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# PROCEEDINGS

## *MICHAEL SHANKS MEMORIAL LECTURE*

# What Is a Company For?

PROFESSOR CHARLES HANDY

*Visiting Professor, London Business School, and a Vice-President of the RSA Council*

*Delivered to the Society on Wednesday 5 December 1990 with Bob Tyrrell, Managing Director, The Henley Centre for Forecasting Ltd, in the Chair*

*This lecture was sponsored by The Henley Centre for Forecasting Ltd, the BOC Group plc and Midland Bank plc*

THE CHAIRMAN: It is a very great pleasure to be able to spend a few minutes at the start of this evening's proceedings paying tribute to Michael Shanks. I was in my teens in the mid 1960s when I read one of his first books, and the one with the most resonant of titles: *The Stagnant Society*. It convinced me that there was a fairer and more rational means to resolve the conflicts between wealth creation and wealth distribution and to ameliorate the tensions that arise between free enterprise and social responsibility in a mixed economy than the adversarial politics and the confrontational industrial relations that were so prevalent at that time. The issue of the resolution of those tensions is still highly pertinent in Britain in 1990 and it is a very large part of our subject tonight. Further books by Michael Shanks which influenced me in the years that followed included *The Innovators*, *The Quest for Growth* and *What's Wrong with the Modern World*. He became one of my heroes. Then, in 1976 when he was coming to the end of his tour of duty as Director General of Social Affairs at the European Commission, James Morrell, Director of the Henley Centre, announced to the staff that he would be joining us as a Director. So I met Michael personally and I worked closely with him between 1976 and his untimely death in 1984. At the time of his death besides being Director of the Henley Centre, he was a Director of BOC and of Environmental Resources Ltd; Chairman of George Bassett & Son and the National Consumer Council; and he had a seat on the National Economic Development Council.

Twenty-five years after I first came across Michael Shanks and six years after his death, the diagnosis of Britain's malaise may have changed and the prescriptions that are offered for the way forward may be different but the need for people like Michael Shanks – people who understand the demands and the realities of wealth creation in a dynamic industrial society but who retain their humanity and their sense of compassion – is as great as ever. In this evening's speaker I believe we have such a person. Charles Handy is author, academic, business consultant, coiner of terms *extraordinaire*, Irishman, humanist and, along with Rabbi Lionel Blue, one of my personal favourite Radio 4 providers of Thoughts for the Day. I would also like to thank BOC and Midland Bank who joined the Henley Centre in the initiative of organising the Michael Shanks Memorial Lecture and to welcome Patricia Shanks and other members of the Shanks family.

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I was due to meet with Michael Shanks a week after his untimely and unexpected death in 1984. I do not now remember what the meeting was to be about; it could have concerned any number of things because Michael was the ultimate portfolio person. At ease in board-rooms, government offices or consumers' campaigns, he bestrode the different citadels of our business society, concerned always and only to make it a better society. His passing left a big gap in the lives of many.

I was delighted and honoured to be asked to deliver this first Michael Shanks Memorial Lecture and the topic I thought appropriate in his memory was clear: in



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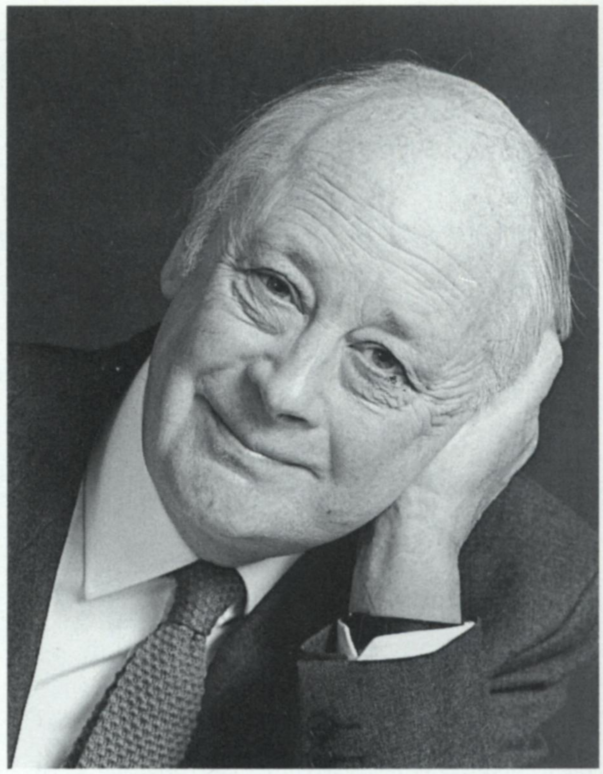
this changing world we had to face up to the question 'What is a company really for today?' Do our rules and laws and institutions reflect that purpose or do they, perhaps, get in its way?

I am going to argue that some of the rules of our business game do today get in the way of its well-intentioned players. I shall even suggest that those rules and traditions are causing us to score some own-goals and to shoot ourselves in our collective feet (if I may mix my metaphors). I shall in the process trample on one or two precious myths, hallowed though they are in our corporate mind-set. I really do believe that we may have got it wrong and that we should at least question received wisdom. It is, of course, easier to raise the questions than to give the answers. I will dare only to point to the directions in which I think the answers may lie, because they won't be simple answers or easy ones, but to my mind it would be a great step forward to argue that some new answers were needed at all. Things do outlive their purpose, and what was once sensible may now seem crazy. We do not have to be slaves to our history.

When I started to consider this topic I realised that I was treading in illustrious footsteps. It is nearly 18 years since the Watkinson Committee reported its deliberations on the responsibilities of the British Public Company. It said many sane and sensible things, but fine words do not, in this instance, seem to have buttered any parsnips. I am delighted to see George Goyder here tonight because it was his book *The Just Enterprise* (published in 1987) which set me thinking about all this, intertwining as it did in a marvellous way the just enterprise and William Blake. Earlier this year another book, this time by Sir Adrian Cadbury, on the company chairman, also examined some of the issues as they look to one well-intentioned player, the former chairman of a big and concerned company. Recently, too, there has been a spate of seminars, talks and articles on short-termism in and around the City. I see short-termism as a symptom of a much bigger problem but the arguments have been interesting. To me most helpful were the survey on capitalism by the *Economist* in May 1990 and a recent publication from the Institute of Public Policy Research on Takeovers and short-termism. I have also found most helpful my talks with Philip Baxendale who has spent much of the last ten years trying to bend the rules of the game as they currently exist to make possible his vision of a just enterprise in the Baxi Partnership. I have named the most illustrious and helpful of the footsteps to follow but there are many more. They demonstrate that there is a growing sense of unease in many quarters about the unintended consequences of being in business.



*photograph: Elizabeth Handy*

*Charles Handy*

The topic, however, was given a new urgency for me by a recent visit to South Africa and meetings with the African National Congress, and then a trip to Hungary. In the first country they look with some suspicion on the institutions of capitalism but recognise that a healthy democracy needs a healthy business sector, while in Hungary they yearn for the institutions of a free market but are dismayed to find that the first results are 40 per cent inflation, pollution and growing unemployment. In both countries they were asking what was a company really for – itself or society? The answer is, I hope, both. But is the pursuit of self-interest bound to be for the common good or do we need to recognise that Adam Smith lived in a simpler world, at a time when, for instance, you loved both yourself and your neighbours because you knew them and could not



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ignore them? Do we need new rules for a new and more complicated world?

What is a company for? In my American business school in the sixties the answer was clear, it was inscribed above the blackboard in every class, it was 'to maximise the medium-term earnings per share'. Not short-term earnings, mark you, and not optimise, but maximise. From this all else flowed, given, of course, a perfect market and an intelligent one and managers who were clever, energetic and wise – something to which my business school was attending. Looking back, it is amazing that we never challenged either the statement or its premise.

Yet my own life before that should have given it the lie. I had been a lowly regional manager in a distant outpost of a great oil company. I suppose I saw the published results of the company but its earnings per share, its profitability, did not keep me awake at night, nor get me leaping out of bed in the morning. I knew, of course, that any project proposals must earn a rate of return above a stated cost of capital, and every proposal of mine always did of course, but I was never around long enough to see if the reality lived up to the proposal. I had other things on my mind and I don't just mean my social life.

I had, for instance, to deal with the village of Kapit and its headman, 200 miles up the Rejang River in Borneo. There had been an unusually large crop of the wild nuts that are used in the making of chocolate and the tribes-people had loaded them into their canoes and sped down-river with their outboard motors to sell them to the merchants in Kapit. Now they wanted to get back but I had failed to anticipate their demand and the town was out of petrol. It would take a week for the steamer to come up river with the new supplies. We were the only oil company there. The little town had no space and no food for all those people. I was not the most popular or respected white man around. I'm afraid that the possibility of milking my monopoly position and trebling the price of the petrol when it did arrive did not occur to me. In fact, I sold it at a 50 per cent discount to say I was sorry. In Kapit, that week, my concern for my customers far outweighed my consideration of earnings per share.

Not so, my business school would have argued. They come to the same thing. If you had exploited your customers, you would in the end have lost your monopoly because a competitor would have come in. In their perfect world, perhaps, but not in Kapit in the sixties. The cost of entering that market was prohibitive relative to any likely profits. No – I had a little local monopoly, the dream of any small business, but, if I'm honest, it was my own self-respect which drove me, and the need to preserve my reputation as the company's representative. The connection with maximum earnings per share was very remote, very long-term, very intellectual, very unreal.

With this everyday story of business folk I am making the rather obvious point that out there in the real world of business it is producing things for people on time, in good condition, and at a fair price which matters, without mucking up a decent town like Kapit, or upsetting the local government, or taking unreasonable advantage of a short-term profit opportunity. I was not there, I felt, to maximise the earnings of some anonymous shareholders. I had, I was sure, a much more serious social function, as I told a maiden great-aunt back in Ireland who complained that I was the first member of her family to go into trade. It was a form of social contract but it needed profits to make it work and go on working. That, too, I knew.

My business school in America was wrong, I am now convinced. The principal purpose of a company is not to make a profit – full stop. It is to make a profit in order to continue to do things or make things, and to do so even better and more abundantly. Late in those same sixties Jim Slater came to talk to the students at the new London Business School. He was at the height of his fortunes and he was happy to explain his secret to the young men and women. 'I am the only person in British business,' was his message, 'who is interested in making money. All the rest make money in order to do something else. That makes it easy for me to look at assets and investment decisions in a totally uncluttered way'. Three years later his business was finished. I never got to ask him if he still felt that way.

To say that profit is a means to other ends and is not an end in itself is not a semantic quibble, it is a serious moral point. In everyday life, those who make the means into ends in themselves are usually called neurotic or obsessive, like that great-aunt of mine who was meticulous about how we were dressed and adorned for church each Sunday, the way we knelt and the prayer book we carried, but seemed not to understand or be interested in the theology of it all, the content of the preaching or the praying. In ethics, to mistake the means for the ends is to be turned in on oneself, one of the greatest of sins, said St Augustine.



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Let us be clear, profits – and good profits – are always essential, and not just in business. But the myth dies hard, the myth that profit is the purpose. I attended a gathering of senior managers in one corporation where they were discussing their new mission statement, with its declaration of intent to serve customers, society, employees and the environment with as much enthusiasm as its shareholders. The chief executive, pressed to make a personal statement of priorities said: 'When it comes to the crunch I'm a bottom line guy.' The room cheered. He was macho. Why, I wondered, did they cheer? They weren't shareholders, the company was not in financial peril, there was nothing in it for them. Wouldn't it have been more exciting to be the best in their industry, or the most innovative, or the most respected, or even the biggest? But no, they wanted to be the most profitable. 'Profits is the principal yardstick,' said the Watkinson Committee, but yardstick of what for what, and how can a yardstick be a purpose? It is like saying that you play cricket to get a good batting average. It's the wrong way round. You need a good average to keep on playing cricket in the first team.

The second myth is equally pervasive, that those who pay the money own the company. In this case the purpose of the company would be to meet the requirement of the owners, which might or might not be to maximise the medium-term earnings per share. I have, for instance, been impressed by the sense of trusteeship that you sometimes find in long-standing family businesses. 'We had to sit out two world wars,' said the head of one such business in Belgium, 'but they counted on us' and he pointed down to the roofs of the little town that surrounded his plant which had been, for generations, the principal employer in that place. Most shareholders in a public company, however, do not survey their corporate holding from the top of the factory. They are more akin to punters at the races, as the *Economist* described them, placing their money on their financial runners.

To expect the punters who had backed the bay gelding to stay with that horse throughout its career, or to give their advice to its trainer, would not be reasonable. If they don't like its form, they transfer their money to another. Punters or speculators they may be, owners in any real sense they cannot be. Nor, in my view, will devices to lock them into their bets by tax incentives or legal requirements be more than an irritation in a free market. Andy Cash and his co-authors call this 'throwing sand' into the market and that, I think, is about all that it would do. Nevertheless, those punters have an extraordinary privilege. They are, for the price of their bets, given a vote from time to time in the auction ring as to who should own their horse. This means that they need to be wooed, continuously, for who knows when the bell for the auction ring may toll? Every company, under these rules, is effectively up for sale every day.

It is argued that the constant possibility of the auction ring concentrates the mind of the trainer. It certainly diverts his attention to the price and away from the animal – the company in this case. I asked one supermarket chairman why he was expanding so energetically into France and Belgium, buying up competitors wherever possible. Was it to prepare for the enlarged market of 1993? No, he replied, we want to make ourselves so big and so complicated that no one will be tempted to swallow us up. The best defence against being bought is, it appears, to buy. Yet all the evidence suggests that the bidder does worse, most times, than the loser at the end of the day. It is, as someone said, a funny old world.

It is worse than that, it is a form of suicide. During the ten years 1972–82 one-third of the biggest 730 quoted companies in Britain changed ownership, with all the complications and expense and distractions which such a change involves. The comparable figure for Japan was under 8 per cent. In Germany, of the 450 companies quoted on their stock exchange only 30 or so are actively traded. The auction ring is seldom used. In contrast, remember that there are 2,400 companies listed on the London Stock Exchange, almost all of them candidates for the auction ring at any time.

To keep the punters happy we have to pay them. UK dividends are nearly twice as high as German dividends and three times as high as Japanese. That raises the effective cost of capital since most large companies would like to finance their investment out of retained earnings. If you don't have enough of these you have to borrow and even if you do have enough the profitability of the investment has to beat the cost of the dividend to make it worthwhile. So it is that British companies currently look for a return of 25 per cent on new projects, German companies 15 per cent or so and Japanese ones 8 per cent. Guess which countries invest most in long-term manufacturing plant and which go for the less capital-intensive service industries. It is not due to stupid or shortsighted management. It is the pressure of the auction ring.





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Some say that making the managers and perhaps also the workers into the owners removes the pressure of the auction ring. But the history of management buy-outs in recent years suggests that owner-managers are just as susceptible to large offers as anyone else. I have known quite a few who profess a dedication to long-term stewardship in October, only to be out to pasture, richer by several millions, in November. Others look to create a consortium of proper owners, banks, other companies, institutions who will effectively guarantee the long-term existence of the company, leaving the punters to flutter, in the margin. Pension funds, however, who own over half of British shares, are directly responsible for other people's monies and have always shied away from so locking themselves in. Acting in unison they might be persuaded to change their ways, but it would be a fundamental change. And as for individual shareholders, a recent forecast predicts that the last individual shareholding in Wall Street will be sold in 2003. The idea that we are becoming a nation of small shareowners is, I'm afraid, a myth.

More fundamentally, perhaps we should ask the basic question. Why should those who pay the piper call the tune to such an extent? It does not have to be that way. The financier could be treated as we treat the providers of a mortage on our house. They hold the deeds. If we default they can sell it over our heads but only if we default on our agreed payments. Those agreed payments are equivalent to a fixed dividend. The financiers' basic security is partly the estimated income stream or profits of the occupier, partly the underlying value of the building, which it is hoped increases over time. Of course, the mortgage company is locked into the deal for twenty-five years or so. The shareholder could and should be able to take his money out at will.

It works that way, or seems so to me, in Japan, where shareholders are effectively preference debenture holders, paid a dividend related to the par value of the share. The dividend is effectively fixed and is low but is seldom if ever passed. A Japanese company will borrow to pay the dividend, something that is anathema to our practices.

More fundamentally still, I want to ask how and why the concept of property ever entered the debate? George Goyder argues persuasively that in English law the corporation is something different from its shareholders and quotes Lord Justice Evershed summing up a case in 1947: 'Shareholders are not in the eyes of the law part owners of the undertaking. The undertaking is something different from the totality of its shareholdings.' He also points to the government's wartime take over of Short Brothers when the courts also held that the shareholders did not own the company and were not therefore necessarily entitled to the full asset value of the company. My legal friends are not sure that this is the last word on this matter and believe that the law has not fully made up its mind, or, to put it another way, might overrule its precedents.

My reasoning is much simpler. Companies used to be physical assets, run by families and their helpers. Nowadays they are largely people, helped by physical assets. Owning people is, I think, wrong. Buying and selling people is wrong. The concept is out of date, just as the idea that a man owned his wife is now out of date. In Victorian times the concept of limited liability was a wonderful piece of social invention, which enabled the family company to strut the globe. No one there thought of the resulting paradox, that owners by law have limited liability. How odd, when you stand back and look at it. The more I reflect on it, the more I think that we are today the victims of our ancestors' creativeness, that the idea of a company as a piece of property is fairly bizarre, and that the idea that those who bet on it can sell it is just crazy and may be costing our children their livelihoods. I would like it to be another myth that bites the dust.

Where does this get us? To a version of stakeholder theory no doubt, in which all those with some interest in the company have some say in its conduct and future? I do not, myself, like the idea. I don't really know who all the stakeholders are or who would properly represent them. Financiers of various types I can see, and employees. Customers clearly have a stake but how would their interest be represented other than through the market place where, in an open market, if such a thing really exists, they can vote with their feet? And the surrounding community, the environment, society at large? Stakeholders language is a nice way of talking about the balancing act that companies have to perform, but I don't think, myself, that it answers the question, 'what is a company for?' except in a very blurred way. It is certainly difficult to see how one could give it any teeth.

Except there are some new straws in the wind. The 1985 Companies Act requires directors to have a proper concern for their employers. That's just 'rhubarb, rhubarb' might be one slightly cynical reaction. But



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enter the accountants who have until now put people down as costs in the profit and loss statement, costs being things you try to minimise, with as much proper concern, of course, as you can muster. People, however, are now becoming more than mere 'hands' or 'temporary role occupants'. They increasingly represent valuable 'intellectual property'. Slowly the auction ring for companies is realising that assets don't have to be made of bricks or steel or wood but can be made of brain. The misbegotten concept, property, has once again been trusted, but this time in effect to put people on the balance sheet as assets, not on the profit and loss as costs. It happens in the auction ring where companies are valued way beyond the worth of their physical assets and you cannot account for the difference with 'goodwill' or 'Research and Development in the pipeline' or 'patents pending' or 'brands', all of which are also part of intellectual property. People matter more now. Companies are uncomfortably aware that people are assets which could walk out of the door. Now *there* is a reason for showing proper concern for our employees.

Or take the environment. Accountants are beginning to realise that there are some gaps in their view of the world. For instance, in accounting, ownership does not have the notion of stewardship attached to it. In fact, under accounting principles, if you own something you are entitled to destroy it. Furthermore, if no one owns something then that something has no price, like air, sea or those things not reflected in the price of land, such as its ability to support life. Companies have been getting away with murder because thinking about the environment has not been in our scheme of things. Long ago it did not matter too much perhaps because there was an awful lot of land, sea, air and forests. Taking a bit of them for free was, maybe, one of those victimless crimes. No more. But the trouble is, that what is not counted does not count where it hurts, in the accounts. We may therefore expect a lot of pressure from the environmental lobbies for the accountants to fill in the gaps in their system. It has already been felt with the Pearce Report prepared for Chris Patten when Secretary of State for the Environment. Accountants have, unintentionally, skewed our idea of the world. Now they have a chance to set it straight again. I hope they will.

Even with these new numbers, however, I do not see that the stakeholder concept provides a sensible answer to the question 'what is a company for?' It may be analytically convenient to say that the company is working for all the stakeholders, but that does not tell you what to do or where to go, if you are the Chairman. Inevitably, one or other of the stakeholders has priority and, given our current system, it is going to be the shareholder. Stakeholders become, then, the constraints upon the maximisation of profits. That too easily becomes 'do what you have to do to satisfy the other stakeholders, then go for profit'. Back in Borneo I would still have been dissatisfied. Profit I would still see as the necessary but not sufficient condition for my company's continued existence and I would still be looking for its driving purpose.

I see the company as operating in a bounded space, a sort of hexagonal ring, surrounded by competing pressures from financiers, the employees, the customers, the suppliers, the environment and the community – the so-called stakeholders. There is no easy way to square the circle, or the hexagon. Undirected, the company will bounce from one side of the ring to the other, and many do – the oldest law of organisations is the pendulum. This time it swings six ways. Within that ring of forces I want to see the development of the 'existential corporation'. By that I mean the corporation whose principal purpose is to fulfil itself, to grow and to develop to the best that it can be, given always that every other corporation is free to do the same. It owes something to each of the ring-holders, but is owned by no one. It is in charge of its own destiny, and it is immortal or would like to be. It is not a piece of property, inhabited by humans, it is a community, which itself has property. It also has shares, traded publicly, bought by punters, but those punters have limited powers. They cannot go into the auction room unless the company defaults, or assists them to.

Communities have members not employees. Or rather, if they do have employees they are people outside the community not inside. Communities like all human kind need to grow and develop or they die. (Properties can and do remain static.) But they don't have to grow in size. Last month, in northern California, I had a blissful day as a wine tourist. I spoke to the owner manager of one winery. He was passionate about the future of his winery, but he wanted it to be better not bigger, and he needed lots of profits to make that possible. Businesses seem always to want to grow bigger, perhaps because their managers want bigger empires, perhaps because that makes them



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less easy to be bought. They miss a trick or two I sometimes feel, for bigger is not always better, or more profitable. But communities cannot be bought, except with the consent of their members, and doing the same only better is what has motivated craftsmen, artists and professionals down the ages, so it cannot be easily disparaged.

A community responsible for its own destiny, not to be bought except with its consent, is on the face of it a license for management to do as it pleases. After the constraints of its bounded space have been met, it is accountable only to its members. This kind of self-determination has been a charter for scoundrels through the ages, or so it will be argued. I would agree that some form of authority is necessary through whom the management would be accountable – a board of trustees, perhaps, whose task is oversight not direction, with the ultimate power to replace the management should they fail in their task of growing the community. If this seems close to the supervisory boards of Germany, I would be tempted to say, 'Well, why not, it doesn't seem to have done them too much harm?' but there are other variants, including Tricker's notion of a twin board, half non-executive, which meets separately for some of the time with clearly-defined duties, and half executive. An independent Chairman presides over them both when they meet as one. The details, however, are less important than the principle, that the board of trustees holds the accountability of the membership of the corporate community within that hexagonal ring.

It is my belief that the businesses of Germany and Japan are thought of more as communities than as properties. They see themselves as immortal and plan for 'life beyond the grave', as one of them so nicely put it. That in turn gives a sense of security to its members who in turn are likely to think beyond the grave, without worrying about that one in three chance that the business will be sold over their heads in the next ten years. They will be prepared to sit out two world wars, for the survival of the community is to them of first importance, and they will make sure to honour their commitments to their financiers, even if they have to borrow to do it, because only if they default can the financiers move in. They will invest in their own development and they will grow the children in the local school because there will still be life beyond the grave. They will take care of their environment because it may be their own grandchildren's environment, and they will invest heavily in research, development and innovation because in that lies the hope for their children. That's what they do in Germany and Japan, for the most part, and I don't think that it is just a Germanic characteristic or a Japanese one, I think it is due to the way they think of a company, and practise it. Julian Franks, a colleague of mine at the London Business School, described on the BBC *Analysis* programme last week how, when German companies took over other German companies, nearly always by agreement, they did not close plants and cut staff but instead invested more in training, research, new equipment. New management had come in to grow the community, not to make the most of the property. It really is a different way of thinking.

But if the company as a self-governing community, not a piece of property, is such a good idea, why don't we see more of them? The answer is striking. George Goyder gives it in the first chapter of his book. Philip Baxendale reminded me of it the other day. It is given in quotation from Lord Eustace Percy in 1944:

> Here is the most urgent challenge to political invention ever offered to the jurist and the statesman. The human association which in fact produces and distributes wealth, the association of workmen, managers, technicians and directors, is not an association recognised by the law. The association which the law does recognise – the association of shareholders, creditors and directors – is incapable of production or distribution and is not expected by the law to perform these functions. We have to give law to the real association and to withdraw meaningless privilege from the imaginary one.

Having read that out I am conscious that all my preamble was unnecessary. The point is that the rules do not allow for a wealth-creating community.

What then can we do? We can work within our existing rules and exhort our managers to work as if they were an immortal community responsible for its own destiny, paying proper heed to the hexagonal space and the six stakeholders. Many large companies are trying to do this. They produce statements of vision and values, establish social responsibility departments, care for the environment and plan to be in business for the indefinite future. My feeling is, however, that they are forever looking over their shoulders. We are asking them to play fair when the rules of the game allow everyone else to play rough. It is unfair. No wonder





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that they sometimes play only lip service to the other stakeholders and pander to the short-term needs of the punters, just in case. In the world of mega-millions, after all, almost no one is immune.

Alternatively, we can seek to build truly self-determining communities under our existing property rules. The John Lewis Partnership is one very well-known example. The Baxi Partnership is another. The trustees of that Partnership own a minimum of 51 per cent of the shares on behalf of the workers. They will sell only if disaster threatens but immortality is their aim. The workers can directly own another third of the shares, to hold or to sell. The Partnership Council has twelve elected members who represent the interests of the current partners (note the word) and four trustees who represent the interests of the future partners. Their job together is to oversee in general terms the board of directors who run the business.

These two organizations, and a few others like them, genuinely seek to control their own destinies, to look beyond the grave and beyond the boundaries of their sites. But their shares are not publicly traded, they are not exposed to the auction ring and they cannot therefore be example to all of us. Likewise I know family businesses which run benevolent dictatorships for the benefit of whole communities. They, too, look beyond the grave and some of them have taken their shares to the stock exchanges. They, however, are exposed to the chances of heredity. Not all heirs or heiresses are destined to be great business leaders and too often they fall foul of what my Italian friends call the third generation malaise, when the talent peters out.

I am persuaded, now, that small experiments and examples at the edge will never be enough, that we need a wholesale review of the governance of our companies, that asking managers to do it despite the rules is unfair, and that playing to the rules will inevitably emphasise the short-term, increase the costs of our investments and put us at a disadvantage to our competitors. What precise form that governance should take I do not know, but I suspect that at this point the principles are more crucial than the details.

That is my short-term worry. My long-term worry is that property prevails over community. As the world shrinks and companies aim for global reach, property will inexorably annex communities. Paradoxically, the Anglo-American system which, I have argued, works less well for everyone than the German or Japanese models, may prevail, driving the whole world into a fever of short-term speculation, forcing companies to become asset traders rather than wealth producers, and leaving Adam Smith's invisible hand to do a lot of probably unavailing overtime.

You will notice that I still have not answered my question 'what is a company for?' I will now respond that I cannot answer it. It is something that each corporate community must do for itself, but we must set them free, legally, to do so. To talk of profits is no answer because I would say 'of course, but profits for what further purpose?' Talk of meeting the requirement of the stakeholders I would also regard as a necessary but not sufficient condition of existence. To have survived is not, in my view, sufficient justification for a life, either for oneself, or for one's corporate community. To make that life worthwhile one must, I feel, have a purpose beyond oneself.

What that purpose is has to be the major concern for my boards of trustees, and they should think laterally. If all aim to be number one, then 99 per cent will be disappointed. You don't need to be big to be great, or even big to be global these days. I think I would say to these trustees, as I would to any individual that what you are is as important as what you do, and will last longer in the hearts and minds of people. A company is not an instrument, it is, or should be, a living and growing community. There is a difference.

I have said some moderately heretical things this evening. They are:

1. Profits are a necessary but not sufficient condition of success. The bottom line should be a starting post not a finishing post.
2. Owners with limited liability will never be owners, only punters, so don't expect too much from them. Turn them into mortgage men instead.
3. Stakeholder interests will not count unless they can be counted, seriously. Accountants to the rescue please.
4. Owning people is wrong. Companies are collections of people these days; they are communities not properties.
5. The law does not recognise this. It should.
6. Asking our managers to behave better than the rule book is unfair and unrealistic, so let us change the rule book.
7. If we don't, we shall endanger our children's future, and maybe even bring down our opponents with us.

Above all I want to say that in a time of change we



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must always question whether the things that used to work will work so well in future. We must not be slaves to our history but trustees of our destinies. Our businesses are too precious to be lost because we have not dared to question the past, or to dream the future. Let us start now, before it is too late.

# DISCUSSION

DONALD B. BUTCHER (Management & Engineering Consultant): You have equated shareholders throughout your talk with punters. I believe this to be misleading. At least one should distinguish between private and institutional shareholders. My personal experience of private shareholders in big companies and in small, unquoted companies – particularly family businesses – is that they are loyal and keenly identified with the success of the company. The problem is that too few companies make significant efforts to engage and maintain private shareholder support.

THE LECTURER: I am a great advocate of family business. The strength of Germany lies in medium-sized family businesses that are not included on the stock exchange. Shareholders in that sense do want an immortal company. In the larger public companies, even if the shareholders are interested as individuals, I find it difficult to conceive that they can have any influence and I was very discouraged by the American forecast that there won't be any shareholders in ten to twelve years time.

DR DAVID BUDWORTH (Self-employed): In his lecture Professor Handy made one or two slightly uncomplimentary remarks about accountants. I am not an accountant but I find that at the moment most of the intelligent thinking about business is coming from the accountants and accountancy bodies.

THE LECTURER: I was only uncomplimentary about accountants in the past and I agree that accountants are now realising that they have a lot to contribute. I applaud all the initiatives currently coming from the accountancy bodies.

SIR GEOFFREY CHANDLER (Industry Adviser, RSA): What are the stimuli to bring about change in the short and medium term? Stimuli within the company include the exercise of leadership. A potential external stimulus is the market: the market operates on information and at the moment the information provided is basically financial, not concerned with training and qualifications. If there were a compulsory human audit, and indeed an environmental audit, then you would begin to get the market working on information addressed to the medium and longer term. Other external stimuli are regulation and law. The Watkinson Report has sat on the shelf for nearly twenty years, but is still relevant in many respects.

THE LECTURER: I think that the most hope lies in the internal side of the companies. If more chairmen, managing directors and chief executives saw their company as an immortal community and, therefore, accepted the need to invest in its surrounding stakeholders and its future, things would begin to change. Too many of our companies are, in a sense, asset traders and proud of it. A slight change of language might do a lot to create a different atmosphere. In the end, however, I am cynical enough to think that if we don't change some of the rules nothing much will change. The fine words of the Watkinson Report will just go on being fine words. I would like business to begin to say to rule makers 'You are putting us at a competitive disadvantage and we actually need desperately to change those rules'.

ANNE FERGUSON (Management Editor, The Independent on Sunday): I would like to question the assumption that immortality is possible for companies, or desirable. There are natural life cycles for everything from the individual to governments and civilisations. The company is a relatively new organisation. What do you suggest is a natural life-cycle for a company?

THE LECTURER: Not many companies that I know deserve immortality at the moment but I would rather they died than were gobbled up by other people before they were even sick. I want companies to aim for immortality, though few will probably achieve it. I don't know what the natural life cycle is. It seems at the moment to be something like 40 or 50 years for big companies which isn't even close to immortality but is something to aspire to. You must plan beyond the grave because if you don't, you won't invest in long-term developments. When companies take on people it is implicitly for 45 years and yet most don't last that long. If you have really taken people on for 45 years, you ought to make a huge investment in them.



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PETER MORGAN (Director General, Institute of Directors): I did not wholly agree with your thesis because you had not given enough evidence about the failures you described. By contrast, Paul Marsh's recent publication on short termism showed quite a healthy situation. Nonetheless, the Institute of Directors has just commissioned a study into company law to see whether the laws devised to help float railway companies in the nineteenth century are necessarily what companies will need in the twenty-first century.

You referred to the strength of the private company sector on the continent. The British family company has been destroyed since the war by inheritance tax and corporation tax. To rebuild that essential business base we need tax reforms.

You talked about the short-termism of shareholders but the main shareholders are the institutions and institutional shareholders are held on average for about four years. I know this as a director of an insurance company. This is not quick in and out punting.

In my experience I have found that the ethos of the company is the focus on survival. When you have got over the problem of survival there may also be an opportunity to thrive but the truth is that most factors in the company environment tend to cause it to fail. Successfully running a company is not like administering a bureaucracy. Companies must win every day in the market place and conditions change every day in the market. The stakeholder plays a role in terms of the pressure he brings to bear on the bottom line which is the ultimate measure of company survival but the stakeholders are absolutely essential partners. Any company that is not working in a partnership to survive through the co-operation of suppliers, distributors, employees, customers and the surrounding community would, in fact, fail.

THE LECTURER: I don't disagree except to say that I wish companies would plan beyond survival. The companies I see that are focusing only on survival do not in some cases deserve to have a mandate.

PETER MORGAN: I don't mean just surviving the recession until the second half of 1991 but anticipating technologies and markets, consumer preferences, social factors which affect employment, maintaining a vibrant formula of success, and looking as far forward as appropriate.

THE LECTURER: Maybe that is what I call assuming immortality.

GEORGE GOYDER CBE: Thank you for the kind things you said about my book. Your final quotation was part of the 1944 Riddell Lecture given by Lord Eustace Percy and I agree that it is still as valid as when he wrote the words. From your review I was moved to think of the doctrine of trust. I believe we need a legal instrument which is based on trust, and trust is trusteeship. I see the future of large companies involving a supervisory board, which is responsible to the trustee function, while the ordinary board gets on with the management. England is the country which developed the idea of trust beyond all others. Reading F. W. Maitland in his work at Cambridge on Trusts made me realise that this was a principle which was part of our British inheritance. We ought to return to it in finding a way of balancing the hexagonal responsibilities.

THE LECTURER: The idea of trusteeship is very important in my scheme of things.

G. R. ELLERTON (Personal Banking Director, Midland Bank plc): Why do you think so little progress has been made to realising your very seductive vision? Is there some social, cultural, or political factor at work which allows more to develop in Germany and Japan as opposed to in Great Britain?

THE LECTURER: It is the problem of having an undisturbed past. We just accept that this is the way of doing things. We don't stand back and ask 'Is it any longer sensible?' It is very good for societies to be disrupted from time to time and it is interesting that people who lose wars sometimes in the end come out of them quite well.

JOHN FARAGO (Fellow of the Society): Have you any comments on the apparent failure of the co-operative movements?

THE LECTURER: The co-operative movements don't quite fit what I am talking about. They come out of the slightly different ethos which is about a style of management rather than the ownership of companies and treating the company as a community. The co-operative movement is about the way you run that community. They are idealistic and perhaps slightly naïve about how you run communities. So I think it is a fault in the management practices not the ownership status.

STUART ROCK (Editor, *Director* magazine): Would you say that graduates emerging from, say, the London Business School would be cheering this lecture to the rafters? How do you see the task of educating the education system to play a part in effecting change?

THE LECTURER: The students I meet in London fall into two categories: about 70 per cent of the class are very



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content to work within the existing system because they can see how they can thrive in it. Another 30 per cent genuinely feel it is an odd way to run a country but they also wonder whether change will come in their lifetime and they tend to put it on one side which is a pity. There is a quiet secret minority, maybe a majority, out there who I want to stand up and say 'This is a bit odd'.

A MEMBER OF THE AUDIENCE: Following the Brinton Report and fears from the government and public about global warming and other major aspects of environmental deterioration, all parties in this country and the international community are committed to achieving sustainable development nationally and globally. How do you fit your new enterprise into this context?

THE LECTURER: Fully, but the commitment has to be more than just words. I would like to think that they were committed but I am cynical enough to think that there must also be some rules and laws. We scoffed about seat belts but as soon as the law came in we all starting using them. In our heart of hearts we knew it was sensible. My new company is more likely than present companies to act on environmental issues without the law but it would help them if there were a law.

PAUL JERVIS (Bristol Business School): What relationship do you see between the board of trustees and what we call the management or executives? Do you see the board of trustees as part of the board of directors or separate from it and, if separate how does it communicate its sense of mission to the organisation as a whole?

THE LECTURER: I see it as a symbiotic relationship. The board of trustees hold the responsibility for the definition of the company's *raison d'être* but clearly it is going to be fed with ideas and wishes by the people who run the company.

ANNE JONES (Department of Employment and Member, RSA Council): How we can enable people to have a better understanding of Japan? We think about it mainly as being competitive and for its technical skill but I have been struck by the philosophy and the social aspects of work there. When I visited Canon, they talked first about their active philosophy and goals, which were to create a harmonious, global, interdependent community. There was nothing about profit and when I asked about it and the shareholders, they said that our shareholders in Britain would have a better chance of surviving long term if we thought more about strategy and less about short-term profit.

THE LECTURER: We have to find a way of getting companies to understand that they are not just assets to trade on the stock market. The Japanese don't think like that. What impresses me about Japan is they have these statements about values and missions and they all believe them. We have them and nobody pays any attention. They really are immortal communities, and are striving for the good of Japan. To return to Geoffrey Chandler's point, it would make a lot of difference if more people at the tops of companies stood up and said that was what they were about, that profit was part of it but was a means to an end.

THE CHAIRMAN: Charles Handy's lecture has shown an understanding of the dynamics and the demands of an industrial society and has, I hope, struck chords with those who are in the camp of wealth creation. He has stretched our imagination and challenged us.

SIR AUSTIN PEARCE (Member of RSA Council): One of the very few privileges and pleasures that a Treasurer of the RSA has is to be told that a lecture has been sponsored. Tonight we are triply helped because we have three sponsors: BOC, The Henley Forecasting Centre and Midland Bank and I would like to say a very big thank you to all three of those organisations for deciding that one of the purposes for which they exist is to sponsor events like this one. In one period of my career I was receiving on average sixteen appeals per working day, for money towards sponsorship. Our three co-sponsoring organisations, I am sure, receive even more requests so I am delighted that they have chosen the RSA, and in particular this lecture, as one to which they have so handsomely contributed.

MARK GOYDER (Programme Director, RSA): The RSA's Manufactures and Commerce Committee has already begun to gather together a group of people (some chief executives, some with an academic background), to tackle the questions that Charles Handy raised. Will those interested in joining us in a search for the new shape of the company please contact me so that I can given them more details and make sure they are part of our network?



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