carbide in Bhopal in 1984, the Corporation will spend more money on public perception than on amelioration.

This is inexcusable. It happens because most managers, concentrate on tomorrow's problems and never think of the long term, the truly long term of five and ten years, though they would plan personally for their retirement. If, as a result of such vacuous planning, they need to take decisions that improve profitability today but damage the environment, they will do so. An interesting defence of such decisions is to look at the competition and say; "if I don't take this decision, they will anyways." There are no material prizes for pursuing the Real Purpose of the corporation.

Yet, for everyone, there is really no other way. A Corporation which wishes to survive well into the Twenty First century, be respected as an honourable member of society and enrich its balance sheet, must change the thinking that drives it today. If the World, after a dalliance with disaster in the years of the Cold War and Arms Accumulation, is no safer today, it has less to do with modern terrorism and more to do with the peregrinations of the uncaring, profit-centric Corporation, whose imprint on a globalised society has brought with it a deterioration in the quality of air, water, food and leisure available to the citizens of the World. It cannot escape this responsibility by pitting the process of 'development' against conservation, by mouthing the platitude of eggs having to be broken to make an omelette.

If the Corporation accepts these tenets of Purpose and Effectiveness, the World will become, over a period, a better and safer place. Yet, it would take an incurable optimist to believe in the ability of all those in power to change their mantras, their staple diet, their tunneled-vision. Which is why - and here is a prognosis - those that change will flourish in this Century, while those that don't will see their economic value erode as enlightened citizens seek safer products and services, in an effort to reclaim the quality of life that the Corporation has taken away from them. There is, I repeat, no other way.