

Financialization at work: Shareholder primacy and stagnant wages in the United States

Competition & Change

2021, Vol. 25(3–4) 382–400

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DOI: 10.1177/1024529420934641

journals.sagepub.com/home/cch**Lenore Palladino** 

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Abstract

Financialization has been ‘at work’ in the United States for nearly half of a century, as corporate executives have increasingly prioritized shareholder payments over other productive uses of corporate resources. Over the same period, employee bargaining power has fallen and wages for non-executive workers have stagnated across sectors. This article examines the effects of shareholder primacy on labour compensation in the United States in the neoliberal era at the aggregate, sectoral and firm level. Specifically, the article analyses changes in the relationships between rising profits, shareholder payments, and wages over the past four decades, finding evidence that shareholders’ gains come at the expense of employees in publicly traded corporations. The growing power of shareholders has been neglected compared to traditional arguments for wage stagnation, including globalization, de-unionization, rising market power and changes in industry composition. To disincentivize corporate behavior that prioritizes shareholders, a policy agenda is proposed that ends the practice of stock buybacks and institutes a stakeholder approach to corporate governance.

Keywords

Corporate governance, financialization, inequality, low-wage employment, shareholder primacy, stock buybacks

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Introduction

How has financialization been ‘at work’ in the United States in the neoliberal era?¹ Has the rising dominance of finance and power of shareholders directly affected labour compensation for typical US workers? This article argues that shareholder primacy – the financialization of the corporation – is a crucial and under-studied cause of rising income inequality in the United States, as rising claims from shareholders hurt labour’s claims to revenue from corporate value creation (Lazonick and O’Sullivan 2000; Lin, 2016; Thompson, 2003). This article makes an original contribution to the research on wage stagnation and shareholder primacy by demonstrating that rising shareholder payments are negatively associated with wage stagnation, net of other factors, for publicly traded companies in the United States. The findings build on Lazonick and O’Sullivan’s ‘downsize-and-distribute’ model by directly examining the relationship between ‘downsize’ – stagnant labour compensation – and ‘distribute’ – increased shareholder payments – in US publicly traded corporations (Lazonick and O’Sullivan, 2000).

Since the 1970s, real wages for non-executive employees have not grown in proportion to productivity, and labour’s share of income has fallen (Barradas, 2019; Baumol et al., 2003; Karabarbounis and Neiman, 2012; Mishel, 2015; Piketty, 2014).² Over the same period, the ‘shareholder primacy’ approach to corporate governance has come to dominate corporate decision-making as one facet of the rising financialization of the economy, in which financial outcomes have grown in importance in all facets of economic life in the United States (Epstein, 2015; Lazonick, 2014). This article builds on the literature that focuses on the relationship between rising shareholder claims and power of the financial sector and the reduction of labour’s power (Aglietta, 2015; Crotty, 2003; Fligstein and Shin, 2003, 2007; Lazonick and O’Sullivan, 2000; Lin, 2016; Lin and Tomaskovic-Devey, 2013; Stockhammer, 2004). Evidence is provided at the aggregate, sectoral and firm level that rising shareholder primacy is associated with wage stagnation. An empirically rigorous connection between rising shareholder payments and stagnant wages, net of other drivers of wage stagnation, can be found at the firm level, since shareholder primacy is primarily practiced in America’s large publicly traded corporations. It is worth noting that shareholder payments could, of course, increase even without a reduction in labour compensation, if funded through rising productivity or market share. It is the stylized fact of broad wage stagnation for typical workers in the United States that motivates examining the specific relationship between rising shareholder payments and stagnant wages.

Shareholder primacy is a legal and economic framework for corporate governance that claims that the sole purpose of corporate activity is to maximize wealth for shareholders; thus, executives and boards of directors should prioritize increasing share prices over all else (Lazonick, 2014; Lazonick and O’Sullivan, 2000). This article investigates at the aggregate, sectoral and firm level whether, as shareholder primacy emerged as the guiding ideology for corporate governance, corporate executives increasingly used corporate funds for shareholder payments at the expense of labour in the United States. Multiple forces in the economy are responsible for the decline of worker bargaining power and the resultant declining ability of employees to claim a share of value creation, including declining union representation (Mishel, 2015), increased globalization (Stiglitz, 2002), increased market concentration and buyer power (Wilmers, 2018), the fissuring of the workforce (Weil, 2014), and sectoral shifts in the economy (Hein, 2015). Yet, the impact of rising shareholder power on wage stagnation has remained under-examined (Cushen and Thompson, 2016).

In one sense, decisions about wages and shareholder payments occur separately. Wages are considered to be one of many costs that companies pay out of revenues from company sales, and they are determined by company management. Shareholder payments – defined in this article as corporate dividends and stock buybacks – are approved by boards of directors after expenses have been paid and can be interpreted as allocations that leave fewer funds available for productive investment (Lazonick, 2014; Mason, 2015).³ In another sense, decisions about whether to raise wages or shareholder payments reflect the bargaining power that each group of stakeholders has within the corporation (Lin, 2016).

The empirical approach taken in this article is to examine the relationship between shareholder payments and wages at the aggregate, sectoral and firm level, using both descriptive and econometric approaches for the United States in the neoliberal era. Both publicly traded and large private corporations can face pressure to provide greater shareholder return, as private equity and hedge fund investors demand higher dividends. Since wage stagnation is a phenomenon occurring across businesses of various sizes, it is useful to see whether rising shareholder power affects the broader economy. However, since shareholder primacy mainly affects large firms, viewing the evidence at the level of the publicly traded corporation provides the clearest evidence. Economy-wide, there is an increasing association over time between profits and shareholder payments and a decreasing association between profits and wages. In order to examine the presence of a meaningful shift in the relationships among profits, payments and wages that suggests rising shareholder primacy, two time periods – 1979 to 1997 and 1998 to 2016 – are contrasted. However, no specific relationship can be assumed, and other drivers of wage stagnation cannot be isolated. Descriptive data are then presented on the trends in shareholder payments and labour compensation at the sectoral level to show that the trends are not concentrated in a segment of the economy. Finally, a firm-level empirical analysis for US corporations from 1984 through 2018 is conducted, examining the association between shareholder payments and wages in the context of other economic dynamics, including de-unionization, increased income from foreign sources, and changes in industry concentration. The firm-level analysis provides the strongest evidence that rising shareholder payments have a direct effect on wage stagnation, net of other factors, supporting the conclusion that shareholder primacy affects employees of publicly traded corporations directly.

The paper proceeds as follows. Firstly, the literature analysing the impact of financialization on labour is summarized. Next section provides an original empirical analysis that supports the hypothesis that shareholder primacy has, over the past several decades, driven firms to prioritize shareholder payments at the expense of labour. The concluding section summarizes the research and presents policies to reorient corporate governance away from shareholder primacy, by limiting stock buybacks and instituting a stakeholder governance model.

Approaches to financialization and labour

The rise of shareholder primacy

The rise of shareholder primacy redefined the purpose of business corporations as maximizing shareholder wealth, rather than improving operational performance for the benefit of multiple stakeholders (Froud et al., 2000; Ireland, 2008; Lazonick and O’Sullivan, 2000; Van der Zwan, 2014). Shareholder primacy is a crucial facet of financialization, defined as

‘the increasing role of financial motives, financial markets, financial actors and financial institutions in the operation of the domestic and international economies’ (Epstein, 2005: 3). The focus on shareholder returns – a financial metric – replaces an earlier focus under ‘managerialism’ on maximizing ‘real’ economic outcomes – increasing sales or product prices (Davis, 2009; van der Zwan, 2014; Wartzman, 2017) . In the mid-20th century, large dominant firms were directed by powerful executives, who prioritized capital investment and productivity growth (Galbraith, 1952). In the 1970s, market value at many firms dropped below book value, prompting a wave of hostile takeovers in the 1980s and a shift to viewing the firm as a collection of financial assets, while at the same time institutional investors consolidated their shareholdings as pension funds shifted to investment in corporate equity (Fligstein, 1990; Minsky and Whalen, 1996). Though trends towards shareholder primacy have been widespread across Western countries, the focus for this article is the particular trends that have occurred in the United States, as the largest capital market.

Shareholder primacy aligned the interests of executives (who were increasingly financial experts, rather than those with industrial expertise) with shareholders by tying management compensation directly to share price, and held out the threat of hostile takeovers or activist investor action to discipline management when shareholder rewards were not forthcoming (Crotty, 2003; Davis, 2009; Manne, 1965; Wartzman, 2017). As shareholder primacy shifted power in corporate governance, executives deprioritized the growth of sales over the long term, focusing on short-term cost-cutting in order to maximize payments for shareholders (Davis, 2009; Krippner, 2011; Lazonick and O’Sullivan, 2000). Though shareholder primacy dominates corporate decision-making, it is contested as a matter of corporate law and based on a flawed underlying theory of the corporation, promulgated by financial agency theorists in the 1970s (Admati, 2017; Friedman, 1970; Jensen and Meckling, 1976; Lazonick, 2017; Palladino, 2019; Stout, 2012; Yosifon, 2018). As an economic theory, shareholder primacy lacks an account of how companies actually innovate – in other words, ‘generate a good or service that is of higher quality products at lower unit costs than those that had been previously available’ (Lazonick, 2017: 5). It jettisoned an earlier conception of the firm as a real entity from institutional economists, in which the firm is understood as a ‘dynamic system of interactions, interdependencies, and complementarities’ (Biondi et al., 2007: 6; Gindis, 2009).

There is a robust debate over whether or not financialization should be understood as a ‘structural transformation of contemporary capitalism’ (Lapavitsas, 2013: 794) or a continuation of previous trends, and whether the shift should be interpreted as beginning in the decisions by management in the conglomerate movement of the 1950s and 1980s or as a break resulting from the post-Reagan shareholder revolution (Knafo and Dutta, 2020). There is also a debate over whether financialization is a new regime of accumulation, seen in increased reliance on financial income and holding of financial assets by non-financial corporations (Krippner, 2005) (although Froud et al. (2006) and Rabinovich (2019) have critiqued whether the claim of rising financial profits holds true when considering the difficulties in disentangling truly financial profits and the ‘dustbin’ category of miscellaneous financial assets). As Froud et al. (2006) point out, the rising *narrative* of shareholder primacy does not automatically lead to a sharp break in firm-level outcomes: management may claim that they are laser-focused on increasing profits for the benefit of shareholders, while they are actually focused mainly on value-skimming for their own benefit (Froud et al., 2006). The focus for this article is on the impact of shareholder wealth maximization on employees.

Shareholder primacy and labour in the United States: Theory and empirical evidence

Untangling the specific relationship between financialization and labour is a complex task. Threaded throughout the financialization literature is regard for its impact on labour. However, as Cushen and Thompson (2016) note, there has been comparatively little attention paid to the actual micro-level mechanisms that show exactly how financialization changes the experience of workers: that is, how financialization was ‘at work’ inside the corporation (Erturk et al., 2008). Attitudes toward shareholder value and the role of labour in the large corporation are partial breaks from an earlier industrially focused economy in the United States, in which labour-capital social accords meant comparative employment stability for corporate employees.⁴

Lazonick and O’Sullivan (2000) laid out an important framework for how to interpret financialization at the firm level: from ‘retain and reinvest’ to ‘downsize and distribute’ (Lazonick and O’Sullivan 2000). Retention and reinvestment in the earlier period referred not only to the use of funds but also to labour: firm success required organizational integration and investment in the skills of employees. The shift in the 1980s to ‘downsize’ was in direct response to the growing hostile takeover movement, which sharpened executive focus on increasing returns on equity, rather than risk losing their own jobs. As Lazonick and O’Sullivan note, ‘leading the downsizing of the 1980s and 1990s were many of America’s largest corporations’ (p. 19) and job losses were concentrated in exactly the types of jobs that provided security to the white middle class: stable jobs in the manufacturing sector (Crotty, 2003).

Insecurity in the labour market has shifted from downsizing to stagnant wages and a shift to a fissured workplace (Weil, 2014).⁵ There is a wide body of scholarship in many disciplines on the trends impacting wage stagnation; the contention of this article is that the rise of shareholder primacy on wage stagnation, particularly for large corporations, has been under-examined relative to other trends. These trends include downsizing, fissuring, and de-unionizing; globalization; changes in the sectoral composition and skill requirements of the economy (and education levels of its workers); and increased concentration and market share of the largest corporations. Baumol et al. (2003) showed that the downsizing in large corporations in the 1970s and 1980s was effective at holding down wages, as large corporations did not keep smaller workforces but instead replaced unionized labour with a non-union workforce (see also Fligstein, 1990; Useem, 1986). Weil (2014) extends the analysis to the 2000s, showing that the fissuring of the workplace has depressed wages and led to less secure employment. The diffusion of the workforce to both smaller firms and outside of formal employment pushes down wages (Davis and Cobb, 2010). The large-scale decline in manufacturing and the shift from manufacturing to the service sector has a clear impact on job quality and quantity (Fligstein and Shin, 2007; Harrison and Bluestone, 1998). Autor et al., (2020) claims that the declining labour share is due to the reallocation towards highly profitable firms, rather than redistribution from workers to shareholders. Mainstream arguments focus on the increasing requirement for technical skills in the workforce, which has widened the gap between highly skilled workers and those left behind (Acemoglu, 2009; Blanchard, 1997), and the impacts of stratified education on wages (Goldin and Katz, 2007). Declining union density is a clear contributor to wage stagnation, as unionized workforces have an institutional mechanism to bargain for higher wages (Freeman, 1980; Western and Rosenfeld, 2011). Yet, the decline of union density should not necessarily be considered a separate stream from rising shareholder primacy – in many cases, it is rising demands for

short-term shareholder return that have led, in part, to pressures to de-unionize the workforce. The increase in outsourcing and globalization is another oft-cited source of increased pressure on firms to cut labour costs or globalize their US workforce (Davis, 2009; Hein, 2015; Stiglitz, 2002).

There has been a growing literature examining the impacts of financialization on labour, though with a focus on aggregate labour share or employment changes, rather than firm-specific wages (Barradas, 2019; Cushen and Thompson, 2016; Fligstein and Shin, 2007; Froud et al., 2000; Lin, 2016; Lin and Tomaskovic-Devey, 2013; Thompson, 2003). In surveying the literature, Hein (2015) describes several ways that rising financialization drives down labour's share of income: through the sectoral change in the economy, as finance grows (and government's share declines, although this may be less relevant for the United States); through rising shareholder value orientation, as corporations' value becomes expressed through financial metrics, and executive compensation becomes tied to shareholder value; and through the deterioration of union density. Fligstein and Shin (2007) find evidence of rising shareholder value practices, including mergers and layoffs, although such practices were not actually linked to rising profitability (supporting Froud's claim of financialization as narrative). Barradas (2019) finds that financialization and neoliberalism have a negative impact on the labour share across advanced economies in Europe by affecting the sectoral composition of the economy, through the channel of increased shareholder value orientation and declining worker bargaining power. Lin (2016) documents how a firm's shareholder value orientation affects total employment size, emphasizing that different occupational groups are affected differently. He finds that the return to shareholders has a long-term, negative effect on the size of employment for all occupational types, although the effect is strongest for service occupations (and rising demands on revenue by creditors diminished the bargaining power of production and service workers, focusing on the slower growth in employment). Lin and Tomaskovic-Devey (2013) find that increased corporate earnings from financial activity (as opposed to 'traditional' productive and commercial activity) is associated with a decline in the labour share, higher compensation for top executives, and increased earnings dispersion among workers.⁶ Using a counterfactual technique, they also find that financialization accounts for nearly 60% of the decline in labour's share between 1970 and 2008. Dünhaupt (2013, 2014) conducts a similar analysis across 13 countries in Europe, finding evidence of a distributional conflict between shareholders and wage earners.

Yet as noted by Cushen and Thompson in 2016, 'scholarship has yet to uncover the novel and distinctly financialized activities taking place within organizations that both affect and are affected by labor' (p. 353). Thompson (2003) developed the Disconnected Capitalism Thesis (DCT) to shed more light on the micro-economic consequences of financialization inside the firm. The DCT claims, as this article investigates, that the pursuit of shareholder value has put pressure on firms to reduce labour costs, which 'manifest[s] in delayering, disaggregating, downsizing and divestment' (Thompson, 2013: 473). Power in the workplace has shifted to the board of directors and executives who are directly accountable to shareholders, away from managers whose primary focus and knowledge was related to the substantive industry (Cushen and Thompson, 2016).

One specific micro-economic consequence of financialization is the impacts of rising shareholder payments on employment compensation. This paper contributes to the gap identified by Cushen and Thompson (2016) by focusing on the relationship between two key metrics: the rise of shareholder payments and labour compensation, in the context of the

other trends impacting wages identified above. This article adds to the recent body of literature that empirically examines the relationship between shareholder primacy and labour compensation, with a specific original focus on the wage bill in the United States.

Evidence for financialization at work

To consider whether rising shareholder primacy comes at the expense of employees, this article examines how corporate leaders use profits at the aggregate level and analyses the relationship between changes in shareholder payments and labour compensation at the sectoral and firm level. The analysis addresses the claim of Cushen and Thompson (2016: 353) that ‘there is an acknowledged failure to specify and explore the mechanisms through which these trends take place’ regarding financialization in the workplace. Given the multiple interrelated factors affecting the ability of workers to bargain for a share of value creation, the claim here is that rising shareholder primacy needs to be understood as *one of the crucial channels* contributing to wage stagnation of typical workers in the United States – not that it is the exclusive channel (Thompson, 2013). The focus here is on US-based sectors and corporations, as the United States is where shareholder primacy took root and is the world’s largest capital market and economy (Lazonick and O’Sullivan, 2000).

Shareholder payments and wage stagnation at the aggregate and sectoral levels

This section aims to demonstrate how wages and shareholder payments expressed as a percentage of profits have been trending in opposite directions over the past several decades, starting at the aggregate level. Growth rates of shareholder payments and wages at the sectoral level then demonstrates that these trends are not specific to a few sectors of the economy but are more widespread. This motivates more robust empirical methods at the firm level to look at the association between shareholder payments and wages, net of other factors.

The dominance of stock buybacks, in which companies repurchase their own stock on the open market, pushing up share prices, is one of the clearest examples of shareholder primacy (Lazonick, 2014). While dividends have been issued to shareholders since the origin of the corporate firm, stock buybacks (also known as share repurchases) are a newer practice. Despite significant concerns about their potential for market manipulation within the Securities and Exchange Commission (SEC) in the 1970s, the practice became effectively legalized in 1982 and has grown rapidly over the subsequent decades (Lazonick, 2014; Palladino, 2018). Figure 1 below shows the rise in spending on stock buybacks and dividends – which, together, are termed shareholder payments – and wages as shares of corporate assets from 1979 to 2017.

Given the data on shareholder payments and stagnant wages, the first empirical question this article addresses is whether a shift away from wages and towards shareholder payments, both expressed as a percentage of corporate profits, can be observed. Although such a finding would not support a causal relationship, it is important to establish the trend of rising shareholder power and declining worker power in the economy as a whole. Bureau of Economic Analysis (BEA) Integrated Macroeconomic Accounts data, including profits, employee wages and salaries, and dividends, are used for the non-financial sector. Corporations with publicly traded stock are required to report materially relevant data as part of regular filings with the SEC. Because the only businesses that conduct stock buybacks are publicly traded corporations, the shareholder payments variable is constructed by

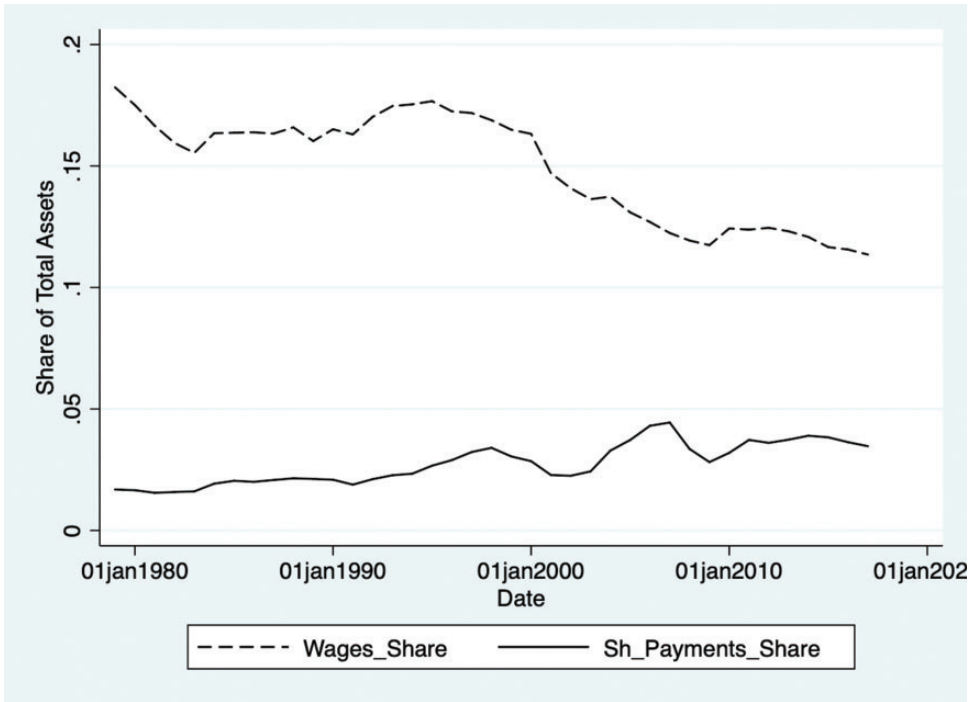


Figure 1. Shareholder payments and wages as a share of total corporate assets. This figure shows the decline in the wage bill as a percentage of total corporate assets, and growth in shareholder payments, for nonfinancial corporations. (Source: BEA Integrated Macroeconomic Accounts and S&P Compustat.)

adding non-financial corporate business dividends from the Federal Reserve to non-financial corporate business stock buybacks data from S&P Compustat, a commercial database that aggregates data from corporate SEC filings. All variables are normalized by total corporate assets.

The data are presented from 1979 to 2017. All data are converted to 2018 dollars using the 2018 Consumer Price Index (CPI). One limitation here is that a growing wage bill represents both an increase in the wage of a given worker and the expansion of employment; the labour expense figures also include top executives, whose rising incomes dampen the fall of compensation of non-executive employees in aggregate statistics (Hein, 2015). This analysis, thus, explores the changing relationship between rising profits and payments to labour as a whole (i.e., payments to labour include both rising wages and increased employment).

The purpose in analysing the aggregate data for the non-financial corporate sector is to see whether there is any evidence that the relationship between corporate profits, shareholder payments and employee compensation shifted in a way that is consistent with the argument that the neoliberal era has seen a rise in shareholder power and a decline in worker power. The data show that wages fell relative to corporate assets, while shareholder payments rose. The decline in the wage bill represents a much larger proportion of assets; corporate funds freed up by the decline in the wage bill proportionate to assets are not completely captured by rising shareholder payments, but are also available for other uses.

Table 1. Profits, wages and salaries, and shareholder payments as a share of total assets for selected years.

	1975	1985	1995	2005	2015
Profits	3.30%	1.19%	2.65%	3.23%	2.56%
Sh. Payments	1.56%	1.96%	2.62%	3.34%	3.45%
Stock Buybacks	0.05%	0.64%	0.61%	0.61%	1.39%
Dividends	1.51%	1.32%	2.01%	2.07%	2.06%
Wages	18.0%	16.4%	17.2%	12.7%	11.6%

Source: BEA Integrated Macroeconomic Accounts and S&P Compustat.

As shown in Figure 1, the wage bill fell steadily, from 21% of total corporate assets in 1972 to 11% in 2017. Total wages have been below 15% of assets every year since 2001. Meanwhile, payments to shareholders have doubled as a percentage of assets, from 1.7% in 1972 to 3.5% in 2017. These shifts are consistent with a story of rising shareholder power and declining employee bargaining power, although at this stage no causal connection can be inferred from the data presented. Table 1 presents data on profits, wages, and shareholder payments as a share of total assets for selected years.

To further examine the trends, the sample period is divided in half, with two time periods: 1979–1997 and 1998–2017. Figure 2(a) and (b) presents scatterplots showing the changing relationship between profits and shareholder payments, on the one hand, and profits and payments to employees. The variable for wages here represents the rising wage bill, which includes both rising wages per worker and expanding employment. All data are normalized by total corporate assets.

Figure 2(a) shows a horizontal–sloping relationship between profits and shareholder payments over the first period, but a sharp upward slope for the relationship between profits and payments in the second period, suggesting the growing bargaining power of shareholders. Figure 2(b) shows the opposite: although profits and wages had a slightly upward-sloping relationship in the first period, the relationship reverses in the later period, as higher profits are associated with a lower wage bill. The shifting relationship between profits and payouts and wages, respectively, establishes that trends in how profits are deployed were shifting in the later period. It is important to note that some of the positive relationship will reflect the variation of assets over time, and the positive relationship in the first period between profits and shareholder payments may be exaggerated. However, this factor does not explain the shift in the relationship between the first and second periods; it actually makes the second period's negative relationship between profit growth and the growth of the wage bill all the more striking.

Analysing the impact of financialization at the sectoral level complements the firm-level analysis (discussed below) by providing evidence on whether or not trends that are occurring at the firm level are occurring at the broader sectoral level, and also distinguishing among trends in different product markets (Fligstein and Shin, 2007). Wage growth is calculated using sector-level average wage data for nonproduction and supervisory employees from the Current Employment Statistics, a monthly survey conducted by the Bureau of Labor Statistics (2017a, 2017b) that is based on 149,000 businesses and government agencies that represent 651,000 worksites throughout the US.⁷ This variable measure changes in yearly average wages directly, disaggregating the growth of the total wage bill into the portion attributed to growth of average wages per worker, rather than the growth in

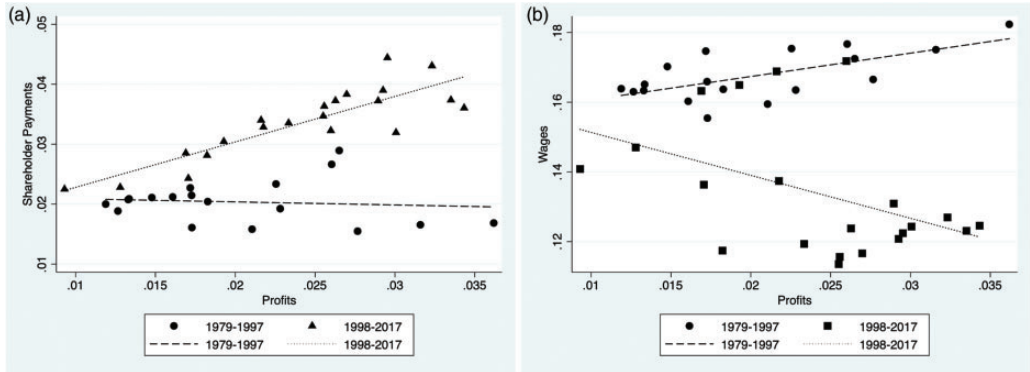


Figure 2. (a) Shareholder payments and profits, 1979–2016. (b) Wages and profits, 1979–2016. (Source: BEA Integrated Macroeconomic Accounts.)

employment. Firm-level data are aggregated at the two-digit sector from Compustat for stock buybacks, dividends and corporate profits, taken as a ratio of GDP. Of course, the average non-executive wage is partially set outside of the publicly traded company; comparing growth rates gives only a partial picture of the relationship between the two corporate decisions.

Table 2(a) and (b) presents the growth rate of shareholder payments alongside the growth rate of average wages for each sector, for decades over the time period.

The comparison shows the much higher growth rate of shareholder payments versus the growth rate of average wages for non-production and supervisory employees. Of course, this does not indicate that rising payments to shareholders has *necessarily* had any impact on the slower growth rate of average wages. But the analysis does show that the rise in shareholder payments is not driven by any one sector, and that, similarly, the slowdown of wage growth is not limited to one or two areas of the economy. Manufacturing, the sector arguably most exposed to international competition, saw the slowest wage growth, with just 1% wage growth in 1985 to 1995 and 10% from 2005 to 2015. Retail and transportation are sectors that have been affected both by the shift towards services and automation, and wage growth slowed to eight and seven per cent, respectively, in the last decade. Meanwhile, shareholder payments grew 125% in manufacturing from 1985 to 1995 and 172% from 1995 to 2005; while for retail they grew 136% and 400%, respectively. In the most recent decade, four out of seven sectors had growth rates for average wages of 10% or less. In those same sectors, shareholder payments grew between 73% and 167%. The FIRE and information sectors did see a slowdown in the growth rate of payments in the last decade, but the overall level of shareholder payments had already reached extreme heights in 2005, at nearly half a billion dollars in one year. Therefore, the slower growth rates should not be interpreted as representing low dollar levels of spending on shareholder payments.

Firm-level empirical analysis

Firm-level data can shed further light on the relationship between shareholder payments and labour compensation. By controlling for other factors that impact wages, discussed in

Table 2. Growth rates of shareholder payments and average wages for nonsupervisory and production employees, selected sectors, 1975–2015.

	1975–1985	1985–1995	1995–2005	2005–2015
A. Growth Rates of Shareholder Payments				
Sector				
FIRE	399%	290%	527%	12%
Info.	322%	73%	353%	11%
Manufacturing	330%	125%	172%	73%
Retail	257%	136%	400%	110%
Transp.	464%	31%	281%	167%
Utilities	1,395%	–30%	213%	81%
Wholesale	231%	58%	236%	107%
B. Growth Rates of Average Wages for Nonsupervisory and Production Employees				
Sector				
FIRE	121%	43%	119%	47%
Info.	21%	9%	54%	30%
Manufacturing	33%	1%	21%	10%
Retail	26%	36%	52%	8%
Transp.	65%	55%	11%	7%
Utilities	11%	72%	25%	8%
Wholesale	5%	22%	30%	28%

Source: CES survey of the BLS and S&P Compustat.

Approaches to financialization and labour section, regression estimations allow for a clearer examination of the association between changes in shareholder payments and labour compensation. This section presents panel data on the relationship between shareholder payments and labour compensation for the period 1984 to 2017. The crucial caveat is that firm-level labour compensation is sparsely reported. A low percentage of firms actually report labour expenses broken out from a more general administrative expenses category; the Securities and Exchange Commission does not require companies to report this information unless it is seen to be materially relevant to shareholders, and thus, a minority of firms (and an even smaller percentage of non-financial firms) actually reports such data. Because of data limitations, it is not possible to further break the sample into sub-categories by firm revenue; if further labour compensation data become available, this would be a fruitful area for further research, as it is clear that stock buyback activity is more prevalent in the largest firms by revenue. The scarcity of data also limits the ability to test for survivorship bias. Figure 3 presents average spending on stock buybacks as a ratio of market value for four different sub-categories of firms, organized by revenue, showing that the average ratio of stock buybacks to firm market value grows as firms grow in size (categorized by revenue).

For the empirical analysis, a panel data fixed-effects regression is employed to look at the relationship at the firm level. The direction of the relationship is useful for analysing whether the hypothesis that rising capital markets' pressure has affected labour compensation is borne out by the data. The outcome variable is logged firm-level wages. Firms report a labour compensation variable that includes wages and salaries as well as other compensation-related benefits. The lag of logged labour compensation expenses is taken

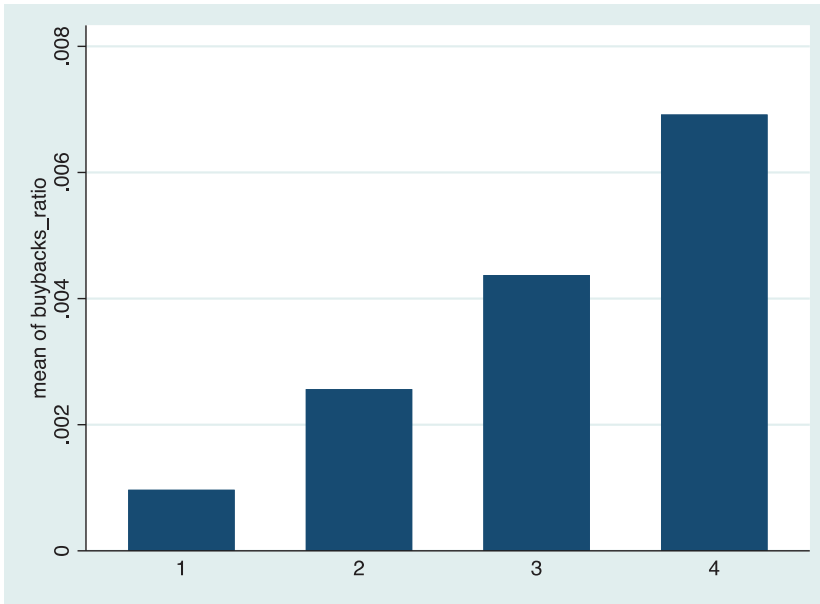


Figure 3. Average stock buybacks/market value, by firm revenue. (Source: S&P Compustat.)

to avoid testing for the relationship in the same time period (Wilmers, 2018). Companies report total dividends and repurchased stock on an annual basis, which combined gives a shareholder payments variable that is reported as a ratio of operating expenses, expressed as a log (Lin, 2016; Wilmers, 2018).

To control for other common influences on wages, a set of firm-level and industry-level controls are used. At the firm level, technological change is measured with logged investment, computed from capital expenditures and R&D expense. Logged assets and logged revenue are included to account for firm size. Profit margin is measured as the ratio of earnings before interest, taxes, depreciation and amortization (EBITDA) over revenue (Wilmers, 2018). Globalization is measured as a ratio of the firm’s foreign income to total income (imputed as zero when no foreign income is reported ; Lin, 2016; Wilmers, 2018). Productivity is measured by controlling for logged revenue per logged employee (Barth et al., 2016). Union representation and industry concentration are both measured at the industry level, using the Current Population Survey reporting of union density at the three-digit NAICS level (Fligstein and Shin, 2007; Western and Rosenfeld, 2011). Industry concentration as a percentage of industry revenue is generated by the top five firms for the three-digit industry (calculated from Compustat) (Autor et al., 2020; Grullon et al. 2019; Wilmers, 2018).

Firm and year fixed-effects are used to account for time-invariant characteristics of unique firms and macroeconomic conditions, respectively. All observations are required to have complete samples for all variables; the resulting sample used for the regression analysis contains 12,700 firm-year observations and 2194 unique firms for the period of 1984 to 2017. The Hausman test supports using a fixed effects model; the Heckman selection correction test is used to determine if variation in reporting labour compensation biases the results.⁸ Summary statistics on the key variables are provided in Table 3.

Table 3. Firm-level analysis: summary statistics for key variables.

Variable	Observations	Mean	Std. Dev.	Min.	Max.
Labor Compensation	20,552	3.866	2.964	−6.907	11.08
SP/OpExp	20,437	0.0858	0.7471	−0.0054	70.84
Investment	20,184	2.951	3.184	−6.907	11.09
Revenue	20,058	5.362	3.196	−6.907	13.06
Assets	21,447	5.472	3.199	−6.098	13.08
Profit Margin	19,968	−5.821	1.148	−7.28	0.61
Productivity	19,363	1.311	0.7272	−5.742	28.35
Foreign Income	21,486	0.0594	4.044	−325	429.7
Unionization (Industry)	15,172	0.1695	0.1569	0	0.8900
Industry Concentration	21,131	0.4642	0.2007	0.092	1.001

$N = 12,700$; unique firms = 2194.

The model estimated is as follows:

$$\log(\text{LaborCompensation}) = \alpha_i + \beta((\log)\text{ShareholderPayments}/\text{OpExp}_{i,t}) + \beta(\text{Firm Controls}) + \beta(\text{Industry Controls}) + \eta_{i,t}$$

Results are reported in Table 4. The analysis finds that a 10% increase in shareholder payments expressed in proportion to operating expenses is associated with a 1.5% decline in logged wages. Several variations of the model with different controls are analysed, and find negative coefficients in the range of -0.04 to -0.12 for a one per cent increase in the shareholder payments/operating expenses ratio, depending on whether or not the model includes industry concentration and unionization, or both. In terms of the firm-level controls, investment and firm size (measured with revenue and assets) have a positive impact on wages, while profit margin has a nearly neutral impact and productivity and foreign income are statistically insignificant. In terms of industry-level controls, again as in the sectoral analysis the union rate has a negative effect, while industry concentration is statistically insignificant. This finding supports the hypothesis that rising shareholder power, expressed as rising shareholder payments as a percentage of firm operating expenses, has a negative impact on the change in wages.

Conclusion

This article offers evidence of how financialization is ‘at work’ in the United States by investigating the relationship between shareholder payments and wages at the aggregate, sectoral and firm level, using the downsize-and-distribute framework (Lazonick and O’Sullivan, 2000). In this section, specific proposals for policy reform are presented to rebalance power among corporate stakeholders, especially shareholders and workers, on two issues: first, how to limit stock buybacks; and second, how to broadly reorient corporate law towards a stakeholder-centred corporate governance framework. The research findings are then summarized to provide evidence for the argument that rising shareholder power is one factor behind American wage stagnation.

Table 4. Firm-level analysis: regression results.

Variable	Coefficient	Standard error	P-value	Confidence interval (low)	Confidence interval (high)
Sp/OpExp (log)	-0.1444	0.0257	0.000	-0.1947	-0.0939
Investment (log)	0.0571	0.0045	0.000	0.4835	0.0658
Revenue (log)	0.3570	0.0072	0.000	0.3427	0.3713
Assets (log)	0.3735	0.0084	0.000	0.3568	0.3902
Profit Margin	-0.0005	0.0000	0.000	-0.0005	-0.0004
Productivity (Revenue/Employment)	-0.0001	0.0000	0.304	-0.0001	0.0000
Foreign Income	-0.0002	0.0006	0.732	-0.0012	0.0009
Unionization (Industry)	-0.0832	0.0582	0.153	-0.1974	0.0310
Industry Concentration	0.036	0.0499	0.001	-0.0617	0.1338

$N = 12,700$; unique firms = 2194; R^2 : Within = 0.6817; dependent variable: Wages (log).

There is a wide range of policies that could limit unproductive stock buybacks. For example, Congress can ban open-market share repurchases by passing affirmative legislation that prohibits such stock buybacks, or, if not an outright ban, establish bright-line limitations. The proposed ‘Reward Work Act’ (S. 915, 2020) bans open-market share repurchases, while the proposed ‘Worker Dividend Act’ (S. 2505, 2018) and ‘STOP Walmart Act’ both limit corporate use of stock buybacks unless certain labour compensation standards are met. Congress could also choose to condition or prohibit a company’s ability to conduct repurchases based on other corporate variables. For example, policymakers could prohibit buybacks if companies have unfunded pension liabilities, have engaged in layoffs, have failed to meet a certain level of productive investment, have wage dispersion below a certain threshold or have executive compensation above a certain limit. Finally, Congress could institute a stock buyback transaction tax, in which each stock buyback transaction costs the firm a certain percentage of the dollar value of the trade in taxes (Palladino, 2018). All other jurisdictions that represent the ten largest capital markets have a set of conditions on stock buybacks that are stricter than the United States (Kim et al., 2005).

Although limiting stock buybacks is necessary in the near term, the law of corporate governance itself must be reformed if shareholder primacy is to be reined in. Corporations are privileged business entities that shield individuals from liability, have perpetual life, and are able to organize large amounts of capital. As a result, they stand to make a large impact, positive or negative, in the communities they occupy and our economy and society. Shareholder primacy should be replaced with a more effective framework for corporate law in which all corporate stakeholders have a role in decision-making and are considered when corporate choices are made. Board fiduciary duty should run to all corporate stakeholders. Currently, under state law, board ‘fiduciary duty’ – the legal standards of care and loyalty owed by directors – states that directors are accountable only to shareholders for their decisions. The proposed ‘Accountable Capitalism Act’ (S.3348, 2018) requires consideration of multiple stakeholders in board decisions, as well as requiring that 40% of the directors are elected by employees. Corporate boards should be required to show that they considered the interests of all other corporate stakeholders as well – although, importantly, board decisions would still be covered under the legal standard of the ‘business judgment rule’, meaning that a court would review the procedural fairness used

to determine a decision, but leave considerable discretion to the board as to the substance of the decision.

Another area for policy reform is to mandate employee representation on the company's corporate board, as is the case in Germany and much of continental Europe (Silvia, 2013). Currently, large corporations have boards elected solely by shareholders. This appointment mechanism ensures that board members serve the interests of the investment community and corporate executives and that there can be no significant buy-in from employees. Firms could be required to reserve a set of board seats for worker representatives, and these seats could be nominated by the workforce or union members, as in the 'Reward Work Act'. On a broader level, employees can be brought 'inside' corporate governance through other mechanisms (Bodie, 2016). For example, employees could have nonbinding votes or could be surveyed regularly. McDonnell (2011: 108) writes: 'One can classify possible laws along three axes: the level within a corporation at which employees have a voice, the scope of decisions over which they have a voice, and the degree or kind of voice they have over a particular matter'. Along these axes, a policy to include workers on boards would boost workers' voices to the highest level within a corporation, expose them to the greatest scope of decision-making, and grant them voting power on par with senior executives.

The rise of shareholder primacy is one critical factor for the long-term wage stagnation for typical workers in the United States. The demand for rising shareholder payments constrains the ability of employees to bargain for higher wages; it is one example of the financialization of the US economy, in which value created by the corporate sector is captured by share-sellers and workers lose bargaining power (Lazonick, 2014; Lin and Tomaskovic-Devey, 2013). This article has examined the relationship between shareholder primacy and labour compensation at the aggregate, sectoral, and firm levels in order to test the hypothesis that demand for shareholder returns plays a part in explaining the long-term stagnation of wages for typical workers in the United States. The evidence shown provides support for the argument that rising shareholder payments are associated with downward pressure on wages, and that the relationship can be seen net of other drivers of wage stagnation at the firm level for publicly traded corporations.

The aggregate analysis shows that shareholder payments as a percentage of profits have been rising over the past few decades, while wages, measured across the entire economy, have stagnated. It is hardest to isolate specific factors that impact wages at the aggregate level, and there are certainly a variety of factors in addition to (and related to) rising shareholder power that makes disentangling the effects difficult. These include de-unionization, offshoring, changes in the sectoral composition of the economy and related changes in the labour intensity of the production process, and rising market concentration. I show that at the aggregate level, wages fell from 21% of total corporate assets in 1972 to 11% in 2017, and wages have been below 15% of total assets in every year since 2001. Meanwhile, shareholder payments measured as a percentage of assets have doubled over the same time period, from 1.7% in 1972 to 3.5% in 2017. I break the study period in half, dividing it into two sub-periods, 1979 to 1997 and 1998 to 2016, in order to further examine the changes in each key variable's relationship to profit. I find that in the later period, there is a stronger association between profits and payments, while at the same time a weaker association between profits and wages.

The association between firm-level data on wages and shareholder payments for publicly traded US corporations is empirically evaluated using a panel data fixed-effects approach. The measurement at the firm level for publicly traded corporations is the strongest indicator

for rising shareholder power because such power is expressed through the capital markets. The increase in shareholder payments as a percentage of operating expenses is statistically associated with a decline in wages when holding other factors that impact the wage level constant; specifically, a 10% increase in shareholder payments as a share of operating expenses is associated with a 1.5% slowdown in logged wage growth. Although the analysis is not causal in nature, and the available data on firm-level wages limited, the finding supports the hypothesis that rising shareholder power is one factor in the long-term wage stagnation faced by US workers. Policies to rebalance power over the value created by large publicly traded corporations are necessary to reduce wage inequality.

Author's Note

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Declaration of Conflicting Interests

The author(s) declared no potential conflicts of interest with respect to the research, authorship, and/or publication of this article.

Funding

The author(s) received no financial support for the research, authorship, and/or publication of this article.

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Notes

1. Original use of this phrase is in Erturk et al. (2008).
2. According to Mishel (2015), in the 30 years after World War II, real hourly compensation of most workers grew 91%, well in line with overall productivity growth of 97%. But since the early 1970s, the gap between these two indicators has widened dramatically. Between 1973 and 2013, productivity increased 74%, while hourly pay of a “typical” worker (i.e. production and nonsupervisory) grew only 9%. In turn, labour’s share of income has declined.
3. ‘Payments’ should not be taken to indicate that the shareholder paid something in to the firm. The vast majority of shareholders purchase their shares from other shareholders and therefore never contribute any funds to shareholders. The concept here is the payments that the company is making to all who hold shares.
4. Workers who were not able to access corporate employment, in particular women and people of color, experienced employment insecurity during this period.
5. Of course, one well-documented caveat to the falling labour share is the rise in compensation of top executives (Atkinson et al., 2011; Bebhuk and Grinstein, 2005; Froud et al., 2006).
6. Notably, their research finds that financialization had an impact on labour outcomes comparable to the more common explanations for increased income inequality, including globalization, technological change, capital investment and declining rates of unionization.
7. Monthly data is obtained that includes seasonally adjusted employment levels and weekly earnings for nonsupervisory and production employees at the sector level. After calculating the 12-month average for each variable, average weekly earnings are adjusted to average annual earnings, and

multiplied by average employment levels to create an annual worker compensation variable for each sector. From there, CES industry sectors are matched to the NAICS sectors from Compustat to merge the data.

8. I estimate the Hausman test and find that the P -value is 0.000, justifying the use of the fixed-effects model. To implement the Heckman selection correction test, I model selection into firms reporting labour compensation (Shin, 2014; Wilmers, 2018). I use a probit regression model with a dummy variable for 'Selling, General and Administrative Expense' to test whether there is a time-variant selection decision for reporting the aggregate, required variable, or a more specific labour compensation variable. I find a P -value of 0.000.

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