Share buybacks: Symptom of a decaying economic order

Nick Beams
26 September 2014

The extent of the parasitism at the centre of the US economy and financial system is indicated by recent figures on the level of corporate buybacks.

Rather than using profits to finance increased investment in equipment, as well as research and development, corporations are buying back their own shares in order to boost the price. No additional value is created but financial traders and speculators, including the corporate executives of the firms concerned, can reap large gains through share market trades.

An article by *Financial Times* columnist Edward Luce published earlier this week reported that, according to Barclays, US companies spent more than $500 billion in the past year on stock buybacks, "a multiple of what most are spending on research and development and other capital investments." In the first six months of this year, buybacks totalled $338.3 billion, the biggest half-year amount since 2007.

Buyback operations have become one of the chief reasons for the escalation in the remuneration of corporate chiefs and other executives. In what amounts to a wholesale looting operation, a company buys up shares, reducing the number in the market and thereby increasing their price. The CEOs and management upper echelons, who took the decision on the buyback, then reward themselves with hefty salary packages on the basis that they have boosted shareholder value. Luce noted: "If you need an explanation for why the top 0.1 percent is doing so well, start with equity-based compensation."

Research carried out by William Lazonick of the University of Massachusetts Lowell reveals that seven of the top 10 largest corporations carrying out share repurchases laid out more on buybacks and dividends than their entire net income between 2003 and 2012.

Apple, one of the leading US corporations, spends more on share repurchases than any other company. It keeps profits offshore in order to avoid paying US corporate taxes and last year borrowed $17 billion in order to fund share buybacks.

In an article published in the September edition of the *Harvard Business Review*, entitled "Profits without Prosperity," Lazonick indicates the extent of these operations across the US economy.

"Consider the 449 companies in the S&P 500 index that were publicly listed from 2003 through 2012. During that period those companies used 54 percent of their earnings—a total of $2.4 trillion—to buy back their own stock, almost all through purchases on the open market. Dividends absorbed an additional 37 percent of their earnings. That left very little for investments in productive capabilities or higher incomes for employees."

In other words, over this nine-year period, the top companies in the S&P 500 spent 91 percent of their net income on boosting "shareholder value." The most recent data cited by Luce shows that the trend is continuing in the supposed US economic "recovery."

Given the crucial role of investment in economic expansion, the escalation of share buyouts is another expression of the worsening economic malaise, as it indicates there are few opportunities for profitable investments in the real economy.

Lazonick provides valuable data on this process, but it is another story when it comes to furnishing an explanation of their meaning. He contrasts the 30-year period following World War II, in which profits were reinvested in plant and equipment in order to expand production, giving rise to jobs growth and increased wages, with the trends over the past 30 years.

According to Lazonick, the "retain-and-reinvest" regime that characterised corporate governance in the

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first period has been replaced by a “downsize-and-distribute regime” that has come to dominate since the 1980s.

Seeking to explain this process in an article on the *Salon* web site in April 2012, Lazonick put it down to “financialisation,” that is, the creation of conditions in which corporate executives base all their decisions on the need to “jack up corporate stock prices” while “other concerns—economic, social and political—took a backseat.” He wrote: “From the 1980s, the talk in the boardrooms and business schools changed. Instead of running corporations to create wealth for all, leaders should think only of ‘maximising shareholder value’.”

The clear implication is that these profound shifts in the functioning of the capitalist economy arise from a change in the mindset of those in charge of its operations. This is to stand reality on its head.

Marx explained in the course of writing *Capital* that insofar as he dealt with the individual capitalists it was as the personification of objective economic processes.

The drive to accumulate, Marx made clear, did not arise from the individual greed of the capitalist as such, but from the inherent objective logic of capital itself as expanding value. This logic is enforced through the dictates of the market. Those who fail to obey, by expanding capital through the accumulation of profit, are wiped out in the competitive struggle, that is, they cease to be capitalists.

The driving force of capitalist production has never been the production of wealth to meet the needs of society but the endless expansion of the value of capital itself. For three decades after World War II, this expansion took place through the investment of profits in new plant and equipment, the hiring of additional workers to increase production, thereby securing additional profits. Capital expanded, new investment was carried out, jobs were created and wages rose.

However, from the beginning of the 1970s, the rate of profit began to fall. Capital responded to this shift through a vast restructuring, enforced by the pressure of the market. Major industrial concerns in the advanced capitalist countries were downsized or completely shut, cost-cutting technologies based on computerisation were introduced, manufacturing operations were transferred offshore to take advantage of cheaper sources of labour, while workers in the advanced economies suffered ongoing cuts in their real wages.

The process of “financialisation” was also rooted in this transformation. Ever-larger sections of capital, facing growing problems in the real economy, sought to expand via the financial markets, that is, to accumulate not by production but through the trading and manipulation of financial assets.

The shift in corporate ideology and the insistence that the central objective of every business must be to maximise shareholder value, as expressed in the price of the company’s shares, was an outcome of this development. In other words, the change in ideology was not the cause of the deep-going transformation in the functioning of the capitalist economy but rather one of its consequences.

The observation that there are “no innocent philosophies”—that is, they all have a definite political and class content—applies with even greater force in the sphere of political economy.

Lazonick’s assertion that the growth of corporate parasitism and outright looting is the product of an ideology or a business-school mindset leads him to advance the bankrupt perspective that corporate actions can be altered by changes in outlook.

In his *Salon* article, published in the immediate aftermath of the Occupy movement, Lazonick asserted that “properly governed, corporations can be run for the 99 percent.”

The real lesson to be drawn, not least from the figures and long-term trends Lazonick himself has documented, is that the capitalist profit system, driven by its own internal contradictions has entered an advanced stage of putrefaction, sending deadly toxins—mounting social inequality and mass impoverishment—coursing through the body of society.

The way forward lies not in a futile attempt to return to a mythical “golden age” of the past but to prepare the future by fighting to overturn the historically-outmoded profit system and establish a higher socio-economic order based on socialist foundations.

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