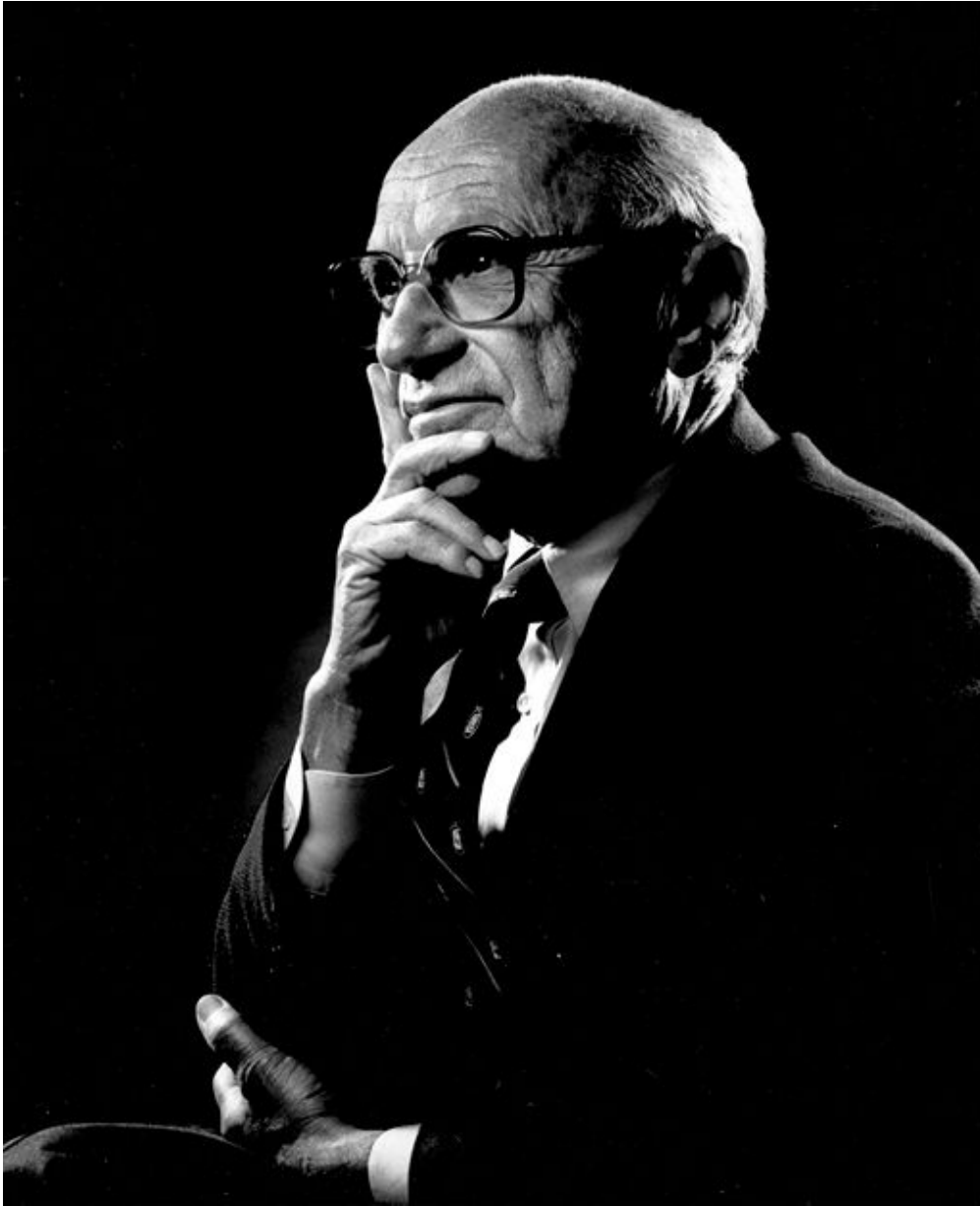


## 1.3 Business objectives

# Growth and profits: protecting shareholder value

As mentioned in Subtopic 1.1 ([/study/app/y12-business-management-a-sl-may-2024/sid-352-cid-174703/book/the-big-picture-id-36828](https://study/app/y12-business-management-a-sl-may-2024/sid-352-cid-174703/book/the-big-picture-id-36828)), it was historically accepted that the main objective of business should be to maximise profits for shareholders or owners. This view was prioritised over other kinds of value, or over serving stakeholders other than shareholders. This view was also popularised by the influential American Economist Milton Friedman (<https://www.nytimes.com/1970/09/13/archives/a-friedman-doctrine-the-social-responsibility-of-business-is-to.html>), when he declared in 1970 ‘the business of business is business’. But this view is changing.



**Figure 1.** Milton Friedman promoted the view that the only responsibility of businesses is to provide profits to shareholders.

Source: [The Friedman Foundation for Educational Choice](https://commons.wikimedia.org/wiki/File:Portrait_of_Milton_Friedman.jpg)

([https://commons.wikimedia.org/wiki/File:Portrait\\_of\\_Milton\\_Friedman.jpg](https://commons.wikimedia.org/wiki/File:Portrait_of_Milton_Friedman.jpg)), CC0

(<https://creativecommons.org/share-your-work/public-domain/cc0/>), via Wikimedia

Commons

When a business sees its main purpose as maximising profits, it prioritises value for shareholders because they receive the profits. Doing this usually involves objectives focused on growth, which you will learn more about in Subtopic 1.5 ([/study/app/y12-business-management-a-sl-may-2024/sid-352-cid-174703/book/the-big-picture-id-36864](https://study/app/y12-business-management-a-sl-may-2024/sid-352-cid-174703/book/the-big-picture-id-36864)). When a business grows, it can increase its revenue and reduce its unit (average) cost of production, resulting in increased profits. As you learned in Subtopic 1.2 ([/study/app/y12-business-management-a-sl-may-2024/sid-352-cid-174703/book/growth-and-profits-protecting-shareholder-value-id-3684...](https://study/app/y12-business-management-a-sl-may-2024/sid-352-cid-174703/book/growth-and-profits-protecting-shareholder-value-id-3684...)).

[174703/book/the-big-picture-id-36838](#)), some level of profit is desirable and necessary to sustain businesses in the private sector. And the growth and profit focus of many businesses has generated enormous wealth for shareholders and owners. However, excessive focus on growth and profit can also result in significant downsides for other stakeholders and for the natural environment.

Prioritising profits for shareholders can result in what economists call excessive value extraction. This is where one group of stakeholders captures for itself a very large portion of the value created by the business. This can occur, for example, when shareholders take very large profits from the business. These profits may have been earned by paying workers below the living wage, cutting costs by using processes that damage the environment, or by starving the business of the investment needed to sustain it in the long term.

This kind of value extraction is more likely to occur where shareholders or business managers are only considering short-term profit-making objectives, rather than the long-term health of the business. The average holding time of stocks declined from eight years in the mid-20th century to just five months (<https://www.reuters.com/article/us-health-coronavirus-short-termism-anal-idUSKBN24Z0XZ>) in 2020. It is clear from this that many shareholders do not have a long-term perspective.

## Theory of Knowledge

The meaning of the word 'value' in a business context has been contested over time. This leads to some interesting Theory of Knowledge questions:

- If we agree that businesses should be creating value, how do different understandings of 'value' impact the way businesses behave?
- To what extent is profit a good indicator of the value that businesses create?
- To what extent is the price of a product an indicator of value?

In the following video, economist Mariana Mazzucato explores the meaning of value creation for business and the economy. She highlights the need to distinguish between value creation and value extraction, two ideas which have become blurred in the modern economy.

Mariana Mazzucato is a leading economist who studies value creation in business and economies. Her website (<https://marianamazzucato.com/books/the-value-of-everything>) describes her book on the subject, entitled *The Value of Everything*. It also includes many links to other writing she has done, as well as podcasts and videos of speeches for further study.

## What is economic value, and who creates it? | Mariana ...



**Video 1.** Economist Mariana Mazzucato discusses the meanings of and differences between value creation and value extraction.