What BlackRock, Vanguard and State Street Are Doing to the Economy

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When I got on the phone with Vivek Ramaswamy on Tuesday afternoon, I was not expecting to find common cause. Ramaswamy is a tech entrepreneur, a frequent contributor to conservative outlets including The Wall Street Journal's editorial page and the author of a book whose very title sounds as if it were formulated in a lab at Fox News to maximally tickle the base and trigger the libs: "Woke, Inc.: Inside Corporate America's Social Justice Scam."

I'd reached out to Ramaswamy to discuss his new venture, Strive Asset Management, an investment firm that he says will urge corporations to stay out of politics. Among Strive's funders, though, is one of the more politically active people in business, Peter Thiel, the billionaire venture capitalist who supported Donald Trump and is now funding a slate of Trump-loving congressional candidates.

It turned out I was right: I did not agree with a lot of what Ramaswamy had to say. Not only are our politics radically at odds, we also differ on what "politics" means in modern American capitalism. Yet despite our disagreements, something odd happened. I found myself nodding along with what is perhaps Ramaswamy's fundamental point: that three gigantic American asset management firms — BlackRock, Vanguard and State Street — control too much of the global economy.

The firms manage funds invested by large institutions like pension funds and university endowments as well as those for companies and, in some cases, individual investors like me and perhaps you, too. Their holdings are colossal. BlackRock manages nearly $10 trillion in investments. Vanguard has $8 trillion, and State Street has $4 trillion. Their combined $22 trillion in managed assets is the equivalent of more than half of the combined value of all shares for companies in the S&P 500 (about $38 trillion). Their power is expected to grow. An analysis published in the Boston University Law Review in 2019 estimated that the Big Three could control as much as 40 percent of shareholder votes in the S&P 500 within two decades.

Why is this a problem? Ramaswamy argues that the main issue is that the firms are using their heft to push companies in which they hold large investments into adopting liberal political positions — things like focusing on climate change or improving the diversity of their work force. I think that's a canard, as I'll explain below.

The real danger posed by the three is economic, not political. The American economy is lumbering under monopoly and oligopoly. In many industries, from airlines to internet advertising to health care to banks to mobile phone providers, Americans can do business with just a handful of companies. As the journalist David Dayen has argued, this increasing market concentration reduces consumer choice, raises prices and most likely harms workers.

BlackRock, Vanguard and State Street have been extraordinarily good for investors — their passive-investing index funds have lowered costs and improved returns for millions of people. But their rise has come at the cost of intense concentration in corporate ownership, potentially supercharging the oligopolistic effects of already oligopolistic industries.

John Coates, a professor at Harvard Law School, has written that the growth of indexation and the Big Three means that in the future, about a dozen people at investment firms will hold power over most American companies. What happens when so few people control so much? Researchers have argued that this level of concentration will reduce companies' incentives to compete with one another. This makes a kind of intuitive sense: For example, because Vanguard is the largest shareholder in both Ford and General Motors, why would it benefit from competition between the two? If every company is owned by the same small number of people, why fight as fiercely on prices, innovations and investments?

Indeed, there is some evidence that their concentrated ownership is associated with lower wages and employment and is already leading to price increases in some industries, including in airlines, pharmaceuticals and consumer goods. The firms dispute this. In a 2019 paper, Vanguard's researchers said that when they studied lots of industries across a long period of time, "we do not find conclusive evidence" that common ownership led to higher profits.

But if the Big Three keep growing, the effects of their concentrated ownership will get only worse. Einer Elhauge, also of Harvard Law School, has written that concentrated ownership "poses the greatest anticompetitive threat of our time, mainly because it is the one anticompetitive problem we are doing nothing about."

Ramaswamy says his new firm, Strive, will aim to limit the Big Three's power through competition. If Strive attracts enough investors to gain a say in how companies are run — a huge "if," considering that Ramaswamy has said that Strive has raised only about $20 million compared with the trillions managed by the Big Three — Ramaswamy says that he will push for companies to focus on "excellence" rather than wading into heated political issues.

But the goal of staying out of politics in 2022 is about as realistic as staying dry in a hurricane. Last year, for example, BlackRock, Vanguard and State Street supported a successful effort to shake up the board of Exxon Mobil by installing new members who promised to take climate change more seriously. Was that because of excessive wokeness, as Ramaswamy says, or because Exxon Mobil had been underperforming its peers for several years, and it was woefully ill prepared for the transition to renewable energy that has been transforming energy markets? The move seems well within what the investment firms say is their main goal, looking out for the long-term interest of shareholders. And what if the firms hadn't backed the climate initiative — wouldn't that have been construed as a political decision by the activists who have called on shareholders to push corporations to address the climate? (In any case, BlackRock announced this week that it would most likely vote for fewer climate-related shareholder proposals in 2022 than it did in 2021.)

In late 2018, a few months before his death, John C. Bogle, the visionary founder of Vanguard who developed the first index fund for individual investors, published an extraordinary article in The Wall Street Journal assessing the impact of his life's work. The index fund had revolutionized Wall Street — but what happens, he wondered, "if it becomes too successful for its own good?"

Bogle pointed out that asset management is a business of scale — the more money that BlackRock or Vanguard or State Street manages, the more it can lower its fees for investors. This makes it difficult for new companies to enter the business, meaning that the Big Three's hold on the market seems likely to persist. "I do not believe that such concentration would serve the national interest," Bogle wrote.

Bogle outlined several ideas for limiting their power, but he pointed out problems with a number of them. For example, regulators could prohibit index funds from holding large positions in more than one company in a given industry. But how then would they offer an index fund that invested in all companies in the S&P 500, one of the most popular kinds of funds?

Coates, of Harvard, argues that policymakers will have to move carefully to manage the dangers of concentration without limiting the benefits to investors of these firms' low-cost funds. "No doubt getting the balance right will require judgment and experimentation," he wrote.

But the most pressing issue is for us to recognize the problem. The growing influence of three large fund managers is not likely to diminish. Ramaswamy's take on the problem is wrong, but he's right that it's a problem. How much power do the three companies have to accumulate before we decide it's too much?