

Reforming the Business of Pharmaceutical Innovation

Advising research, policy, and practice
March 16-18, 2021 | 9:00 am - 12:00 pm EST



Executive summary

Workshop #2 - After the Business Roundtable Proclamation; moving from shareholder primacy to benefiting all stakeholders

In 2019, the Business Roundtable issued a “Statement on the Purpose of a Corporation” that rejected the previously held position “*that corporations exist principally to serve shareholders*” and committed to a position that the purpose of companies is to “*benefit of all stakeholders – customers, employees, suppliers, communities and shareholders.*”¹ What does this mean for the biopharmaceutical industry? This workshop will explore the consequences of maximizing shareholder value, the business practices that perpetuate this purpose, and the changes necessary to assure the accessibility and affordability of innovative medicines that reduce the burden of disease.

The goal of this workshop is to identify key research questions that may better inform the pharmaceutical industry to serve the needs of all stakeholders.

Background

An extensive body of research has documented the untoward consequences of the principle that corporations exist primarily to serve shareholders and the resultant financialization of policies and practices designed to promote shareholder interests. The Academic-Industry Research Network (AIRnet), led by Dr. William Lazonick, has been in the forefront of this research.² Among these consequences are aggressive drug pricing, drug shortages, misalignment between the pipeline of products in development and the burden of disease, inadequate investment in antibiotics and vaccines, neglect of pediatric therapies, and the distribution of resources (profits) to shareholders in the form of dividends and stock buybacks, rather than reinvesting these resources in workers, patients, communities, or innovation.

The Business Roundtable statement echoes the famous statement by George Merck that “*We try never to forget that medicine is for the people. It is not for the profits. The profits follow, and if we have*

¹ Statement on the Purpose of a Corporation. opportunity.businessroundtable.org/ourcommitment/

² The Academic-Industry Research Network: <https://theairnet.org/>

remembered that, they have never failed to appear. The better we have remembered it, the larger they have been.”³ This workshop will ask the question: “what comes next?”

Our work

This workshop is part of a collaboration between the Center for Integration of Science and Industry and AIRNet focused on the business models for pharmaceutical innovation.

William Lazonick’s research has documented and analyzed the evolution over the past half century of the New Economy Business Model (NEBM), under the influence of which major U.S. corporations have transformed their mode of corporate resource allocation from innovation to financialization.⁴ Justifying this transformation has been the ideology, articulated from the late 1980s, that a company should be governed to “maximize shareholder value.” This ideology was reflected in the 1997 Business Roundtable proclamation that endorsed shareholder-primacy, which replaced the previous stakeholder statement of purpose, promulgated in 1981.

Lazonick’s analytical framework centers on the “social conditions of innovative enterprise” (SCIE).⁵ Guided by this framework, research at the AIRNet focuses on industry and company-level analyses of the social conditions related to strategy, organization, and finance that support or undermine drug innovation. AIRNet researchers have been able to analyze if, when, and why the strategy of particular drug companies turns from innovation—the development and delivery of safer, more effective, more accessible, and more affordable drugs—to financialization—the use of a drug company by those who exercise strategic control over its resource allocation for value extraction at the expense of value creation. Specifically:

- Using the SCIE framework, AIRnet researchers have been studying the evolution of the tension between innovation and financialization at the largest pharma companies. U.S. pharmaceutical companies claim that high drug prices fund investments in innovation. Yet, as AIRnet research shows, the 19 drug companies in the S&P 500 Index in February 2020 that were publicly listed from 2010 through 2019 distributed 116% of their profits to shareholders over the decade, 65% as buybacks and 51% as dividends.⁶
- Through the accumulation of case analysis on companies based in the United States, namely Merck and Pfizer, and in Europe, namely Roche, AstraZeneca and GlaxoSmithKline, AIR research examines the extent and resolution of the innovation-financialization tension among major pharmaceutical companies engaged in global competition.⁷

³ Address to Medical College of Virginia, December 1950.

⁴ Lazonick, W. (2012). The financialization of the US corporation: What has been lost, and how it can be regained. *Seattle UL Rev.*, 36, 857, at <https://heinonline.org/HOL/LandingPage?handle=hein.journals/sealr36&div=28&id=&page=>

⁵ Lazonick, W. (2015) The theory of innovative enterprise: A foundation of economic analysis, AIR Working Paper #13-0201, at http://www.theairnet.org/v3/backbone/uploads/2015/08/Lazonick.TIE-Foundations_AIR-WP13.0201.pdf

⁶ Lazonick, W., Tulum, Ö., Hopkins, M., Saking, M.E. and Jacobson, K. (2019) Financialization of the U.S. pharmaceutical industry, Institute for New Economic Thinking Working Paper, December 2, at https://www.ineteconomics.org/uploads/papers/Lazonick_financialization.pdf

⁷ Tulum, Ö. and Lazonick, W. (2018) Financialized Corporations in a National Innovation System: The U.S. Pharmaceutical Industry, *International Journal of Political Economy*, 47(3-4): 281-316. Also see Tulum, Ö., Andreoni, A., and Lazonick, W. (2021). F Innovation, financialization and productivity in the UK pharmaceutical industry: A comparative analysis of GlaxoSmithKline and AstraZeneca, GoFinPro Working Paper, SOAS University of London.

Separately, the Center for Integration of Science and Industry has documented the scale of profit and value extraction by the 35 largest pharmaceutical companies.⁸ Key findings of this work include:

- From 2000-2018, 35 of the largest pharmaceutical companies reported \$11.5 trillion of sales with gross profits of \$1.9 trillion, distributing \$1.7 trillion to shareholders in the form of dividends or stock buybacks, and funded \$1.7 billion in R&D.
- The median annual profit margins of pharmaceutical companies (net income 13.8%) was significantly greater than other S&P 500 companies (net income 7.7%). The difference was smaller when considering only companies reporting R&D expense and controlling for company size and year.

The collaboration between AIRnet and the Center for Integration of Science and Industry focuses on how different types of business models in the pharmaceutical industry influence its performance in producing safe, effective, accessible, and affordable drugs. Specifically, this research effort seeks to:

- Understand government-business collaborations (GBCs) in the development and distribution of safe, effective, accessible, and affordable medicines. Building on the Center's analysis of NIH funding for research related to recent drug approvals, AIRnet research delves deeply into particular cases to see how GBCs actually function and perform. Particularly, within the context of the pandemic, the AIR-CISI collaboration has been exploring the role of GBCs in the development and delivery of vaccines and antiviral drugs for COVID.
- Develop a new method of evaluating the innovativeness of new drugs in terms of safety, effectiveness, accessibility, and affordability, which is critical to assessing the cost and benefit of each medicine for all the patients and payers across different national health systems. A systematic approach to drug-price determination provides insights into the social priorities of GBCs in allocating R&D dollars to address unmet medical needs.

Questions raised by this workshop

The principle of maximizing shareholder value, however, is deeply ingrained in corporate strategy and practice, corporate governance and the concept of "shareholder rights," executive compensation, accounting, finance, and government regulations. Refocusing the pharmaceutical industry on a stakeholder perspective, which vests innovations in the treatment and prevention of disease, public health, public value, and equity as appropriate goals of the corporation, would require fundamental changes in the nature of business.

Our expectation is that this workshop will move beyond examining the consequences of maximizing shareholder value to consider what a stakeholder-focused pharmaceutical industry would look like, the path forward to achieve that goal, and what new research or policy may be required.

⁸ Ledley et al. "Profitability of large pharmaceutical companies compared with other large public companies." *Jama* 323.9 (2020): 834-843. <https://jamanetwork.com/journals/jama/article-abstract/2762308>

Convenors

- **Fred Ledley, M.D.**, Bentley University, Professor, Natural & Applied Science, Management; Director, Center for Integration of Science and Industry.
- **Öner Tulum, M.B.A., Ph.D.**, Senior Research Associate, The Academic-Industry Research Network; Research Affiliate, The William R. Rhodes Center for International Economics & Finance, The Watson Institute, Brown University.

Discussants

- **Edward Freeman, Ph.D.**, Professor, Business Administration, University of Virginia; Academic Director, Business Roundtable Institute for Corporate Ethics; Co-Academic Director, Institute for Business in Society.
- **Cynthia Clark, Ph.D.**, Professor, Management, Bentley University; Director, Harold S. Geneen Institute of Corporate Governance.
- **Pascale Lehoux, Ph.D.**, Professor, Department of Health Management, Evaluation & Policy, University of Montreal
- **Rick Wartzman**, Head of the KH Moon Center for a Functioning Society, Drucker Institute
- **Dana Brown**, Director, The Next System Project, Democracy Collaborative
- **Rick Alexander, J.D.**, Founder, Shareholder Commons
- **Judy Samuelson**, Executive Director, Aspen Business+Society Program; VP, Aspen Institute

Workshop plan

The session will begin with an informal introduction to the theme of this workshop, followed by 5-8 minute comments from each discussant, describing their perspectives based on their work and experience. We hope these introductory comments will provide an opportunity for an open discussion between the discussants and other participants in the workshop.

If you wish to ask a question during the session, please indicate yourself or directly post the question in the Zoom Chat box. A member of our team will be monitoring this and will invite you to ask your question at an appropriate time.

For more information, please email SciIndustry@bentley.edu