

The Research Centre of the Faculty of Economics
cordially invites you to a research seminar
on **Tuesday, 11th July 2017**
at **12 p.m.** in room **P-119**
at the **Faculty of Economics, University of Ljubljana**

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Author: **William Lazonick, PhD, Professor,**
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will present the article:

“The Functions of the Stock Market and the Fallacies of Shareholder Value”

“Conventional wisdom has it that the primary function of the stock market is to raise cash for companies for the purpose of investing in productive capabilities. The conventional wisdom is wrong. Academic research on sources of corporate finance shows that, compared with other sources of funds, stock markets in advanced countries have been insignificant suppliers of capital for corporations. The purpose of this essay is to build a rigorous and relevant conception of the evolving role of the stock market in the U.S. corporate economy. In fact, the functions of the stock market go well beyond “cash” to include four other functions, which can be summarized as “control,” “creation,” “combination,” and “compensation.” In this paper, I argue, based on historical evidence, that in the growth of the U.S. economy the key function of the stock market was control. Specifically, the stock market enabled the separation of managerial control over the allocation of corporate resources from the ownership of the company’s shares. Yet, assuming that the key function of the stock market is cash, economists known as agency theorists see this separation of control from ownership as the “original sin” of American capitalism, and argue that the evils of managerial control can be overcome by compelling corporate managers as “agents” to maximize the value of corporate shareholders as “principals.”

What is missing from the agency-theory argument is a theory of the value-creating firm, or what I call a “theory of innovative enterprise.” The value-creation process requires three social conditions of innovative enterprise: strategic control, organizational integration, and financial commitment. The functions of the stock market may support the types of strategic control, organizational integration, and financial commitment that can result in the generation of high-quality products at low unit costs—the economic definition of innovative enterprise. It is possible, however, that the functions of the stock market may undermine the types of strategic control, organizational integration, and financial commitment that the innovation process requires.

In this paper, I provide a brief overview of the role of the control function of the stock market in supporting innovative enterprise in the historical rise to dominance of U.S. managerial capitalism from the early decades of the twentieth century. Then I elaborate the five functions of the stock market—control, cash, creation, combination, and compensation—in terms of the ways in which, from the perspective of the theory of innovative enterprise, each function can support value creation or, alternatively, empower value extraction. I then turn to a discussion of the evolving roles of the five functions of the stock market in major U.S. business corporations over the past century. The concluding section draws on the history of the actual functions of U.S. stock markets to critique the dominant ideology that, for the sake of superior economic performance, a company should be run to “maximize shareholder value” (MSV). I indicate how MSV undermines the social conditions of innovative enterprise: strategic control, organizational integration, and financial commitment.”

You can register for the free seminar by phone (01) 58-92-490, or via e-mail:
research.seminars@ef.uni-lj.si by Monday, 10th July 2017.

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We look forward to seeing you!

