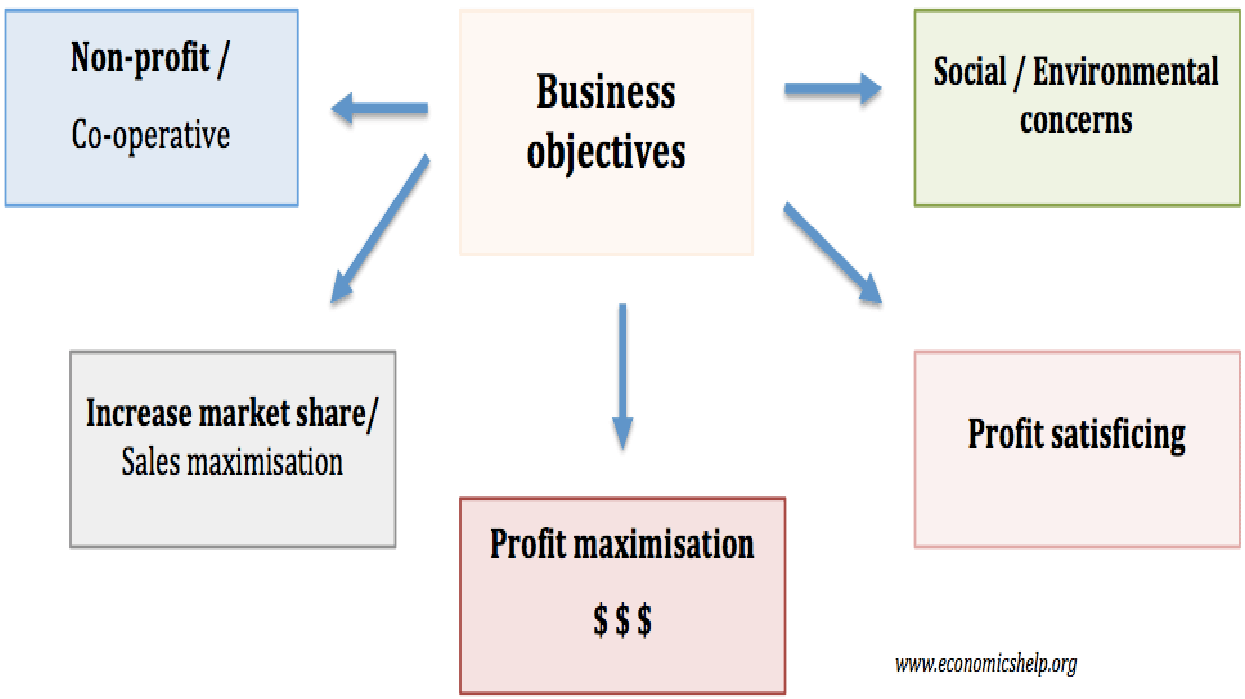
Economic objectives of firms

The main objectives of firms are:

- Profit maximisation
- Sales maximisation
- Increased market share/market dominance
- Social/environmental concerns
- Profit satisfying
- Co-operatives.

Sometimes there is an overlap of objectives. For example, seeking to increase market share, may lead to lower profits in the short-term, but enable profit maximisation in the long run.



Profit maximisation

Usually, in economics, we assume firms are concerned with maximising profit. Higher profit means:

Higher dividends for shareholders.

More profit can be used to finance research and development.

Higher profit makes the firm less vulnerable to takeover.

Higher profit enables higher salaries for workers

Alternative aims of firms

However, in the real world, firms may pursue other objectives apart from profit maximisation.

Profit Satisficing:

- In many firms, there is a separation of ownership and control. Those who own the company (shareholders) often do not get involved in the day to day running of the company.
- This is a problem because although the owners may want to maximise profits, the managers have much less incentive to maximise profits because they do not get the same rewards, (share dividends)
- Therefore managers may create a minimum level of profit to keep the shareholders happy, but then maximise other objectives, such as enjoying work, getting on with other workers. (e.g. not sacking them) This is the problem of separation between owners and managers.
- This ‘principal-agent‘ problem can be overcome, to some extent, by giving managers share options and performance related pay although in some industries it is difficult to measure performance.
- More on profit-satisficing.

2. Sales maximisation

Firms often seek to increase their market share – even if it means less profit. This could occur for various reasons:

- Increased market share increases monopoly power and may enable the firm to put up prices and make more profit in the long run.
- Managers prefer to work for bigger companies as it leads to greater prestige and higher salaries.
- Increasing market share may force rivals out of business. E.g. the growth of super markets have lead to the demise of many local shops. Some firms may actually engage in predatory pricing which involves making a loss to force a rival out of business.

3. Growth maximisation

This is similar to sales maximisation and may involve mergers and takeovers. With this objective, the firm may be willing to make lower levels of profit in order to increase in size and gain more market share. More market share increases their monopoly power and ability to be a price setter.

4. Long run profit maximisation

In some cases, firms may sacrifice profits in the short term to increase profits in the long run. For example, by investing heavily in new capacity, firms may make a loss in the short run but enable higher profits in the future.

5. Social/environmental concerns

A firm may incur extra expense to choose products which don't harm the environment or products not tested on animals. Alternatively, firms may be concerned about local community / charitable concerns.

- Some firms may adopt social/environmental concerns as part of its branding. This can ultimately help profitability as the brand becomes more attractive to consumers.
- Some firms may adopt social/environmental concerns on principal alone – even if it does little to improve sales/brand image.

6. Co-operatives

Co-operatives may have completely different objectives to a typical PLC. A co-operative is run to maximise the welfare of all stakeholders – especially workers. Any profit the co-operative makes will be shared amongst all members.