

# Strategic Management/Business Policy in a Catholic Business School

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## Class # 3: What is the purpose of business?

As the accompanying syllabus shows, the topic covered in the third class of the course is “the nature and purpose of business.” Before one can begin to consider how to manage a business or develop a strategic plan for the future of any organization, one is faced with a very important fundamental and philosophical question – What is the purpose of the business? Why does it exist? This discussion might also occur in a strategy course under the topic of “mission, vision and core values.”

Undergraduate students may enter the course having received mixed messages about the purpose of business and what really matters. Perhaps they learned in Finance or Economics class that the purpose of business is to maximize profits or to increase shareholder wealth. In Marketing class they may have been taught that the customer is king while in HR classes they hear that employees are the firm’s most valuable resource. Amid the mixed messages, confusion may reign so a thorough discussion of this fundamental issue is important.

### Case Studies

To sort through this question and to engage students in a discussion of the purpose of business, I use the Johnson & Johnson case involving the Tylenol poisonings in 1982. After reviewing the tragic facts of the case, seven deaths from ingestion of cyanide-laced Tylenol, students are challenged to think about how they would have managed the crisis and what that means about the purpose of business. I challenge students to consider how J&J responded to the crisis, asking “At the initial meeting of the J&J response team, what do you think the team did first?” Students are often surprised to learn that the meeting began not with a review of facts or a definition of the problem, a risk assessment, a situation analysis or a legal liability briefing. Before any of this was discussed, the meeting started with a reading of the J&J corporate credo. The credo identifies the people and stakeholders to whom J&J has an obligation and the priority order of those obligations. The credo states very clearly that the company’s first responsibility is not to stockholders:

“We believe our first responsibility is to the doctors, nurses and patients, to mothers and fathers and all others who use our products and services.... We are responsible to our employees, the men and women who work with us throughout the world... We are responsible to the communities in which we live and work... Our final responsibility is to our stockholders... When we operate according to these principles, the stockholders should realize a fair return.” (J&J Corporate Credo)

An interesting and unfortunate twist to the J&J case is the company’s more recent problems and ethical lapses regarding serious quality and safety violations at one of its plants. The violations

led to a May 1, 2010 shutdown of a J&J (McNeill) manufacturing plant and recall of some 50 children's versions of non-prescription drugs, including Tylenol, Motrin and Benadryl (see Kavilanz, Shocking Conditions at Tylenol plant, [www.money.cnn.com](http://www.money.cnn.com)). A video of J&J CEO Bill Weldon responding to questions about the plant closure and product recall, with specific references to the J&J Credo, is available at [http://money.cnn.com/video/fortune/2010/05/14/f\\_500\\_weldon\\_tylenol\\_motrin\\_recall.fortune/](http://money.cnn.com/video/fortune/2010/05/14/f_500_weldon_tylenol_motrin_recall.fortune/).

More contemporary cases of the disastrous effects of confusing the pursuit of profit as the sole purpose of business are, unfortunately, plentiful. *The New York Times* reported in 2007 the case of Habana Health Care Center, a 150-bed nursing home in Tampa, FL.

The Center was struggling when “a group of large private investment firms purchased it and 48 other nursing homes in 2002. The facility’s managers quickly cut costs. Within months, the number of clinical registered nurses at the home was half what it had been a year earlier, records collected by the Centers for Medicare and Medicaid Services indicate. Budgets for nursing supplies, resident activities and other services also fell, according to Florida’s Agency for Health Care Administration.

The investors and operators were soon earning millions of dollars a year from their 49 homes. Residents fared less well. Over three years, 15 at Habana died from what their families contend was negligent care in lawsuits filed in state court. Regulators repeatedly warned the home that staff levels were below mandatory minimums. When regulators visited, they found malfunctioning fire doors, unhygienic kitchens and a resident using a leg brace that was broken.” (NYT, [www.nytimes.com](http://www.nytimes.com), September 23, 2007).

## **Readings and Discussion**

Before discussing the case, students are assigned readings on the topic. It is important to assign background readings that cover the range of positions on the topic. For instance, one might assign a classic from Milton Friedman emphasizing the primacy of the profit motive, such as “The Social Responsibility of Business is to Increase its Profits,” *The New York Times Magazine*, September 13, 1970:

In a free-enterprise, private-property system, a corporate executive is an employee of the owners of the business. He has direct responsibility to his employers. That responsibility is to conduct the business in accordance with their desires, which generally will be to make as much money as possible while conforming to the basic rules of the society, both those embodied in law and those embodied in ethical custom... (T)he key point is that, in his capacity as a corporate executive, the manager is the agent of the individuals who own the corporation or establish the eleemosynary institution, and his primary responsibility is to them.

In contrast, students should read material from business leaders, scholars and Catholic Social Teaching that present an alternative point of view. For example, Charles Handy in “What’s A Business For?” (*Harvard Business Review*, 2002) states:

But to turn shareholders' needs into a purpose is to be guilty of a logical confusion, to mistake a necessary condition for a sufficient one... The purpose of a business is not to make a profit, full stop. It is to make a profit so that the business can do something more or better.

Mitroff (2004) makes a similar point in arguing against the profit motive as the basis for contemporary business education. In an open letter to deans and faculty of business schools, Mitroff chastises business educators and criticizes the fundamental assumptions of business education:

To be perfectly clear, I am arguing that the philosophical foundations of business are in need of fundamental and serious revision. We have founded modern day management on a series of outmoded and highly dubious assumptions.

Students at Catholic business schools need to understand that business is not exclusively about profits or maximizing anything. Yes, profit and returns to shareholders are important, but they are a necessary not a sufficient condition for successful business. Catholic Social Teaching (CST), particularly with its emphasis on the common good and respect for human dignity, is a rich resource for a discussion of the purpose of business. From its earliest expression in *Rerum Novarum*, modern CST has had much to say about the management of business. From broad strategic questions about the purpose of business to more specific questions about wages and working conditions, CST has not been reticent about offering moral direction. John Paul II expresses a century of thought about business when he states:

The Church acknowledges the legitimate role of profit as an indication that a business is functioning well. When a firm makes a profit, this means that productive factors have been properly employed and corresponding human needs have been duly satisfied. But profitability is not the only indicator of a firm's condition. It is possible for the financial accounts to be in order, and yet for the people--who make up the firm's most valuable asset--to be humiliated and their dignity offended. Besides being morally inadmissible, this will eventually have negative repercussions on the firm's economic efficiency. In fact, the purpose of a business firm is not simply to make a profit, but is to be found in its very existence as a community of persons who in various ways are endeavoring to satisfy their basic needs, and who form a particular group at the service of the whole of society. Profit is a regulator of the life of a business, but it is not the only one; other human and moral factors must also be considered which, in the long term, are at least equally important for the life of a business. (CA, 35)

Lest students dismiss CST as irrelevant to business and management or naïve to the complexities of modern corporations, they may wish to read more from some of the leading management thinkers of our time, including Peter Drucker or Gary Hamel. In “Moon Shots for Management” (*Harvard Business Review*, February 2009), Hamel reports on the recommendations of a group

scholars and business leaders assembled in May 2008 to identify the “great challenges” we must tackle to reinvent management and make it more relevant to a volatile world. The first great challenge is to “ensure the work of management serves a higher purpose,... the achievement of noble, socially significant goals.”

It might also help students to see the relevance of CST if they understand that the dominant profit maximizing view of corporate purpose suffers from a fundamental conceptual confusion at its very heart. Every advocate of the profit purpose apparently feels compelled to justify the perspective by offering moral arguments for why management should pursue shareholder profit as their primary objective. Most often, these arguments attempt to show that management focus on shareholder gain will result in increases to the collective welfare. (Students should be alerted, however, to the difference between this utilitarian understanding of the common good as aggregate welfare and the richer CST notion of the common good as the satisfaction of the basic human needs of each and every person. Of course, the utilitarian understanding of the common good famously allows for increases to the aggregate to be purchased at the expense of the frustration of some persons’ basic needs. CST’s understanding of the common good expressly prohibits trade-offs of this sort.) Less frequently, defenders of the shareholder profit model of corporate purpose defend their view by arguing that the rights of the shareholder “owners” require it.

These defenses of the view that the purpose of the corporation is to maximize profit are ultimately self-defeating. That is because they implicitly admit that the justifying purpose of the corporation is an ethical one: to promote the (utilitarian) common good or support the rights of owners. The single-minded pursuit of shareholder profit, then, even on this view, is at best a means to another end and not the basic purpose of the corporation. By their very arguments, the advocates of the shareholder profit perspective are implicitly admitting that the true purpose of the corporation is to satisfy the needs of people or to protect their rights.

The disagreement between the prescriptions of CST and this shareholder primacy view, then, is ultimately not a substantial disagreement over corporate purpose but a disagreement over what management strategy and tactics are most likely to best achieve the moral ends that constitute the agreed purpose of the corporate form. The crux of the disagreement, then, turns on factual analysis of the likely respective outcomes of a single-minded attention to profit and a broader attention to the welfare of all affected by corporate policy and practice.

From this point, it should be easier to convince contemporary students, impacted by the Great Recession, that CST has viable and realistic advice. One non-CST resource for making that argument to students can be found in the eminently readable *The Shareholder Value Myth* by Lynn Stout (2012). Stout argues that the single-minded pursuit of profit is damaging not only to society broadly but also ultimately to shareholders themselves, especially to shareholders with more than a short-term focus. She suggests that the constant pursuit of profit is like fishing with dynamite. While it may be a short-term approach to catching lots of fish, it destroys the resources necessary for longer-term welfare of both the business and the broader society. She argues that effective corporate management means coordinating variety of groups and getting them to cooperate in a team production process that leads to their collective flourishing.

This focus on the interests of a broader range of stakeholders also accords better with an ethically grounded approach to rights. Any adequate notion of rights will recognize that we are obligated to consider the impacts of our actions on the rights of others; it is morally unacceptable to ignore the basic interests of others in our pursuit of our own benefit. (It is only the most extreme forms of libertarianism that would reject this obligation.) Seeing profit as the sole purpose of business, however, obscures this fact and tends to encourage management attention only on the rights of shareholders. It is partly for this reason that Ed Freeman (2011) has argued in “Managing for Stakeholders,” that a shareholder primacy perspective is inconsistent with a basic ethics.

Once students see that serious scholars are increasingly moving away from the view that the purpose of the corporation is to maximize profit, and that they offer good reasons to challenge the dominant view, they will be more open to see the advice of CST as reasonable. And they may be drawn by the fact that that advice has been constant since the beginnings of the modern economic era.