Shareholder Value and the Jobs Crisis

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In this article, Jerry Davis explains

- Why increasing corporate access to capital is an outdated plan for solving employment challenges.
- Why creating shareholder value and creating jobs are no longer aligned.
- How encouraging new kinds of corporate structures such as co-ops and using high-tech tools do more for increasing employment.

The jobs crisis in the United States seems to defy solution. Although the stock market has been on a tear since early 2009, and many corporations are reporting robust profits, employment growth is stagnant. What accounts for this disconnect?

One diagnosis, popular in business circles, is that regulation holds back entrepreneurs: Politicians overreacted to the financial scandals of the late 1990s by burdening job creators with onerous demands and making it more difficult to raise capital. Thus, the JOBS (Jumpstart Our Business Startups) Act of 2012 allows companies that go public to opt out of some of these requirements.

But we have solved the wrong problem. Creating shareholder value and creating jobs are no longer aligned, and solutions aimed at the financial markets will not fix the problems in the labor market. We need to look beyond the public corporation for solutions.

The Public Corporation as an Employer

Public corporations have been central to the U.S. economy since the turn of the twentieth century. Economies of scale in manufacturing and a continent-wide system of distribution enabled by railroads encouraged the creation of huge national corporations in this country.

By the 1930s, a few dozen companies controlled the bulk of business assets. Moreover, as Adolph Berle and Gardiner Means pointed out in their 1932 book *The Modern Corporation and Private Property*,[1] the ownership of most of these companies was highly dispersed among thousands of shareholders, giving professional managers great discretion over how these new behemoths were run.

After the labor struggles of the 1930s and the mobilization for World War II in the 1940s, the largest corporations evolved a standard employment package: stable jobs organized into career ladders, health insurance, and company-funded pensions. As corporations continued to grow during the postwar boom, they employed an ever-increasing proportion of the labor force and provided opportunities for upward mobility. By 1970, the twenty-five largest corporations employed more than 6.2 million workers—almost 11 percent of the total size of the private labor force in the United States.

Policymakers at the time could rely on a stylized image of the corporation to guide their efforts at employment reform. General Motors was not just the largest corporation but also a stand-in for corporate America. But since the bust-up takeovers of the 1980s and the outsourcing movement of the 1990s, corporate employment has become much less concentrated.

A hostile takeover wave in the 1980s saw nearly one-third of the Fortune 500 change hands, often to be split up into parts. Newly empowered investors demanded allegiance to "shareholder value," and executives—whose compensation was increasingly tied to share price—delivered, often at the expense of employees.

Even "academy employers" like AT&T and IBM engaged in large-scale layoffs in the early 1990s, whereas others, like Westinghouse and ITT, morphed out of existence. By 2005, the largest employers were overwhelmingly in retail, where turnover was high, wages were low, and benefits were meager. Walmart is by far the largest American employer, with more than ten times as many workers as General Motors.

Figure 1 shows the rise and fall of employment at General Motors from 1923 to today. By 2012, the company had almost exactly the same number of employees as it did in 1928. Few looked to such iconic companies for a career full of opportunities for advancement.

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Nikefication and Employment

The process of vertical disintegration that began with the outsourcing of peripheral functions in the 1990s has spread to nearly every industry in the United States. Pressures from the financial markets have led companies to abandon the GM model in favor of the Nike model. In many cases, the corporation that oversees the brand has become little more than a node in a network of production and distribution. Instead, production is often done by generic turnkey vendors with names like Jabil Circuit and Flextronics.

Apple exemplifies this new model. During the 1980s, Apple produced its original Macintosh computer at a well-appointed factory in Fremont, California, a short drive from where it was designed. Today, nearly all of Apple's products are assembled in Chinese factories owned by Taiwanese parent companies. Even as Apple came to be the largest corporation in the United States in terms of stock market value, it was only seventy-fifth in employment.

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Apple's latest annual report states: "As of September 29, 2012, the Company had approximately 72,800 full-time equivalent employees and an additional 3,300 full-time equivalent temporary employees and contractors. Approximately 42,400 of the total full-time equivalent employees worked in the Company's Retail segment." In other words, the typical Apple employee is not a software engineer but a sales clerk in a blue T-shirt at the mall. These retail employees are paid as little as $11 per hour and have relatively high turnover and limited prospects for advancement—working at an Apple store is a classic dead-end job.[2]

Overall employment in the computer and electronics products industry has collapsed in the United States, thanks to widespread Nikefication,[3] as shown in Figure 2. Similar trends can be seen in many other industries, where the high-value tasks of design and marketing have been separated from production and distribution.

One of the consequences of this trend is that tiny new entrants can rapidly scale up production and achieve vast revenues with only minimal employment. The largest-selling television brand in the United States in 2010 was Vizio in Irvine, California, with 196 employees. The biggest brand of portable video camera in 2009 was San Francisco's Flip, with 100 employees. And the world's second-largest distributor of classical music is Sweden's X5 Music Group AB, with 43 employees.

Companies such as these look less like General Motors than like the project teams that construct buildings or create Hollywood movies. It makes little sense

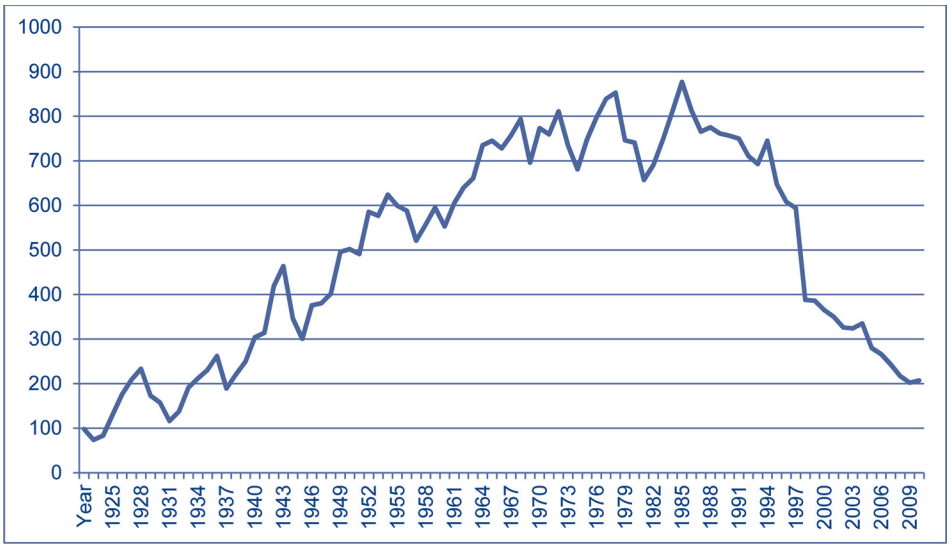

Figure 1. Employment levels at General Motors, 1923–2011 (in thousands).
Source: Moody's Industrial Manual and Compustat.

to expect them to put in place elaborate job ladders and to provide pensions and retiree health benefits. They are the corporate equivalent of a temporary employee.

Yet their model poses a challenge to the traditional twentieth-century corporation. Operating a large public corporation is costly. In many industries, the economic benefits may no longer justify the expense. In May of this year, financial analysts wrote that Sony should abandon its money-losing electronics business in favor of insurance and movies, where it was still profitable. "Electronics is its Achilles' heel and, in our view, it is worth zero," wrote one analyst.[4] When Sony is being outsold in its core industry segments by lightweight competitors like Vizio and Flip, it is hard not to take this critique seriously.

IPOs and the JOBS Act

An implication of this analysis is that public corporations are no longer the engine of job growth and the source of opportunity that they once were. The notion of the "death of the career" has been widely accepted at this point, but we may be witnessing the death of the corporations that provided the careers as well. The numbers are stark: Where the United States had more than 8,800 domestic companies listed on stock markets in 1997, it had only 4,100 fifteen years later.

> [Corporations] are failing to hire because they simply don't need employees to do business . . .

Some have attributed sluggish job growth in the United States to the declining number of companies going public. The regulations created in the wake of the financial scandals at the turn of the century—particularly the Sarbanes-Oxley Act of 2002—were argued to create onerous burdens on public companies, whereas the so-called JOBS Act made it easier for firms to opt out of some requirements.

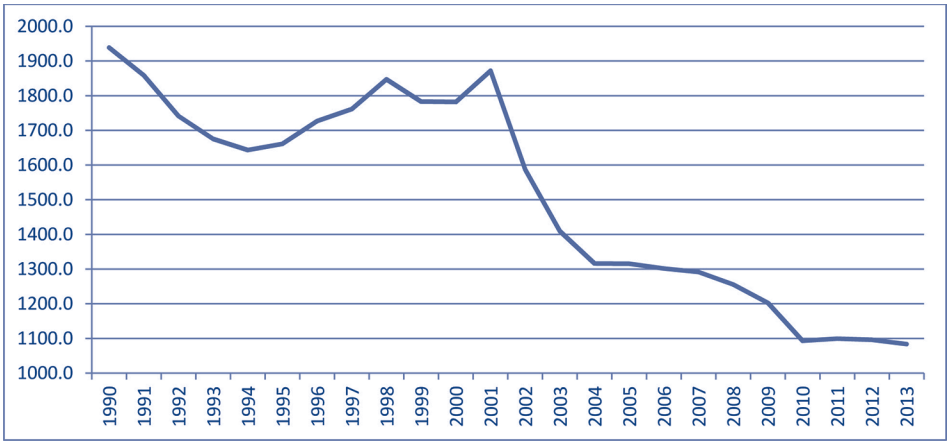

Figure 2. Employment levels in the computer and electronics industry, 1990–2013 (in thousands).
Source: Bureau of Labor Statistics.

Relaxing corporate requirements solves the wrong problem, however. Companies are not failing to hire because they lack access to capital. They are failing to hire because they simply don't need employees to do business: They can easily scale up by renting capacity rather than building it.

"Creating shareholder value" and "creating jobs" have become effectively de-coupled in the U.S. economy. For example, outside of its retail stores, Apple has about as many employees as the number of workers Hewlett-Packard laid off last year. This is not because Apple is low on funds or unable to access the capital markets. It simply doesn't need employees.

To further explore this dynamic, I tracked the employment levels of all U.S.-based companies that went public on a major market (NASDAQ, the New York Stock Exchange, and AMEX) from January 2001 through mid-2012, using data from the Wharton Research Data Service. The 1,200 companies in this group included Domino's Pizza, Google, J. Crew, MasterCard, Northwest Airlines, Tesla Motors, and Zynga.

I then calculated the change in employment levels between the year the company went public and its last year in the data set (either 2012 for those still operating independently or earlier if the company was de-listed or acquired). This calculation gives the maximum possible net job creation that can be attributed to U.S. companies that went public after 2000 and includes jobs "created" through acquisitions.

The result? Across all U.S. companies that went public between 2001 and 2012, the maximum net number of jobs created worldwide was 866,000. For comparison purposes, the United States lost 741,000 jobs in January 2009 alone.

Who were the biggest job creators among newly public companies? The biggest by far was GameStop, a strip mall retailer that sells video games. When GameStop went public in 2002, it had 13,500 employees, which increased to 71,000 by the end of 2011. According to its latest annual report,

> Each of our stores employs, on average, one manager, one assistant manager and between two and ten sales associates, many of whom are part-time employees. . . . We have approximately 17,000 full-time salaried and hourly employees and between 30,000 and 48,000 part-time hourly employees worldwide, depending on the time of year.

The third largest job creator was Stream Global Services (31,000 net jobs), which operates outsourced call centers in twenty-two countries around the world, primarily in the Philippines. The sixth largest was Las Vegas Sands (29,600), which operates casinos in Macao, Singapore, Las Vegas, and Bethlehem, Pennsylvania—this last on the grounds of a shuttered Bethlehem Steel plant.

Perhaps the iconic IPO in recent years is Facebook. Facebook had 2,431 employees on March 31, 2011; 3,539 one year later, on the verge of its IPO; and 4,900 one year after that. At this rate of growth, it would take roughly 8,000 years for Facebook to hire all of those currently unemployed and looking for work in the United States.

Conclusion

For most of the twentieth century, public corporations were the central institutions of the American economy. They created goods and services, provided stable employment, and yielded returns for their investors. But the link between creating employment and creating shareholder value has been severed.

The U.S.-based companies that have gone public since the turn of the twenty-first century have subsequently created relatively few jobs, and the jobs they have created are often not in the United States, not full time, or not well-paid. Moreover, according to the Bureau of Economic Analysis, U.S.-based multinationals have shed 2.9 million jobs in the United States since 2000, while creating 2.4 million jobs abroad.

Two positive signs are the newly revitalized cooperative movement and the vastly lower cost of capital equipment. Cleveland, Detroit, and other cities are seeing networks of cooperatives arise with an explicit goal of creating employment and neighborhood revitalization, with Cleveland's Evergreen Cooperatives providing an explicit model suitable for replication elsewhere (see http://-evergreencooperatives.com).

The prospects for "locavore" manufacturing are also enhanced by dramatic declines in the cost of computer numerically controlled tools, such as routers, laser cutters, mills, and sewing machines. Training requirements for operating this equipment are modest; with minimal guidance, almost anyone can render much of the Ikea catalog on a ShopBot router. More-elaborate designs can be sourced through 100kgarages.com, a network of small-scale digital fabricators aimed at bringing manufacturing back to local communities.

Policymakers need to stop looking to the capital markets to solve our jobs problem. Access to private capital on a large scale is not the solution; meaningful jobs come from aligning organizations built for growth in the new economy.

Editor's note: Davis has written elsewhere about new, high-tech "locavore" production using digital tools in twenty-first century sustainable business models. See, for example, his "Buying Furniture on iTunes: Creative Destruction in a World of 'Locavore' Production" on the Network for Business Sustainability website (http://nbs.net/buying-furniture-on-itunes-creative-destruction-in-a-world-of-locavore-production). See also a condensed version of his "Re-imagining the Corporation" article in the members-only section of LERA's website (leraweb.org). The complete research paper is available on the Employment Policy Research Network website (http://www.employmentpolicy.org topic/23/research/re-imagining-corporation).

Notes

1. Adolph Berle and Gardiner Means, *The Modern Corporation and Private Property* (New York: MacMillan, 1932).
2. David Segal, "Apple's Retail Army Long on Loyalty, But Short on Pay," *New York Times*, May 27, 2013, http://tinyurl.com/86hngqu.
3. As I wrote in 2012, "Over the past generation, the North American economy has been substantially 'Nikefied,' as industry after industry has adopted a modular production model. From consumer electronics to pet food to pharmaceuticals, the goods North Americans buy are routinely manufactured and distributed by anonymous generic producers, not the company whose name is on the label." ("Buying Furniture on iTunes: Creative Destruction in a World of 'Locavore' Production," Network for Business Sustainability, November 7, 2012, http://tinyurl.com/pzc938d).
4. Hiroko Tabuchi, "Sony's Bread and Butter? It's Not Electronics," *New York Times*, May 27, 2013, http://tinyurl.com/p2gvp9k.

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