Higher Purpose, the Greater Good and Finance

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Abstract

Organizational higher purpose is gaining increasing traction in both research and policy discussions about the (desired) role of corporations in society. What is higher purpose and how does it affect corporate governance? This paper defines higher purpose and surveys the literature in economics, finance, organization behavior and management strategy on organizational higher purpose. Key research questions addressed in these strands of the higher purpose literature are identified and the available insights are discussed and synthesized. Higher purpose is a contribution goal that is distinct from shareholder value maximization, but in firms that implement higher purpose effectively, decisions are made at the intersection of purpose and value maximization. Higher purpose is not charity, and it will worsen governance and fail to be sustainable when it is either viewed as charity or used merely for "virtue signaling". Moreover, mandating the adoption of a higher purpose is generally unadvisable.

Keywords: higher purpose, prosocial corporate behavior, corporate governance, banking, financial literacy

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by

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ABSTRACT

Organizational higher purpose is gaining increasing traction in both research and policy discussions about the (desired) role of corporations in society. What is higher purpose and how does it affect corporate governance? This paper defines higher purpose and surveys the literature in economics, finance, organization behavior and management strategy on organizational higher purpose. Key research questions addressed in these strands of the higher purpose literature are identified and the available insights are discussed and synthesized. Higher purpose is a contribution goal that is distinct from shareholder value maximization, but in firms that implement higher purpose effectively, decisions are made at the *intersection* of purpose and value maximization. Higher purpose is not charity, and it will worsen governance and fail to be sustainable when it is either viewed as charity or used merely for “virtue signaling”. Moreover, *mandating* the adoption of a higher purpose is generally unadvisable.

HIGHER PURPOSE, THE GREATER GOOD AND FINANCE

1. INTRODUCTION

This paper reviews the role of higher purpose (and related concepts of prosocial behavior by firms) and its interaction with Finance, as a way to highlight the research findings on the prosocial role Finance can play in elevating social welfare. There are papers being written in a number of different areas on the topic, so the existing literature fragmented and dispersed, and many papers touch on Finance-related issues, but there is little integration. This makes it hard to have a unified sense of what the key research questions are, let alone how a research agenda should be built to address important issues. For example, relevant questions have been addressed in numerous papers in the economics of incentives, corporate finance (including corporate governance)[1], healthcare and biotech R&D[2], organization behavior, management and so on. Many of these papers have made profoundly important points that should lead to further research. Yet, progress is hampered because there is often a lack of depth in the understanding of even basic issues like the difference between higher purpose and Corporate Social Responsibility

[1] See, for example, Benabou and Tirole (2003, 2006, 2010).
[2] See, for example, Lo and Thakor (2021, 2022)

(CSR), or between higher purpose and the mission of the corporation. This lack of understanding is not only among corporate executives, but also academics.

In this paper, I attempt to address this issue by bringing together the many insights that have already been generated, sorting through them, synthesizing them, and presenting clear definitions and relationships of seemingly disparate ideas, ending with a discussion of the important questions that have already been answered and those that still remain. Hopefully, this can spur insightful future research on this topic. The importance and promise of this cannot be overstated, as many have long recognized the enormous importance of economics (and even more pressingly, finance) to be a "moral discipline", in contrast to being "values-free", as has been the tradition. For example, in his Presidential address to the *American Economic Association* in December 1968, Kenneth Boulding presented his famous "Economics as a Moral Science" paper (Boulding (1969)) that rejected the idea that economics is value-free. Since then, many have written about the role of Economics in promoting the greater good. For Hausman and McPherson (1993) write:

"To be a good person, one must take ethics seriously. But can the same be said about being a good economist? Does morality matter to economic analysis? It would be idle to suggest that economists should spend a large part of their time studying moral philosophy, and moral sophistication may be more important in some areas of economics, such as political economy, than in others, such as econometrics. Yet we would argue that a moderate does of reflection on the relations between economics and

morality could help many economists work more effectively. We should emphasize our concern to show the relevance of moral thinking to the conduct of both positive and normative economics. Not only do moral principles bear on issues concerning evaluation and policy, but they also influence the questions positive economists ask and the answers they find plausible."

There has apparently not been the same interest in defining finance as a "moral discipline" for the greater good. In fact, the Friedmanian view of the virtue of profit maximization as a singular objective for the firm is often taken as a justification for not "polluting" the shareholder value maximization objective with "greater good" concerns; such pollution would worsen corporate governance. This point is further buttressed by valid concerns that allowing non-shareholder-value-maximization factors into the firm's objective can cause us to lose "research discipline" and also open the door for a host of political considerations to come into play, things we want to avoid as researchers since these could be potential diluters of credibility and independence of thought. While these are very valid concerns, we need to tackle them head-on and discuss the research implications of finance contributing to the greater good. Not doing this has so far represented a missed opportunity for the field for two reasons. First, it tends to shroud the many prosocial contributions that finance already makes, thus not only obscuring them to the general public and the students we teach, but also to researchers who fail to appreciate that working on these topics may lead to publications success, besides contributing to the greater good. Second, it robs the field of the opportunity to counter the criticism from many in society that the field of finance is just about opportunistic behavior, stock markets and greedy traders , agency costs, rent extraction and financial crises, i.e. we miss the opportunity to argue that finance has social value. We tend to take our social value for granted as finance professors, but others do not (including our many colleagues in other parts of the university).

The goal of this paper is to fill this void, not only by providing a careful survey and synthesis of the relevant literature, but also highlighting the many existing prosocial contributions of finance, and then discussing the opportunities and challenges before us in the form of research questions that remain to be addressed. The survey will cover the following areas in which research on organizational higher purpose and prosocial organizational behavior has been conducted: economics of contracting in organizations; organization behavior and management; and finance. The literature in finance will be reviewed as four distinct sub-literatures: (i) banking and fintech as ways to increase credit access (including for underserved communities); (ii) biotech R&D, medical innovation and health; (iii financial literacy; and (iv) increasing job satisfaction and employee productivity.

Research Questions: This survey is organized around research questions (RQs) that we have some answers to in the literature. It will conclude with those that remain to be answered and represent topics for future research. The research questions for which the literature offers insights are:

(RQ1) Higher Purpose and Related Concepts:

How should "higher purpose" be defined relative to the more familiar concepts of CSR, mission, vision and the firm's objective function? Specifically, what is the relationship of higher purpose to shareholder value maximization and where are the tensions?

(RQ2) Higher Purpose and the Economics of Prosocial Behavior:

What does the economics literature say about prosocial behavior by organizations higher purpose? Specifically, how does higher purpose interact with incentive contracting in organizations?

(RQ3) Higher Purpose and the Organization Behavior and Management Strategy Literature:

How does organizational higher purpose affect employee job satisfaction and productivity?

(RQ4) Higher Purpose and Finance:

How could the integration of higher purpose by organizations into their objective function improve welfare by:

(i) Increasing access to credit?

(ii) Closing the "funding gap" between the demand for welfare-enhancing R&D (and drug development) and the availability of such financing for biotech firms?

(iii) Improving financial literacy?

(iv) Improving governance and elevating employee job satisfaction, productivity and happiness?

Summary of Key Findings

On RQ1, higher purpose is a contribution goal and thus differs from CSR, mission and vision. It is often in tension with shareholder value maximization, but surprisingly it sometimes enhances shareholder value.

On RQ2, the literature on prosocial behavior (including CSR and ESG)[3] behavior by firms has theories and empirical evidence that paint a mixed picture. While some theories and empirical evidence highlight the positive aspects of prosocial initiatives, others highlight the dark side of it. On the positive side, the literature finds more of a long-term orientation in investments, greater employee satisfaction and improved economic outcomes. But on the dark side, papers have found a decline in economic output and a failure to achieve social objectives. The literature aimed specifically at higher purpose finds that it is potentially socially valuable when it is prosocial, but it need *not* be prosocial. Effectively implemented higher purpose influences incentive contracting within the firm.

On RQ3, *authentic* higher purpose can potentially elevate employee job satisfaction and productivity, but the empirical evidence is mixed. It appears that for higher purpose to positively influence economic outcomes variables, both authenticity of higher purpose – the senior leadership can credibly convey that it values the adopted

[3] ESG stands for environmental, social and governance, a term often interchangeably with social investing.

higher purpose for its own sake as opposed to valuing it as a “virtue signaling” slogan – and the clarity of its communication are required. However, the potential exists for higher purpose to not only worsen economic outcomes but also to not produce the desired social impact. Much more causal empirical research is needed to uncover the circumstances in which higher purpose has unambiguously positive impact on economic and social outcomes.

On RQ4, finance has a potentially important role to play in the integration of higher purpose with the usual business goals like shareholder value maximization. When this can be done, governance improves and value creation is enhanced. There is already a movement afoot to have firms include social objectives as part of their fiduciary responsibilities; I argue that “mandating” a prosocial focus in this way is likely to be unadvisable, and that purpose is most effective when voluntarily and authentically adopted. Specifically, one must be cautious to avoid the potentially dark side of higher purpose. A hint about what this could be is provided by the broader literature on CSR and ESG alluded to earlier. This literature indicates that a direct focus on social outcomes by mutual funds, for example, leads to a misallocation of funds and often results in investments in companies that do not contribute positively to even the stipulated social goals. So much more research is needed to identify conditions under which the firms can make sustainable decisions at the intersection of higher purpose and shareholder value.

In this discussion. I focus especially on how the adoption of higher purpose by banks can not only contribute to a welfare-enhancing increase in access to credit, but can also help banks gain a potential competitive advantage over non-intermediated lending (e.g. P2P platforms). Banks can also help to close the R&D funding gap that can in turn lead to more investments in life-saving therapeutics. Moreover, by joining together with educational institutions, banks can help to improve financial literacy and help households make better choices. Finally, combining the insights of the organizational behavior and strategy research on higher purpose with the nascent research on the topic in finance, one sees that there is potential for higher purpose to increase employee satisfaction and loyalty, lower wages and increase shareholder value, but this result requires specific conditions to hold. Specifically, it require the firm to make decisions that are at the intersection of shareholder value maximization and higher purpose. I discuss the channels through which higher purpose affects incentives to ensure that the intersection is not the null set. Thus, effective higher purpose is not charity.

The rest of the paper is organized as follows. Section 2 discusses the relationship of higher purpose to more familiar concepts like mission and vision (RQ1). Section 3 examines higher purpose and the economics of prosocial behavior (RQ2). Section 4 takes up the literature on higher purpose in organization behavior and management strategy (RQ3). Section 5 is devoted to the relevance of higher purpose in Finance. Section 6 concludes.

2. HIGHER PURPOSE, MISSION VISION, STRATEGY AND THE FIRM'S OBJECTIVE FUNCTION

In this section, I provide definitions of various related ideas and discuss the literature briefly. I begin with higher purpose.

Higher Purpose has been extensively studied in the organization behavior and management literatures. Bartlett and Ghoshal (1994) posit that higher purpose is an essential precursor of effective strategic management, and empirical evidence on the economic effects of higher purpose appears in numerous papers (e.g. Gartenberg and Serafeim 2019, and Grant et al. 2007).

There is not a consensus definition of higher purpose in the literature, but there are some common elements. Bartlett and Ghoshal (1994) define it as “the statement of a company’s moral response to its broadly defined responsibilities, not an amoral plan for exploiting commercial opportunity”. Gartenberg, Prat, and Serafeim (2019) state that purpose need not be explicitly prosocial but should be viewed more broadly as the company’s “reason for being”. Henderson and Van den Steen (2015) define purpose as “a concrete goal or objective for the firm that reaches beyond profit maximization”. Quinn and Thakor (2018, 2019) define it as a prosocial contribution goal that transcends the typical business goals like profit maximization but is intrinsically a part of the business of the organization. While the differences in these definitions are obvious, what they have in common is that higher purpose represents a contribution goal of the company that goes beyond business goals like shareholder value maximization. An interesting point emphasized in this literature is that the *authenticity* of purpose is important. For example, Gartenberg, Prat and Serafeim (2019) state that a company’s primary purpose is not necessarily that which is stated in written documents or plaques on the wall. They state: *"It is precisely this implicit aspect of purpose – that purpose is only effective insofar as it is actually adopted by employees within the firm – that creates the challenge for academics to study it meaningfully, across firms and over time"*

The idea is that employees will not be influenced by an organizational higher purpose unless they view it as authentic. Higher purpose statements that are viewed as "virtue signaling" or public relations initiatives may be worse than ineffective – they may breed cynicism and be counterproductive as they risk being viewed by employees as inauthentic and even manipulative (see also Quinn and Thakor (2019)). While an organization may be able to "dress up" something as higher purpose for external consumption even though it is not, it is much more difficult for it to mislead its own employees into believing it because they are "on the ground" and can see whether the stated purpose acts as an arbiter of all decisions.

Mission: A concept sometimes confused with higher purpose is mission. But a firm's mission is *not* its higher purpose. A mission is a "level objective" – the level of effectiveness in the operation of its business that a firm seeks to achieve. For example, a university might state its mission as producing world-class research and achieving excellence in teaching. DTE Energy defines its mission as follows: "To be the best-operated energy company in North America."[4] In contrast, a higher purpose is the *raison d'etre* of a firm's existence, its highest contribution intent. DTE Energy's higher purpose

[4] See Quinn and Thakor (2018, 2019) for a discussion of DTE Enter and its higher purpose.

has four pillars, one of which is to contribute to the growth and well-being of the communities in which it operates.

Vision: A vision statement provides an inspiring image of the future. It is related to the products/services the firm produces, but it's *not* literally meant to be an achievable short-term goal. Rather it is meant to be a picture of an inspiring future possibility. For example, Nike's vision statement says: "To bring inspiration and innovation to every athlete in the world." This points (for Nike's shareholders) an inspiring future possibility, one in which every person on the planet is an athlete and a Nike customer.

Strategy: This is meant to provide a decision-making framework for the firm. Given an objective function like "maximize shareholder value", strategy tells managers *how* to achieve that objective, i.e., what activities and investments to pursue and what to avoid. It is a roadmap for the allocation of resources. For example, when Michael Eisner took over as Disney CEO in 1984, he articulated the new strategy as focusing sharply on the film business in the firm's portfolio and significantly increasing investments in film. *Figure 1* provides a pictorial summary of these various concepts.

Figure 1:

<u>Higher Purpose</u>	**<u>Vision</u>**	**<u>Mission</u>**	**<u>Strategy</u>**
Statement of Contribution	Image of the Future	A Level Objective	A roadmap for allocating resources to achieve business goals like shareholder value maximization.
"We nurture growth in all we do" - Marzetti	"A computer on every desk in every home" – Microsoft	"To be the best operated energy company in North America." – DTE Energy	"Locate cafes close to places of work and provide an affordable luxury – A European coffee *experience*" - Starbucks
Answers: "<u>Why</u> do we exist; what justifies our collective existence?"	Answers: <u>Where</u> are we going?	Answers: <u>What</u> objective are we going to accomplish to get where we are going?	Answers: <u>How</u> are we going to get where we are going?
• Inclusive (Everyone) • Inspiring (Intrinsic) • Authentic (Arbiter) • Constant (North Star) • Covenant (Community) • Differentiate (Positive Deviance)	• Audacious • Grounded • May not be achievable	• Tangible • Achievable	

In addition to these, two other concepts are relevant.

Firm's Objective Function: The firm's objective function defines its short-term and long-term business goals and provides clarity for its decision-makers. Since an authentic higher purpose is meant to be arbiter of all business decisions, the firm is tasked with making decisions that serve the dual purpose of maximizing the objective function and also being consistent with its higher purpose. Herein lies the rub. What if the two are in conflict? I will discuss later that if this occurs, the situation is untenable. The pursuit of higher purpose while sacrificing long-term shareholder value is unsustainable. Maximizing shareholder value with decisions that are inconsistent with the stated higher purpose means that the higher purpose is not authentic. The challenge for the firm is to come up with a higher purpose that is related to the firm's business activities and *jointly* develop a strategy and a higher purpose statement such that the set of decisions that lie at the intersection of higher purpose and shareholder value maximization is not empty[5].

CSR: Perhaps the key difference between CSR and higher purpose is that the former need not be intimately tied to the firm's day-to-day decision-making, whereas higher purpose is meant to act as an arbiter of all business decisions. So a manufacturing company that makes industrial chemicals can practice CSR by contributing money to fund scholarships for minority students in the city in which it operates and also contributing money to clean up the inner city and provide housing for the homeless. This is prosocial but unrelated to its core business. In contrast, a higher purpose is inextricably linked to the firm's business, but needs not to be prosocial, although most effective higher purpose statements serve the greater good by being either explicitly prosocial, customer-centric or employee-centric.[6]

3. HIGHER PURPOSE AND THE ECONOMICS OF PROSOCIAL BEHAVIOR

In this section I discuss higher purpose in the context of the economics of prosocial behavior. This is a fairly well-developed literature in economics and it has valuable insights for understanding the potential for higher purpose to influence economic outcomes.

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[5] Indeed, I argue later that it is probably not a good idea to mandate that the firm's objective function be formally (legally) modified to also attend to objectives besides shareholder value.

[6] See, for example, Quinn and Thakor (2019).

The economics literature on prosocial behavior has focused mainly on "socially responsible" investments by firms, the provision of public goods and CSR. At a very high level, the papers in this strand of the literature ask whether prosocial behavior by firms has positive effects on economic outcomes like external financing costs and, employee motivation and firm profits, or whether it distorts economic outcomes, possibly even reducing social welfare.[7] Unfortunately, there does not seem to be a consistent theoretical framework for analyzing the issues, so the results tend to be "all over the place."[8]

Morgan and Tumlinson (2019) assume that shareholders care about the provision of a public good and develop a model to show that managers redirect more profits toward public goods than shareholders would acting separately. That is, investing in prosocial activities imposes a direct financial cost on the firm. Cheng, Ioannou and Serafeim (2011) conduct an empirical analysis to examine whether superior performance on corporate social responsibility (CSR) affects the firm's access to external finance. They document that superior CSR performance improves the firm's access to external finance because CSR strategies reduce agency costs and informational asymmetries.

Another strand of this literature deals with other aspects of CSR, e.g., Bénabou and Tirole (2010). A theoretical examination appears in Bénabou and Tirole (2006) who develop a model in which doubt about the true motive for good deeds leads to an

[7] It may seem strange that behavior intended to be prosocial could reduce social welfare, but such is the (second-best) world of unintended second-order effects.
[8] See also Malik (2014).

"overjustification effect", with diminished prosocial behavior; see also Seabright (2009).[9] The empirical evidence on how the adoption of CSR affects organizational performance is mixed. Some papers report a positive effect on firm profits (e.g., Waddock and Graves (1997)), while others report mixed, negative or no effects (e.g., Barnett and Salomon (2012), Godfrey, et al, (2009), and Servaes and Tamayo (2013)). Most of these studies focus on how CSR is a tool for firms to engage in "virtue signaling" to customers who value CSR.

Other papers focus on how CSR works through the labor supply channel in firms, in terms of affecting the motivation of employees. The empirical evidence of CSR on firm performance through this employee behavior channel is also mixed. On the positive side, Hedblom, Hickman and List (2019) also use a field experiment and document that CSR has both a selection effect in employee hiring and a treatment effect in positively influencing their effort and output. Similarly, Eccles, Ioannou and Serafeim (2014) conduct an empirical examination of 180 companies and show that companies that adopt environmental and social policies related to CSR have more stakeholder engagement and adopt more long-term oriented policies than firms that do not; these CSR-adopting firms also exhibit better accounting and stock performance over the long run. Dijk and Holmen (2017) show in a lab experiment with a principal-agent setting that CSR generates a "warm glow" in employees that makes them work harder.

[9] More tangentially related is Bénabou and Tirole (2003) in which a tension between extrinsic and intrinsic motivations arises because giving high-powered incentives may convey bad news about the task or agent ability. Bolton, Brunnermeier and Veldkamp (2013) examine the impact of the organizational leader in overcoming a misalignment of incentives that inhibits coordination.

However, there is other empirical evidence highlighting the dark side of CSR. List and Momeni (2017) use a large-scale field experiment to document that the adoption of CSR increases employee *misbehavior*—there is a greater propensity for employees to shirk on their primary job responsibility. The paper suggests that this is due to "moral licensing" in the sense that the "doing good" feeling associated with CSR induces workers to misbehave on another dimension. There is also other research which suggests that CSR initiatives may not produce the intended outcomes either financially or from a social impact perspective (e.g. Bhagat (2022)); I will discuss this evidence a bit later. Thus, it is not clear that supposedly prosocial initiatives are even producing the purported social outcomes. Thus, they may be sacrificing shareholder value without generating the social benefits to arguably offset this loss. This suggests a need for more research that can help us to sort through these conflicting findings and reach more definite conclusions. Note also that such CSR initiatives are often *not* directly linked to the firm's core business and should therefore be distinguished from higher purpose.[10]

Some papers have modeled how some types of prosocial behavior can help match employees and firms in a socially productive way. Besley and Ghatak's (2005) work on "mission-oriented" organizations. That paper focuses on how matching mission-oriented employees to principals who have the same mission economizes on the need for high-

[10] For example, in the Dijk and Holmen (2017) lab experiment, agents were told that the company would contribute its profits to the Swedish Red Cross. This is CSR, but it has little to do with the firm's business itself, so it is *not* higher purpose as I define it. One possible reason for the mixed results in the empirical literature on the impact of CSR on firm performance may have to do with the fact the literature does not distinguish between broad CSR initiatives unrelated to the firm's core business and the special subset of activities representing higher purpose, so in cases involving authentic higher purpose the performance impact may have been positive and in other cases it may have been insignificant or negative.

powered incentives, and it explains why non-profits may function differently from profit-seeking organizations.

A small but distinct strand of this literature has focused directly on higher purpose and its economic consequences, distinguishing the analysis from the CSR literature. Henderson and Van den Steen (2015) present a theoretical model of organizational higher purpose that explains why purpose has to be prosocial and authentic to be effective and why employees care deeply about it. The main insight of the paper is that organizational purpose creates value beyond its social contribution because it develops its employees' (social) identity and reputation. Thakor and Quinn (2021) build on that insight in their paper to provide a microfoundation for why employees may prefer that the firm invest in its articulated higher purpose rather than having the firm pay that investment out as cash to the employees. This analysis also finds that organizational higher purpose induces employees to work harder for the same wage and lowers the firm's equilibrium wage, but it differs in many respects. Specifically, it focuses on the channels through which higher purpose investments are crowded out, and thereby explain the large cross-sectional heterogeneity in higher purpose investments. Moreover, it shows that higher purpose investments may decline when social pressure to make them increases.

The Thakor and Quinn (2021) paper emphasizes two important points. First, to have a positive impact on employee effort incentives, the pursuit of higher purpose by the firm should be *authentic*, i.e. employees should believe that the firm truly attaches value to it and is not just doing it for the virtue signaling or to elicit higher effort from employees as a rent extraction device.[11] Second, higher purpose must be integrated with the firm's routine business decisions in order to be effective, which distinguishes it from the broader class of prosocial activities like CSR.

4. THE HIGHER PURPOSE LITERATURE IN ORGANIZATION AND BEHAVIOR AND MANAGEMENT STRATEGY

This literature is largely descriptive, but also contains important empirical evidence gathered from large-sample studies as well as field experiments that seek to provide causal evidence.

The microfoundation for higher purpose to matter that this literature relies on comes from self-determination theory in psychology (e.g., Deci and Ryan (1985, 2000), and Ryan and Deci (2000)) which emphasizes the idea that people value personal and professional growth, and this growth is higher with intrinsic motivation to do the job. This motivation, in turn, is stronger when employees share a collective higher purpose that has been articulated by the firm (e.g, Sekerka and Fredrickson (2008)).

Using these insights, various papers in this literature have focused on providing evidence on what higher purpose does in organizations. See, for example, Bartlett and Ghoshal (1994), Chapman et al (2017), Gartenberg, Prat and Serafeim (2019), Gartenberg and Serafeim (2019), Grant et al (2007), Hedblom, Heckman and List (2019),

[11] See also Quinn and Thakor (2018, 2019). In fact, Thakor and Quinn (2021) show that when social pressure crowds in virtue-signaling higher purpose investments, it crowds out the authentic higher purpose investments and may reduce welfare.

Hollensbe et al (2014), and Quinn and Thakor (2018). Some of these papers are randomized controlled trials, some are empirical, some provide interview-based and survey-based evidence and some are qualitative in nature. They have provided a host of stylized facts for future theories to explain. The overall message from this body of work is that authentic higher purpose does, in most cases, seem to positively affect employee effort incentives and job satisfaction.

There is also recent empirical evidence on the *effect* of higher purpose pursuit on economic outcomes. The broad thrust of the findings in this literature is that the adoption of authentic higher purpose impacts economic outcomes positively. Gartenberg, Prat and Serafeim (2019)) used a sample of nearly 500,000 people across 429 firms involving 917 firm-year observations from 2006 to 2011 and found that an authentic higher purpose communicated with clarity positively impacts both operating financial performance and stock price.[12] Quinn and Thakor (2018) provide interview-based evidence that organizations in which leaders embrace an authentic higher purpose, employees provide exceptionally high effort and creativity.[13] Hedblom, Hickman and List (2019) provide evidence based on a field experiment that "…when a firm convinces its workers that their

[12] Specifically, they found that the high performers had both clarity of higher purpose and comradery among employees. In other words, the mere adoption of higher purpose does not positively affect output; authenticity of purpose and clarity of communication are also needed.

[13] The definition of authenticity is that the leader is not using higher purpose merely as a public relations tool, but truthfully attaches positive utility to it. Therefore, the leader is willing to make decisions that may sacrifice economic output and personal wealth to pursue the higher purpose. When this happens, it generates positive emotions in employees. Fredrickson (2003) reviews the empirical literature on how positive emotions impact collective behavior. Lack of authenticity can actually backfire, especially when employees view the firm's intention as only to increase profits by using higher purpose solely as a motivational tool. See, for example, Cassar and Meier (2018).

efforts make the world a better place (as opposed to purely making money)…", output increases and wage costs go down. Grant et al (2007) conducted a field experiment in which treatment-group call center employees tasked with fund raising for a university were connected to the higher purpose of that activity,[14] and they performed significantly better in fund raising than employees in a control group who had the same "fund-raising script" for calls but were not similarly connected to the higher purpose.

This evidence notwithstanding, I do not believe we have closed the empirical book on this issue. The evidence on CSR (including ESG) suggests that in some instances these initiatives negatively impact economic outcomes—the theory on CSR also leaves open room for such findings (e.g. Green and Roth (2021)). Indeed, the earlier-discussed empirical evidence on CSR highlights some of the channels through which this could occur, e.g. List and Momeni's (2017) evidence on the moral licensing effect. So it is possible that there are circumstances in which higher purpose could backfire as well, not only in terms of negatively impacting economic outcomes, but also decreasing employee morale, job satisfaction and other "soft" outcomes often studied in connection with higher purpose. The theory suggests that this is likely when the articulated higher purpose is viewed as being inauthentic (especially by employees).

The bottom-line takeaway from this literature is that an *authenti*c higher purpose that is integrated with the routine business of the firm and that employees believe in has a

[14] Specifically, they were given some time to interact with scholarship recipients, i.e., those who benefit from the fund-raising.

causally positive effect on a host of economic outcomes. The channel for this positive effect is that it enhances employees' assessment of their own self-worth and makes them proud to work for the organization, i.e., it positively affects intrinsic motivation to work. In the context of the standard principal-agent model, this as a reduction in the agent's marginal cost of effect or an increase in the perceived marginal benefit of effort. However, much empirical work remains to be done to establish a robust causal link between higher purpose and improved economic outcomes.

5. HIGHER PURPOSE IN FINANCE

In his 2018 letter to shareholders, Larry Fink (see Fink (2018)) of BlackRock stated,

"Without a sense of purpose, no company, either public or private, can achieve its full potential… And ultimately, that company will provide subpar returns to the investors who depend on it to finance their retirement home purchases, or higher education."

This has attracted considerable attention as the world's largest investor has endorsed higher purpose. Many have proposed that firms take on as their objective function Enlightened Shareholder Value (ESV) which includes stakeholders besides shareholders. ESV is being increasingly embraced in many quarters— it was adopted by the U.K. Companies Act, is being considered for inclusion in the Restatement of Corporate Governance Law, and seems to have the support of corporate leaders as well as institutional investors (e.g. Bebchuk, Kastiel and Tallarita (2022)). Legal scholars have begun opining on how Rule 14a-8, the SEC shareholder proposal rule, can be used by shareholders to put up for a proxy vote proposals to expand the fiduciary responsibility of the directors and officers to include a broader class of stakeholders than shareholders (e.g. Fisch (2022)). It seems there is also a concomitant rise in executive bonus schemes being made dependent on environmental and social objectives, especially among firms that signed on to the Business Roundtable statement on corporate purpose. While executive compensation is still predominantly based on shareholder value (e.g. Rajan, Ramella and Zingales (2022)), a significant shift seems to be underway to dilute the focus on shareholder value in favor of including ESG and other social objectives in the firm's objective function; see e.g. Plerhoples (2022). This raises an important question of how these initiatives will affect corporate governance.

The earlier-mentioned paper by Eccles, Iannou and Serafeim (2014) suggests that firms engaging in prosocial behavior can lead to better long-run accounting and stock price performance, consistent with the Fink assertion. Others have expressed similar views; see, for example, Edmans (2021) and Mayer (2021), suggesting that overall governance will improve while also contributing to the greater good. Because of such research findings and high-profile statements like Larry Fink's, the pressure to focus on social objectives has also been felt by fund managers. Those who manage asset portfolios are being influenced to make portfolio allocation decisions that incorporate social value. Moreover, many *investors* are also interested in funds that invest in companies that pursue prosocial agendas[15]. As of December 2021, there was $2.7 trillion under

[15] It is unclear from the literature whether investors do this because they are willing to sacrifice (risk-adjusted) financial return from investing in such companies in order to serve a personally-favored social purpose, or they

management in "sustainable funds" with ESG investment objectives. Hartzmark and Sussman (2019) provide causal evidence that on a marketwide basis, investors value sustainable funds. During the time period they examined, "low-sustainable funds" experienced outflows of $12 billion, while high-sustainable funds experienced *inflows* of $24 billion[16]. However, their evidence indicates that deviating from the usual portfolio selection rules to implement social agendas may not only sacrifice returns but may also be counterproductive from an overall social welfare perspective. They find that the high-sustainable funds do not outperform the low-sustainable funds. In like vein, in his review of the evidence, Bhagat (2022) notes that sustainable funds with ESG objectives do poorly in terms of risk-adjusted financial returns compared to other funds, and they also invest in companies that have *worse compliance records for both labor and environmental rules.*[17] This is reminiscent of the List and Momeni (2017) moral licensing phenomenon at the *firm level,* and suggests that the social motivations of investors and the funds they invest in may be deleterious to social welfare.

A theoretical explanation for why this may be so is provided by Green and Roth (2021), who argue that socially-motivated portfolio strategies are often misguided. They develop a model in which there are "commercial" and "social" investors who compete.

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believe that investing in such companies not only serves a social purpose but is also good for the investors financially.

[16] These classifications of high and low sustainability are based on sustainability ratings published by Morningstar. In March of 2016, Morningstar published global sustainability ratings of mutual funds for the first time. More than 20,000 mutual funds were ranked on a percentile basis and given a global rating based on their holdings. The worst 10% of the funds were rated one as low sustainability ("one globe") while the best 10% were rated as high sustainability("five globes").

[17] This may also be a comment on flaws in the metrics used to measure how effective organizations are in their prosocial activities.

They show that social investors can achieve better results by pursuing strategies other than simply requiring investments that conform to their social preferences. In particular, from an enterprise perspective, focusing on increasing profitability can have greater *social impact* than focusing directly on increasing social value creation. They also provide empirical evidence that socially-guided mutual funds engage in inefficient capital allocation from the standpoint of maximizing social impact and financial returns[18].

Of course, this research is about ESG and CSR, *not* higher purpose *per se*. Nonetheless, it suggests two important points. First, mandating prosocial corporate behavior may be misguided. In addition to the reasons identified above, giving corporations a multidimensional objective function also creates the possibility of managers performing poorly either due to inadequate effort or inadequate competence and explaining away this performance as being caused by their focus on social goals on which performance may be hard to measure, a variant of multi-tasking moral hazard. That is, governance may worsen and it may be harder to hold management responsible for it. Moreover, it makes it all too easy for corporations to get embroiled in divisive political issues that may serve neither their shareholders nor the greater social good (at least not in an unambiguous way); the recent examples of social media platforms and Disney serve as warnings. Second, it highlights the kinds of empirical challenges that lie ahead of us in examining the causal impact of higher purpose on a host of outcomes. At present, there is a

[18] There are other examples of unintended consequences in this regard. Colonelli, Gormson and McQuade (2021) show that when people are made more conscious of the social responsibility of corporations, they become more averse to bailouts. Moreover, attempts to cast businesses in a positive light can backfire as such attempts end up focusing people's attention on policy decisions about which they have entrenched negative views. This may be another illustration of the importance of authenticity in corporate prosocial activities.

noticeable paucity of finance research on higher purpose, so the field is wide open for examining numerous interesting questions; I will return to these later. For now, we begin with the four areas (identified in the Introduction) in which finance research can benefit from an integration with higher purpose research.

Access to Credit:

One area in which more research attention devoted to integrating finance with higher purpose is likely to pay dividends—pardon the pun—is how adoption of it by banks and other lenders can increase access to credit and more generally welfare-enhancing economic growth. In Thakor (2021b), I discuss extensively where banks and their regulators are at present on the issue of higher purpose. I had two major conclusions there. First, the idea of higher purpose is still in its infancy in banking, and examples of authentic higher purpose that have made an impact in banking are hard to find. Second, there is considerable opportunity for banks to be creative in defining higher purpose, either in an employee-centric, customer-centric or explicitly prosocial way such that higher purpose can be pursued in a manner consistent with also maximizing long-run shareholder value. Moreover, regulators in Europe and the U.S. are beginning to take actions to move banks in this direction, but I also cautioned that in the end mandating such things via regulation is likely to be counterproductive due to the oft-encountered law of unintended consequences[19].

[19] Song and Thakor (forthcoming) make a similar point in the context of ethics. Specifically, they discuss how regulators could influence banks to adopt higher ethical standards, but that this will come at the expense of financial innovation and also result in talent migration out of depositories.

But this does not mean banks cannot proactively pursue authentic higher purpose. Thakor (2021b) mentions one such example, which provides a useful illustration of how banks can make a difference by expanding access to credit:

"*This dialogue can point to examples of how some banks are authentically pursuing higher purpose. An interesting example is the Bank of Bird-in-Hand in southwestern Pennsylvania. It is now a full-service bank whose purpose is to provide banking services to the underbanked Amish community. It seeks to foster local economic development and does so in part by supporting community projects like hay auctions (see Volz, 2019).*"

While this is just one example, I think there is substantial potential in melding authentic higher purpose with relationship banking to achieve a non-empty intersection of higher purpose and shareholder value maximization[20]. Focusing on relationship banking is also promising because it is this aspect of banking that most sharply distinguishes it from shadow banking and fintech (e.g. Thakor (2020), and where the greater potential ability of depositories to develop rust has the most value (e.g. Thakor and Merton (2021)). With relationship lending, the lender and the borrower are engaged in a repeated game that potentially generates proprietary payoff-relevant information about the borrower that the lender possesses, and this has real effects (e.g. the evidence in Banerjee, Gambacorta and Sette (2021)). Rajan (1992) and Sharpe (1990) focused on the dark side of relationship lending due to ahold-up problem that

[20] For text book discussions of these issues, see Greenbaum, Thakor and Boot (2019), and Thakor (2019).

allows relationship lenders to extract rents, whereas Boot and Thakor (2000) focused on the value enhancement due to relationship lending. Boot and Thakor (2000) show that while relationship lending volume shrinks when there is more competition among banks and from the market, banks also make their relationships deeper and thus add more value per dollar loaned. Song and Thakor (2007) showed that because longevity of the relationship is important in relationship lending, banks that make such loans prefer to finance with "sticky" core deposits than more runnable types of deposits like brokered CDs and other types of "purchased money".

The idea that the value of relationship lending is dependent on the longevity of the relationship was developed by Boot and Thakor (1994) who used an infinite horizon model to show that contract terms for borrowers improve with relationship duration. Borrowers who start out getting secured loans may be able to switch to secured loan later in the relationship. Lopez-Espinosa, Mayordomo and Moreno (2017) provide empirical evidence that the benefits of relationship borrowing kick in for borrowers only after two years.

These insights suggest two possible ways in which banks could define authentic higher purpose. One is a customer-centric higher purpose, which is to focus on the welfare of their relationship borrowers. This implies that banks would need to focus not only on the value they add to their borrowers, but also on the likelihood of continuation of the relationship.[21] The other is an explicitly prosocial higher purpose, which may be to minimize the risk exposure of the government safety net while providing privately and socially valuable liquidity services to depositors, with the value of these services decreasing in the bank's idiosyncratic risk (e.g. Merton and Thakor (2019))[22]. Both purposes can be served with banks keeping high capital ratios, those that may be well in excess of regulatory capital requirements, since this reduces the bank's risk and increases its continuation/survival probability, even in the face of a systemic crisis (e.g. Berger and Bouwman (2013)). Higher capital also makes it more likely that a bank that has made a loan commitment to a (relationship) borrower will honor the commitment and not invoke the Material Adverse Change (MAC) clause (e.g. Boot, Greenbaum and Thakor (1993)), thereby serving a customer-centric higher purpose,. Moreover, there is ample empirical evidence that when banks have more capital, they create less systemic risk (e.g. Berger, Roman, and Sedunov (2020)), lend more and create more liquidity (e.g. Peek and Rosengren (2000), Berger and Bouwman (2009), Donaldson, Piacentino and Thakor (2018)), exhibit fewer distortions in lending (e.g. Purnanandam (2011), and Thakor (2015, 2021))[23], develop stronger safety-oriented cultures (Song and Thakor (2019)), and have higher ethical standards (Song and Thakor (forthcoming)). Thus, the evidence suggests that the adoption of a higher purpose that

[21] There is no suggestion here that banks should not be profitable because they care about the welfare of their relationship borrowers. Some of the most authentic practitioners of higher purpose operate high-margin businesses and are very profitable e.g. Tata's in India.

[22] This means avoiding strategically lowering capital ratios to increase fragility, as in Thakor (2021)).

[23] These distortions refer to zombie lending and lending to borrowers who have not been adequately screened.

leads to banks maintaining higher capital ratios has the potential to create a non-empty intersection of shareholder value maximization and authentic higher purpose.

The goal, of course, is to encourage welfare-enhancing lending and liquidity creation as opposed to zombie lending, evergreening, or other forms of excessive risk-taking that may occur in economic booms due to more lax credit standards[24]. High capital ratios in banks will help in this regard, as there is both theoretical and empirical support for the notion that banks with higher capital engage in more prudent lending (e.g. Thakor (2014)). Market timing may be an issue if banks are to raise equity capital through secondary equity issues; Baker and Wurgler (2002) provide evidence that equity is typically issued during bull markets, and Dittmar and Thakor (2007) provide a theory (with supporting evidence) that this is because manager-investor disagreement is low during such times. However, banks raise most of their capital through retained earnings (e.g. Uluc and Wieladek (2018)), so the build-up of capital can be achieved by lowering dividend payout ratios[25].

Some work on the interaction of bank capital and higher purpose has begun. Bunderson and Thakor (forthcoming) provide survey evidence on higher purpose pursuit by U.S. households and its link to organizational higher purpose of the firms they work

[24] Thakor (2015, 2016) provides theories of how bank lending policies vary through the credit cycle and how these credit standard become more lax during economic booms, encouraging risky investments by banks that can raise funds with low risk premia. In Thakor (2015), this relies on investors being behaviorally biased, whereas in Thakor (2016), this occurs even with investor rationality as long as there is model uncertainty.

[25] Gambacorta, Oliviero and Shin (2020) document that banks typically have higher payout ratios than firms in other industries and that banks with lower market-to-book ratios tend to pay higher dividends. So reducing their payout ratios can only move banks in the direction of being more like other industries in this regard, and not an outlier for investors.

for. They find that employees of firms with written higher purpose statements are more likely to have their own written personal higher purpose statements, and they personally deal better with stress. Bunderson and Thakor (forthcoming) use this evidence to motivate a theoretical model in which optimal contracting within a bank that pursues a higher purpose leads to higher wages, higher monitoring effort by the bank and a lower failure probability for the bank when it has higher capital. This happens despite the fact that the bank's capital does not directly affect its higher purpose investment.

Closing the Funding Gap in Biomedical R&D:

The U.S. spends a staggering amount of money on healthcare, both in absolute terms and as a percentage of GDP. By 2028, annual healthcare spending is predicted to reach $ 6. 2 trillion (see Lo and Thakor (2021, 2022)). Healthcare therapeutics are critical to the well-being of people all over the world, especially as populations' age. Yet, there is a significant underinvestment in in medical R&D relative to the social optimum, something referred to as the "R&D funding gap" (e.g. Schumpeter (1942), Arrow (1963), Hall and Lerner (2010), and Kerr and Nanda (2015)). Closing this funding gap promises unambiguous welfare benefits, especially if it can be done without substantial government subsidies or tax breaks that may produce other types of (possibly unanticipated) distortions. Lo and Thakor (2021) point out that this funding gap is especially acute in biomedical R&D. This is a finance problem—the funding gap exists because of a variety of frictions that impede the flow of funds into biomedical R&D. The title of Andrew Lo's 2021 paper "Can Financial Economics Cure Cancer?" (Lo (2021)) provides the appropriate mindset to think about how we can begin to visualize the formulation of higher purpose in finance. From this perspective, financial markets and institutions can play a big role in helping to close this funding gap. Lo and Thakor (2022) explain how this can be facilitated by financial intermediaries like banks, and provide a framework for analyzing the possibilities. I will focus on how banks can formulate an authentic higher purpose based on closing the biomedical R&D funding gap.

Lo and Thakor (2022) highlight three frictions that contribute to the funding gap, and emphasize that while these frictions exist in other contexts as well, they are hugely magnified for biomedical research firms:

(i) High agency costs of debt due to the very technical nature of biomedical research that makes it relatively easy for those firms to engage in risk shifting to the lender's detriment.

(ii) High cost of reducing information asymmetries through information disclosure due to the two-audience signaling problem wherein any information disclosed to investors is also inadvertently disclosed to one's competitors.

(iii) Possible lack of continuation financing because the research firm cannot credibly communicate to investors the proprietary research information acquired post-initial-financing.

These three frictions provide useful guideposts or how banks can think about their organizational higher purpose statements. In line with our earlier discussion, this too is related to relationship banking. As for (i), in their role as relationship lenders, banks can do much to reduce the agency costs of debt financing through direct monitoring (e.g. Holmstrom and Tirole (1997)) and the design of multiperiod credit contracts (e.g. Boot and Thakor (1994)). The monitoring incentive is stronger when the bank has more capital, so a bank that has a higher purpose that revolves around financing biomedical R&D to help cure diseases can lend credibility to this statement and integrate it into its routine business by keeping a higher capital ratio than is the norm and hiring experts for post-lending monitoring of loans for biomedical research. A higher purpose statement could be: "We are financially strong and capable of taking risk … to fund biomedical R&D to improve the human condition."

As for (ii), a higher purpose statement could be built around something like: "a lender you can trust—contributing to the greater good by keeping your biomedical R&D confidential and funding it". The important contribution of Bhattacharya and Chiesa (1995) highlights the advantage that banks have over financial markets in protecting the confidentiality of borrower information and keeping it secret from the borrower's competitors. Tangible resources could be devoted to this as the bank develops expertise in processing such information acquired over time in its role as a relationship lender, using it to increase its supply of credit to the borrower, and also keeping it confidential to increase borrower demand for credit from the bank.

Finally, on (iii), a bank that protects the confidentiality of its borrower's proprietary R&D information and keeps sufficiently high capital to effectively monitor the borrower can also assure borrowers that its financial strength will enable it to be around to engage in long-term relationships without worry of interim failure. A higher purpose statement along these lines could be something like: “We maintain our financial strength to be here for the long haul to finance the biomedical research of our customers and contribute to finding cures for all major diseases”.

Since banks provide debt financing, the frictions associated with borrower bankruptcy can be impediments to increasing funding for biomedical R&D. In this regard, innovations in the institution of bankruptcy, such as “no-fault default” (e.g Merton and Thakor (forthcoming)) can help, and banks can play a role in pushing such innovations. The Merton and Thakor (forthcoming) proposal for reforming Chapter 11 bankruptcy allows for less costly transfer of ownership and control from shareholders to bondholders than current practice, thereby significantly reducing bankruptcy costs. Similarly, banks can also be actively involved in pioneering innovations in financial contracts beyond the standard debt and equity to reduce financing frictions for biomedical R&D. Jørring et al (forthcoming) analyze one such innovation, the “FDA hedge”, which can increase both the supply of financing from investors and the demand for such financing from biomedical research firms.

Such higher purpose initiatives can help banks build greater trust with their stakeholders as well as with society at large. In their role as “trusted lenders”, banks can gain a competitive advantage over non-bank providers of credit, like P2P platforms, since the bank’s financiers and customers value trust; see Thakor and Merton (2021) and the references therein. This trust enhances the banks' likelihood of securing uninsured financing at favorable terms and therefore being able to provide continuation financing to its relationship borrowers.

Improving Financial Literacy:

Financial literacy is essential for households to make informed life decisions. The Organization for Economic Cooperation and Development (OECD) defines financial literacy as including not only the relevant financial knowledge, but also the skills and willingness to apply this knowledge (see, for example, Lusardi (2019)). Yet, financial literacy is low even in advanced economies. Lusardi and Mitchell (2011) reckon that only a third of the world's population is familiar with even the most basic concepts that underlie everyday financial decisions, like interest rates, inflation and risk diversification; see also Lusardi, Mitchell and Curto (2009). And financial literacy, as defined by the OECD, is much lower than that number. The costs of poor financial literacy are enormous, as the 2007-09 financial crisis illustrated.

I have long been an advocate of the viewpoint that banks can play a major role in improving financial literacy by joining forces with universities. Business schools deal with banks and other financial institutions on a routine basis and have multifaceted relationships. These should be expanded to launch large educational programs to improve financial literacy. While this will impose costs on banks in the short run, it can be integrated into their higher purpose statements. An example would be: "we help educate the world to make better financial decisions and finance these to help people achieve their dreams". In the long run, this also has the potential to produce tangible economic benefits for banks as households make better financial decisions and defaults decline. Moreover, such educational initiatives may also help to grow the client base, so this would be an initiative at the intersection of purpose and profit.

Enhancing Employee Motivation Within the Firm and Increasing Shareholder Value:

Motivated by the research in organization behavior and strategy that authentic higher purpose can positively affect employee incentives, Thakor and Quinn (2021) develop a formal model of higher purpose and how it affects contracting and employee incentives. Their main findings are that higher purpose qualitatively affects incentive contracts and elicits higher effort from employees. However, it also has the direct first-order effect of reducing the firm's revenue since the allocation of revenue to higher purpose serves as a credible indication of the firm's commitments to that purpose. In their model, employees' beliefs about the authenticity of the owner's (principal's) commitment to higher purpose matters because employees derive utility from the firm's pursuit of purpose but only when their work is meaningfully connected to the firm's higher purpose. The resources the firm commits to making this connection for its employees depends on the strength of the CEO//owner's belief in the purpose. A CEO/owner who does not authentically believe in the higher purpose invest little in this activity. The paper defines the owner's authenticity of purpose in terms of the owner deriving positive utility from the pursuit of that purpose, and the higher this utility, the stronger the owner's belief in the purpose. The analysis thus implies that higher purpose is more effective in organizations in which the leader believes more strongly in the purpose.

While employees may be able to infer whether the owner authentically believes in the higher purpose, the analysis also allows for the utility the owner derives from the purpose to be shrouded from the employees and others. In this case, they establish that social pressure on firms to adopt a specific higher purpose—either due to general societal pressure or activism by investor groups that results in it being part of the firm's charter and the board's fiduciary responsibility— can have a counterproductive effect in that it may *crowd in* higher purpose investments by firms whose owners do not authentically believe in that purpose and *crowd out* higher purpose investments by firms whose owners authentically believe in that purpose. Welfare may decline as a result. Thus, as we saw with the earlier research on ESG, "mandating" higher purpose may not only diminish shareholder value but also worsen the firm's performance on the very dimensions the purpose seeks to focus on. On the other hand, we have numerous examples of firm that elevated both shareholder value and the prosocial outcomes their purpose focused on when they adopted an authentic higher purpose voluntarily.

Setting up a model:

Although there are many ways to model higher purpose in a contracting setting, I provide a simple model to below highlight the key points. The model below borrows heavily from Thakor and Quinn (2021).

Suppose we have a firm with *N* employees and each produces a random output *z*, which is $Z > 0$ with probability e and 0 with probability $\text{I} - e$ where *e* is effort, chosen from $[0,1]$. For simplicity, suppose all outputs are conditionally perfectly correlated, i.e., conditional on each employee choosing a particular $e > 0$, each *z* is either *Z* or 0. Each employee gets an output-contingent wage of $w > 0$ if the employee's output is positive and 0 otherwise. The firm visibly allocates a fraction $f \in [0, 1]$ of its overall output or revenue to a higher purpose. So firm's output is *NZ* in the success state and in the failure state it is 0.

Let the owner derive utility $\beta U(fNZ)$ from pursuing the firm's higher purpose, where $\beta > 0$ represents the "strength" of the owner's higher purpose commitment and it may vary in the cross-section. Let $V(fZN)$ be the utility an employee derives from the firm's higher purpose. As usual, $U' > 0, U'' < 0, V' > 0, V'' < 0$ and $U'(0) = \infty, V'(0) = \infty$. Let the employee's reservation utility be $\bar{v}$. Let the employee's cost of supply *e* units of effort be $ke^2/2$ where $k > 0$. For simplicity, we can assume everybody is risk neutral. The owner seeks to maximize his expected utility over net profit and higher purpose. For now, assume no external financing is needed.

There are two simple questions this model can answer right away:

(i) What do optimal wage contracts look like and how will they be affected by the strength of the owner's preference for purpose?

(ii) How much will the owner invest in higher purpose?

The formal maximization program of the owner looks like this:

$$\underset{f,w}{\mathrm{Max}}\ e\left\{N\left[1-f\right]Z+\beta U\left(fNZ\right)-Nw\right\} \tag{1}$$

subject to

$$e\{w+V(fNZ)\}-\left[\frac{ke^2}{2}\right]\geq \bar{\mathrm{v}} \tag{2}$$

(Individual Rationality Constraint)

$$e\in \underset{e\in[0,1]}{\arg\max}\left\{ew+V(fNZ)\right\}-\left[\frac{ke^2}{2}\right] \tag{3}$$

(Incentive Compatibility Constraint)

An analysis of this shows that, because the employee's effort now contributes positively to both her wage and the expected utility she derives from higher purpose, she works harder for any *w*. The owner will, of course, take this into account in setting *w* and will find it optimal to elicit higher effort; this claim relies on an Envelope Therom argument.

The owner faces a tradeoff in determing *f*. On the one hand, it reduces revenue and hence the owner's utility. On the other hand, it increases employee effort and hence the probability of success. This leads to an interior optimum in the owner's choice of *f*, with a higher *f* chosen by an owner with a higher β. This tradeoff captures in a simple way the first-order tension between the pursuit of higher purpose and the maximization of shareholder value.

This simple model can be embellished to examine a host of other questions. For example, one can introduce external financing with some friction like the possibility of the owner investing in a private-benefit project at the expense of investors. Moreover, one can introduce capital structure and examine how the preferences of outside shareholders and bondholders vary with respect to the firm's investment (*f*) in higher purpose and (given some benefit of debt, like taxes) how that in turn may affect the owner's capital structure. These issues represent a rich agenda for future research.

Even issues related to whether higher purpose is authentic or mere virtue signaling – and the shareholder value implications of that – can be examined in this model. For this analysis, one would want the employee's utlity from purpose to be $\alpha(\beta)V(fNZ)$, where $\alpha(\beta) > 0$ for all positive β and $\alpha(0) = 0$ to capture the idea that the employee derives utility from purpose only if the owner authentically believes in that purpose. Interesting results may be derived about the implications of virtue signaling and other inauthentic pursuits even if employees can only infer but not see the owner's β. One way to do this would be to introduce unobservable but privately costly effort by the owner to " connect" the firm's higher purpose to the employee's job, with owners who attach more value to the chosen higher purpose exerting more effort. This would correspond to one of the important actions identified by Quinn and Thakor (2018, 2019) as influencers of the effectiveness of implementing higher purpose in organizations.

6. CONCLUSION

This paper has reviewed the literature on organizational higher purpose developed in multiple disciplines and placed it within the broader context of prosocial behavior. Higher purpose is distinct from CSR and it requires special conditions to be satisfied in order to have a positive effect on economic outcomes. This literature informs us about the nature and magnitude of the positive effects of prosocial goals on firm performance. But it also highlights some of the negative effects of either mandating or putting pressure on firms to adopt prosocial goals like CSR and ESG, and these findings serve both as a warning as well as a precursor of future research on higher purpose and its intersection with shareholder value. Much of this literature has developed in management, strategy, organization behavior and economics. Finance research has paid scant attention to this issue, despite its growing prominence on Wall Street. The time is ripe for devoting greater research attention to it. The main insights emerging from this review are summarized in *Table 2.*

TABLE 2 SUMMARY OF KEY RESULTS	
RQ1: What is a higher purpose?	Higher purpose is a contribution goal that revolves around the contribution the organization intends to make to improve the well-being of its employees or customers or society at large. It is not CSR, ESG or even the firm's mission. It is intimately connected to the firm's routine decision-making and acts as an arbiter of all its business decisions.
RQ2: What is the literature on the economics of prosocial behavior by organizations and what is its message for higher purpose?	The broad literature on prosocial behavior (including ESG and CSR) paints a mixed picture. Some papers find that CSR and ESG can improve economic and social outcomes, whereas some papers find they worsen both. The literature specific to higher purpose says that authentic higher purpose affects incentive contracting and improves employee effort provision, but it need not be prosocial.
RQ3: What does the organization behavior and management literature say about how higher purpose affects employee job satisfaction and productivity?	The theories say that authentic higher purpose positively affects employee job satisfaction and productivity. Considerable empirical evidence supports this view. However, there is some evidence that does not, so more research is needed to establish a robust causal relationship between higher purpose and economic outcomes.
RQ4: What is the link between higher purpose and Finance?	• The empirical evidence on broad prosocial initiatives like CSR and ESG is mixed while some papers find a positive effect on accounting and stock price performance and there is evidence that investors value things like ESG, there is also evidence that mutual funds with ESG objectives do worse than other funds and portfolio companies have worse records on those social objectives. • There is considerable potential for banks to adopt an authentic higher purpose that deepens relationships with borrower and expands credit supply, but the adoption of higher purpose in banking is in its infancy. Banks can create a link between their higher purpose and their capital ratios, with higher-capital banks possessing the ability to more soundly and authentically serve their purpose. • Banks can also define their higher purpose in terms of helping to close the funding gap in biomedical R&D. • Another way that banks can define their higher purpose is in terms of improving the financial literacy of households. • Firms can also integrate higher purpose with incentive contracting to improve employee motivation and elicit higher effort without increasing wage costs. There are unanswered questions about the implications of this for financial policy.

Some of the important open questions that remain to be answered are as follows:

- Under what general conditions can the pursuit of higher purpose be consonant with maximizing shareholder value?
- What is the potential dark side of higher purpose for corporations and what are the conditions under which it can be avoided?
- How does organizational higher purpose affect capital structure?[26]
- How does organizational higher purpose affect dividend policy? [27]
- What affects the credibility or perceived authenticity of higher purpose in the eyes of the employees and how does this affect agency frictions within the firm?

[26] The human-capital-based capital structure theory of Jaggia and Thakor (1994) suggests a way in which capital structure and incentives for firm-specific human capital development are linked. The pursuit of organizational higher purpose is a kin d of firm-specific investment in human capital by employees.

[27] For instance, in the context of banks, dividend policy affects capital accumulation within the bank and thus is potentially linked to its higher purpose.

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