



Critical Review: Milton Friedman's CSR and the Shareholder Theory

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Word Count: 2493

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Introduction

A Nobel Prize-winning American economist ([Forder and Monnery, 2019](#)), Milton Friedman is known for his essay on corporate social responsibility published in the 1970s in which he shared his thoughts regarding the social responsibilities of businesses for the betterment of society. He clearly indicated in his doctrine that the only social responsibility that a firm has to increase the profits and those businessmen who are working to improve the social ills by using the funds of the firm in which they are working are playing their roles in weakening the foundations and infrastructure of a free society.

The arguments, concepts, and thoughts of Friedman were not admired initially; however, his idea of generating end-profit ([Epstein, 2020](#)) for shareholders got recognition in 1976, six yrs later, when a well-known paper highlighting the importance of shareholders value was published. Friedman's shareholder theory was considered to be a huge contribution ([Hetzel, 2007](#)) to the world of the business economy.

Critical Review

I. The Doctrine

According to Friedman's doctrine: *generating more profits for shareholders is the only social responsibility of businesses*, ([Friedman, 1970](#)). This states that for any private entity organization, business is all about generating more return on investments (profits) for shareholders and not getting involved in some society improving activities considering a firm to be responsible for countering and helping for incidents happening in society.

Additionally, according to Friedman's shareholder theory, the shareholders were viewed to possess an upper hand in their corporation with business executives as their employees ([Epstein, 2020](#)). In regards to this, business executives were to act following the demands of their business owners (shareholders) only while conducting business; by indulging in socio-economic acts pursued strictly with the intent of generating more profits; in conducting business following all the legal laws, rules, regulations, and ethical values.

II. Persuasion Invoked

Friedman wanted to persuade the readers to understand that a business executive holds no authority or right to make any financial decision regarding social responsibilities ([Martin and Mertens, 2013](#)). According to Friedman, the common concept of CSR opted by corporations for the betterment of society was a false one. Friedman was against the idea of business executives spending corporate money in the name of social causes without the proper consent of business owners (shareholders). This was something that Friedman considered to be unethical as it seems inappropriate to use other's resources for your own needs and that too without informing them.

Friedman earnestly held onto the idea that businesses should only put in their efforts to generate better revenues and should not get into activities like charities as he did not consider these responsibilities to be a social obligation for business executives.

III. Type of Judgement

Friedman, in his famous CSR doctrine, made use of analytical and qualitative statements. Throughout his essay, readers were convinced to understand that the common concept of CSR held by people regarding corporations having a responsibility towards social development and public good was not valid and that the corporations were only responsible for satisfying their shareholders by generating maximum profits.

The doctrine's very statement is a normative one in which Friedman states the only responsibility of an organization to follow the revenue generation protocols so that profits can be maximized. From this statement, Friedman wants to clear that a corporate can go for social acts depending upon the desirability of the situation and should not do it considering it to be its responsibility.

In Friedman's doctrine, the value of the shareholders was placed on top priority, over other stakeholders ([Smith, 2003](#)) and the business executives who were not working to increase the profits of a firm were not playing their roles justly. This was a synthetic judgment ([Troy, 2021](#)) that Friedman derived from an empirical analysis ([Friedman, 1959](#)).

IV. Ethical consistency and persuasiveness

With Friedman's doctrine gaining momentum in the business world, it was almost readily accepted by business owners who firmly agreed with Friedman's idea of businesses working to please their shareholders by maximizing profits ([Scott, 2007](#)). It was not only the business owners who approved of Friedman's arguments rather his ideas were supported by different researchers and academicians too ([Cheffins, 2020](#)).

However, some businesses find it to be consistent enough at some points only and this was something that stopped them from incorporating it as a whole in their business strategy. While some found the shareholder theory ([Mansell, 2013](#)) to be persuasive enough, others failed at deriving a sense of ethical consistency out of it ([Cosans, 2008](#)). Consequently, the doctrine was subjected to severe criticism from critics ([Shea, no date](#)).

One of the statements put forward by Friedman stating that 'the sole aim of a corporation is to engage in acts that help increase the profits by considering the rules also implying that it should avoid any type of fraud' was highly criticized. Critics were of the idea that this was unethical, however, Friedman clearly indicated that steps taken for maximizing the profits should be according to the laws.

Furthermore, the slogan of 'only money matters' also raised people's concerns about Friedman's doctrine. Friedman's statement: 'the social responsibility of a business is to increase overall profits' was considered to be a bold statement by some critics who took it mistakenly as business executives going to any extent to generate more revenue for the shareholders ([Wagner-Tsukamoto, 2007](#)).

Another statement that got immense criticism was about corporations possessing no responsibilities of their own. Friedman elaborated the statement in his CSR essay stating that only people have

responsibilities. Critics criticized it by saying that corporations hold various responsibilities([Kemper and Martin](#), 2011)and that the corporations act as persons in the society ([Ripken](#), 2009-2010.)

The whole of this criticism indicates that Friedman's essay was not following ethical values([Cosans](#), 2008)and the denial of business from social responsibilities regarding society and capitalism rendered the famous doctrine as not persuasive enough to be employed rigorously in the world of the business economy ([Carson](#), 1993).

In short, Friedman's theory was rejected and criticized to the point that towards the end of the 20th century, the shareholder theory lost ground with the newly devised, put forth by other renowned economists of the time as a rival to shareholder theory, that was more persuasive and ethically consistent alternatives employing socio-economic growth and capitalism([Retolaza and Jose](#), 2011)as a key towards business success.

V. Do arguments stand the test of time or have circumstances changed?

Even after showing immense criticism of Friedman's doctrine, it was indicated by several research papers ([Orlitzky](#), 2015)that some of the corporations opted for this by considering the doctrine to be a sacred business objective. In addition to this, different business schools([Ghoshal](#), 2017)added Friedman's doctrine to their curriculum as they considered it to be the best method for evaluating the performance of a business.

Defenders of the shareholder theory believe that the theory, even though, in its true words negates the corporates considering work for social cause an obligation, however, if the act promises to return the corporate an enhanced value of shares and stocks, those acts can be regarded as ones consistent with Friedman's maxim. Holding on to this view, there are multiple corporations like IBM that still make use of the shareholder theory in their corporate structure ([Sanford](#), 2005). However, most contemporary business corporations have withdrawn from integrating the shareholder theory into their corporate structure.

Friedman's arguments have failed to stand the test of time for modern-day business because today businesses can survive only if both the social and corporate responsibilities are taken into consideration side by side. Opting for one and leaving the second won't offer the right outcomes and this can result in affecting both the businesses as well as society. Research has shown the doctrine to be too limited for the present-day business of the 21st century([Merrick](#), 2021) because of intense political polarisation.

Alternatives to Friedman's shareholder theory

Friedman's famous statement regarding the financial economy blew the world of economics. This was not only taken up by the business owners but they incorporated it as an effective marketing tool for measuring the success of their business.

However, with time, business owners took benefit from their experience and discovered the results for their performance by considering the shareholder theory. To their surprise, the results were not according to their thoughts even though the famous shareholder theory was widely accepted and was the winner of a Nobel Prize too. It was indicated by research that the incorporation of shareholder theory was responsible for economic inequality on a greater level([Fligstein and Shin, 2004](#)).

Environment and Climatic Danger Imposed

Friedman's theory was responsible for causing a huge setback to economic equality thus giving rise to disparity and imbalance([Jahn, 2016](#)). By considering the agenda of no social responsibility, different corporations opted for ways that can help disintegrate the ecological effects and to cover up the hazards that had adversarial effects on climatic changes ([Lyon and Maxwell, 2008](#)).

It was because of the deception offered by organizations that the human race was subjected to different consequences and this resulted in putting a great number of lives at greater risks. This was explained by different academicians and research papers that indicated that the shareholder theory was not only harmful to the businesses but the human race and environment too.

Thus, this was the crucial reason for bringing a change in Friedman's doctrine regarding monetary economics. To be more specific, this situation played an important role in modifying the social responsibility of organizations.

I. Stakeholder Theory

A stakeholder theory was suggested by R. Edward Freeman in 1984 with an idea to reverse and to count for the social responsibility paradigm proposed by Friedman's doctrine ([Friedman and Miles, 2022](#)). This stakeholder theory was an alternative perspective that suggested that business executives were responsible for creating better values for business stakeholders and that too without falling back on negotiations.

It was also indicated in Freeman's theory that the shareholders of Friedman's theory are just like many of the stakeholders of different firms and organizations. Apart from this, business executives are not only responsible for creating values for stakeholders but the shareholders too.

According to Freeman's theory, a stakeholder can be defined as the one who holds an investment in a company or in any way is involved or associated with a corporation. Furthermore, everyone who affects an organization directly or indirectly is considered to be the stakeholder of that particular organization. For instance, customers, employees, vendors, and environmentalists all come under the category of stakeholders in the light of Freeman's theory([Gomes, 2006](#)).

According to Freeman, Different public corporations and government institutes and any person who holds greater or smaller affinity with an organization are all stakeholders. Similarly, those people without which a corporation can't work effectively and efficiently and without whom different tasks of an organization are ceased are all stakeholders of that firm.

Stakeholder Ecosystem

The stakeholder theory is considered to be imparting a positive impact on sustainable business practices in contrast to Friedman's shareholder theory ([King, et. al., 2015](#)) This is because the shareholder theory plays an important role in painting the habitat of a corporation as an ecosystem, and this ecosystem, contains different groups that are closely associated with one another in terms of business. This also indicates that the success of a business lies in the success of all of its groups, so, it is significantly important to keep all these groups closely linked and contented.

By keeping the groups closely linked, Freeman's theory has played an important role in resolving the economic inequalities and different environmental and societal issues ([Shea, no date](#)). However, Freeman's theory has been criticized by some academicians as it makes different management procedures complex and complicated ([Wixted and Holbrook, 2012](#)). These complications arise because of the different conflicts that are always present but require certain negotiations to deal with. As a result of this, different range of groups has to compromise so that these conflicting interests can be settled down.

Stakeholder theory helps introduce corporations with the approach of shared value distribution for all the groups and not only considering the shareholders and stakeholders to be of the highest value. However, in reality, the approach of shared value distribution is considered to be more ethical ([Harrison, Freeman and Abreu, 2015](#)) and comprehensive as it follows a consistent and sustainable business approach.

II. Creating Shared Value: CSV Model

Porter and Kramer later modified the theory of Freeman by introducing a model known as Creating Shared Value, a CSV model ([Porter and Kramer, 2018](#)). According to this model, corporations can go well if they incorporate social and environmental considerations within their business strategies.

This can be done better by turning societal concerns into business opportunities by corporations. This can also help in generating better returns in investments. CSV model is the widely used approach by different businesses these days ([Engstrom and Johansson, 2019](#)). For instance, Nestle is adopting a CSV model with the intent of providing healthy water and nutrition to rural areas which not only helps feed the farmers growing the crop for the firm but also helps the firm itself with business growth ([Nestle, no date](#)).

The Nestle company operates its business on the grounds of committing development and sustainability for the environment, society as well as the economy with the intent of returning better financial results to not only the shareholders but its entire network of stakeholders which includes farmers, suppliers, distributors, and so on - thus making use of CSV model. This indicates the consistent approach of the CSV model for different sustainable business practices these days.

Conclusion

With the introduction of the the capitalism method, the doctrine of Milton's Friedman lost its importance and became a concept of the past. The instability and uncertainty of Milton Friedman's theory were responsible for the implementation of shareholder capitalism that also helped in improving the performance of a firm overall.

Though shareholder theory played an important role in increasing the profits of a firm significantly, it brought certain side-effects too. With the implementation of Milton Friedman's theory, environment, society, and all the stakeholders have to suffer a lot and that too in different ways.

So, one positive point of shareholder theory that was to increase the profits of a firm was not enough to support Friedman's approach. Thus, opting for shareholder theory would have only resulted in an unfair compromise on different negative effects. That's why it was better to avoid this theory as it was not according to the ethics of the the business industry.

To conclude, Friedman's essay on corporate social responsibility was worthwhile in the 20th century and also in the starting decades of the 21st century. However, in the present-day world of the 21st century, economists have given rise to ethical, more effective and justifiable practices to be followed by corporations.

But if we say that it was because of Friedman's CSR theory that gave rise to the modern-day productive and functional economic policies, then it would not be an exaggeration.

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