

Sustainable Business Research Peak of Lee Kong Chian School of Business

**Workshop on Corporate Purpose:
Corporate Purpose and the Need to Move
towards System-level Investing**

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The Big Picture and Its Framing

- The workshop is entitled “Corporate Purpose”
 - Typically such conversation is framed around Milton **Friedman**’s 1970 NYT op-ed on shareholder capitalism vs. **Freeman**’s stakeholder view
 - **Focus of this talk**: Two key questions
 - 1) What’s the role of “**time**” in this debate?
 - 2) Does this framing from the 1970s still fit the big (new) picture, or would a **new framing** be more fruitful?



vs.



#1) The Role of Time & Corporate Myopia

- What's the role of "time" in this debate?



- Friedman: maximize long-term firm value

- Underlying assumptions:

- 1) **Governments** implement effective public policies

- 2) **Managers** adopt a long-term horizon and maximize long-term profits

- ➔ Yet, do those assumptions hold in reality? **What if they don't hold?**

#1) The Role of Time & Corporate Myopia

- Managers' **myopic behavior**
 - Large literature in psychology and economics (e.g., Ainslie, 1975; Thaler & Shefrin, 1981; Loewenstein & Prelec, 1992; Meier & Sprenger, 2010; O'Donoghue & Rabin, 1999; Frederick, Loewenstein, & O'Donoghue, 2002)
 - Common theme: individuals are **“hyperbolic discounters”**
 - Preference for short-term rewards over long-term rewards, even if the latter are substantially higher.
 - Reasons: Cognitive limitations, instant gratification, impatience, etc.
 - **For executives**, myopic behavior further **reinforced** by
 - Career concerns (e.g., Gibbons & Murphy, 1992)
 - Analyst pressure to meet or exceed analysts' earnings forecasts (e.g., DeGeorge, Patel, & Zeckhauser, 1999)
- ➔ As a result, myopic managers tend to favor short-term investments that pay off in short run at expense of long-term investments (e.g., Flammer & Bansal, 2017; Graham et al., 2005; Holmstrom, 1999; Stein, 1988, 1989)

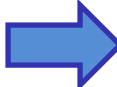
#1) The Role of Time & Corporate Myopia

➤ **“Time-based agency conflict”** (Flammer & Bansal, *SMJ* 2017):

Managers have an excessive preference for the present, and hence need not act in shareholders’ (long-term) best interest.

➤ Well-designed governance structures (e.g., executive compensation tied to long-term financial and ESG performance criteria) can improve sustainable practices and ultimately contribute to firm value

- Flammer & Bansal (*SMJ* 2017)
- Flammer, Hong, & Minor (*SMJ* 2019)



Corporate short-termism is hampering business success—Absent incentives, executives tend to underinvest in long-term projects, hurting companies, investors, society, and the natural environment.

#2) New Framing: The Need to Move towards System-level Investing

- Time to Reframe

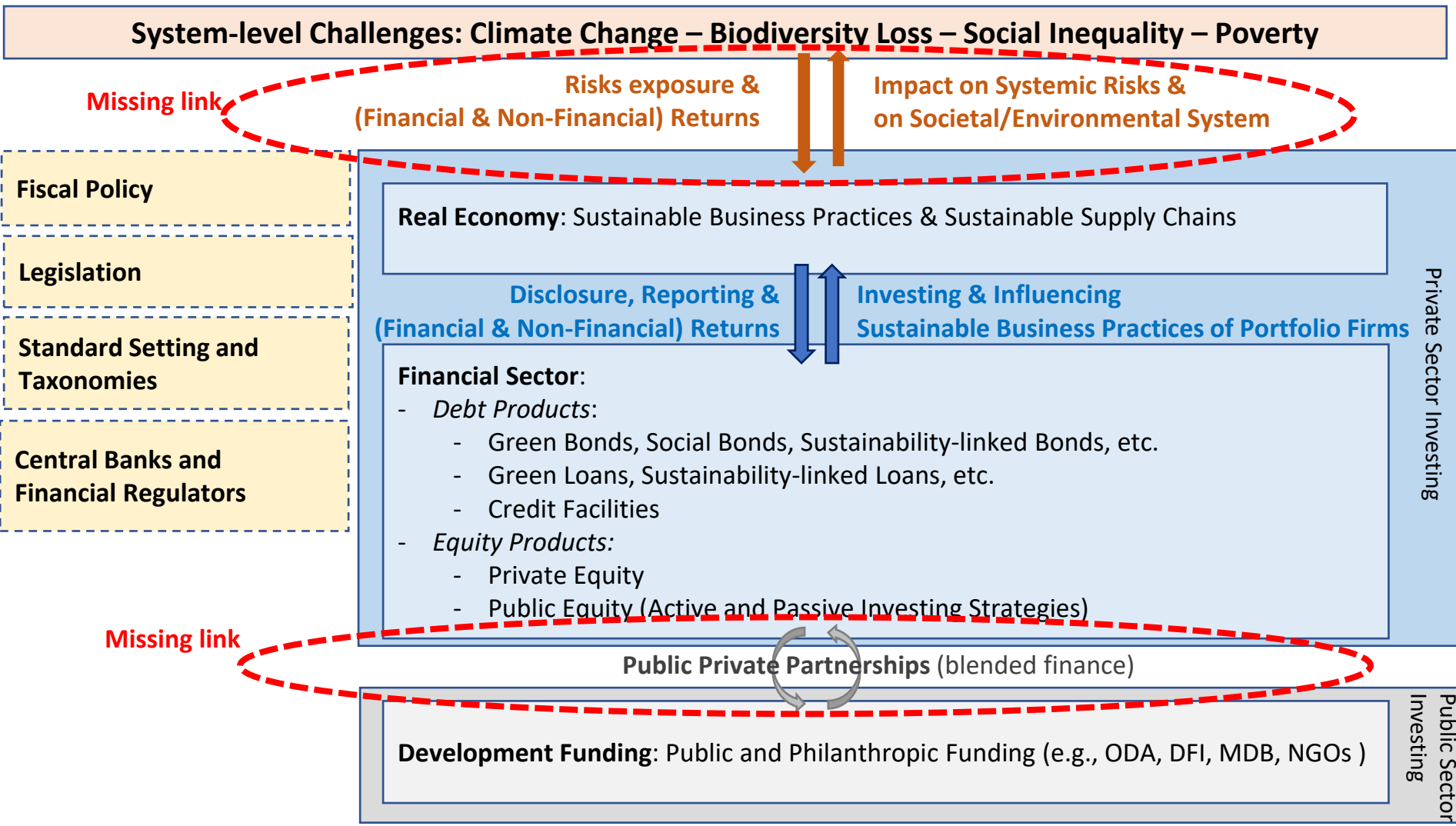
- Does this framing from the 1970s still fit the big (new) picture, or would a new framing be more fruitful?



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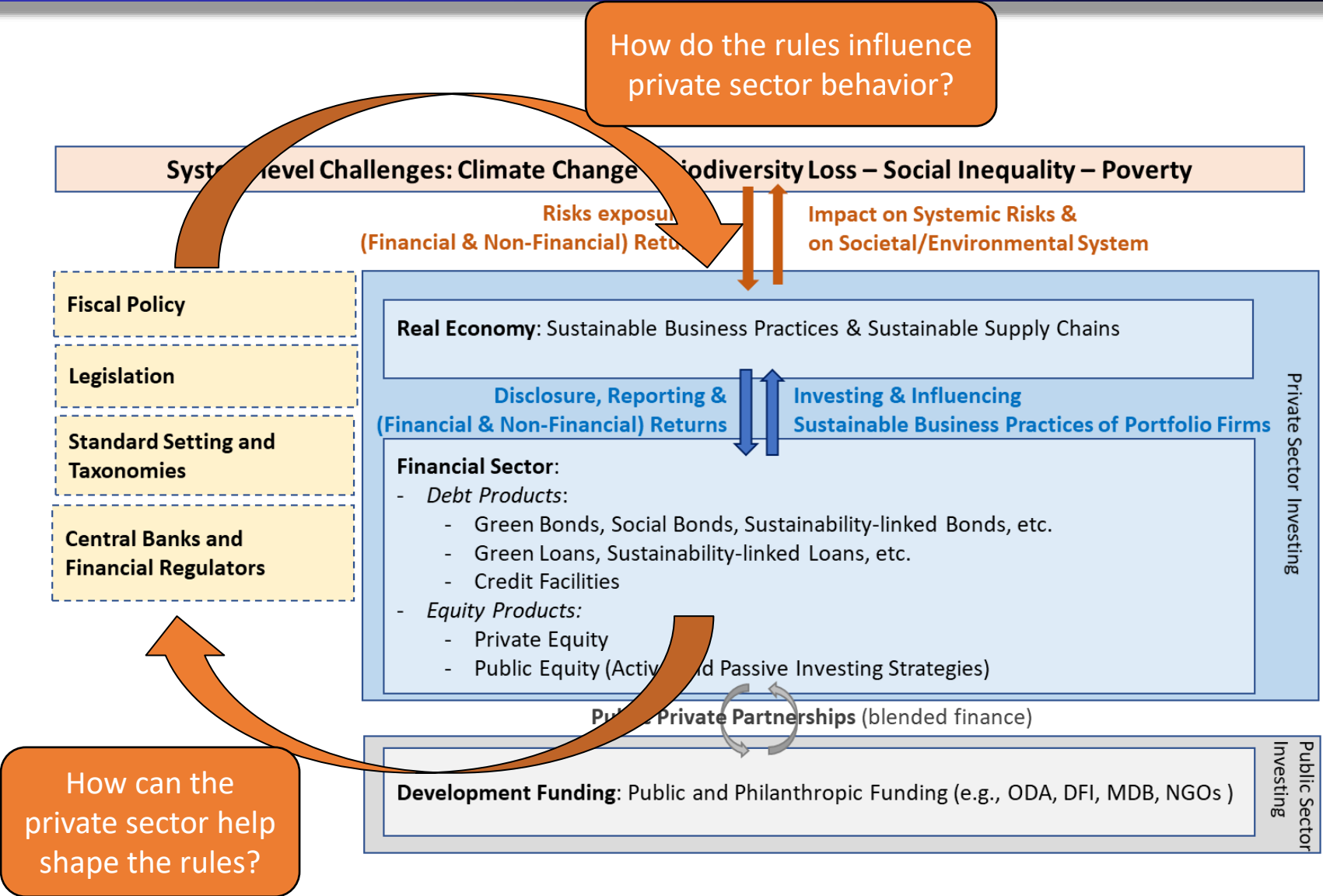


#2) New Framing: The Need to Move towards System-level Investing



(Source: SIRI <https://siri.sipa.columbia.edu/>)

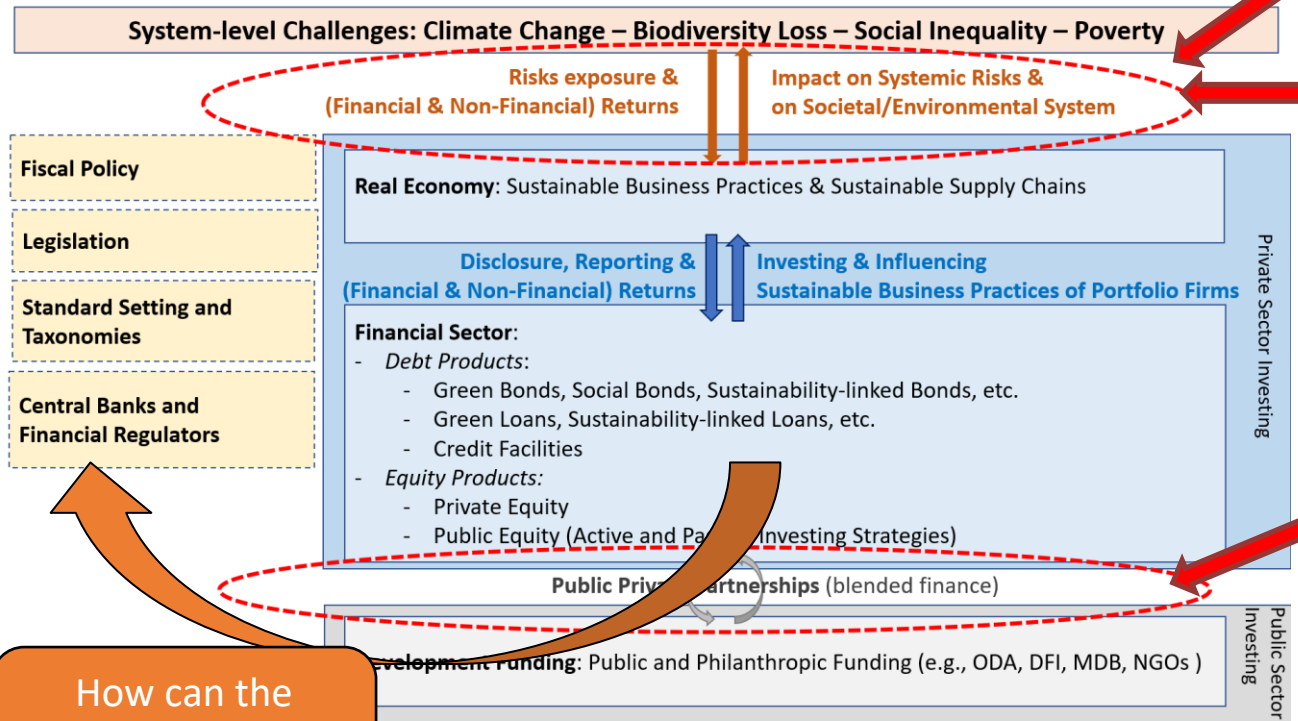
#2) New Framing: The Need to Move towards System-level Investing



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#2) New Framing: The Need to Move towards System-level Investing

- Critical Factors to mitigate system-level challenges and achieve a more sustainable world



Develop better measures to track progress toward the mitigation of system-level challenges

Adopt a systems-focused approach taking into account

- how business and investment practices impact the broader (environmental, social, and economic) system and, vice versa,
- how the system impacts business and investment practices

Create PPPs (blended finance) to fill the financing gap, i.e., use development funding to increase private sector investments in addressing system-level challenges

How can the private sector help shape the rules?

(Source: SIRI <https://siri.sipa.columbia.edu/>)

Conclusion

Thank You!

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