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Index funds and employee welfare: some exploratory insights

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Abstract

This brief Article offers some reflections on the relation between the increasing prominence of large institutional investors, such as index funds, in the corporate governance of public firms, and employee welfare. The Article addresses two intertwined issues: how the growing concentration of public equity ownership in the hands of such institutional investors may have contributed to wage stagnation and the degradation of labor conditions more generally, and how the established presence of such institutional investors as stable, long-term shareholders in today's public firms might help improving those conditions in the future.

Keyword: Index funds; Institutional investors; Constitutional Court; Labor conditions; Corporate governance; ESG.

1. Introduction.

Workers of developed economies are not doing well, or at least not as well as they used to in the recent past. The "labour share", namely the fraction of national income that goes to employees via wages, generally thought to be stable,[1] has been declining in recent years,[2]

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[1] As reported by recent research conducted by the International Labour Organization (ILO) and the Organisation for Economic Co-operation and Development (OECD) with contributions from International Monetary Fund and World Bank Group, "[a]t least until the 1980s, a stable labour income share was accepted as a 'stylized fact' of economic growth" (footnote omitted). *See* ILO-OECD, *The Labour Share in G20 Economies* (Report prepared for the G20 Employment Working Group Antalya, Turkey, 26-27 February 2015), https://www.oecd.org/g20/topics/employment-and-social-policy/The-Labour-Share-in-G20-Economies.pdf

[2] *See* generally ILO-OECD, nt. (1); Mai D., Mitali D., Zsoka K., Weicheng L., *Why Is Labor Receiving a Smaller Share of Global Income? Theory and Empirical Evidence*, IMF Working Paper No. 17/169, 2017.

notwithstanding productivity in developed countries has generally increased.[3] Wage stagnation, in turn, contributed to today's high levels of income inequality.[4]

There are multiple competing explanations for these economic trends. Among others, foreign technological convergence (i.e., the "catching-up" of foreign countries in the production of hi-tech goods) driven by globalization,[5] technology and the increasing use of robots in production processes,[6] concentration in the labor[7] or product[8] market, the rise of "superstar firms" dominating entire industry sectors,[9] reduced worker power caused by de-unionization and other factors.[10]

This Article looks at capital markets and focuses on a well-known phenomenon: the concentration of stock ownership in the hands of institutional investors and – more recently – in those of large index funds.[11] The Article offers some reflections on two intertwined issues: how the growing concentration of share ownership in the hands of such institutional investors might have contributed to wage stagnation (and the degradation of employment conditions more generally), and how the established presence of such institutional investors as stable, long-term shareholders in today's public firms might help *improving* those conditions in the future.

Capital markets – and especially public stock markets – have undergone deep transformations in the last decades.

Shares in large public companies, once widely dispersed across a myriad of small investors, are increasingly held by large institutional investors, namely professional money managers who invest on behalf of retail investors. Investment by such professional money managers, in turn, increasingly occurs via index funds (a trend that is often referred to as "indexing" or "indexed investing").[12] Index funds are investment vehicles that track some market index (such as the U.S. S&P 500) with a view to delivering to the fund's investors the same returns

[3] *See* ILO-OECD, nt. (1), 8.
[4] *See*, e.g., Goshen Z., Levit D., *Common Ownership and The Decline of the American Worker*, ECGI Law Working Paper No. 584, 2021, https://ssrn.com/abstract=3832069 ("As wages have stagnated, income inequality has skyrocketed" [footnote omitted]).
[5] *See* Cozzi G., Impullitti G., *Globalization and Wage Polarization*, in *The Review of Economics and Statistics*, 98, 5, 2016, 984.
[6] *See* Acemoglu D., Restrepo P., *Robots and Jobs: Evidence from US Labor Markets*, in *Journal of Political Economy*, 128, 6, 2020, 2188.
[7] *See* Azar J., Marinescu I., Steinbaum M., *Labor Market Concentration*, in *Journal of Human Resources*, 2020, 1.
[8] *See* Barkai S., *Declining Labor and Capital Shares*, in *Journal of* Finance, 75, 5, 2020, 2421.
[9] *See* Autor D., Dorn D., Katz L. F., Patterson C., Van Reenen J., *The Fall of the Labor Share and the Rise of Superstar Firms*, in *Quarterly Journal of Economics*, 135, 2, 2020, 645.
[10] *See*, e.g., Stansbury A., Summers L. H., *The Declining Worker Power Hypothesis: An explanation for the recent evolution of the American economy*, NBER Working Paper No. 27193, 2020), https://www.nber.org/papers/w27193, arguing that reduced worker power is the cause of the decrease in the labour share and other related macro-economic phenomena; Farber H. S., Herbst D., Kuziemko I., Naidu S., *Unions And Inequality Over The Twentieth Century: New Evidence From Survey Data*, in *Quarterly Journal of* Economics, 136, 3, 2021, 1325, finding evidence consistent with the idea that unions reduce inequality.
[11] *See*, e.g., Langevoort D. C., *The SEC, Retail Investors, and the Institutionalization of the Securities Markets*, in *Virginia Law Review*, 95, 4, 2009, 1025; Bebchuk L., Hirst S., *The Specter of the Giant Three*, in *Boston University Law Review*, 99, 2019, 721-741.
[12] *See* Coffee J. C. Jr., *The Future of Disclosure: Esg, Common Ownership, And Systematic Risk*, in *Columbia Business Law Review*, 2021, 606, fn. 7.

of the index. Index funds offer effective, low-cost diversification to household investors,[13] a feature that in the view of many explains their success.[14] Today, most index funds are marketed and managed by three large U.S. asset managers (usually referred to as "the Big Three"): BlackRock, Vanguard, and State Street Global Advisors. Ownership concentration in the hands of the Big Three is relentlessly on the rise and there are no signs that this trend will stop or slow down in the near future.[15]

These trends are more pronounced in the United States and the U.K., where share ownership of large public firms was traditionally highly dispersed.[16] Yet the growing importance of institutional investors – and index funds more in particular – is a phenomenon that characterizes EU capital markets as well. Also there, an increasing number of public firms has one or more of the Big Three as a significant shareholder in their shareholder base.[17]

The growing concentration of share ownership in the hands of few "mega" institutional investors raised concerns over the potential anticompetitive effects that such concentration may bring about.[18] More generally, the economic power that such large money makers are amassing is impressive and, at least for some, worrisome.[19]

According to some accounts, these transformations may have also played a role in wage stagnation and the degradation of worker conditions more generally.

For starters, ownership concentration produced a corporate governance system more tightly focused on shareholder value maximization. Such a stronger focus on shareholder

[13] *See*, e.g., Kahan M., Rock E. B., *Index Funds and Corporate Governance: Let Shareholders Be Shareholders*, in *Boston University Law Review*, 100, 5, 2020, 1774.

[14] *See*, e.g., Fisch, J., Hamdani A., Solomon S. D., *The New Titans of Wall Street: A Theoretical Framework for Passive Investors*, in *University of Pennsylvania Law Review*, 168, 1, 2019, 19, arguing that "an increasing number of retail investors invest through indexed mutual funds and exchange-traded funds" "drawn [also] by the lower costs of these products". The growth of index funds has been astonishing. An astounding and ever-increasing part of household savings is invested through these investment vehicles. *See*, e.g., Fichtner J., Heemskerk E. M., *The New Permanent Universal Owners: Index Funds, Patient Capital, and the Distinction Between Feeble and Forceful Stewardship*, in *Economy and Society*, 49, 4, 2020, 494, documenting a massive shift of investor money from actively managed equity funds to passive ones, like index funds.

[15] According to recent research conducted by professors Lucian Bebchuk and Scott Hirst, the average combined stake of the Big Three in S&P 500 companies essentially quadrupled from 1998 to 2017, raising from 5.2% to 20.5%. According to their projections, if the past trend continues the Big Three could be able to cast "about 34% of votes in the next decade, and about 41% of votes in two decades". *See* Bebchuk L., Hirst S., nt. (11), 723-4. *See* also Coates J. C., *The Future of Corporate Governance Part I: The Problem of Twelve*, Harvard Public Law Working Paper No. 19-07, 2018, https://ssrn.com/abstract=3247337, noting that if ownership concentration in the hands of The Big Three continues, in the near future control over the majority of U.S. public companies will practically be in the hands of a handful of individuals.

[16] *See supra* nt. (15).

[17] In Italy, for example, BlackRock holds a 5% participation in the country's two largest banks, Unicredit and Intesa San Paolo, making BlackRock the largest shareholder at Unicredit (*see* https://www.unicreditgroup.eu/it/governance/shareholders/shareholders-structure.html?intcid=INT-IG_CTA0022) and the second largest shareholder at Intesa San Paolo (*see* https://group.intesasanpaolo.com/it/chi-siamo/azionariato).

[18] *See* generally Elhauge E., *Horizontal Shareholding*, in *Harvard Law Review*, 129, 5, 2016, 1267.

[19] *See*, e.g., Bebchuk L., Hirst S., nt. (11), 725, arguing that ownership concentration in the hands of the Big Three may lead to reduced checks over corporate managers and thus to an increase of managerial agency costs; Coates J. C., nt. (15), 2, stressing the legitimacy and accountability issues raising from the concentration of economic power in the hands of index funds managers.

value is thought to have had a negative impact on employee welfare, with an increasingly smaller fraction of the firm's surplus being assigned to employees.[20]

Second, investment diversification offered by index funds and other similar investment vehicles made shareholders less risk averse. This increased tolerance toward risk translated into higher risk-taking by public firms. Higher risk-taking harms employees, as their firm-specific investments may not be easily redeployed elsewhere once the firm goes bankrupt.[21]

Finally, massive ownership concentration in the hands of few large institutional investors is thought to have stifled private investment and thus to have depressed demand in the labor market. Reduced demand in the labor market, in turn, would be at the root of current wage stagnation.[22]

However, there is also a bright side of the story. The increasing prominence of index funds in corporate governance may contribute to the improvement of worker conditions, as part of index funds' increasing pressure toward a more socially responsible behavior of investee companies.[23]

Importantly, index funds may have an interest in promoting worker welfare *beyond* what would be justified by a narrow firm-level cost-benefit calculus.[24] Index funds are stable, long-term shareholders holding a widely diversified portfolio. As such, in principle they are not interested in promoting actions that may increase the value of any particular stock (unless the weight of that stock is so large to significantly affect the value of the entire portfolio, a rather uncommon scenario). Rather, they are interested in actions that may increase overall portfolio value by either increasing returns of all portfolio firms or by reducing "systematic risks", namely risks that affect the entire portfolio.

Increasing worker welfare – in the form of, e.g., a generalized increase in wages or pensions – may have both effects. When offered by a sufficiently large number of firms, higher wages or pensions would increase aggregate demand and therefore increase firm profits throughout the economy. Consequently, also portfolio returns would increase. Furthermore, better labour conditions would reduce systematic risk by increasing social and political stability (e.g., via a reduction in income inequality and a curb on populism). So long as such gains outweigh the losses that portfolio firms experience because of a higher share of profits (net of any productivity increase) going to employees, index funds should be expected to side with employees.

[20] See *infra* section 2.1.
[21] See *infra* section 2.2.
[22] See *infra* section 2.3.
[23] See *infra* sections 3 and 4.
[24] It should also be noted that index funds usually do not possess the necessary firm-specific knowledge required to make that calculus. *See* Enriques L., Hansmann H., Kraaakman R., Pargendler M., *The Basic Governance Structure: Minority Shareholders and Non-Shareholder Constituencies*, in Kraakman R., Armour J., Davies P., Enriques L., Hansmann H., Hertig G., Hopt K., Kanda K., Pargendler M., Ringe W., Rockeds E. (eds.), *The Anatomy of Corporate Law: A Comparative and Functional Approach*, 3rd edn., Oxford: Oxford Univeristy Press, 2017, 107, for the general observation that "diversified institutional shareholders usually lack both the knowledge and the incentives necessary for […] interventions [aimed at advancing public good objectives at portfolio companies]". I argue that as far as portfolio-wide interventions are concerned, index funds may have sufficient incentives.

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2. Are index funds (and institutional investors more generally) responsible for wage stagnation, economic insecurity, and ultimately greater income inequality?

According to some accounts, share ownership concentration in the hands of large institutional investors might be among the factors that *contributed* to wage stagnation and the degradation of employment conditions more generally.

2.1. Stronger focus on shareholder value maximization as a result of ownership concentration.

As pointed out in section 1, institutional investors – and especially large index funds – own an increasingly large fraction of public equity. This process of ownership concentration – linked, among other causes, to the wide acceptance of portfolio theory[25] and the related concept of diversification as the guiding principle of investment strategy – had a profound impact on corporate governance.

First, ownership concentration mitigated the classic coordination problems affecting shareholders in widely-held companies,[26] making it easier for shareholders to discipline managers through the exercise of shareholder rights (mostly, via the statutory right to appoint and remove directors through a shareholder vote at the general meeting).[27] Today, the presence of large active shareholders in companies once characterized by high ownership dispersion makes it easier to win proxy fights and "vote no" campaigns against management at those companies.[28]

Second, shareholders' increased influence led to corporate governance reforms that removed a number of arrangements that contributed to insulating boards from that influence. One prominent example is the elimination of the staggered board, an arrangement that prevents shareholders from contemporaneously removing all board directors. [29] The effect of these reforms has been to increase director and manager exposure to shareholder pressures.

As a result of these changes, today's corporate governance environment is one in which shareholders have stronger influence over managers and may more easily hold them accountable for their actions.

[25] *See* Markowitz H., *Portfolio Selection*, in *Journal of Finance*, 7, 1, 1952, 77-91; Markowitz H., *Portfolio Selection: Efficient Diversification of Investments*, New Haven: Yale Univ. Press, 1971.
[26] *See*, e.g., Gordon J. N., *Is corporate governance a first-order cause of the current malaise?*, in *Jourmal of the British Academy*, 6, 1, 2018, 411.
[27] *See*, e.g., Gordon, nt. (26), 410, "A shift in public equity ownership from diffuse retail owners to asset managers and other institutional investors has empowered 'shareholders' and correspondingly reduced the autonomy of management).
[28] Emblematic in this respect is the Exxon Mobil case recalled *infra*, nt. (53) and accompanying text.
[29] The staggered board is commonly viewed as a powerful anti-takeover arrangement, capable of effectively insulating management from shareholder pressure. *See*, e.g., Bebchuk L., Coates J. C. IV, Subramanian G., *The Powerful Antitakeover Force of Staggered Boards: Theory, Evidence and Policy*, NBER Working Paper No. 8974, 2002, http://www.nber.org/papers/w8974.

In the view of some commentators, these corporate governance changes led public companies to focus more strongly on shareholder interests, and thus, as these interests are often epitomized, on the goal of share value maximization. [30]

This stronger focus on shareholder value may have had a negative impact on workers. This is mainly because in today's environment of tightened managerial accountability towards shareholders it is more difficult for firms to indulge in practices that sacrifice profits to cater to the interests of other firm constituencies.[31] Managers who indulge in such practices will be more easily replaced than in the past.

In such a corporate governance environment of strong shareholder primacy, workers' welfare will be improved only to the extent it benefits shareholders *by increasing shareholder value*. This is to say, for instance, that wages will be increased only if the benefits for shareholders, in terms of increased firm profitability due to higher worker productivity and loyalty, justify the costs. To the contrary, costly actions aimed at increasing workers' welfare will not be undertaken when the benefits are uncertain or certain but unable to outweigh the costs.

2.2. Diversification as risk-shifting from shareholders to employees.

Index funds and other similar investment vehicles, such as actively traded mutual funds, provide investors with effective, low-cost diversification. Diversification, in turn, affects shareholder preferences toward risk. More precisely, diversification increases shareholders' risk appetite.[32] Firm-specific risk, i.e., risk that pertains to any given firm, can be easily eliminated through diversification. A fully diversified investor bears only so-called "systematic risk", namely risk that affects the entire portfolio, and cares only about that type of risk.[33] Accordingly, diversified investors want their portfolio firms to invest in all projects having positive net present value with little concern over the possibility that if the investment turns out badly the firm may go bankrupt.[34] These are indeed firm-specific risks that can be diversified away.

[30] *See*, e.g., Gordon J. N., nt. (26), 410. To be sure, other factors might be at play in promoting "strong" shareholder primacy at public firms. *See*, e.g., Schwartz J., *De Facto Shareholder Primacy*, in Maryland Law Review, 79, 3, 2020, 652, pointing to securities laws and arguing that the transparency that such laws afford to the investing public allows hedge funds to easily "identify, and force companies to adopt, strategies that increase share prices".

[31] *See* Gordon J. N., nt. (26), 421, linking the decline of the "labour share" in corporate profits to the decreasing managerial "slack" induced by stronger corporate governance.

[32] *See*, e.g., Gordon J. N., nt. (26), 424, "Diversification means that shareholders will favour risk-taking by single firms".

[33] Systematic risks are risks that affect the entire economy. As such, they can't be hedged by holding a diversified portfolio. *See*, e.g., Coffee J. C., nt. (12), 619; Gordon J. B., *Systematic Stewardship* 2, ECGI Law Working paper No. 566, 2021, http://ssrn.com/abstract_id=3782814. Systematic risks include financial crises (as the one of 2008-09), climate change, or the outbreak of a pandemic. *See* Coffee J. C., nt. (12), 619-620, discussing climate change and the COVID-19 pandemic as examples of systematic risk.

[34] See Gordon J. B., nt. (33), 31, "investors would support firms/management teams that took the highest net present value business risks, even if failure was a possible outcome".

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Contrary to shareholders, however, employees made firm-specific investments that are difficult to diversify. Consequently, they suffer if their employing firm conforms to shareholders' preferences and takes on much risk. Indeed, as the company engages in riskier projects, employees are exposed to a higher risk of losing their jobs because of their firm's bankruptcy (or significant downsizing) due to the investments' failure in delivering the promised payout. Diversification can thus be viewed as a cause of increased employee insecurity.[35] Through diversification, shareholders effectively shift risk to employees.[36]

Furthermore, investor diversification indirectly affects the scope of the firm. Diversified investors dislike firm-level diversification, such as that provided by large conglomerate firms operating across several unrelated businesses. Instead, they prefer highly focused firms producing a relatively homogeneous set of products or services.[37] The reason is that firm-level diversification is more efficiently conducted by investors at the portfolio level rather than by managers at the firm level. Increased business focus, however, increases firm risk, negatively affecting employees and other stakeholders unable to diversify away that risk.[38]

2.3. Reduced investment as a consequence of common ownership.

Ownership concentration in the hands of few "mega" institutional shareholders holding significant blocks in most public firms is thought to reduce investments at public firms and with that job creation.[39] We observed in section 2.1 that share ownership concentration increases shareholder power vis-à-vis managers: the latter enjoy less discretion and are exposed to a higher risk of being fired for decisions that shareholders dislike.

Tighter managerial accountability towards shareholders has several benefits: managers, for instance, are discouraged from engaging in unfair self-dealing (e.g., awarding themselves excessive compensation)[40] or other opportunistic behavior, and from investing in

[35] *See* Gordon J. N., nt. (26), 423-4. Gordon J. N., *Addressing Economic Insecurity: Why Social Insurance Is Better Than Corporate Governance Reform*, in *The Columbia Law School Blue Sky Blog*, August 21, 2019, https://clsbluesky.law.columbia.edu/2019/08/21/addressing-economic-insecurity-why-social-insurance-is-better-than-corporate-governance-reform/.

[36] *See* Gordon J. N., nt. (35), "There's been a risk shift away from the shareholders, who now can and do diversify away all firm-specific and idiosyncratic risks, and toward employees and all the other stakeholders who benefit from and indeed depend on the existence and stability of particular corporations".

[37] Gordon J. B., nt. (33), 31.

[38] Gordon J. B., nt. (33), 31. *See* also Coffee J. C., nt. (12), 626-629, describing the role of activist hedge funds in promoting higher risk-taking and arguing that undiversified retail shareholders are also likely to lose from strategies aimed at increasing firm risk.

[39] *See* generally Goshen Z., Levit D., nt. (4). *See* also Gutiérrez G., Philippon T, *Investment-Less Growth: An Empirical Investigation*, NBER working paper No. 22897, 2016: https://www.nber.org/system/files/working_papers/w22897/w22897.pdf (providing empirical evidence consistent with this hypothesis).

[40] For a discussion of the problem of managerial self-dealing, or conflict of interest, from a comparative law and economics perspective, *see* generally Enriques L., *The Law on Company Directors' Self-Dealing: A Comparative Analysis*, in *International and Comparative Corporate Law Journal*, 2, 3, 2000, 297.

unprofitable projects that waste corporate resources (e.g., "empire building", namely expanding the size of the firm beyond its optimal level).[41]

At the same time, however, tighter managerial accountability discourages managers from investing in profitable but hard-to-understand projects (typically, projects having a long-term horizon or characterized by a high inherent complexity), for fear of being disciplined or dismissed by a shareholder base with high power but insufficient firm-specific knowledge.[42] Put differently, in a corporate governance system strongly tilted toward shareholders, managers have weak incentives to develop projects that, because of their inherent complexity, innovative character, or long-term horizon, investors may not fully understand.[43]

According to this view, the ultimate effect of ownership concentration is a significant reduction in corporate investments. Indeed, because of the ensuing stronger shareholder influence over corporate managers, a larger number of both unprofitable (inefficient) and profitable (efficient) projects will be forgone.[44] Lower corporate investment leads to less new jobs being created and thus to lower demand in the labor market. Reduced demand in the labor market, in turn, depresses wages.[45]

3. May institutional investors – and especially index funds – improve worker conditions?

Section 2 showed that ownership concentration and the ensuing changes in corporate governance may be among the causes of poor labor conditions. However, there is also a flip side of the coin. There is reason to believe that the ascent of index funds as key corporate governance players might *improve* worker conditions and ultimately grant workers a larger share of the firm surplus.

Apparently, large index funds give significant weight to non-shareholder interests. In its much-discussed 2018 letter to CEOs of investee companies, Larry Fink, BlackRock's CEO, declared that "[t]o prosper over time, every company must not only deliver financial performance, but also show how it makes a positive contribution to society. Companies must benefit all of their stakeholders, including shareholders, employees, customers, and the communities in which they operate".[46]

41 *See*, e.g., Romano R., *A Guide to Takeovers*, in *Yale Journal on Regulation*, 9, 1992, 148, considering empire-building a manifestation of managerial self-aggrandizement and including it among the inefficient, agency-cost driven motives for takeovers.
42 Recent scholarship stresses the negative governance implications of shareholder error (and bad faith) in assessing managerial strategy. *See* generally Goshen Z., Squire R., *Principal Costs: A New Theory for Corporate Law and Governance*, in *Columbia Law Review*, 117, 767, 2017.
43 Goshen Z., Levit D., nt. (4), 6.
44 Goshen Z., Levit D., nt. (4), 6.
45 Goshen Z., Levit D., nt. (4), 5. The Authors also note that "[b]ecause shareholders tend to be wealthier than wage-earners, this process not only causes wages to stagnate but also exacerbates income inequality".
46 *See* Fink L., *A Sense of Purpose*, in *Harvard Law School Forum on Corporate Governance*, January 17, 2018, https://corpgov.law.harvard.edu/2018/01/17/a-sense-of-purpose/.

Index funds attention toward stakeholder interests is further witnessed by their strong focus on "ESG" (environmental, social and governance) issues at portfolio companies.[47] In the U.S. and elsewhere, initiatives aimed at addressing ESG issues dominate index funds activism and engagement at publicly traded firms.[48]

Interestingly, there is also mounting evidence that institutional investors' ESG engagements produce real effects. Two recent empirical studies, conducted with different methodologies, find correlations between institutional ownership and portfolio firms' corporate social responsibility performance.[49] Another recent study finds a robust negative correlation between institutional ownership by "The Big Three" and carbon emissions of investee companies.[50] Thus, institutional investors' attention toward stakeholder interests appears capable of influencing corporate action and inducing more responsible behavior in investee companies.

So far, index funds (and other ESG-minded investors) appear to have mostly focused on the "E" and "G" of ESG, namely on environmental and governance issues.

Climate change is currently at the centerstage of investor activism. Institutional investors are increasingly putting pressure on companies to reduce their "carbon footprint" (i.e., their greenhouse gas emissions), in an attempt to fight global warming. These pressures already produced some resounding victories, such as the much-publicized defeat of Exxon Mobil's management at the 2021 annual election of the company's board. Thanks to the support of large index funds, the small activist hedge fund Engine No. 1 managed to appoint three directors to the board of Exxon Mobil, the U.S. largest oil & gas company[51] and one of the largest carbon emitters,[52] in an attempt to accelerate the company's transition toward decarbonization.[53]

[47] ESG investing is a burgeoning phenomenon, with an increasing amount of investor money flowing into ESG funds and other "sustainable investing" initiatives. *See*, e.g., Martin M., *ESG: A Trend We Can't Afford to Ignore*, in *Financial Times*, November 26, 2020, https://www.ft.com/content/87a922a1-8d60-4295-a9d8-d2c1ab5d788e, reporting that according to a 2020 study by the U.S. SIF foundation "roughly one of three dollars invested in the U.S. […] has a sustainable mandate".

[48] As reported in a recent article by Professors Dorothy Lund and Elizabeth Pollman, citing data from The Conference Board, "during the 2019 proxy season, more than half of the shareholder proposals brought involved ESG issues, including topics such as disclosing climate change risk and increasing board diversity". *See* Lund D. S., Pollman E., *The Corporate Governance Machine* 38, ECGI Law Working Paper No. 564, 2021, http://ssrn.com/abstract_id=3775846.

[49] *See* Dyck A., Lins K. V., Roth L., Wagner H. F., *Do institutional investors drive corporate social responsibility? International evidence*, in *Journal of Financial Economics*, 131, 3, 2019, 693-714, finding, among other things, that "institutional ownership is positively associated with E&S performance"; Chen T., Dong H., Lin C., *Institutional shareholders and corporate social responsibility*, in *Journal of Financial Economics*, 135, 2020, 485, finding, among other things, that "exogenous increases in institutional ownership lead to better CSR ratings".

[50] Azar J., Duro M., Kadach I., Ormazabal G., *The Big Three and corporate carbon emissions around the world*, in *Journal of Financial Economics*, 142, 2, 2021, 674-696.

[51] *See* Sönnichsen N., *Leading U.S. oil and gas producers based on market cap October 2021*, in *Statista*, October 4, 2021, Exxon Mobil ranks first among top U.S. oil producers by market capitalization, with a market cap of $ 257.95 bn.

[52] According to recent estimates elaborated by the Climate Accountability Institute, Exxon Mobil ranks among the world's top four carbon emitters throughout the 1965-2017 period. *See* https://climateaccountability.org/carbonmajors.html.

[53] *See* Phillips M., *Exxon's Board Defeat Signals the Rise of Social-Good Activists*, in *N.Y. Times*, June 9, 2021, https://www.nytimes.com/2021/06/09/business/exxon-mobil-engine-no1-activist.html.

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Governance issues, such as the proper composition of the board of directors (also with respect to aspects, such as gender and race diversity and inclusion, with a clear social connotation), have similarly received widespread attention and have been the object of many engagement campaigns.

Instead, social issues (the "S" of ESG), including employee conditions, seemingly received less attention. Yet anecdotal evidence suggests that the "S" of ESG – and labor-related issues more specifically – may quickly get at the centerstage of investor activism.

In its 2019 letter to CEOs, Larry Fink, Blackrock's CEO, put retirement issues under the spotlight, declaring that "companies must embrace a greater responsibility to help workers navigate retirement".[54]

Recently, a number of large institutional investors and financial institutions have formed the Platform Living Wage Financials (PLWF), an "investor coalition [of 18 financial institutions] with over €4.6 trillion of Assets Under Management and advice" "that encourages and monitors investee companies to address the non-payment of living wage in global supply chains". [55]

Drawing on this and other indications, observers argue that labor conditions will soon be at the forefront of shareholder engagement, with more shareholder proposals on human capital management[56] and on the offering of a "living wage" to employees.[57]

4. Why should institutional investors care about employee welfare?

Institutional investors' attention toward stakeholder interests raises the obvious question why such investors care about these interests at all.

Let us consider employee welfare. Why index fund managers – who represent the interests of shareholders and owe precise fiduciary duties toward their funds' investors[58] – should be willing to accept lower corporate profits (and therefore reduced portfolio returns) in order to increase employee welfare? After all, index funds are profit-seeking investors and rational profit-seeking investors are expected to prioritize shareholder interests (i.e., their own interest in share value maximization) over conflicting stakeholder interests.

One rather intuitive answer, sometimes referred to as the "doing well by doing good" or "enlightened shareholder value"[59] rationale, is that taking care of those interests maximizes

[54] *See* Fink L., *Purpose and Profit*, in *Harvard Law School Forum on Corporate Governance*, January 23, 2019, https://corpgov.law.harvard.edu/2019/01/23/purpose-profit/.
[55] This is how PLWF describes itself in its website. *See* https://www.livingwage.nl (last visited October 29th, 2021).
[56] *See* also e.g., https://www.conference-board.org/webcast/ondemand/Governance-Watch-July-2020.
[57] *See* Michael W. Peregrine, *A Living Wage: The Latest ESG Challenge for Corporate Governance*, HARV. L. SCH. FORUM ON CORP. GOV. (April 13, 2021), https://corpgov.law.harvard.edu/2021/04/13/a-living-wage-the-latest-esg-challenge-for-corporate-governance/.
[58] *See* generally Schanzenbach M.M., Sitkoff R. H., *Reconciling Fiduciary Duty and Social Conscience: The Law and Economics of ESG Investing by a Trustee*, in *Stanford Law Review*, 72, 2020, 381.
[59] *See*, e.g., Bebchuk L., Tallarita R., *The Illusory Promise of Stakeholder Governance*, in *Cornell Law Review*, 106, 2020, 108-110.

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long-term shareholder value.[60] For instance, improving labor conditions may help attract or retain the most talented individuals and may increase workforce productivity and employee loyalty, thus increasing long-term firm profits.[61] Obviously, according to this rationale index funds and other institutional investors would agree to favor stakeholder interests only to the extent the long-term gains outweigh the costs (i.e., up to the point at which the marginal cost of providing further benefits to stakeholders equals the marginal gain). Intuitively, according to this rationale investor willingness to advance stakeholder interests should be rather limited when the relevant costs are high relative to the benefits. This is likely the case of significant and generalized wage increases: the relevant expenditures may not be justified by the long-term gains deriving from increased employee productivity (especially when less expensive and equally effective techniques, like controls and the threat of being fired, are available) or loyalty.[62]

Another answer might be found in agency theory.[63] In promoting stronger care of stakeholder interests at investee companies, index fund managers might be advancing their personal social or ethical preferences (or maybe some kind of personal political agenda) against their investors' interest. The agent here (the index fund manager) would thus be acting in a way that maximizes her own utility function, rather than that of the principal (the fund investors). However, we already noted that asset managers owe fiduciary duties toward their investors.[64] Investment strategies that knowingly reduce portfolio value to advance societal interests violate those duties.[65] Note that index funds' clients may often be themselves workers who save for retirement:[66] ironically, promoting corporate strategies that reduce profits to advance labor interests would backfire on those interests, as workers who are saving for retirement would be harmed.[67]

[60] For a broader discussion of the idea that serving stakeholder interests may be instrumental to shareholder value maximization *see*, e.g., Bebchuk L., Tallarita R., nt. (59), 108-114.

[61] This general observation is shared by many commentators: *see*, e.g., Bebchuk L., Tallarita R., nt. (59), 109, noting that "how the company treats employees could well affect its ability to attract, retain, and motivate the members of its labor force". *See* also Edmans A., *The Link Between Job Satisfaction and Firm Value, With Implications for Corporate Social Responsibility*, in *Academy of Management Perspectives*, 26, 4, 2012, 1-19, providing empirical evidence supporting the idea that employee job satisfaction increases firm value.

[62] Another case in point is that of costly investments in green technologies: these investments may not be justified by the long-term gains from, e.g., reduced exposure to sanctions or improved standing among consumers. Furthermore, as we noted in nt. (24), index funds and other broadly diversified institutional investors are unlikely to engage in this kind of firm-specific cost-benefit calculations, as they often require deep firm-specific knowledge that those investors usually do not possess.

[63] *See* generally Jensen M. C., Meckling W. H., *Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure*, in *Journal of Financial Economics*, 3, 4, 1976, 305.

[64] *See* nt. (58) and accompanying text.

[65] *See* Schanzenbach M.M., Sitkoff R. H., nt. (58), 385-386, arguing that under U.S. law "ESG investing is permissible for a trustee of a pension, charity, or trust […] if: (1) the trustee reasonably concludes that the ESG investment program will benefit the beneficiary directly by improving risk-adjusted return; and (2) the trustee's exclusive motive for adopting the ESG investment program is to obtain this direct benefit.".

[66] It is a commonplace observation that index funds attract an increasing number of retail investors, who in turn are often themselves workers: *see*, e.g., Fisch, J., Hamdani A., Solomon S. D., nt. (14), 19; Coffee J.C., nt. (12), 608.

[67] Thus, it is no surprise that the U.S. Department of Labor more than once stressed that pension plan fiduciaries are not allowed to sacrifice returns or increase investment risks to promote "social policy goals". *See* Schanzenbach M.M., Sitkoff R. H., nt. (58), 407.

There might also be a "marketing story" beyond institutional investors' attention towards ESG issues. Younger investors, such as millennials, are generally more sensitive towards environmental problems and the social responsibility of businesses, relative to older investors.[68] Like all investors, they tend to prefer investment products that reflect their individual preferences and thus that variously incorporate environmental, social and governance considerations into the investment process. Large asset managers wish to attract these investors, who will soon inherit the wealth of previous generations.[69] Promoting more sustainable behavior at investee companies might be a strategy to attract and retain these customers.[70]

Another explanation of index fund attention toward ESG can be found in the mechanics of "portfolio primacy".[71] "Portfolio primacy", as opposed to shareholder primacy, refers to the idea that index fund managers seek to maximize the value of the entire portfolio, rather than that of any specific stock comprised in it.

An important implication of this intuition is that index funds are expected to internalize inter-firm externalities. When share value maximization at one set of portfolio firms produces negative externalities at another set of portfolio firms and such externalities are larger than the gains obtained by the firms producing the externality, index funds have a rational incentive in promoting actions that in reducing the externality may also reduce the value of the shares of the externality-imposing firms. Indeed, an action of this type maximizes portfolio value, since the benefits of reducing or eliminating the externality outweigh the costs.

The externality-internalization theory has been advanced to explain index funds activism against climate change.[72] Actions addressed at accelerating decarbonization and transition to green energy production at large fossil fuel companies (such as the one targeted at Exxon Mobil recalled above)[73] or aimed at reducing greenhouse gas emissions from "big polluters"[74] can be viewed as a strategy to induce such companies to internalize the costs that their business imposes to other companies (and the larger economy).

Portfolio primacy also implies that index funds will care about systematic, rather than firm-specific or "idiosyncratic", risk.[75] We already noted that diversification allows investors

[68] *See* Barzuza M., Curtis Q., Webber D. H., *Shareholder Value(s): Index Fund ESG Activism and the New Millennial Corporate Governance*, in*Southern California Law Review*, 93, 2020, 1250, 1291-1303.
[69] This wealth shift is expected to be sizable: *see* Tett G., *Millennial Heirs to Change Investment Landscape*, in *Financial Times*, September 20 2018, citing studies by US Trust and Deloitte respectively estimating that in the U.S. $12 trillions and $24 trillions will be passed on to millennials by baby boomers and other older generations in the next years.
[70] *See* Barzuza M., Curtis Q., Webber D. H., nt. (68), 1250, "Using their voting power to promote their investors' social values, and doing so publicly and loudly, is a way for [index] funds […] to give millennial investors a reason to choose them".
[71] *See* Coffee J. C., nt. (12), 604-5.
[72] *See* generally Condon M., *Externalities and the Common Owner*, in *Washington Law Review*, 95, 2020.
[73] *See* nt. (51)-(53) and accompanying text.
[74] *See* Taylor M., Watts J., *Revealed: The 20 Firms Behind A Third Of All Carbon Emissions*, in *The Guardian*, October 9, 2019, https://www.theguardian.com/environment/2019/oct/09/revealed-20-firms-third-carbon-emissions, citing recent research documenting that just 20 companies "have contributed to 35% of all energy-related carbon dioxide and methane worldwide".
[75] *See* generally Gordon J. B., nt. (33).

to hedge against firm-specific risks but not against systematic risk. As long-term holders of a fully diversified portfolio that in many respects mirrors the entire economy, index funds have strong incentives in promoting actions that reduce systematic risk and foster economic growth at the macro level. Indeed, both actions would improve portfolio performance.

Index funds environmental activism can also be thought of as a strategy of systematic risk reduction.[76] Climate change is a type of systematic risk, as its negative effects are deemed to affect the entire economy.[77] Inducing large fossil fuel producers and other "big polluters" to cut carbon emissions (also via actions that reduce firm profits) can be viewed as a strategy to curb systematic risk and thus to improve portfolio risk-adjusted returns.

Importantly, actions aimed at improving employee welfare in portfolio firms might also fit this framework.

First, an economy-wide improvement of worker conditions might increase portfolio long-term returns by promoting long-term economic growth. Higher wages increase employee income and therefore consumption.[78] Similarly, better retirement terms increase consumption by reducing uncertainty and therefore inducing employees to assign a larger share of their income to consumption. Increased consumption, in turn, would increase aggregate demand and therefore corporate profits. To be sure, portfolio returns might decrease in the short term because of a higher fraction of firm profits going to employees. However, this short-term negative effect might eventually be offset by the larger long-term returns generated by higher consumption and stronger economic growth.

Second, an economy-wide improvement of worker conditions might reduce systematic risk and thus increase portfolio *risk-adjusted* returns.[79] Improved worker conditions are likely to reduce socio-economic risks that – as other types of systematic risk – might affect the entire economy.[80] Better working conditions increase overall social stability by reducing income inequality – a powerful source of social discontent – and economic insecurity. By reducing poverty via the offering of decent (living) wages, other sources of socio-economic instability, such as poverty-related crime, are also likely to be alleviated. Improved worker conditions are also capable of delivering greater political stability, reducing the type of social discontent that fuels populism and other destabilizing political movements.

A similar rationale might also underlie actions aimed at improving racial and gender diversity and inclusion in the workplace. Indeed, a corporate system that does not promote (or even hinder) diversity and inclusion might subject itself to political risks (such as that of invasive and overreaching regulatory intervention).[81]

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[76] *See* Gordon J. B., nt. (33), 3.
[77] *See* Condon M., nt. (72), 6 citing research showing that unchecked increases in global temperatures may have "a devastating effect on the world economy".
[78] This is especially true for low-income workers, since it is more likely that any extra-income earned by them will go to consumption rather than to savings.
[79] *See* Gordon J. B., nt. (33), 3, for the general observation that reducing systematic risk improves portfolio risk-adjusted returns.
[80] *See* Gordon J. B., nt. (33), 30-33, classifying social stability risk caused by worker economic insecurity as a form systematic risk that index funds might be willing to address.
[81] *See* Coffee J. C., nt. (12), 620-621, "If our corporate system cannot offer inclusiveness and promote diversity, it may subject itself to a political risk that capitalism (or, at least, contemporary corporate governance) will be politically challenged and could conceivably yield to a more state-run system of corporate governance."

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Index fund managers appear to be conscious of the impact of poor worker treatment on systematic risk. In his 2019 letter to CEOs, Blackrock's CEO Larry Fink affirmed that "[workers'] lack of preparedness for retirement is fueling enormous anxiety and fear, undermining productivity in the workplace and amplifying populism in the political sphere. In response, companies must embrace a greater responsibility to help workers navigate retirement, lending their expertise and capacity for innovation to solve this immense global challenge. In doing so, companies will create not just a more stable and engaged workforce, but also a more economically secure population in the places where they operate". [82]

Index fund managers thus seemingly know that inadequate retirement programs are not only a source of reduced profitability for the employing firm (in the form of reduced workforce productivity), but also a source of systematic risk, in the form of political instability.

Thus, the logic of portfolio primacy might eventually produce a positive impact on worker conditions. For the reasons briefly outlined above, index funds appear rationally interested in the promotion of strategies that improve employee welfare also beyond what firm-level cost-benefit calculations would justify. Indeed, index funds (and other largely diversified investors) may accept (and perhaps actively promote) improvements in workers' welfare that shift value from shareholders to employees in the short run to the extent the positive macro-economic effects associated with those improvements may generate long-term returns and a reduction in systematic risk that outweigh those losses.

5. What about controlled firms?

However, a significant limit to index fund activism comes from the presence of controlling shareholders in investee companies.

Most public companies outside the U.S. and the U.K. have controlling shareholders, typically families or the State.[83] Where there is a controlling shareholder, there are good reasons to expect that institutional investors' ability to affect corporate policy be low or at least not as effective as in companies without controlling shareholders.[84]

[82] *See* Fink L., nt. (54).

[83] *See*, e.g., Gutiérrez M., Sáez Lacave M. I., *Strong Shareholders, Weak Outside Investors*, in *Journal of Corporate Law Studies*, 18, 2, 2018, 279, showing that in continental Europe listed firms with a controlling shareholders account for more than half of all listed firms, except for Sweden and Finland. *See* also generally Aminadav G., Papaioannou E., *Corporate Control Around the World* 1, NBER Working Paper No. 23010, Dec. 2016, finding that the share of controlled firms is high in civil law countries relative to common law countries.

[84] With respect to index fund activism *see*, e.g., Gozlugol A. A., *Controlling Shareholders: Missing Link in the Sustainability Debate?*, in *Oxford Business Law Blog*, July 16, 2021, https://www.law.ox.ac.uk/business-law-blog/blog/2021/07/controlling- shareholders-missing-link-sustainability-debate; Dharmapala D., Khanna V.S., *Controlling Externalities: Ownership Structure and Cross-Firm Externalities*, ECGI Law Working Paper N° 603, 2021, https://ssrn.com/abstract=3904316. This is not to say that institutional investor activism is totally missing in controlled firms. Professor Kobi Kastiel, for instance, documents the existence of hedge funds activism in U.S. controlled companies. *See* Kastiel K., *Against All Odds: Hedge Fund Activism in Controlled Companies*, in *Columbia Business Law Review*, 2016, 60.

Controlling shareholders are mostly under-diversified, where not totally undiversified.[85] Therefore, they are likely to oppose any strategy of externality-internalization (such as those aimed at accelerating decarbonization at large fossil fuel companies).[86] If a given corporate action or strategy imposes negative externalities on other firms (or on the entire economy, in the form of systematic risk) but is profitable, the firm's controlling shareholder is expected to support that action and to oppose any initiative aimed at blocking or changing it.[87] Indeed, as an undiversified investor with most of his wealth invested in the firm, she does not bear the costs of the externality produced by her firm.

However, economy-wide improvements of employee welfare do not follow a logic of externality-internalization. The goal is not to induce some firms to undertake value-reducing actions that would increase overall portfolio value by eliminating or limiting the negative externality that those firms impose on other firms. Rather, the goal is to promote coordinated behavior among portfolio firms that might produce benefits for each of them via improvements at the macro-economic level.

As we hinted at in section 4, portfolio firms as a group might gain from a general (economy-wide) improvement of worker conditions to the extent such improvement yields a net increase in firm-level profits as a consequence of increased aggregate demand and improves each firm's prospects by reducing systematic risk.[88] Clearly, however, no single firm will autonomously undertake any initiative in this direction. For firms operating in competitive markets, unilateral actions aimed at improving worker conditions would likely undermine the firm's position in the product market.[89] The firm will either be forced to raise prices or to impinge on shareholders' hardly earned competitive profits, impairing the firm's ability to sell its products or raise new capital.[90] In addition, any unilateral action will likely be unable to affect demand at the macro level and therefore will likely be unable to induce any increase in long-term profitability.[91] To the contrary, coordinated action will have smaller adverse effects on the single firm's competitive position (since it will be more likely that also rival firms will undertake the same action) and stronger efficacy in producing beneficial macro effects.

As "common owners" with significant equity stakes in most public firms, index funds may act as coordinating agents of such firms.[92] Controlling shareholders might not oppose

[85] *See* most recently Dharmapala D., Khanna V.S., nt. (84), 5.

[86] *See* nt. (51)-(53) and accompanying text.

[87] *See* Gozlugol A. A., nt. (84), "Although [controlling shareholders] can be long-term value-maximisers, they are also likely to impose negative externalities if profitable".

[88] As risk that affects all the economy, systematic risk negatively affects also most individual firms. Thus, most of the times an undiversified shareholder such as a controlling shareholder would be rationally interested in promoting actions that mitigate such risk.

[89] *See* Roe M. J., *Corporate Purpose and Corporate Competition* 2, ECGI Law working paper No. 601, 2021, 11-12.

[90] Roe M. J., *ibid.*

[91] As we already pointed out (*see* supra section 2.1), in the absence of coordination firms will undertake actions that improve worker welfare only to the extent those actions maximize share value (e.g., by increasing employee productivity).

[92] Disclosure mandates on labor conditions in publicly-traded firms, like those currently provided by securities regulation as part of "ESG" reporting (*see*, e.g., the provisions of the Directive 2014/95/EU of the European Parliament and of the Council of 22 October 2014, amending Directive 2013/34/EU as regards disclosure of

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these initiatives, since they are not addressed uniquely at their firms but at all portfolio firms. As such, strategies aimed at improving labor conditions across the board may not encounter the same fierce opposition that strategies of externality-internalization might encounter.

The presence of a controlling shareholder might also bring about benefits of its own to the firm's employees.

First, controlling shareholders are likely to effectively counteract index funds' appetite toward risk,[93] decreasing risk at firm level to the benefit of employees. As undiversified investors with most of their wealth invested in the firm, controlling shareholders are naturally more risk averse than fully diversified investors. Such a higher risk aversion would induce controllers to run their firms more prudently. This more conservative behavior, in turn, would increase employee welfare since it would indirectly increase job security.[94]

Second, in many controlled firms the State is the (direct or indirect) controlling shareholder.[95] Where the State is the controlling shareholder, one might expect a higher propensity to support (or at least not to oppose) actions aimed at internalizing negative externalities and, more generally, advancing non-shareholder interests, especially when those interests are politically salient.[96] Note, however, that the State as controlling shareholder may also act differently. Politicians (those who ultimately shape corporate policy at State-controlled firms) may not care about harmful corporate externalities or corporate socially responsible behavior because of their political orientation (a number of prominent political leaders, for instance, believe that climate change is not a major problem and acted accordingly),[97] or because their action is driven by other concerns (a mercantilist approach to global trade, for example, suggests disregarding corporate externalities and even domestic workers' welfare in order to gain market share in world trade and increase the country's economic influence).

non-financial and diversity information by certain large undertakings and groups), might help index funds in this respect, to the extent they provide useful, standardized (and thus comparable) firm-level information.

[93] As we pointed out in section 2.2, diversification increases shareholder appetite toward risk by allowing shareholders to hedge against firm-specific risk.

[94] Note, however, that to the extent this more conservative behavior negatively affects the firm's competitive position (e.g., by retarding efficient investments), it may harm employees in the long run, as the company may ultimately be outcompeted by more efficient rivals.

[95] *See*, e.g., De La Cruz A., Medina A., Tang Y., *Owners of the World's Listed Companies*, in *OECD Capital Market Series*, 5, 26, 2019, www.oecd.org/corporate/Owners-of-the-Worlds-Listed-Companies.htm (documenting that the public sector is the second largest category of owner of publicly traded firms around the world, holding 14% of the global market capitalization, and that it owns *de iure* or *de facto* control stakes in almost 1.200 of the 10.000 firms considered in the study.

[96] This might well be the case of labor interests, at least in some countries.

[97] One of them is former U.S. President Donald Trump, who weakened or rolled back a number of U.S. environmental regulations (*see* Gross S., *What is the Trump administration's track record on the environment?* , in *The Brookings*, August 4, 2020, https://www.brookings.edu/policy2020/votervital/what-is-the-trump-administrations-track-record-on-the-environment/) and, most notoriously, withdrew the United States from the 2016 Paris Climate Agreement (*see* Friedman L., *Trump Serves Notice to Quit Paris Climate Agreement*, in *The N.Y. Times*, November 4, 2019 (Updated February 19, 2021: https://www.nytimes.com/2019/11/04/climate/trump-paris-agreement-climate.html).

6. Conclusion.

In the last decades, public capital markets and the corporate governance of publicly traded firms have undergone deep transformations. Direct retail investment has largely vanished from public securities markets and has been substituted by "intermediated" investment. Investing is now largely "indexed", meaning that investors increasingly resort to passive investment vehicles tracking market indexes, such as index funds. Share ownership is increasingly amassing vie these vehicles in the hands of few large asset managers – "The Big (and prospectively "Giant")[98] Three": BlackRock, Vanguard, and State Street Global Advisors.

In the view of some commentators, these transformations played a role in the degradation of labor conditions in developed countries. First, ownership concentration led to a corporate governance model more strongly focused on shareholder interests. This stronger focus on shareholder interests, in turn, negatively affected employees and other firm stakeholders having conflicting interests. Second, increased diversification on the part of shareholders prompted higher risk-taking at investee firms, decreasing job security at those firms. Finally, share ownership concentration reduced corporate investments, stifling demand in the labor market and consequently contributing to wage stagnation.

At the same time, however, these transformations may have laid the foundations for a corporate governance system more supportive of worker welfare. As stable, long-term shareholders with a widely diversified portfolio, index funds have an interest in supporting actions that minimize systematic risks (since doing so improves portfolio risk-adjusted returns) and that spur economic growth (since doing so is likely to increase the performance of all portfolio firms and therefore to increase portfolio returns). Improving worker conditions may both reduce systematic risk, by reducing social tensions and leading to greater political stability, and promote economic growth, by sustaining aggregate demand. Index funds may thus actively promote corporate policies aimed at improving worker conditions, as anecdotal evidence already seems to suggest.

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[98] *See* Bebchuk L., Hirst S., nt. (11).

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