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The financialisation of US industry

Andrew Hill

Critics say fragmented ownership, weak internal culture and a fixation on financial results have harmed innovation at many large groups. But some have bucked the trend.

Last October, less than three months into perhaps the hardest job in corporate America, Boeing's chief executive Kelly Ortberg sent a memo to the aerospace company*s staff.

He warned them to brace for further cuts in the face of losses, a costly strike, quality problems and the continuing shockwaves from fatal crashes of two of its 737Max aircraft in 2018 and 2019.

Ortberg also went to the heart of why Boeing, once an icon of US engineering prowess, had lost its way. “We... need to focus our resources on performing and innovating in the areas that are core to who we are,” he wrote.

As Harvard Business School professor Ranjay Gulati wrote in his book Deep Purpose, Boeing “abandoned its larger reason for being - the values and sense of purpose that had fuelled the firm's success throughout the 20th century”.

Even into the 1990s, the company seemed cognisant of itself as dedicated primarily to an ideal - technological progress in aviation, in the form of “grand visions of building ever better, faster, bigger aircraft,” he wrote.

As President Donald Trump introduces tariffs to try to turbocharge a US manufacturing renaissance, critics assert that many industrial titans of the 20th century have shrunk in influence and often in scale after losing touch with the ideologies that made them great Many point the finger at Wall Street. “Anyone who's . . . interacted with investor relations departments and big companies knows that there are people who . . . have shrunk their entire understanding of a business to quarterly earnings numbers versus consensus,” says Dan Davies, an economist and author of The Unaccountability Machine.

Maximising one measure of success - and ignoring information not related to that metric - distracts companies from innovation and better long-term staff relations, he adds.

But a perceived enslavement to quarterly financial reporting is not the only factor behind the struggles of Boeing or other large industrial companies.

Although it still bears the name of its founder, Boeing's shares are owned by thousands of investors, large and small. This diffuse ownership structure, a characteristic of what Colin Mayer of Oxford's Said Business School calls “crisis capitalism”, increases the pressure to maximise short-term profits.

Mayer argues that “dominant, enlightened owners” tend to provide long-term stability to companies and insulate them to some extent from financialisation. They also instil a distinct and resilient culture, which often endures long after they have reduced their day-to-day involvement.

Size is another threat to a coherent industrial culture. As companies develop, they dilute the “original tribe”, says Rita McGrath, professor of management at Columbia Business School.

“Companies develop, they pick up a lot of ‘stuff' - rules that don't make any sense, a lot of bureaucracy,” she adds. “Unless you have companies that bring these things into balance, the entropy of j ust being a large company takes over.”

For over a century, General Electric served as a bellwether for both its engineering and management style. Stock market analysts extolled its financial returns while Jack Welch, chief executive for 20 years until 2001, was celebrated in books and articles.

But the financial crisis forced it to split into three companies and prompted a reassessment of its legacy. In The Unaccountability Machine, Davies recounted how the group “cemented the dominance of financial reporting over any other kind of information system”.

“Rather than making a resource bargain between the operating and strafegic management... every unit had to contribute to a smooth progression of quarterly numbers, often with absurd effects,” he added.

The dispersed ownership model cited by Mayer at Said Business School often contributes to this tendency. Digital image-making killed off Eastman Kodak's analogue film-manufacturing activities, prompting it to file for bankruptcy protection in 2012. In management circles, “a Kodak moment” is now more likely to be used to describe a failure to spot an approaching technological change than a memorable scene worth photographing.

But Kodak had been exploring digital imaging since the 1970s. It was Wall Street that pressured the company to continue milking its analogue film business, even as it became clear that consumers would switch to digital.

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William Lazonick, a professor of economics at the University of Massachusetts Lowell, bemoans the emergence of what he terms a "downsize-and-distribute" strategy, whereby companies hand surplus cash to shareholders as dividends and share buybacks. He contrasts this with the "retain-and-reinvest" approach that prevailed at US companies in the two decades following the end of the second world war.

Pfizer, the US pharmaceutical giant, pursued the former strategy during the 2000s: it pursued profit, often fuelled by acquisitions, increased dividend payouts and repurchased shares.

By2020, a year into his tenure, chief executive Albert Bourla had to explain to analysts that Pfizer had gone too far. "The reason why we don't do right now share repurchases [is] because we want to make sure that we maintain very strong firepower to invest in the business," he said. "The past was a very different Pfizer."

Lazonick argues that this change of course helped position the group to play a leading role, alongside BioNTech, in producing a vaccine for Covid-19 when the pandemic swept round the globe.

Mayer offers the alternative example of Novo Nordisk. Not content with its world-leading franchise in insulin, the Danish group developed obesity drugs Wegovy and Ozempic. He notes that although Novo Nordisk is a listed company, it is controlled by a foundation in an "anchor shareholder" structure. As a result, it has managed to combine social purpose, long-term thinking and financial success - and is now committing record amounts to research in the fight with rivals in the weight-loss sector.

Harvard's Gulati singles out the family-owned Swiss food processing and automotive equipment manufacturer Buhler as an example of a company that has stayed true to its core values. Chief executive Stefan Scheiber says the company aims to spend a steady 4 or 5 per cent of turnover on research and development "in good times and bad times". It is, he says, " a manifestation of purpose [that] creates a lot of credibility" with customers and staff.

For instance, while the pandemic prompted rivals serving the automotive sector to pause investment, Buhler doubled down on the development of "megacasting" machines to press large components for electric vehicles, boosting sales in that division last year.

Public companiesfindit "very hard to make the choice to put the money back into the business" rather than paying shareholders or incentivising executives, says Vai Hollingsworth, chief executive of Hollingsworth & Vose.

He adds that the US manufacturer of industrial paper products, which can trace its roots back to the 18th century, takes the view that "if you have all your eggs in one basket, you had better take good care of the basket".

Dave Whorton, author of a new book about long-lasting companies, Another Way, founded the US-based Tugboat Institute to share best practice between purpose-driven private companies such as H&V. He adds "paced growth" and policies to recruit, retain and develop the best people to the list of attributes that have sustained companies for 100 years or more.

But it is possible for listed companies to secure shareholder backing for bold strategies if the rationale is clearly communicated. Columbia's McGrath cites Adobe as a classic example.

In 2011 the software group decided to divert away from selling hard-copy upgrades of its programs and switch to a cloud-based subscription service instead. It anticipated disruption to sales, heavy capital spending that would hit profit, and customer resistance.

"They gave analysts the bad news, warned about big investment in the transition and gave [Wall Street] markers to measure progress," says McGrath. Revenues and profits went down in the short term before recovering sharply and within five years, Adobe's market value had almost trebled.

Such "critical moments", when executives are thinking about taking a company in a new strategic direction, require both firm leadership and internal support. "You have to have this generous layer of middle managers who really care about the future of the company," she adds.

In many cases, though, profit-seeking leaders hollow that layer out to boost profits - in the process eliminating the managers who transmit the nuances of complex relationships between the company's different activities.

After Boeing's merger with McDonnell Douglas in 1997, senior management became more focused on financial metrics and engineers became less commonplace in senior corporate roles. A February 2024 report to the Federal Aviation Authority about safety management at Boeing found that engineers working outside its Seattle manufacturing hub "felt isolated in work and decision-making processes ... with little organised mentoring or knowledge sharing". In January, Ortberg - himself an engineer - said the group "continued to strengthen important aspects of [its] safety and quality plan".

According to Pedro Monteiro of Copenhagen Business School, Boeing's earlier failure to organise its key engineers had not only created pockets of inexperience in areas critical to making the aircraft safe, but had sent a negative message. "While many companies prioritise attracting top talent and investing in learning and development, the true measure of experts' impact on operations lies in how they are positioned and valued,"

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he wrote in MIT Sloan Management Review.
Contrast aircraft manufacturer Embraer of Brazil. While the company is publicly listed, 42-year Embraer veteran Luis Carlos Affonso, senior vicepresident of engineering and technology development, points out that many top executives are engineers. He adds that having developed 30 new aircraft in 30 years, they “have seen the results of what they've done, which in a longcycle industry is invaluable”.
When you weaken links between boardroom and shop floor, author and economist Dan Davies says, “you're gradually kind of taking out [the group's] cerebrum, brain cell by brain cell. And over time, the world's changed and you need to react - but you no longer necessarily have the capacity to react.”

Between 2002 and 2017, David Cote executed one of the most admired turnarounds of a large industrial company.

When he took charge of Honeywell, it was still struggling to integrate two sets of workers and a variety of conflicting working practices - a legacy of the botched takeover of Honeywell by AlliedSignal three years earlier.
Cote introduced a “One Honeywell” initiative, stressing the importance of a unified internal culture. He prioritised not just financial metrics but developing and motivating staff, as well as “doing right by our customers”.
By the time Cote left, Honeywell's market value had increased from $20bn to $120bn, while self-funded spending on research and development rose from 3.3 per cent of sales in 2003 to 5.5 per cent in 2016.
In Winning Now, Winning Later, his 2020 account of his Honeywell career, Cote wrote: “Planting seeds for the future while also achieving short-term results is much harder to pull off than just aiming for one of these goals exclusively.” His turnaround seems to demonstrate that it is possible to meet both the short-term demands of investors and also long-term objectives.
Yet, six years after his departure, the group is being urged to break itself up by activist investor Elliott. Its pitch to the company's board lauded Cote's work as “one of the great turnaround success stories in corporate history”, but argued that “uneven execution, inconsistent financial results and an underperforming share price” since then had tarnished its record.
Vimal Kapur, Honeywell's current chief executive, later followed Elliott's advice and said the company would explore a sale of its aerospace business, which accounts for two-fifths of sales.
Pfizer is also coming under pressure from Starboard Value, another activist investor, as the short-term boost from the Covid-19 vaccines wears off. Starboard has attacked the drugmaker's underperformance following a drop in sales and falls in the share price.
In October, the investor accused the company of failing to achieve “sufficient revenue returns” on R&D investment and recent acquisitions.
Bourla has fended off the criticism, but in doing so, he has dug deep into the standard Wall Street playbook, promising to cut costs and raising sales and profit forecasts.
McGrath, of Columbia Business School, says the constant evolution of strategy is a vital part of company development. Companies often “top out” after 40 or 50 years of existence “not because they don't have smart people, or don't have resources,” he says, but because they fail to “tune or update” the practices that made them a success.
Hollingsworth confirms the insight. H&V operates with “a very high focus on technology and reinvestment [and] a healthy dose of paranoia that if we don't keep moving forward and look for new products, we wouldn't survive”.
Well-established companies should ask themselves a simple question, says McGrath: “Who in the company is in the business of looking after its future? “In most of the companies I work with, it's in between the head of innovation, with no power, and the C-suite, where it isn't taken really seriously. And I think that's a problem.”

Adobe became massively more US companies are returning huge profitable as service revenue roseamounts of capital to investors Net income Revenue (%)Returns as % of net income ($bn) •— Subscription Dividends M — Product * Buybacks 4 - -100 Mi— o 2009201520202024 Source: William Lazonick • Data for 216 companies that were listed Source: company reportsbetween 1981 and 2020 and were S&P 500 constituents in 2020

‘You’re gradually taking out [the group’s] cerebrum, brain cell by brain cell... you no longer have the capacity to react’ ‘[Adobe] gave

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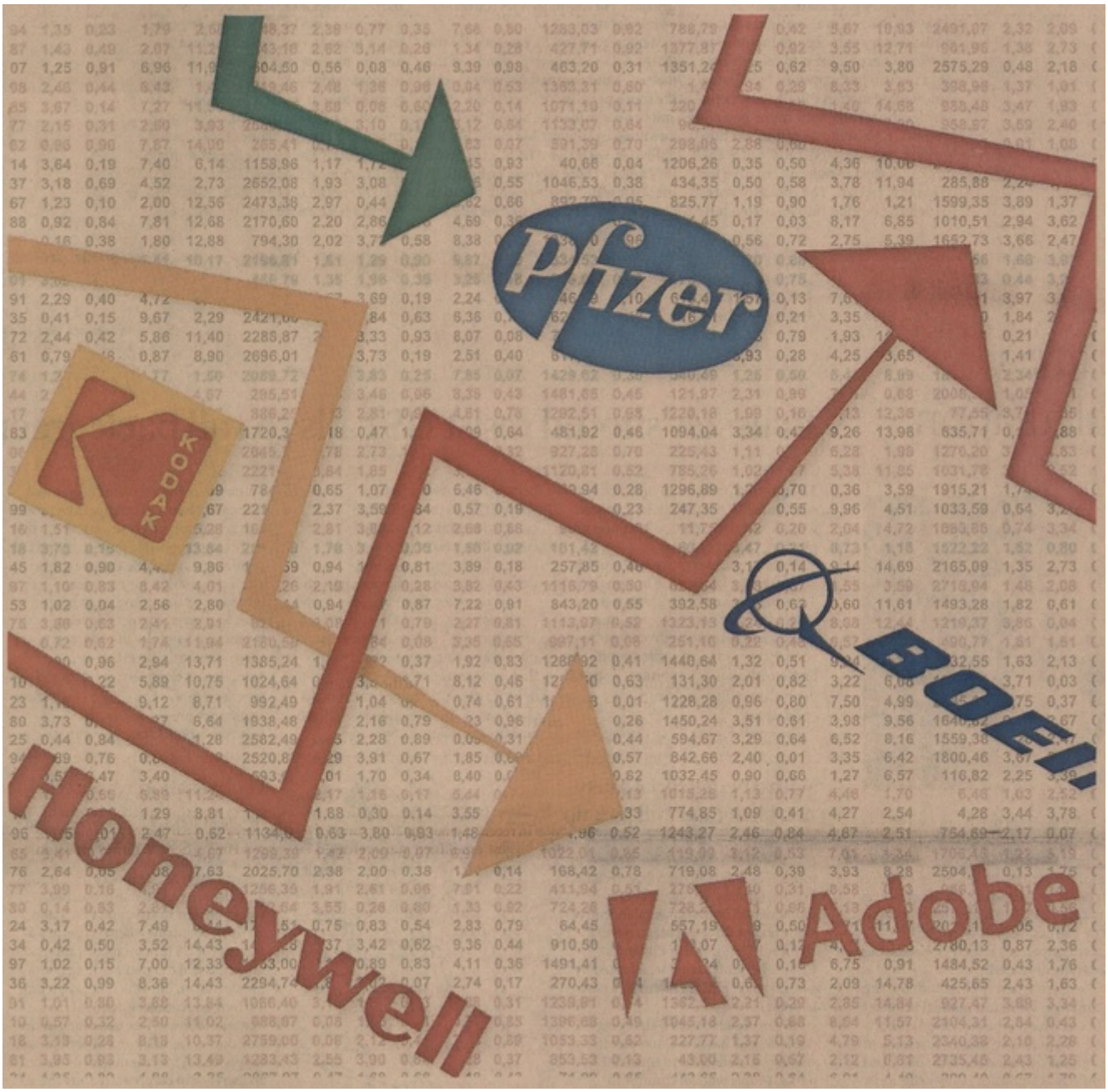

Critics assert that many American industrial titans of the 20th century have shrunk in influence and scale — after losing touch with the ideologies and ideas that made them great.There are, however, some success storiesFT montage; Getty Images

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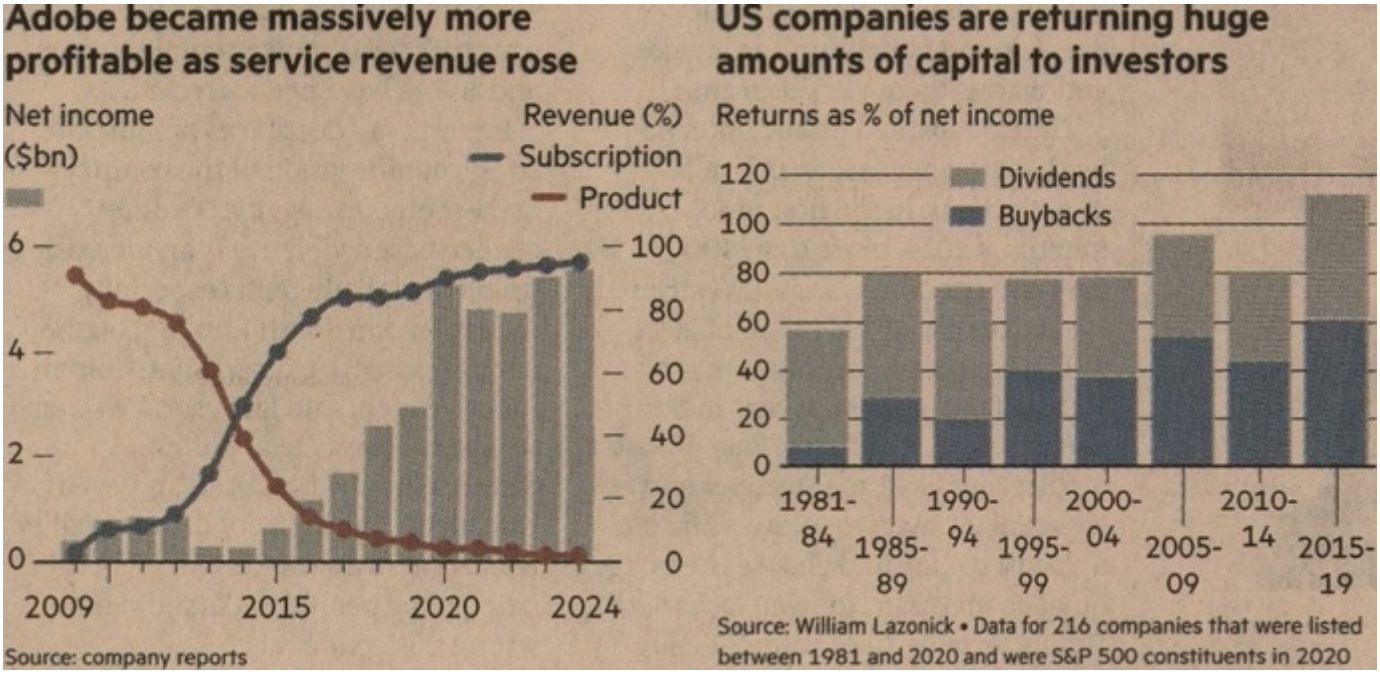

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