AFR Americans for Financial Reform

Our Money for the Long Term

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Short-term value extraction v. long-term value creation

Far-right, extremist forces have orchestrated a coordinated attack on what they call "woke capitalism." But as Senator Whitehouse quipped, "woke screen is a smoke screen." Although woke simply means to be aware of racial and social injustices, some Republicans are using it as a smoke screen to protect big corporations' short-term financial interests at the expense of working class people and their retirement security. Those espousing anti-woke rhetoric are fueling racial resentment in pursuit of policies that serve their corporate donors.

At its core, this fight is about how big corporations should behave in our society: should they focus on short-term, risky value extraction or long-term, sustainable value creation?

Workers' retirement funds are a powerful force pushing corporations in the direction of long-term, sustainable value creation. They can push corporations to address key risks that threaten their long-term viability and the social, environmental, and financial systems on which long-term value creation depends.

But powerful short-term corporate interests — including fossil fuel companies looking to postpone the inevitable decarbonization of the economy — are not fans of having to contend with a force steering them toward long-term sustainability. So they are bankrolling efforts to stomp out the collective influence of workers using their retirement investments to push companies to address the social and environmental concerns that negatively affect them, our financial system, and retirement portfolios.

Risks and opportunities

- Workers' rights:
  - Investments in workers' knowledge, motivation, skills, and experience — referred to as human capital — are essential to long-term, sustainable value creation.
  - Workers who exercise their freedom of association and collective bargaining (including the right to form a union) add value to the companies they work for, which creates value for investors.

- Excessive economic inequality:
  - Excessive economic inequality destabilizes social and financial systems by hollowing out the middle–income sectors of society, impacting consumer spending — a main driver of economic growth. This leads to more frequent and

deeper recessions and hurts long-term investors.
  - Upholding workers' freedom of association and collective bargaining (including the right to form a union) mitigates the risks of weak economic growth and excessive economic inequality.

- Racial inequality:
  - Failure to address racial equity issues within a company creates risks for shareholders, including risk of reputational damage, litigation, and adverse policy and regulatory action. Additionally, company actions that contradict stated positions create substantial risks and raise concerns about the adequacy of governance and oversight of these issues.
  - Failure to address racial gaps for Black Americans in wages, housing, education, and investment has cost the U.S. economy $16 trillion over the last 20 years. If those gaps were closed, $5 trillion could be added to U.S. GDP over 5 years. (GDP growth is a primary driver of returns for long-term investors.)

- Climate change:
  - Companies face both physical risks resulting from climatic events, such as wildfires, storms, and floods, and transition risks from policy action taken to transition the economy off of fossil fuels.
  - Deloitte finds that unchecked climate change could cost the world's economy $178 trillion through 2070, while a diligent net zero transition would create $43 trillion in value over the same timeframe.
  - To avoid the worst of catastrophic climate impacts, the increase in average global temperatures must be held to as close to 1.5 degrees Celsius as possible.

- Political spending and democracy:
  - A company's political spending and lobbying can present significant reputational risk if not disclosed and managed properly. Many customers and the purchasing public are paying close attention to whether a company's lobbying lines up with its corporate values. If there is a disconnect, companies can face bad press, boycotts, or targeted social media campaigns.
  - A functioning democracy is foundational to a stable economy and sustainable long-term value creation. The United States is experiencing an erosion of democracy. The erosion of democracy is visible in decreased public trust in elections, voter suppression efforts, lack of transparency regarding political spending and lobbying, among other concerning trends.

Asset manager accountability

The right-wing forces seeking to maintain the status quo of short-term, risky value extraction by big corporations are trying to influence the asset management industry — often specifically targeting Larry Fink, the CEO of BlackRock (the largest asset management company in the world).

The asset management industry is heavily concentrated, with four asset managers — BlackRock, Vanguard, State Street, and Fidelity — managing about $25 trillion in assets. As of 2019, BlackRock, Vanguard, and State Street owned around 20% of the average S&P 500 company's shares and in 2018, cast around one quarter of votes in director elections at S&P 500 companies.

Large asset managers like these have the power and fiduciary responsibility to address long-term risks and opportunities, especially those that have a portfolio-wide impact. However, the largest asset managers have not been fulfilling their responsibility, and clients lack mechanisms to monitor and hold them accountable.

For example, a recent report analyzing voting results on racial justice issues at 2022 annual general meetings found that while shareholder proposals related to racial equity and justice received high levels of support from shareholders, the four largest asset managers lagged their peers in backing these initiatives and, as a result, prevented dozens of critical shareholder proposals addressing racial equity and justice from reaching majority support. As another example, last year, the four largest asset managers remained strong supporters of the status quo at climate-critical companies.

Members of Congress can take affirmative action to ensure asset managers act in the best interests of the people whose money they manage by proposing or supporting legislation to amend the Investment Advisers Act to:

- Codify the existing ability of advisers to take *all* relevant risks and opportunities into account in their investment decisions, proxy voting, and engagements with companies they are invested in;
- Codify the existing ability of advisers to take into account risks and opportunities companies pose to the overall, diversified portfolios of the investors whose money they manage; and
- Require asset managers to disclose their policies and practices related to the above.

Changing decision-making in the private equity industry

Private equity-owned companies are responsible for some of the most abusive business practices in the country. This is because executives at private equity firms can gain control of companies while risking nearly none of their own money, use a multitude of tactics to extract money from those companies, and then leave workers and communities saddled with the losses and devastated if those companies fail or are downsized. These predatory practices are the epitome of short-term, risky value extraction. To change the rules and incentives of the private equity industry, support the reintroduction of:

- Stop Wall Street Looting Act: This bill would fundamentally reform private equity by closing the legal, tax, and regulatory loopholes that allow private equity firms to capture all the rewards of their investments while insulating themselves from risk.

Changing corporate decision-making at the source for public companies

While workers' retirement funds and asset managers should play a key role in pushing public companies toward long-term value creation and away from short-term value extraction, there are a number of bills that address incentives at the source: the public company itself. To directly change the rules and incentives of public companies, support the re-introduction of:

- The Reward Work Act: This bill would end open-market stock buybacks, which artificially increase share price and wealthy CEOs' paychecks. Every dollar spent on stock buybacks is a dollar not spent on raising worker wages, research and development, and other long-term investments needed for sustainable and equitable economic growth. The bill would also require that public companies let one-third of their board be chosen by their workers.

- The Accountable Capitalism Act: This bill would reorient corporate decision-making toward long-term, sustainable value creation by fundamentally changing the rules and incentives of large corporations. For example, company directors — 40% of whom would be elected by its employees — would be explicitly required to consider the interests of employees, customers, shareholders, and the communities in which the company operates.