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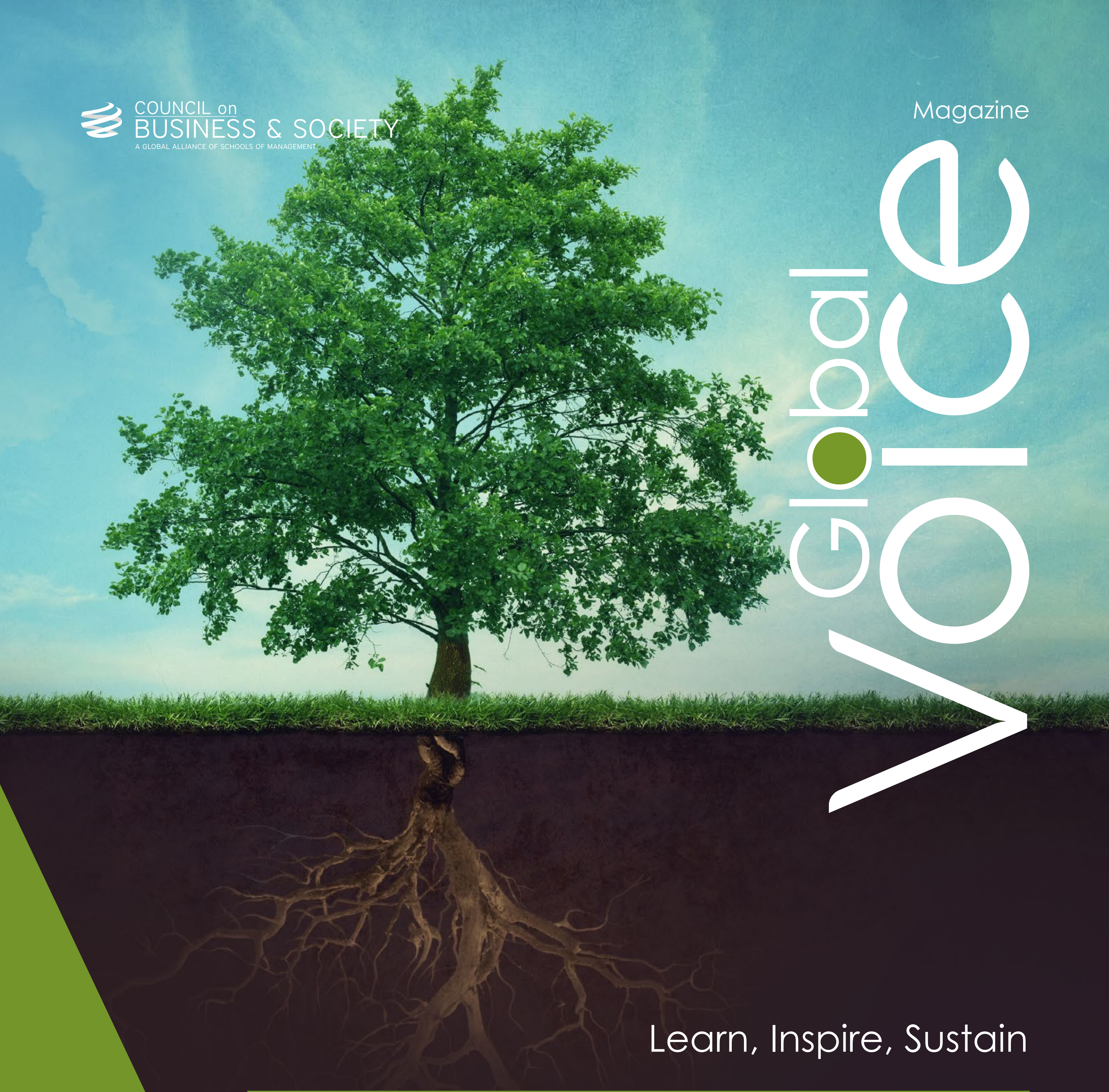
A GLOBAL ALLIANCE OF SCHOOLS OF MANAGEMENT

Global Voice Magazine



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THE UNAVOIDABLE COST OF GOING GREEN

number 13

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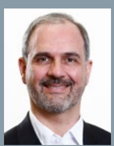

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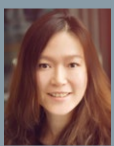

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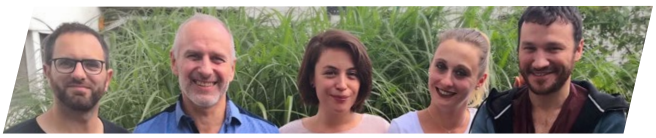

With thanks to CoBS student editors Tanvi Rakesh, Nicolas Desarnauts, Guragam Singh.

ISBN: 978-2-36456-191-5

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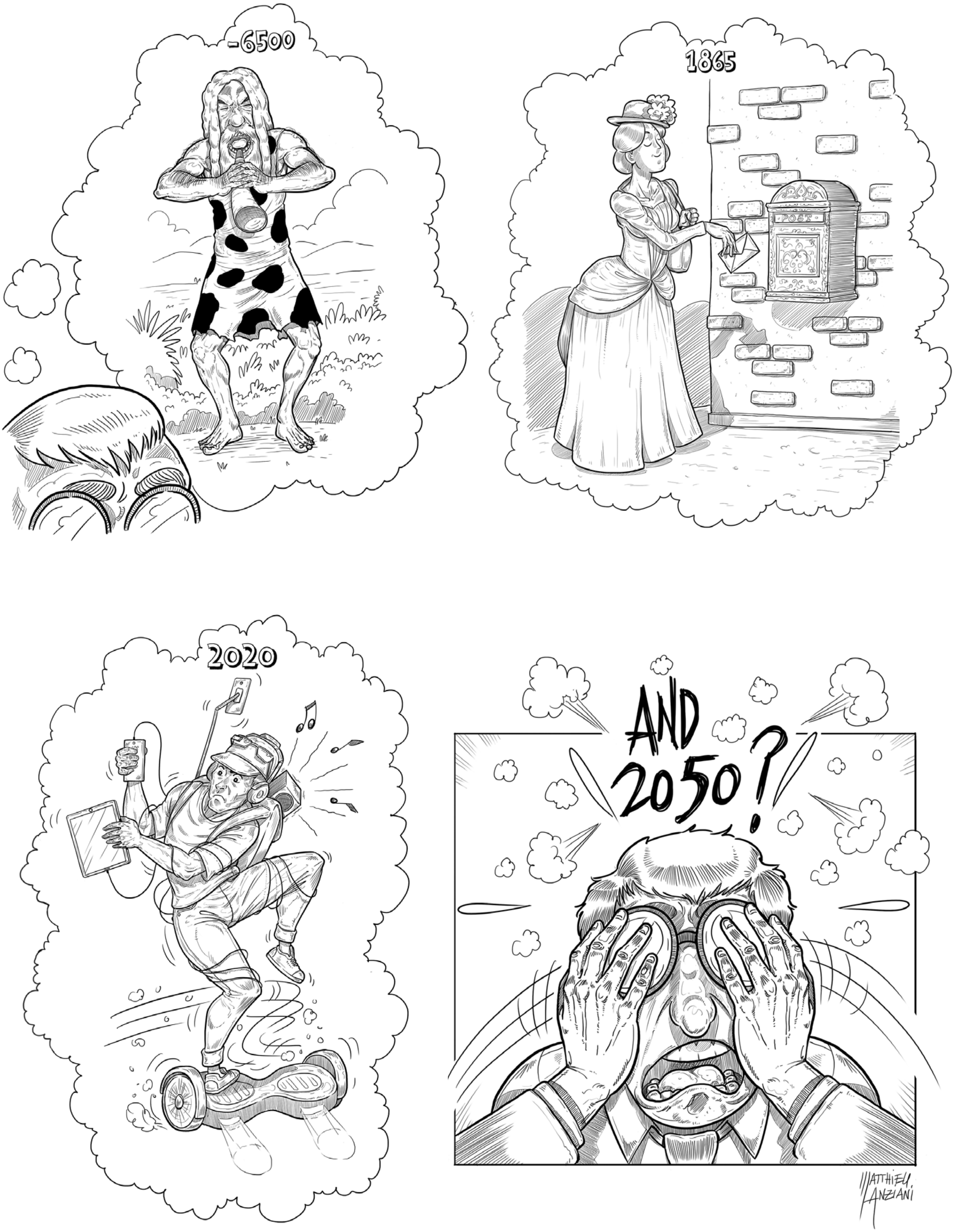
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MATTHIEU LANZIANI

/Editorial

By Adrian Zicari, Executive Director, Council on Business & Society

Dear Readers,

Welcome to this *Global Voice* issue #13. As an opener to the knowledge we can offer you in the articles included in this magazine, it is a fitting occasion to reflect on the passing of the respected academic and business consultant Clayton Christensen who sadly left us on January 23rd of this year.

Clayton Christensen's last(ing) lesson

Professor Christensen was one of the last gurus in Management, and his contribution to theory and practice is immense. His most famous idea remains that of Disruption, the coming up of an unexpected challenger firm that eventually wins over a long standing incumbent. Among his many contributions, I would like to single out an article he published in the Harvard Business Review in 2010 (he also did a TED version). Its title is curious: *"How will you measure your life?"* Being myself a professor in accounting, the idea of measuring is natural. After all, we accountants have been trained to measure sales, cash flows, investments, and the like. We can measure (almost) anything. But measuring one's one life seems a challenging task!

A grand plan

Professor Christensen, as the wise man he was, was able to connect complex theories with concrete realities. He invited his students (and let us scholars and readers of CoBS be his "students" for this sake) to apply management theories to our own lives. Not just to our careers, but plainly to our life. How would each one of us plan one's life? What is our strategy? What matters in the long run?

Looking over the horizon

Curiously, as Christensen emphasized, we human beings are attracted to short-term, tangible achievements. We need to deliver – right now. Real time indicators track our ongoing performance, compared to our peers and to the competition. Making deals, scoring goals, and adding more money to our bank account. In the meantime, we may forget, underestimate, and overlook what really matters in our lives. Perhaps our family, our close friends and the values we deeply care about. We may achieve financial success, but this will not make us happy. Despite our efforts, our lives may end up being "disrupted" by not having focused on the appropriate long-term goals that matter.

In his lasting lesson, Professor Christensen reminds us of the importance to have a purpose in our lives, daring to invest our time and efforts in what we truly cherish, and this despite the everyday short-term pressures that we face. An unforgettable lesson from an unforgettable professor.

Prof. Adrian Zicari
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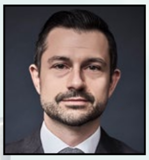

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BUSINESS & SOCIETY

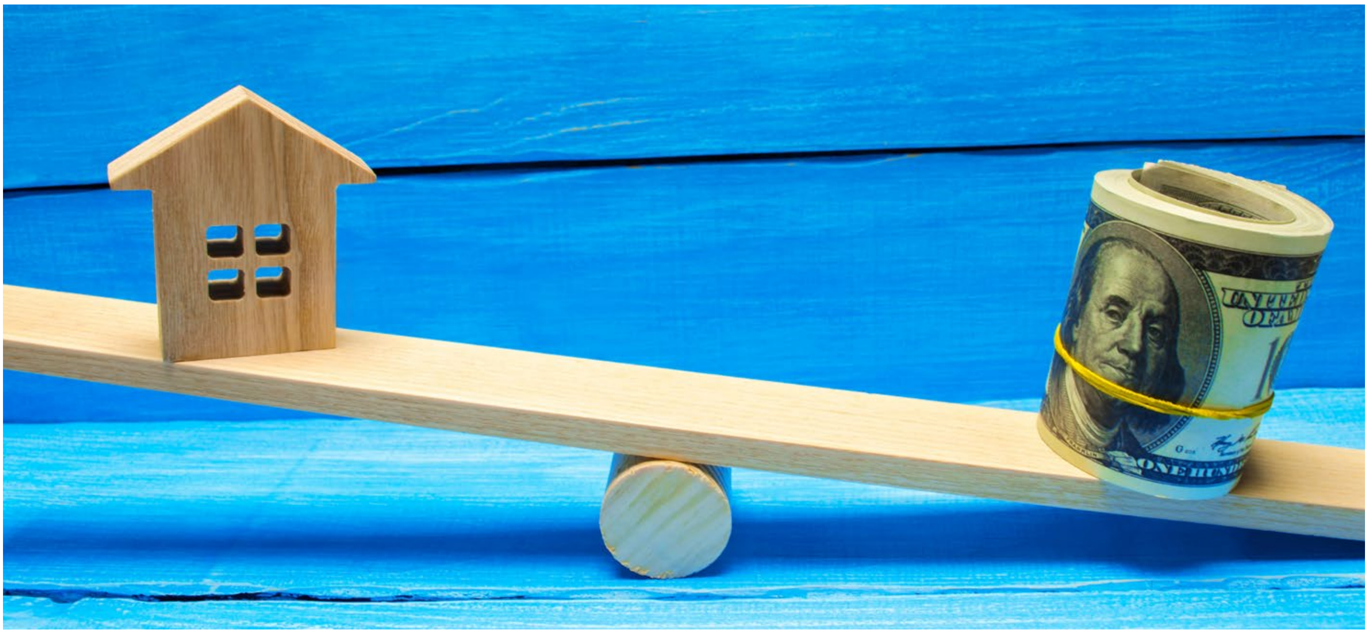
NON-PROFITS & COMMUNITIES: A MUTUAL RELATIONSHIP THAT NEVER WAS

"Governments can become a double-edged sword for non-profit organizations tackling grand challenges"

Prof Liliana Gelabert, IE Business School, sheds light on what makes welfare-oriented non-profits effective at a community-level in the fight against income inequality.

From the paper *Understanding community dynamics in the study of grand challenges: How nonprofits, institutional actors, and the community fabric interact to influence income inequality, by Pascal Berrone, Liliana Gelabert, Frederica Massa-Saluzzo, Horacio E. Rousseau.*

RECENT RESEARCH HAS MOVED towards the investigation of grand challenges – that is, large complex, unresolved societal problems – and the role of organisations in addressing these effectively. Among the multiplicity of such complex social ills, the sustained growth in income inequality is at the top of western governments' policy agenda. Barack Obama has called income inequality the "defining challenge of our time," and the World Economic Forum and the International Monetary Fund have described inequality as one of the greatest problems the world will face in the coming years. Although reducing community income inequality is a daunting task, many organisations are focused on addressing this 'grand challenge', most notably: welfare-oriented non-profits. But what is it that makes them effective?



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Prof Gelabert's research reveals how issues of competition, institutional alignment and community support in the context of grand challenges, particularly income inequality, are more complex than originally thought. Their study – collected from 245 US communities – reveals how community dynamics influence the ability of welfare non-profits to eradicate income inequality. Although it would be natural to assume that a high density of welfare non-profits would benefit a community, Gelabert's study finds otherwise.

While such organisations are beneficial for reducing community equality, this is so up to a point after which competition for resources decreases their effectiveness. Furthermore, such non-profits prove to be more effective when they operate in communities with strong law enforcement capabilities and less so in politically conservative local communities. Contrary to expectations, however, Prof Gelabert found that welfare non-profits are less effective in demographically heterogeneous communities and when the government provides effective social policies, hinting at a possible substitution effect. What's even more interesting is the effect of the presence of financial institutions and thus, more financially oriented citizens. Turns out, that in such a context welfare non-profits fare even better and are more effective. And finally, the study finds that racial diversity, and both the presence and the lack of it, tend to enhance the positive effects of non-profits, and that a conservative political ideology tends to diminish them.

ONE NON-PROFIT, TOO MANY

While evidence finds that a greater density of welfare non-profits is beneficial for reducing income inequality at the community-level, the benefits of agglomeration do not continue indefinitely. At a certain point, greater density spurs competition for scarce resources and produces an inefficient shift in resource allocation. This inefficiency results from the diversion of resources from programme-related initiatives to activities such as fundraising, and advertising aimed at ensuring the non-profit's survival and continued operations. Non-profits compete for donations and grants, volunteer time, and community attention. This sort of competition unfolds not only among non-profits attempting to address a specific grand challenge but also with other non-profits with different goals and constituents. Elite non-profits – non-profits which focus on arts, culture and education issues with an aim to enhance the local cultural context while preserving traditional values – also threaten the continued operation of welfare non-profits since they appeal more to the pockets of status-enhancing elite citizens in the community.

NOT IN THIS ALL TOGETHER, INSTITUTIONALLY

Prof Gelabert's findings regarding local institutional context are even more surprising. She finds that governments can become a double-edged sword for non-profit organizations tackling grand challenges. She reveals, on the one hand, that welfare non-profits are more effective in communities with greater government enforcement capabilities. Through actions such as enforcing labour laws and employer obligations, governments level the playing field and set appropriate rules of corporate behaviour. This facilitates the actions of welfare non-profits. However, on the other hand, weak government social policies also tend to increase welfare non-profits' effectiveness. A plausible explanation, Gelabert claims, is because non-profits arise partly to compensate for market and state failures, and a lack of government intervention signals to community constituents that social problems remain unaddressed, thus increasing the legitimacy of and perceived need for welfare non-profits.

UNIONS: NOT A MATCH MADE IN HEAVEN

The institutional fabric of a community is also defined by its labour and financial institutions which have an unexpected relationship with welfare non-profits' effectiveness, Prof Gelabert divulges. Central among labour institutions are unions, which share with welfare non-profits the common goal of protecting and empowering an economically vulnerable category of individuals. However, their research finds that despite sharing this common goal, labour institutions do not seem to significantly increase the effectiveness of welfare non-profits at reducing income inequality. "A plausible expla-

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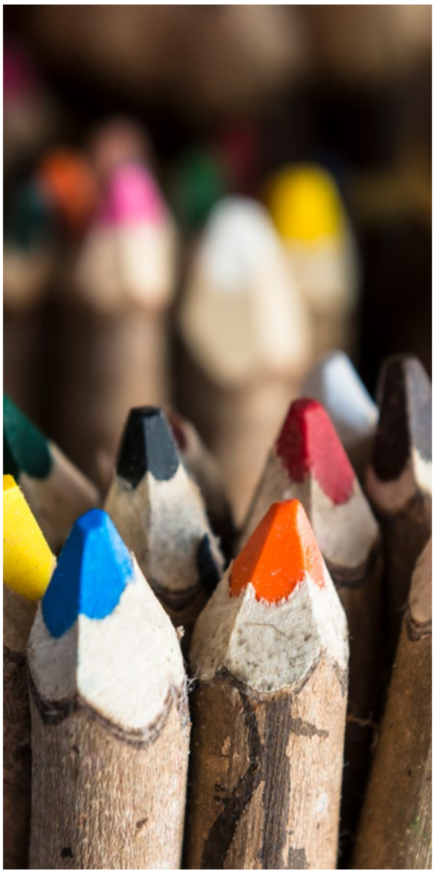
nation for this", Prof Gelabert hazards, "might be a declining degree of trust between welfare non-profit organizations and unions, which prevents both sides from taking advantage of their shared goals and potential congruence". She further explains that a decline in trust could be a result of the recent shift of unions toward recruiting members in community-based welfare non-profits. Moreover, she points out that welfare non-profit leaders have grown quite sceptical about the unionisation of their labour force, not only for financial reasons but also because of the consequences that a culture of unionisation would have on the non-profit sector.

UNEXPECTED SUPPORT

While similar goals may not be conducive to a welfare non-profit's mission, it isn't surprising that seemingly contradictory goals then, are. Prof Gelabert and her fellow researchers found that the presence of financial institutions had a positive effect on the effectiveness of non-profits at reducing income inequality. Local financial institutions are prominent community actors that can influence individual attitudes, including civic behaviour and willingness to participate in civic initiatives. This phenomenon has been



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coined as the 'financialisaton of daily life', wherein citizens adopt a portfolio view of society, and let go of their sense of community bonds and relationships while considering talent, friends, homes and communities as potential securities. Prof Gelabert bridges these seemingly disputing contexts by bringing in evidence which suggests that financial institutions are, however, increasingly willing to support community non-profits provided that these organisations have "a track record, fiscal discipline, good recordkeeping, and committed volunteers" – all features supported in the current trend towards non-profit professionalisation. What's more, financial institutions rationalise their support as a way to increase community goodwill and to promote their business in the local market area.

A QUESTION OF COMMUNITY: IDEOLOGY AND DIVERSITY

How the community fabric impacts the effectiveness of welfare non-profits is in the same vein – unexpected. Prof Gelabert reveals that racial diversity – both high levels and low levels – tend to reduce non-profit effectiveness. At high levels of diversity, the benefits of heterogeneity and integration seem to be outweighed by the effects of segregation and racial prejudice. As a result, social cohesion and civic engagement in communities are undermined, therefore reducing the effectiveness of welfare non-profits. What is interesting, is that at the same time, a low level of racial diversity also diminishes the effects of non-profit density, probably because non-profits then need to invest greater resources in generating awareness. Finally, and as predicted, Prof Gelabert found that political conservatism reduced the welfare-oriented non-profits' effectiveness. This stems from the fact that conservative ideology is usually linked to a system of psychological needs and motivations, some of which are opposed to those advocated by non-profits.

TAKING A STEP BACK: RETHINKING POLICY AND MANAGEMENT

The assumption that greater welfare non-profit participation would yield continuously increasing benefits in reducing income inequality has important policy implications given the substantial amount of resources allocated to non-profits – not only directly through grants, contracts and training but also indirectly through their tax-exempt status. Prof Gelabert proves this assumption false, which means that in periods when the public sector budget is strained, trading direct tax revenues for a larger non-profit sector might not translate into a proportional fall in in income inequality, especially at high levels of competition. In such a case, Prof Galabert and her fellow researchers make two recommendations for local governments. First, local governments may be able to reduce competition by concentrating their resources on those with a demonstrated capacity to help the disadvantaged effectively and substantially. Although this focus can reduce the diversity of welfare-oriented non-profits in a locality, it can help build greater capacity for those with an outstanding track record. Second, local agencies should help non-profits develop more accurate and transparent performance measures. Such measures could also serve as a basis for potential donors to evaluate non-profits, allowing them to choose the ones that they consider to be the most efficient at using resources to achieve their social goals.

On the managerial side, Prof Gelabert identifies ways in which non-profits could respond to resource competition. One possible solution, she emphasises, is the creation of cross-sector collaborations that take advantage of each partner's specific capabilities to solve a complex social problem. Non-profits could also address competition and defend their niches by relying on fine-grained financial and social impact indicators rather than by advertising or fundraising more. She believes that the competitive pressure from other non-profits would also call for a more specialised profile of worker in non-profits, particularly individuals with experience in the private sector, to respond adequately to competition. However, she warns that this rationalisation of the 'third sector' could undermine the nature of voluntary work by infusing it with too much of an instrumental logic. One possibility, she suggests, is that welfare non-profits increase coordination efforts with other non-profits in order to share resources and hence avoid competition.

Profs Gelabert's findings regarding institutional context also suggest several major policy implications. First, considering that greater government enforcement capabilities improve welfare non-profits' effectiveness, she insists that greater enforcement of labour laws can actually set the appropriate context for welfare non-profits to reduce income inequality significantly. Second, since direct government social policies seem to reduce the effectiveness of non-profits, she suggests that greater coordination between government and organisations addressing grand challenges is needed to exploit complementarities and avoid possible crowding out. Finally, she stresses the importance of racial integration policies to reduce the negative effect of segregation on income inequality, and to leverage the activity undertaken by welfare non-profits.

RETHINKING GRAND CHALLENGES

Prof Gelabert's study brings to light consequential relationships, which are both unexpected and far from originally hypothesised theoretical relationships in the context of grand challenges. Her research highlights that communities not only influence organisations but that their collective action can also affect local communities. Moreover, conducted at a community level, the study serves as a reminder that while grand challenges are frequently classified as national-level problems, significant within-country variance remains in the degree to which social problems emerge and influence people's lives. Policymakers and managers must, in light of this study, reconsider and revise pre-existing ideas and assumptions in the context of grand challenges.

Liliana Gelabert

KEY TAKE AWAYS

A GREATER DENSITY OF WELFARE NON-PROFITS WILL NOT REAP CONTINOUS BENEFITS IN ERASING INCOME INEQUALITY. TOO MANY NON-PROFITS ARE LIKELY TO COMPETE FOR RESOURCES AND ALLOCATE RESOURCES TOWARDS FUNDRAISING AND ADVERTISING WHICH IS INEFFECIENT AND OUTWEIGHS THEIR ACTUAL EFFECTIVENESS.

POLICY IMPACT: LOCAL GOVERNEMENTS MUST PROVIDE SUPPORT TO NON-PROFITS WITH A DEMONSTRATED CAPACITY.

POLICY IMPACT: LOCAL AGENCIES MUST HELP NON-PROFITS BUILD MORE ACCURATE AND TRANSPARENT MEASURES WHICH WOULD ALLOW DONORS TO PICK THE MOST EFFICIENT NON-PROFIT.

MANAGERIAL IMPACT: NON-PROFITS MUST ENGAGE IN CROSS-SECTOR COLLABORATIONS AND RELY ON FINE-GRAINED SOCIAL AND FINANCIAL IMPACT INDICATORS RATHER THAN FUNDRAISING AND ADVERTISING

MANAGERIAL IMPACT: WELFARE NON-PROFITS COULD COORDINATE WITH OTHER NON-PROFITS TO SHARE RESOURCES AND AVOID COMPETITION

BOTH STRONG AND WEAK ENFORCEMENT OF GOVERNMENT POLICY TEND TO INCREASE THE EFFECTIVENESS OF WELFARE NON-PROFITS. STRONG ENFORCEMENT LEVELS THE PLAYING FIELD AND SET APPROPRIATE RULES OF CORPORATE BEHAVIOUR. WHEREAS WEAK ENFORCEMENT SIGNALS TO THE COMMUNITY A LACK OF GOVERNMENT INTERVENTION.

POLICY IMPACT: LOCAL BODIES MUST RECOGNISE GREATER ENFORCEMENT OF LABOUR LAWS TO SET APPROPRIATE CONTEXT FOR WELFARE NON-PROFITS TO REDUCE INCOME INEQUALITY SIGNIFICANTLY.

POLICY IMPACT: THERE MUST BE GREATER COORDINATION BETWEEN GOVERNMENT AND ORGANISATIONS ADDRESSING GRAND CHALLENGES TO EXPLOIT COMPLEMENTARITIES AND AVOID CROWDING OUT.

LABOUR INSTITUTIONS, UNIONS PRE-DOMINANTELY, DO NOT INCREASE WELFARE NON-PROFIT EFFECTIVENESS, DUE TO DECLINING TRUST BETWEEN NON-PROFITS AND UNIONS. FINANCIAL INSTITUTES INCREASE NON-PROFIT EFFECTIVESS, SINCE THEY ARE WILLING TO SUPPORT NON-PROFITS THAT HAVE A RECORD OF BEING 'PROFESSIONAL'.

THE PRESENCE AND LACK OF RACIAL DIVERSITY, BOTH SEEM TO INCREASE WELFARE NON-PROFIT EFFECTIVENESS, WHEREAS A COSERVATIVE POLITICAL IDEOLOGY LOWERS THIS EFFECTIVNESS.

POLICY IMPACT: LOCAL GOVERNMENT MUST RECOGNISE IMPORTANCE OF RACIAL INTEGRATION POLICIES TO REDUCE THE NEGATIVE EFFECT OF SEGREGATION ON INCOME INEQUALITY, AND TO LEVERAGE THE ACTIVITY UNDERTAKEN BY WELFARE NON-PROFITS.

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WHO MAKES ALL THE DIFFERENCE? WOMEN IN ENTREPRENEURSHIP DO

Every year billions of dollars are spent on training aspiring men and women in the hope that they can scale their businesses, which will create more jobs and boost economic growth, asserts Prof Mona Mensmann of Warwick Business School.

THIS USUALLY TAKES THE FORM of learning such management and financial skills as book-keeping, stock control or marketing to name a few. The importance of these skills is so deeply felt that such training is given not only by educational institutions, whether physically or digitally, but also by international bodies such as the International Labour Organization and the International Finance Corporation.

A key role in the entrepreneurial education endeavour is that of women, for boosting the number of female entrepreneurs is a global concern, with the World Bank launching a $1 billion fund in 2017 to increase the number of women-led businesses—30 percent of all registered firms globally. But how effective is this knowledge-heavy training? Does it actually work? And do women need it?

In order to better answer these questions, Prof Mensmann and her fellow researchers

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> "Entrepreneurs know better than anybody on how to improve their business—training can only give them the means to do so."

partnered with the World Bank to test a new type of training for entrepreneurs, based on research that showed that psychological factors played an important part in entrepreneurial success. This new personal initiative training (PIT) developed key behaviours to build a self-starting, future-oriented mindset, with additional mentoring in which entrepreneurs worked on projects in their own business to build confidence in their abilities.

ALL IN A GOOD YEAR'S WORK

The researchers gathered 1,500 entrepreneurs in Togo for a randomised controlled trial (RCT) and divided them into groups of 500 each. One group was given a traditional knowledge-based management educational programme, another was provided with the novel personal initiative training while the third served as the control group. After the 12-week programme was over, the groups' progress was tracked for 2 years. The results were stark. Those who undertook the personal initiative training saw a rise in sales of 17 percent and an increase in profits by 30 percent. The results for the traditionally trained group pale in comparison to a statistically meagre 11 percent increase. The new training had effectively paid for itself within a year.

The results were even more encouraging for women entrepreneurs. Those who took part in the personal initiative training saw a 40 percent rise in their profits as compared to a low 5 percent rise in profits of women entrepreneurs who got traditional business training. Proof that the personal initiative training is empowering for women.

MINDING THEIR OWN BUSINESS

Prof Mensmann is convinced that entrepreneurs know better than anybody on how to improve their business—training can only give them the means to do so. The personal initiative training can teach people to develop a mindset with traits that are often assumed to be innate in entrepreneurs. They become self-starters, future-thinkers and are not afraid of failure, instead, seeing it as part of the process and learning from it. As such, entrepreneurs were asked to be self-starting in setting goals for a new project they wanted to pursue. For instance, a tailor wanting to buy a new sewing machine to make their garments more unique.

Both the traditional knowledge-based training and the PIT impacted entrepreneurs' business behaviour despite the fact that the PIT didn't focus only on business practices. In addition, those in the PIT, who effectively taught themselves, were better at all of these activities (except for book-keeping) and produced better performance.

Other key aspects were developing persistence and being future minded. What do entrepreneurs do when problems arrive? It is very easy to let go of a business and start another, but this is not how a business grows. As such, the training taught them how to prepare for problems—current and potential—how to overcome them and how to cope psychologically so that they could keep the business running given the barriers they faced.

FALLING INTO A PIT OF SUCCESS

Another discovery was that entrepreneurs in the PIT group were significantly more innovative than the traditionally trained entrepreneurs and produced more new products. They were also more likely to diversify into new product lines. Moreover, they borrowed twice as much money—proof that they were not afraid of taking risks.

In the mentoring phase, the mentors helped participants reflect on their behaviours rather than focussing on numbers alone—often the case in traditional methods of

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mentoring. For example, mentors didn't walk-in and abruptly announce, based on the mentees' books, a method to change the way they worked. Instead they asked questions that had emotion in them—what they did the previous week, what hurdles they faced, and how they could improve. In addition, the mentoring focused on the three training elements of being self-starting, future-oriented and persistent.

PAIN ONLY MAKES HER STRONGER

After answering questions on the effectivity and impact of the PIT, it is important to understand why women benefitted more. According to theory, men and women developed different roles over time, with women usually seen as being more caring and men usually assigned more daring roles. This leads to stereotypes that are internalised.

But the personal initiative training threw women—and men, alike—into the deep end, forcing them to be proactive and helping them realise they are capable of taking risks and improving their businesses. Women realised they could cope with any negative outcomes, develop resilience and new capabilities. It built a passion for entrepreneurship, rather than being only a means to feed the family. They saw they could grow their businesses. And enjoy it.

FORGING A ROAD INTO THE FUTURE

This research into a new training paradigm does not mean that knowledge is not important. Only that women need to be given the opportunity to develop an entrepreneurial mindset and self-belief to develop their own business in a safe space.

To this end, institutions and organisations at all levels may wish to develop and/or augment their training programmes to help women—an under-tapped source of inclusive wealth creation and economic growth—to overcome cultural barriers to develop an entrepreneurial mindset. As such, it could create a new path into business for millions of people left cold by traditional education.

Mona Mensmann

KEY TAKE AWAYS

BOOSTING THE NUMBER OF FEMALE ENTREPRENEURS IS A GLOBAL CONCERN – WOMEN-LED BUSINESSES REPRESENT 30 PERCENT OF ALL REGISTERED FIRMS GLOBALLY.

RESEARCH SHOWS THAT PSYCHOLOGICAL FACTORS PLAY AN IMPORTANT PART IN ENTREPRENEURIAL SUCCESS.

ACCORDING TO THEORY, MEN AND WOMEN DEVELOPED DIFFERENT ROLES OVER TIME, WITH WOMEN USUALLY SEEN AS BEING MORE CARING AND MEN USUALLY ASSIGNED MORE DARING ROLES. THIS LEADS TO STEREOTYPES THAT ARE INTERNALISED.

WOMEN NEED TO BE GIVEN THE OPPORTUNITY TO DEVELOP AN ENTREPRENEURIAL MINDSET AND SELF-BELIEF TO DEVELOP THEIR OWN BUSINESS IN A SAFE SPACE.

ENTREPRENEURS KNOW BETTER THAN ANYBODY ON HOW TO IMPROVE THEIR BUSINESS—TRAINING CAN ONLY GIVE THEM THE MEANS TO DO SO.

PERSONAL INITIATIVE TRAINING (PIT) DEVELOPS KEY BEHAVIOURS TO BUILD A SELF-STARTING, FUTURE-ORIENTED MINDSET, WITH ADDITIONAL MENTORING WHERE ENTREPRENEURS WORK ON PROJECTS IN THEIR OWN BUSINESS TO BUILD CONFIDENCE IN THEIR ABILITIES.

KEY ASPECTS WERE DEVELOPING PERSISTENCE AND BEING FUTURE MINDED, DEVELOPING AS SELF-STARTERS, FUTURE-THINKERS AND SHEDDING FEAR OF FAILURE, INSTEAD, SEEING IT AS PART OF THE PROCESS AND LEARNING FROM IT.

COMPARED TO TRADITIONAL TRAINING (11 PERCENT INCREASE IN RESULTS), PIT PARTICIPANTS SAW A RISE IN SALES OF 17 PERCENT AND AN INCREASE IN PROFITS BY 30 PERCENT.

WOMEN ENTREPRENEURS SAW A 40 PERCENT RISE IN THEIR PROFITS COMPARED TO 5 PER FOR WOMEN ENTREPRENEURS IN TRADITIONAL BUSINESS TRAINING.

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CHILDREN, ADOLESCENTS AND LARGE-SCALE PROJECTS IN BRAZIL

With the increase of large-scale projects in Brazil, researchers Aron Belinky and Livia Menezes Pagotto of the GVces Center for Sustainability at FGV-EAESP share a guide for companies on how to generate shared value from the full protection of children and adolescents.

With kind acknowledgements to GVces

IN RECENT YEARS, Brazil has experienced a boom in large projects, mostly leveraged by the PAC (Growth Acceleration Program), but not limited to it. They range from huge construction sites, such as the Belo Monte hydroelectric power plant, to smaller interventions, which, however, still affect the territories where they are located. There are roads, ports, railways, hydroelectric power plants and others. Large urban interventions have also occurred, either as a way to try to solve historical issues in our big cities, or as a consequence of the 2014 World Cup and 2016 Olympic Games. Besides, the private sec¬tor has invested and carried out large projects, such as mineral exploration, installation of new manufacturing plants, or the extension of their production chains to other regions in the country.

Many of these projects are carried out in vulnerable territories, where the State is barely present, and are inhabited by groups, families or individuals who are more exposed to the risk of unemployment, poor working conditions, poverty and lack of social protection. It is important to note that vulnerability does not exist only in areas that are distant from urban centers; it may exist, for instance, on the outskirts or in other areas in big cities.

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BRIDGING THE ISSUE

Much of these investments, particularly on the energy sector, have been made on the North of the country, especially in the Amazon region. Historically, due to its more recent occupation, the territories in that region lack institutional resources and a strong public sector, and part of the population is still in vulnerable conditions. We must also consider that the region hosts traditional populations such as indigenous people, maroons, riparian populations and other communities whose organization and lifestyle are closely related to their natural environment. In this context, large projects affect local economic activities, as well as the sense of belonging, identity and cultural bonds. On the other hand, if carried out with proper care, they may be the answer to many social issues and human rights violations.

When it comes to social vulnerability, one of the groups that are most exposed to risks are children and adolescents. Children and adolescents who are in vulnerable conditions are more intensely affected by social inequality, poverty and social exclusion. This is reflected in violations of their rights and weakening of family ties and other areas of socialization, such as schools and others. They ultimately have to abruptly make the transition from childhood to adulthood, and keep suffering with the lack of access to education, work, health, entertainment and culture. With no perspective on the future, they are exposed to many forms of exploitation, which may include child labor, youth labor in extremely poor conditions, and sexual exploitation.

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> "Children and adolescents who are in vulnerable conditions are more intensely affected by social inequality, poverty and social exclusion."

THE ADVANCE OF BUSINESS – AND DEMOCRACY

When a large project is started in a vulnerable territory, it may significantly affect this scenario. It is extremely critical, as established by law, that absolute priority is granted to protect children and adolescents, not just to guarantee their rights, but also as a strategy for local development and overall human rights protection.

As democracy advances in the country, the social role of various actors has changed and, along with the rights granted, new responsibilities have emerged. This is also true for businesses, who should seek to build new competencies and innovate in their management. The attitude of the organizations concerning these challenges will make the whole difference to either convert them into new opportunities and gains for the business, or into obstacles and charges. Proactive companies that are open to dialogue with society will have clear advantages in this scenario.

It is in this context that the Center for Sustainability Studies (GVces) of Sao Paulo Business Administration School at Getulio Vargas Foundation (FGV-EAESP), Childhood Brazil and the Center for Businesses and Human Rights at GV Law School joined forces to discuss children and adolescents' full protection in territories affected by large projects. Specifically focused on the role of companies, the purpose was to offer guidance on how businesses can prepare, through joint participation with other stakeholders, the territories that host large projects, in order to guarantee full protection of children and adolescents. This work sought to assess different perspectives to handle the full protection issue. Specifically, we tried to balance three axes:

- Local development
- Full protection of children and adolescents
- Corporate social responsibility.

Livia Menezes Pagotto

Aron Belinky

KEY TAKE AWAYS

IN RECENT YEARS, BRAZIL HAS EXPERIENCED A BOOM IN LARGE PROJECTS, MANY IN VULNERABLE TERRITORIES, WHERE THE STATE IS BARELY PRESENT, AND ARE INHABITED BY GROUPS, FAMILIES OR INDIVIDUALS WHO ARE MORE EXPOSED TO THE RISK OF UNEMPLOYMENT, POOR WORKING CONDITIONS, POVERTY AND LACK OF SOCIAL PROTECTION.

THESE TERRITORIES, ESPECIALLY IN THE NORTH OF BRAZIL AND IN THE AMAZON REGION ARE HOME TO A LARGE DIVERSITY OF PEOPLES AND ETHNIC CULTURES.

CHILDREN AND ADOLESCENTS WHO ARE IN VULNERABLE CONDITIONS ARE MORE INTENSELY AFFECTED BY SOCIAL INEQUALITY, POVERTY AND SOCIAL EXCLUSION.

THIS IS REFLECTED IN VIOLATIONS OF THEIR RIGHTS AND WEAKENING OF FAMILY TIES AND OTHER AREAS OF SOCIALIZATION, SUCH AS SCHOOLS AND OTHERS. THEY ARE EXPOSED TO MANY FORMS OF EXPLOITATION, INCLUDING CHILD LABOR, YOUTH LABOR IN EXTREMELY POOR CONDITIONS, AND SEXUAL EXPLOITATION.

WHEN A LARGE PROJECT IS STARTED IN A VULNERABLE TERRITORY, IT MAY SIGNIFICANTLY AFFECT THIS SCENARIO. IT IS THEREFORE ESSENTIAL TO PROTECT CHILDREN AND ADOLESCENTS: TO GUARANTEE THEIR RIGHTS AND ALSO AS A STRATEGY FOR LOCAL DEVELOPMENT AND OVERALL HUMAN RIGHTS PROTECTION.

AS DEMOCRACY ADVANCES IN THE COUNTRY, THE SOCIAL ROLE OF VARIOUS ACTORS HAS CHANGED AND, ALONG WITH THE RIGHTS GRANTED, NEW RESPONSIBILITIES HAVE EMERGED.

PROACTIVE COMPANIES THAT ARE OPEN TO DIALOGUE WITH SOCIETY WILL HAVE CLEAR ADVANTAGES. BUSINESSES SHOULD SEEK TO BUILD NEW COMPETENCIES AND INNOVATE IN THEIR MANAGEMENT.

THEIR ATTITUDE CONCERNING CHILDREN'S RIGHTS WILL MAKE THE WHOLE DIFFERENCE TO EITHER CONVERT THEM INTO NEW OPPORTUNITIES AND GAINS FOR THE BUSINESS, OR INTO OBSTACLES AND CHARGES.

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HOW INSTITUTIONS SHAPE CSR IN THE MIDDLE EAST AND NORTH AFRICA

Doctor **Tanusree Jain,** Assistant Professor of Ethical Business at **Trinity Business School,** explores the idiosyncrasies of Middle Eastern and North African institutions and their effect on Corporate Social Responsibility practices.

THE MIDDLE EAST and North Africa region – an amalgamation of over a dozen distinctive nations – is more mosaic than monolith. However, the dominance of petroleum-centric capitalism in the region and its consequent contribution to the climate emergency have raised questions about how institutions in these countries shape their sustainable development agendas. In her recent paper, Doctor Tanusree Jain, assistant professor of ethical business at Trinity Business School, uncovers how corporate social responsibility practices are affected by unique institutional environments in this misunderstood part of the world.

UNDERSTANDING CSR

In recent years, research on corporate social responsibility (CSR) practices in non-western countries has proliferated. This has required a new conception of CSR that considers the distinctive institutional context in which CSR as a practice is embedded. In her paper, Dr. Jain defines CSR as "all those activities that firms identify as responsibility towards improving the social state and well-being of their

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stakeholders including the environment". This involves building and maintaining relationships with these stakeholders, whether undertaken voluntarily or mandated by local rules, norms, or customs. Indeed, "stakeholder theory" has been the dominant paradigm in the last three decades of global CSR research. According to Dr. Jain, however, in non-western countries, this research has required "coupling stakeholder theory with institutional theory to explain how distinctive institutional pressures influence CSR practices". An institutional theory approach enables a comparative examination of CSR practices across different national and cultural contexts as stakeholder identities, expectations, and interests vary cross-nationally. As Dr. Jain states: "Institutions specify the rules of the game by defining rights and responsibilities and by prescribing accepted and legitimized social roles, therefore shaping the identities of social actors in ways that are enduring over time". Therefore, an analysis of institutional environments is critical to understanding the heterogeneity in CSR practices in the Middle East and North Africa (MENA) region.

FROM PATTERNS TO CLUSTERS

To analyse how institutions in the MENA region influence the practice of CSR, Dr. Jain conducted a systematic review of over 180 CSR studies of the region. Through this assimilation of existing knowledge, she uncovered different institutional patterns emerging within the region and their impact on CSR. This research focused on 20 countries including Egypt, Sudan, Algeria, Morocco, and Tunisia from North Africa and Yemen, Bahrain, Iran, Kuwait, Saudi Arabia, Qatar, UAE, Oman, Jordan, Lebanon, Turkey, Syria, Libya, Iraq, and Palestine from the Middle East. To capture distinct patterns in the institutional makeup of these countries, Dr. Jain adopted a two-stage process. First, drawing on the Varieties of Institutional Systems (VIS) framework, she identified "country clusters" within MENA based on their institutions. Then, she integrated the VIS framework with a "patchwork institutions lens". This allowed her to compare and contrast the institutional environments in each country comprising the MENA region. Dr. Jain's review untangles the country-specific institutional factors affecting CSR, thereby "shedding light on the nested complexity of the institutional make-up of MENA countries and how they shape firm-level CSR practices". By emphasizing the heterogeneous, dynamic, and continuously changing aspect of institutions, this research provides a better understanding of complex contexts of the MENA region and its influences on CSR.

A THICK PATCHWORK

Based on the different institutional environments of MENA countries, the region can be divided into distinct clusters. Dr. Jain identifies five: Fragmented with Fragile State, Family Led, Centralised Kinship, Hierarchically Coordinated, and Conflict-affected. These clusters provide a deeper understanding of the MENA region wherein countries' "different colonization histories, state forms, traditions, and norms are likely to combine together to form a thick patchwork that will uniquely shape institutional effects on CSR practices".

1. Egypt and Sudan in North Africa comprise the Fragmented with Fragile State cluster. The role of the state in this cluster is developmental – which impacts CSR practices. The Egyptian government intervenes in and controls some industries by enforcing the Islamic notion of community-centred responsibility through philanthropy. Low levels of general trust in this cluster causes scepticism about CSR practices – especially when these practices are decoupled from religious discourse. However, the elite workforce hired by multinationals values CSR to gain legitimacy locally and competitive advantage internationally.

2. The Family Led cluster is comprised of Algeria, Morocco, and Tunisia. There, state intervention takes both direct and indirect forms. In Morocco, the state primarily promotes CSR policies that improve the competitive strength of local businesses. Although recent political upheavals have weakened its capacity to enforce laws, in Tunisia the state intervenes directly by acquiring ownership in private firms to shape CSR activities. Wealthy families in this cluster exert substantial influence across the economy. The prioritization of their financial interests can have a negative impact as CSR is perceived as a financial cost. Multinationals therefore largely drive the CSR agenda in Morocco in line with international benchmarks and reporting frameworks.

3. Comprised of Oman, Bahrain, Iran, Kuwait, Qatar, Saudi Arabia, and the UAE, the Centralised Kinship cluster is dominated by Middle Eastern countries. The family is at the centre of all social, economic, and political activity in this cluster. The state – where powerful family elites hold political power – intervenes in business affairs directly through ownership and control of firms and indirectly through the legislation of laws and policies. Firms are able to gain legitimacy and societal acceptance in highly-religious societies like Saudi Arabia, Oman, Bahrain, and Qatar, by complying with Islamic prescriptions on CSR.

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4. The Hierarchically Coordinated cluster is comprised of Lebanon, Jordan, and Turkey. In Lebanon, the developmental role of the state is diluted due to weaknesses in its law enforcement capacity, thus creating create gaps in firms' compliance towards CSR, especially for reducing negative externalities. Within Jordan, research reveals direct state intervention in business through public ownership in companies as well as by legislating laws that mandate CSR disclosures. In Turkey, the state has a developmental yet predatory character. While the institutional environment drives firms to adopt western CSR practices to align and compete in European markets, smaller firms embark on philanthropy in a limited way.

5. The Conflict-affected cluster includes Syria, Palestine, Iraq, Yemen, and Libya. These countries are clustered together as they have experienced ongoing political and societal unrest causing massive disruptions to their institutional environments. The state's capacity to contribute to the welfare of its citizens is limited in this cluster. In Palestine, firms' contribution to social work is perceived as a national obligation. In Libya, high religiosity among the population makes religion the primary driver for CSR. Moreover, the interconnectedness of wealthy extended families with substantial economic power increase CSR contributions toward the communities in which their businesses are embedded.

SHAPING CSR

The Middle East and North Africa is a complex, fascinating, and diversified region presenting several institutional idiosyncrasies. Countries in the MENA region exhibit different historical experiences of political systems and financial markets, ownership and management traditions, and human capital organization. When juxtaposed with an environment of political, economic and social flux on the one hand, and popularized western standards of best practices on the other, Dr. Jain argues the combination of institutional forces can create unique CSR opportunities and challenges facing businesses functioning in MENA.


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Tanusree Jain

KEY TAKE AWAYS

THE DOMINANCE OF PETROLEUM-CENTRIC CAPITALISM IN THE MIDDLE EAST AND NORTH AFRICA AND ITS CONSEQUENT CONTRIBUTION TO THE CLIMATE EMERGENCY HAVE RAISED QUESTIONS ABOUT HOW INSTITUTIONS IN THESE COUNTRIES SHAPE THEIR SUSTAINABLE DEVELOPMENT AGENDAS.

DIFFERENT COLONIZATION HISTORIES, STATE FORMS, TRADITIONS, AND NORMS OF MIDDLE EASTERN AND NORTH AFRICAN COUNTRIES UNIQUELY SHAPE THEIR INSTITUTIONAL EFFECTS ON CSR PRACTICES

IN EGYPT AND SUDAN, LOW LEVELS OF GENERAL TRUST IN CAUSE SCEPTICISM ABOUT CSR PRACTICES – ESPECIALLY WHEN THESE PRACTICES ARE DECOUPLED FROM RELIGIOUS DISCOURSE.

FINANCIAL COST IN ALGERIA, MOROCCO, AND TUNISIA NEGATIVELY IMPACTS CSR AS FAMILIES PRIORITIZE THEIR BUSINESS INTERESTS.

FIRMS ARE ABLE TO GAIN LEGITIMACY AND SOCIETAL ACCEPTANCE IN HIGHLY-RELIGIOUS SOCIETIES LIKE SAUDI ARABIA, OMAN, BAHRAIN, AND QATAR, BY COMPLYING WITH ISLAMIC PRESCRIPTIONS ON CSR.

WHILE TURKEY'S INSTITUTIONAL ENVIRONMENT ENCOURAGES LARGE FIRMS TO ADOPT WESTERN CSR PRACTICES TO ALIGN AND COMPETE IN EUROPEAN MARKETS, SMALLER FIRMS EMBARK ON PHILANTHROPY IN ONLY A LIMITED WAY.

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IN VINO VERITAS

For a person, sure. But this adage is now also applicable to sustainability and a key driver in creating value for small and medium enterprises operating in the Italian wine industry. Prof Adrian Zicari of ESSEC Business School, and Laura Broccardo of Università di Torino, Turin share their research.

From the paper Sustainability as a driver for value creation: *A business model analysis of small and medium enterprises in the Italian wine sector* by Laura Broccardo and Adrian Zicari, Elsevier.

ABUZZ WITH WORDS

SUSTAINABILITY is the buzzword of today. As such, firms from fast-food chains to haute couture houses to international bodies such as the United Nations—with tomorrow's interests in mind—have been unable to shake off this hangover. However, certain organisations, more so than others, definitely consider sustainability a core aspect of their business models. And leverage it to obtain economic value and competitive advantage.

But what constitutes a business model is clearly not as well defined. The business model has been confused with other management jargon such as strategy and business concept. For their part, Prof Zicari and Prof Broccardo draw from a vast body of literature to align a model with various definitions and highlight how these interact with each other.

> Business models shape the external environment of which they are a part.

As such, they follow the classical model proposed by Johnson et al. (2008)* that describes a business model as having four elements—a customer value proposition, a profit formula, key resources, and key processes.

This approach allows business models to be tweaked to changing realities—thereby sparking innovation— especially to address those needs arising from potential customers and competitors. In addition, theory supports the view that business models shape the external environment of which they are a part. This flux provides an opportunity to the business model to purposefully engage in social and environmental considerations—and as a result, to the organisation's multiple stakeholders—in addition to simply economic ones.

WINE FOR THOUGHT

To this end, BMs have recently become addicted to sustainability in addition to the lure of profits. As such, theory posits that a firm with a sustainability-centric business model will address economic, social, and environmental concerns in a uniform way—creating superior customer value and contributing to society.

In order to better understand these business models, Prof Zicari and his fellow researcher offer samplings of the Italian wine industry. Close to 800 small- and medium-sized enterprises (SMEs) were shortlisted to obtain data through questionnaires of which 106 firms—representative of the sample—were further studied. It allowed for a better understanding not only of the firms' structure, profitability, and ownership but also of elements of their business models.

The findings proved to be interesting. A basic analysis of these firms, over a period of three years, showed positive profitability indicators, yet their financial situation was leveraged indicating long term financial risk.

SUSTAINABILITY RUNS IN THE BLOOD

The corporate governance of the firms also added a layer of complexity to the results. As such, for other financial aspects being the same, family businesses showed more profitability as compared to non-family businesses. Further, the study showed that for family and non-family firms alike, customer value proposition was a core component. However, there was a major difference. Family businesses catered to foreign demand, while the others did not. Second, and perhaps more important, was the higher importance that family firms played in investing in sustainable projects to boost customer value.

Another major distinguishing factor was how the two kinds of firms viewed sustainability. As such, non-family firms favoured economic factors—reduced energy consumption, for example. By contrast, family businesses focussed on the production process—organic farming, reducing waste, and improving productivity. They also consider social aspects such as employee benefits and product quality under the aegis of sustainability.

Moreover, innovation as a key process of the business model was considered by both types of companies. And innovate to sustain was a key theme. This took the form of laying stress on direct go-green initiatives such as reducing crop protection products.

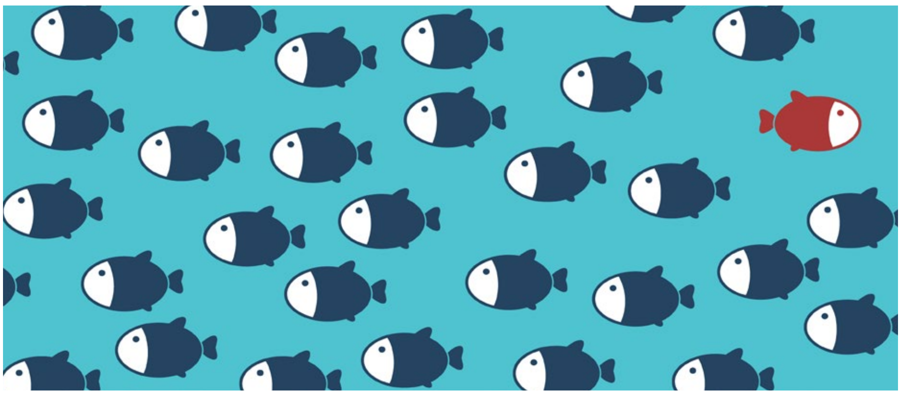
LOYALTY WILL BE REWARDED

As such, the different types of firms can innovate their own different business models to harvest the best possible fruit. Family firms—which also undertake viticulture—benefit from additional revenues from winery tours. This, augmented with a continuous customer-centric approach.

Subsequently, family firms engaged in rewarding loyalty and undertaking sustainable actions, have better economic performance. Even without seeking to reduce costs.

FERMENTING THE FUTURE

Given that the customers for both family and non-family are hospitality businesses and not end consumers, there is a strong demand for high quality products. As such, winegrowers and sellers who consider their product medium-quality should take this opportunity to invest in a more premium offering. And include sustainability as part of the package.



What's more, though sustainability is a key part of a business model 's innovation, there is still a notion of it being related only to the environment without considering the economic and social points of view. For firms have followed strategies that are add-ons and, to this end, they may do well to adopt a proactive approach that entails a complete overhaul of their business model focussed around sustainability.

Innovation need not be exclusively a high technology game. Rather a novel BM can change how the company operates in the market by addressing untapped needs, such as addressing end consumers directly and thereby avoiding costly intermediaries.

Bottling all these complex notes together is a task requiring special attention to processes and management control. Without letting it intoxicate you that you forget: Sustainability is everything—and not just in viticulture.

** Johnson, M. W., Christensen, C. M., & Kagermann, H. (2008). Reinventing your business model. Harvard business review, 86(12), 57-68.*

Adrian Zicari

KEY TAKE AWAYS

CERTAIN ORGANISATIONS CONSIDER SUSTAINABILITY A CORE ASPECT OF THEIR BUSINESS MODELS AND LEVERAGE IT TO OBTAIN ECONOMIC VALUE AND COMPETITIVE ADVANTAGE.

BUSINESS MODELS HAVE BEEN CONFUSED WITH OTHER MANAGEMENT JARGON SUCH AS STRATEGY AND BUSINESS CONCEPT. PROFS ZICARI AND BROCCARDO DESCRIBE A BM AS HAVING FOUR ELEMENTS—A CUSTOMER VALUE PROPOSITION, A PROFIT FORMULA, KEY RESOURCES, AND KEY PROCESSES.

THIS APPROACH ALLOWS BMS TO BE TWEAKED TO CHANGING REALITIES—THEREBY SPARKING INNOVATION—ESPECIALLY TO ADDRESS THOSE NEEDS ARISING FROM POTENTIAL CUSTOMERS AND COMPETITORS.

BMS SHAPE THE EXTERNAL ENVIRONMENT OF WHICH THEY ARE A PART, PROVIDING AN OPPORTUNITY TO THE BM TO PURPOSEFULLY ENGAGE IN SOCIAL AND ENVIRONMENTAL CONSIDERATIONS—AND AS A RESULT, TO THE ORGANISATION'S MULTIPLE STAKEHOLDERS—IN ADDITION TO SIMPLY ECONOMIC ONES.

A FIRM WITH A SUSTAINABILITY-CENTRIC BM WILL ADDRESS ECONOMIC, SOCIAL, AND ENVIRONMENTAL CONCERNS IN A UNIFORM WAY—CREATING SUPERIOR CUSTOMER VALUE AND CONTRIBUTING TO SOCIETY.

NON-FAMILY FIRMS VIEW OF SUSTAINABILITY FAVOURS ECONOMIC FACTORS—REDUCED ENERGY CONSUMPTION. FAMILY BUSINESSES FOCUS ON THE PRODUCTION PROCESS—ORGANIC FARMING, REDUCING WASTE, AND IMPROVING PRODUCTIVITY. THEY ALSO CONSIDER SOCIAL ASPECTS SUCH AS EMPLOYEE BENEFITS AND PRODUCT QUALITY UNDER THE AEGIS OF SUSTAINABILITY.

FIRMS ADOPT A PROACTIVE APPROACH THAT ENTAILS A COMPLETE OVERHAUL OF THEIR BM FOCUSSED AROUND SUSTAINABILITY.

A NOVEL, CSR AND SUSTAINABILITY-ORIENTED BM CAN CHANGE HOW THE COMPANY OPERATES IN THE MARKET BY ADDRESSING UNTAPPED NEEDS, SUCH AS ADDRESSING END CONSUMERS DIRECTLY AND THEREBY AVOIDING COSTLY INTERMEDIARIES.


The pioneering spirit

BASE-OF-THE-PYRAMID DNA: COMPANIES AND THE COMMON GOOD IN BRAZIL

Profs. **Edgard Barki** and **Juracy Parente** from **FGV-EAESP** explain the particularities of Brazil's poorest socio-economic market and what it takes to be in business at the base-of-the-pyramid.

From the paper Edgard Barki and Juracy Parente, "Challenges and opportunities of the last mile for the base of the pyramid: the case of Brazil".

TOUCHING BASE

THE BASE OF THE PYRAMID market (BoP) is used to refer to the demographic of a population which is the largest, but poorest socio-economic group in a marketplace. Since the 1940's there has been plenty of discussion about the poverty penalty, which means that despite being poor, this population usually pays more than the wealthier population for the same products. There are several reasons that explain this phenomenon, such as the need of credit, the behaviour of buying in smaller packages, and the difficulty to access larger, more efficient and cheaper retailers. In Brazil, covering the last mile to reach this market is the toughest, yet some companies have made it. In recent years, businesses have developed new strategies and business models to reach this demographic in an efficient manner, which has had a two-fold impact. For the business, performing well in this tough-to-reach market implies a distinct competitive advantage, while for the population itself, it implies a reduction in vulnerability, improvement in well-being, and access to basic products.

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Profs. Barki and Parente have identified the three criteria which have led companies to success in this market.

JUMPING THROUGH HOOPS AND HURDLES

To start off, Profs. Barki and Parente describe the obstacles that companies accessing this market are confronted with. First, retailers in this market face higher transaction costs. Usually the marketing channel is longer, and for a product to reach its destination, it must pass through several intermediaries. This is made more difficult by the infrastructure – such as roads and transportation – which is poor and costly. Moreover, in the shanty towns of metropolitan regions, there is a lack of urban infrastructure and safety. Geographically speaking, this market is defined by a network of capillaries and as a result, customers are usually far and difficult to reach. Profs. Barki and Parente explain that these factors are responsible for making distribution relatively costly and more challenging. Many decades have thus seen small retailers as the only force that powers this market. The institutional voids and challenges have inhibited large retailers to set shop in Brazil's poor socio-economic areas. As a result of their prolonged exposure to this market, small retailers have managed to build a distinct competitive advantage with their customers – an emotional relationship. Although small retailers tend to be more expensive, these emotional bonds have developed high loyalty among customers, and have transformed the small stores into fierce competitors for large retailers who more recently have been trying to enter the base-of-the-pyramid market.

THE MAGIC DNA

Due to the very distinct nature of this market, some companies have designed specific business units to serve the particularities of this demographic. 'Base-of-the-pyramid DNA' is the term Profs. Barki and Parente use to refer to the strategy and tactics, the fundamental aspects of company culture that are deeply ingrained in an organisation, and which are specific to a typical company successfully doing business in this market. Profs. Barki and Parente emphasise that only a business which 1) recognizes the market potential of the BoP and gives priority to sell and serve this market; 2) develops deep knowledge and understanding of the needs and peculiarities of the market; 3) treats this market with the same respect as it does others and 4) develops an empathic and two-way communication with the BoP players can claim to possess this particular DNA. Companies with base-of-the-pyramid DNA, that understand the peculiarities of the market and have an aligned strategy, are likely to possess a strong willingness to serve this demographic, and consequently more likely to create a satisfactory distribution strategy.

PUSHING COSTS DOWN

Execution is the second ingredient to attain success within this demographic. The institutional void presented by the market, which is characterised by lack of professionalisation, informality, unsafe routes, tedious network capillarity, distance, and lack of infrastructure are responsible for higher transactions costs for businesses. Profs. Barki and Parente's research finds that given the complexity of the market combined with the need to provide 'affordable' goods, business execution is a competitive advantage successful players laud over the rest. Efficient and suitable business execution ensures that overall costs stay low in a price-sensitive and tough-to-reach market. Consequently, small companies are known to be more successful since they are more flexible, more agile and operate in a small region, which ensures efficient distribution and low costs.

EVERLASTING BONDS

Finally, relationships. Given that the base-of-the-pyramid is characterised by a low level of professionalisation and a high level of informality, relationships, although important in any market, have a higher degree of relevance for this one. Difficult-to-access regions, different tastes, and customers are easier accessed with a network of strong partners. Partnerships tie the barely held together network of suppliers and retailers.

Smaller retailers – often under the impression of isolation from suppliers – are exceedingly receptive to supplier friendliness. Part of the same community, retailer-supplier relations are friendly, intense and key to ensuring a strong and extensive distribution network.

THE SUCCESSFUL CASE OF COCA-COLA BRASIL

Coca-Cola's Collective Platform has managed to make significant headway to the base of the pyramid while developing a mutually beneficial relationship with the community. The objective of the Collective Platform is *'to provide and contribute to the improvement of life of the base of the pyramid, offering tools for income generation and education and training to develop working and job skills.'* This project, developed in partnership with local NGOs, illustrates how Coca-Cola Brasil was able to generate positive socio-economic outcomes for the community, while at the same time reaping benefits from the value chain it helped establish. So far, the project has served more than 248,000 youngsters in 67 cities of Brazil. Surely, the company ticked the three checkboxes identified by Profs. Barki and Parente.

1. BoP DNA: To kick-off the program, and in order to develop its understanding and knowledge of the market, Coca-Cola Brasil created a dedicated 'social' business unit and engaged in extensive market research.

2. Execution: The company defined a set of metrics to accompany the project which included a mix of business and social indicators. These metrics, such as youth employment, confidence in the future, retail sales increase etc. allowed Coca-Cola Brasil to monitor, evaluate and execute its business operations in a way which was cost-effective and adapted to the functioning of this particular demographic.

3. Relationship: The Collective Platform has established two distinct relationships. On one hand, it has developed partnerships with NGOs. The company works directly with local NGOs to facilitate interaction with communities, and to help identify potential NGO partners. Moreover, Coca-Cola Brasil developed partnerships with other corporate giants, such as McDonald's and Microsoft. On the other hand, Coca Cola Brasil has organised community mobilisation programs, which necessitate the active participation of the community. To ensure this involvement, the company has developed programmes that are relevant and focused on the youth's need to become financially independent. Combined, these initiatives have helped increase brand love and improve Coca-Cola's relationship with the community.

A MUTUALLY BENEFICIAL RELATIONSHIP

Other crucial sectors face their own set of problems in reaching this set of customers. Health, financial, and education services across Brazil have all seen the development of new business models and innovative alternatives to reach the base-of-the-pyramid consumers. Interestingly, many businesses have employed technology as an ally to distribute services and diminish the distance to the base-of-the-pyramid. Technology has helped bridge the gap between business and this hard-to-reach demographic. Profs. Barki and Parente summarise the impacts of an efficient distribution as threefold: 'It allows consumers to access products and services that otherwise would be difficult to reach,' they state, 'which is more especially pertinent when we think of basic services, such as health, education, and financial services. Secondly, an efficient distribution is likely to diminish the poverty penalty and therefore reduce the vulnerability of the population. And thirdly, it might be developed into a meaningful source of competitive advantage for companies, both large and small.'

> "Coca-Cola's Collective Platform has managed to make significant headway to the base of the pyramid while developing a mutually beneficial relationship with the community."

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KEY TAKE AWAYS

(BOP) IS USED TO REFER TO THE DEMOGRAPHIC OF A POPULATION WHICH IS THE LARGEST, BUT POOREST SOCIO-ECONOMIC GROUP IN A MARKETPLACE.

DESPITE BEING POOR, THIS POPULATION USUALLY PAYS MORE THAN THE WEALTHIER POPULATION FOR THE SAME PRODUCTS DUE TO NEED OF CREDIT, THE BEHAVIOUR OF BUYING IN SMALLER PACKAGES, AND THE DIFFICULTY TO ACCESS LARGER, MORE EFFICIENT AND CHEAPER RETAILERS.

IN RECENT YEARS, BUSINESSES HAVE DEVELOPED NEW STRATEGIES AND BUSINESS MODELS TO REACH THIS DEMOGRAPHIC WITH TWO EFFECTS: FOR THE BUSINESS, PERFORMING WELL IN THIS TOUGH-TO-REACH MARKET IMPLIES A DISTINCT COMPETITIVE ADVANTAGE; FOR THE POPULATION ITSELF, IT IMPLIES A REDUCTION IN VULNERABILITY, IMPROVEMENT IN WELL-BEING, AND ACCESS TO BASIC PRODUCTS.

THE CHALLENGES: RETAILERS IN THIS MARKET FACE HIGHER TRANSACTION COSTS DUE TO A LONGER MARKETING CHANNEL WITH SEVERAL INTERMEDIARIES, POOR ROADS AND RAIL LINKS, SAFETY ISSUES LINKED TO THIS AND GEOGRAPHICALLY REMOTE CONSUMERS.

MANY DECADES HAVE SEEN SMALL RETAILERS AS THE ONLY FORCE THAT POWERS THIS MARKET. THEY HAVE BUILT A DISTINCT COMPETITIVE ADVANTAGE WITH THEIR CUSTOMERS – AN EMOTIONAL RELATIONSHIP.

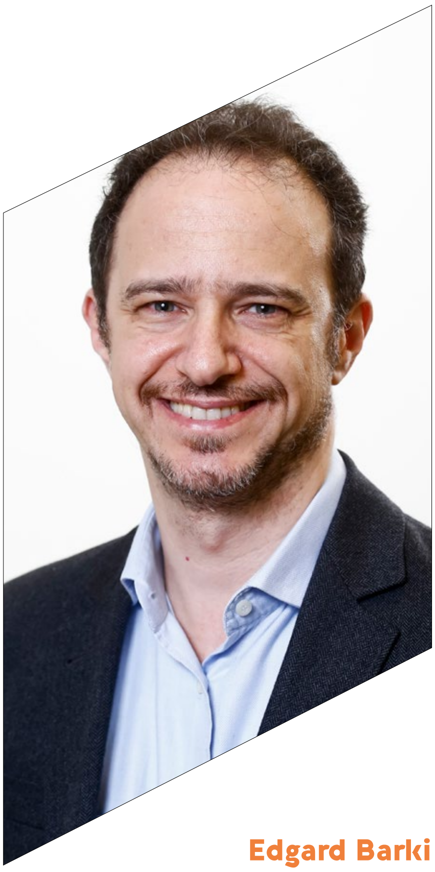
ALTHOUGH SMALL RETAILERS TEND TO BE MORE EXPENSIVE, EMOTIONAL BONDS HAVE DEVELOPED HIGH LOYALTY AMONG CUSTOMERS, AND HAVE TRANSFORMED THE SMALL STORES INTO FIERCE COMPETITORS FOR LARGE RETAILERS WHO MORE RECENTLY HAVE BEEN TRYING TO ENTER THE BASE-OF-THE-PYRAMID MARKET.

SOME BIG COMPANIES, TERMED 'BASE-OF-THE-PYRAMID DNA,' HAVE DESIGNED SPECIFIC BUSINESS UNITS TO SERVE THE PARTICULARITIES OF THIS DEMOGRAPHIC: THEY RECOGNIZE THE MARKET POTENTIAL OF THE BOP AND GIVE PRIORITY TO SELL AND SERVE THIS MARKET; THEY DEVELOP DEEP KNOWLEDGE AND UNDERSTANDING OF THE NEEDS AND PECULIARITIES OF THE MARKET; THEY TREAT THIS MARKET WITH THE SAME RESPECT AS IT DOES OTHERS; THEY DEVELOP AN EMPATHIC AND TWO-WAY COMMUNICATION WITH THE BOP PLAYERS AND CAN CLAIM TO POSSESS THIS PARTICULAR DNA.

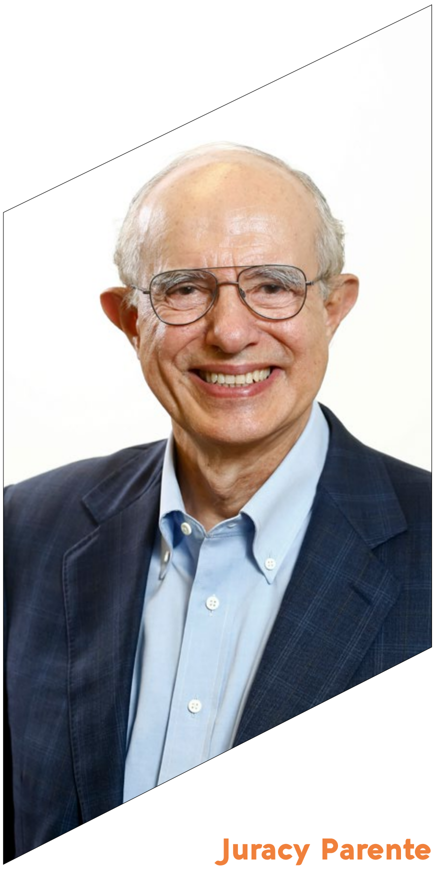
THESE COMPANIES ARE MORE LIKELY TO CREATE A SATISFACTORY DISTRIBUTION STRATEGY. EFFICIENT AND SUITABLE BUSINESS EXECUTION ENSURES THAT OVERALL COSTS STAY LOW IN A PRICE-SENSITIVE AND TOUGH-TO-REACH MARKET.

A SUCCESSFUL EXAMPLE IS COCA-COLA'S COLLECTIVE PLATFORM THAT HAS MANAGED TO MAKE SIGNIFICANT HEADWAY TO THE BASE OF THE PYRAMID WHILE DEVELOPING A MUTUALLY BENEFICIAL RELATIONSHIP WITH THE COMMUNITY, SERVING 248,000 YOUNGSTERS IN 67 CITIES OF BRAZIL.

HEALTH, FINANCIAL, AND EDUCATION SERVICES ACROSS BRAZIL HAVE ALL SEEN THE DEVELOPMENT OF NEW BUSINESS MODELS AND INNOVATIVE ALTERNATIVES TO REACH THE BASE-OF-THE-PYRAMID CONSUMERS. MANY OF THEM EMPLOY TECHNOLOGY AS AN ALLY TO DISTRIBUTE SERVICES AND DIMINISH THE DISTANCE TO THE BASE-OF-THE-PYRAMID.



Edgard Barki



Juracy Parente

FGV EAESP

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MANAGEMENT & LEADERSHIP

POST-TRUTH LEADERSHIP: SAVIOURS WHO AREN'T

> "In the post-truth world, organisations must be wary of turning leaders into strongmen – saviours."

From the charismatic leader who has the answers to it all, to the omnipotent leader who can always save the day, she who can spin a story is the hero. In the context of a world, where facts barely matter, Prof. Marianna Fotaki from Warwick Business School shatters the illusions of the post-truth leader who 'can' do it all.

HEROIC LEADERS have a lot to answer for. For every glossy, magazine-cover worthy Steve Jobs, there exists a Ken Lay – Enron's CEO who was jailed for fraud that led to the biggest bankruptcy in US history at that time. Both leaders boast of strong personalities, charisma in abundance, except that one of them was pulling their company in the wrong direction. Is the post-truth world responsible for the existence of these leaders? In the post-truth world, offering a compelling vision with a simple, resonating message has become the skill needed to 'cut through the noise'. And it has promoted the heroic leader, the strongman who can 'clear up a mess', 'sort things out' or 'defend our rights'.

Although a relatively recently coined term, post-truth has existed as a philosophical and political concept since long. Moreover, the Oxford dictionary defines it as "Relating to or denoting circumstances in which objective facts are less influential in shaping public opinion than appeals to emotion and personal belief".

THE POST-TRUTH LEADER'S RESUME

In her research, Prof. Fotaki explains how a typical post-truth leader operates – driven experts in understanding their audience, in handing them a message they want to hear and in adapting it to suit their purpose. "They master at creating an 'us and them' narrative", Prof. Fotaki points out, "so their side can stand on the side of apparent righteousness". It is not only politicians who are mired in half-truths, alternative facts and innuendo, but businesses too have demonstrated a long history of being less than transparent with the truth and cynically spinning the facts when they need to suit their purpose. One must not go amiss in dismissing that although post-truthism has emerged through the world of politics, it's chief architect Donald Trump built his reputation in the world of business. In its success, post-truthism has eroded, in much of the public's eyes, any genuine difference between pundits' claims and expert or 'scientific' assessment by normalising empty verbiage as a legitimate language.

NARCISSISM REARS ITS NASTY HEAD

In 2004, Michael Maccoby, leadership expert and author claimed that narcissists are good news for companies, because they have passion and dare to break new ground. Narcissism – a term applied to individuals who are incapable of empathy, unable to relate to and completely unaware of other people's needs, or even of their existence – has lulled modern society, with narcissistic leaders possessing a seemingly magnetic pull. Under growing uncertainty and the ruthless striving for innovation that characterises modern capitalism, narcissism can be increasingly observed in business leadership. Prof. Fotaki describes narcissism as a culture of echoes, where leadership and followership are bound by deep unconscious links and a shared identity that cannot easily be separated. As a result of these interconnections, narcissism and thus, narcissistic leadership, are popular because they can be flexibly used and abused, responding to any projection.

THE NARCISSIST'S IRRESISTIBLE PULL

How does the cape-wearing glorious leader turn into an evil narcissistic villain? In the post-truth world, organisations must be wary of turning leaders into strongmen – saviours. Entrusting leaders with such power, Prof. Fotaki maintains, leads inexorably towards disappointed expectations and a cynical workforce. Charismatic individuals, by generating social norms and discourses in an organisation – which pull the firm in a harmful direction – end up creating followers. Individuals or various groups, in order to claim viable social identities, tend to attach themselves to these negative norms and values. Prof. Fotaki emphasises that this is especially pertinent, given that those who aspire to be leaders are prone to narcissistic disorders; indeed, narcissism is often the driving force behind the desire to obtain leadership positions. In any organisation this desire for power can be intoxicating as followers may project their own capacity for thinking and decision-making onto the leader. In this way they become disabled and enter a phase of dependency with the leader. This point, Prof. Fotaki asserts, is where unethical behaviour can go unchecked and begin to be considered as the 'way things are done'. This is easily illustrated through recent corporate history, which is littered with several examples – from the LIBOR scandal, where bankers colluded to manipulate the price of the major benchmark for interest rates and financial products, to Dieselgate at Volkswagen.

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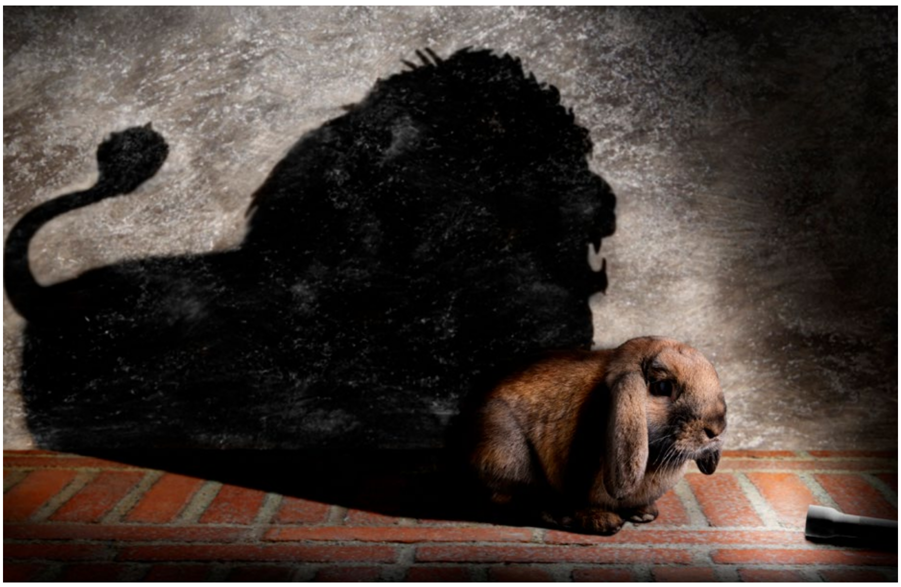

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VISIONARY OR DANGEROUS?

Although narcissism may be what an organisation needs at some point, even productive narcissists are often dangerous. Prof. Fotaki maintains that narcissists are divorced from the consequences of their judgements and actions, whenever these do not affect them directly, and hence, can be cavalier with organisational decision-making. Moreover, they strive at any cost to avoid painful realisations of failure that could tarnish their own image and choose only to listen to information they seek to hear, thus failing to learn from others. Moved by the desire to change the world, leaders can conceive a glorious new vision which may very quickly develop

into omnipotent disorders. Indeed, those who want to be leaders in an organisation have to tread a fine line that can wander into narcissism. Understanding how narcissism becomes increasingly prevalent in socially destructive ways is thus important for business leaders as they look to build trust within and outside their company

BEYOND BUSINESS

The proliferation of the dazzling narcissistic leader has seeped not only into businesses and organisations but also into pop-culture and policymaking. Popular media has contributed to the glorification of portrayals of corporate figures as 'psychopaths' who unscrupulously and skilfully manoeuvre their way to the highest rungs of the social ladder as fundamentally different from the rest of humanity. However, Prof. Fotaki strongly contests this belief. "This is a misconception," she asserts, "which obscures the pervasiveness of narcissism and the mechanisms that enable it to exist in any organisation".

Another victim claimed by pathological perversions is public policy. Take for instance the financial crisis of 2008. While on one hand, the separation of risk from responsibility could be viewed as creating perverse incentives enabling people to engage in greed – through financial bubbles that were bound to burst – on the other hand, this separation also permitted policymakers to disengage from the all-to-predictable consequences of such policies. Closer to home, a dramatic shift in public policy has occurred in Europe. Prof. Fotaki, sheds light on European policy where instead of ensuring liveable wages, access to affordable healthcare, public education and a clean environment, there is an increasing pre-occupation with how to unleash the alleged desire of citizens to enact their preferences of how public services should be provided. This is justified by claiming that citizens wish to choose between different providers to ensure best quality. However, at least within healthcare services, this is not borne out of evidence.

MOVING ONTO A POST-(POST-TRUTH) WORLD

With trust now replaced by cynicism, organisations – in the modern swirl of half-baked facts and vociferous opinion on social media – have to fight harder than ever to build trust and legitimacy with their stakeholders. This means rejecting the heroic leadership style so beloved in popular media and developing a new way forward that highlights and dismantles the strong pull of narcissism that post-truth leaders reveal. To survive the post-truth world of claim and counterclaim, leaders have to ensure their organisation is producing an authentic narrative and that its senior staff are displaying values that give credence to those messages. This requires leaders to be transparent and vigilant for emergent narcissistic tendencies in their organisations.

In the post-truth world for business, the temptation to adopt tactics that work is strong. Following narcissistic tendencies to appeal to emotion and developing half-truthful messages will surely bring in the social media followers. But if organisations are to prosper in the long-term, they need to reject this model of leadership and build trust with their stakeholders in a collaborative way that promotes transparency, as well as caring about the consequences actions have for others. It is the only sure method to banish the post-truth world.

KEY TAKE AWAYS

POST-TRUTH LEADERS ARE FAMOUSLY KNOWN FOR 'CLEARING UP MESSES', HAVE CHARISMATIC PERSONALITIES AND CAN CUT THROUGH THE NOISE TO VOICE A NARRATIVE WITH TWO SIDES – US AND THEM – WHERE THEY CLAIM TO BE ON THE SIDE OF APPARENT RIGHTEOUSNESS.

MODERN SOCIETY BELIEVE GLORIFIES NARCISSISTIC LEADERS AND BELIEVES THEY ARE ESSENTIAL TO THE FUNCTIONING OF MODERN CAPITALISM – WHERE INNOVATION IS PARAMOUNT.

PEOPLE WITH AMBITION TO BE LEADERS ARE PEOPLE WHO ARE PRONE TO NARCISSISTIC TENDENCIES. IF HANDED TOO MUCH POWER, LEADERS CAN CREATE NEGATIVE SOCIAL NORMS AND BEHAVIOURS WHICH CAN GENERATE A FOLLOWING AND SENSE OF ASSOCIATION FROM FOLLOWERS WITHIN AN ORGANISATION. THIS IS WHERE UNETHICAL BEHAVIOUR CAN GO UNCHECKED AND BECOME A NORM.

EVEN PRODUCTIVE NARCISSISTS CAN BE DANGEROUS TO AN ORGANISATION. NARCISSISTS ARE OFTEN DIVORCED FROM THE CONSEQUENCES OF THEIR ACTIONS AND, IMMUNE TO THE NEEDS AND EMOTIONS OF OTHER, AVOID REALISATIONS OF FAILURE THAT CAN TARNISH THEIR IMAGE. LEADERS TREAD A VERY THIN LINE THAT CAN EASILY TURN FROM HAVING A VISION TO BECOMING OMNIPOTENT AND DEVELOPING NARCISSISTIC DISORDERS

POPULAR MEDIA, BUSINESS AND POLICYMAKING ARE ALL FRAUGHT WITH IDEAS OF CORPORATE 'PSYCHOPATHS' WHO ARE IMMENSELY SUCCESSFUL AS A RESULT OF THEM BEING 'DIFFERENT' FROM THE REST. THIS IS A MISCONCEPTION WHICH SIMPLY ALLOWS US TO VIEW THE PERVASIVENESS OF NARCISSISM AND THE MECHANISM WHICH ALLOW IT TO EXIST IN SOCIETY.

ORGANISATIONS MUST REJECT THIS IDEA OF 'HEROIC' LEADERSHIP TO FIGHT HARDER THAN EVER TO BUILD TRUST AND LEGITIMACY WITH THEIR STAKEHOLDERS. LEADERS HAVE TO ENSURE THEIR ORGANISATION IS PRODUCING AN AUTHENTIC NARRATIVE AND THAT ITS SENIOR STAFF ARE DISPLAYING VALUES THAT GIVE CREDENCE TO THOSE MESSAGES. THIS REQUIRES LEADERS TO BE TRANSPARENT AND VIGILANT FOR EMERGENT NARCISSISTIC TENDENCIES IN THEIR ORGANISATIONS.

Marianna Fotaki

CALLING BEHAVIORAL INTEGRITY: WHAT MAKES EMPLOYEE VOICE STRONGER?

Employees giving voice to opinions and suggestions is risky but beneficial to an organisation. Professor He Peng from School of Management Fudan University analyses what makes employees go silent and how leader behavioural integrity can break that silence.

From the paper « Peng, H., Wei, F. How and When Does Leader Behavioral Integrity Influence Employee Voice? The Roles of Team Independence Climate and Corporate Ethical Values. (2019) »

IN HER BLOG POST that went viral in February 2017, Susan J. Fowler revealed what happened when she repeatedly voiced her criticism for the prevalent gender discrimination and sexual harassment at Uber, of which she was a victim. Fowler's story plays out like a broken record, stuck at Fowler voicing her concerns to management and HR, and repeatedly getting ignored. Her story reveals a pattern – of HR and management pedalling lies, wrangling the truth to their convenience to serve private political games, and of unclear management priorities as a result of differences between organisational and managers' personal goals. In the era of the knowledge-based economy where employee voice is crucial to an organisation's survival, where organisations must leverage employee initiatives to carry on, Prof. Peng's latest research highlights the relationship between a leader's behavioural integrity and employee voice.

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UNDERSTANDING EMPLOYEE VOICE

An employee's voice can be a revolutionary tool. Yet, it is not a default choice; employees often withhold suggestions or advice when they may have ideas, concerns, or opinions. Regarded as a key factor that influences creativity and effectiveness at the individual, team and organisational level, employee voice improves effective decision making, organisational learning and improvement, implementation of new practices and better organisational innovation. So why keep it to yourself? Prof. Peng unravels this mystery. He insists that one of the important reasons for withholding advice or suggestions is that voice is a sort of extra upward communication that challenges and seeks to change the status quo although its intention may be constructive. Employee voice may affect other people's feelings, egos, or work routines. Broadly speaking, employee voice is inherently a very risky endeavour. Prof. Peng's research finds that a leader's behavioural integrity helps foster it – when leaders walk the talk, employees are more likely to speak up. What's more, Prof. Peng reveals that team-level climate and the level of corporate ethical values can impact this relationship.

SPEAKING UP: A RISKY BUSINESS

Interestingly enough, employee voice was conceptualised as a response to job dissatisfaction in its infancy. However, soon it took on a more profound definition. "Employee voice is a form of extra-role behaviour", Prof. Peng explains, "which refers to informal and discretionary communication by an employee of ideas, suggestions, concerns, information about problems, or opinions about work-related issues to persons who might be able to take appropriate action, with the intent to bring about improvement or change". Voicing suggestions or opinions in the workplace requires honesty and is risky in nature. And although speaking up may lead to improvement and demonstrate an employee's competence or creativity, it has the potential to upset leaders. Leaders tend to want to insist on established procedures or practices given that they have invested significant time and effort in putting them in place. It is also not surprising, Prof. Peng claims, if leaders feel a strong psychological ownership of the procedures they have established. In this light, if an employee decides to voice their opinions or suggestions, leaders may feel challenged and consider these opinions as a criticism to their own managerial competence, and as result label employees as 'negative' or 'untrustworthy'. It is no wonder then that employees are often uncertain about how their managers may react to suggestions and thus consider speaking up risky. "It is very important for organizations to create environments in which employees feel safe by encouraging them to speak freely, honestly, and openly", Prof. Peng insists. This is where leaders' behavioural integrity comes in to play.

WHEN LEADERS WALK THE TALK

Confusion over what leader behavioural integrity means has haunted researchers. For Prof. Peng, behavioural integrity is "the perceived pattern of alignment between an actor's words and deeds". Observations overtime help develop an employees' perception of leader behavioural integrity. For leaders this means, perceived promise-keeping and the degree of match between espoused and enacted values, usually associated to virtuous behaviour. Prof. Peng points out the overarching influence of leader behavioural integrity. It not only affects leader performance, but also influences 'follower' behaviour in terms of employee/follower organisational commitment, citizenship behaviour, task performance, and creativity. Prof. Peng emphasises that alignment between words and actions can signal to subordinates that the leader is credible. This establishes trust between leaders and subordinates since this match between words and deeds provide certainty, predictability and reliability. As a result, workers experience an open, safe, trustworthy, and supporting working environment where they are more likely to speak up. Moreover, Prof. Peng affirms that when leaders consistently walk their talk, they send clear signals about which behaviours are encouraged and unencouraged. When there is less role-related ambiguity and uncertainty, employees will be more likely to speak up because they can figure out their leaders' actions and feel safe to adopt appropriate ways to voice their concerns. Uncertainty, on the other hand, brought on by a leader's failure to follow through on her espoused values will send mixed and ambiguous signals. Employees, lost in uncertainty, will invest significant time and energy to navigate these murky waters and in the absence of clarity of managerial expectation, will feel unsafe to voice their opinion/suggestions. As such, to instil a safe environment for employees to speak up, Prof. Peng stresses the importance of leader behavioural integrity.

CHECKING THE CLIMATE FOR INDEPENDENCE.

Another ingredient that amplifies an employee's willingness to speak up is a phenomenon Prof. Peng refers to as team independence climate. Employee voice is encouraged in a climate where the norm within a team is to follow their own personal ethical beliefs. A shared ethical perception of what is right or wrong helps create a team climate conducive to employee voice. An independence climate encourages individuals to adhere to their personal independent moral judgments, and subsequently can increase employees' courage to speak up. Moreover, team independence climate may encourage employees to hold higher ethical standards and emphasise the interests of their organisations ahead of their personal interests. Because speaking up is generally regarded as helpful and beneficial, employees in an independence climate may experience an obligation to speak up for the organisational interests. But what creates such a climate? Behavioural integrity, Prof. Peng claims. He explains that an organisation's moral climate reflects the moral development of the organisation's leader. Furthermore, he argues that leaders with high behavioural integrity can help to shape team independence climate, not only by demonstrating adherence to their own principles but also by creating a clear, predictable, and trustworthy environment in which employees dare to insist on their personal morality.

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ETHICS: A DEAL BREAKER

Although leader behavioural integrity is one of the key factors influencing team independence climate, Prof. Peng's research finds that corporate ethical values also play an important role in the formation of such a climate. Corporate ethical values pervasively influence the organisation at all levels and are the underpinnings of all other specific organisational values because they help to establish and maintain basic behavioural standards about what things are right to do and what things are worth doing. When ethical values are highly emphasised in an organisation, employees receive clear signals about what is important in the organisation, and subsequently experience a consistent perception about what is expected of them and what they can expect in turn. This helps develop trust between employees and leaders, and a climate conducive to employee voice.

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TURNING THE VOLUME UP: A PRACTICAL GUIDE

To sum up, Prof. Peng's research highlights the importance for managers to realise the need to walk their talks and keep promises as a means to foster employee voice. For high-tech organizations that urgently need to foster employee voice and encourage team creativity, Prof. Peng suggests that leaders with high degrees of behavioural integrity be recruited. To inculcate greater leader accountability, setting up incentive systems that encourage leaders to be match their words to their actions are recommended. When it comes to fostering an independence environment conducive to employee voice, Prof. Peng recommends organisations add principled values such as moral integrity into their employee selection criteria for example. Organisations may also use employee training sessions to help instil beliefs that are conducive to a principled independence climate. To help build an independence climate, managers can behave as role models who adhere to principled ethical values. In addition, they can provide their employees with the latitude to make decisions in the interest of justice, morality and respect for human rights, regard less of organisational context. Ethical values, another ingredient necessary for employee voice, require top managers to set a personal example. If managers wish to develop a strong sense of moral integrity, they should simply adhere to designated ethical values in addition to establishing reasonable systems of incentives and punishments to help encourage and maintain positive attitudes and behaviours demonstrative of the team's ethical values.

Behavioural integrity is the key to unlocking employee's voice. And unlocked it must be. Susan J. Fowler's example demonstrates two things: First, how the lack of an independence work environment and behavioural integrity from leaders, an inconsistency in ethical values, and ambiguous organisational expectations from employees can supress employee voice and thus be detrimental to an organisation. Second, it highlights the importance of employee voice as well as its relationship with leader behavioural integrity. Where there is integrity, voice will prosper. Luckily for Uber's employees, what was originally intended as a blog post that looked back on Ms. Fowler's time at Uber after she had quit the organisation ended up ousting Uber's then CEO and revealed the many cracks in the tech industry's foundation. But it begs the question if management behavioural integrity might have done the job quicker.

He Peng

KEY TAKE AWAYS

EMPLOYEE VOICE INFLUENCES CREATIVITY AND EFFECTIVENESS AT THE INDIVIDUAL, TEAM AND ORGANISATIONAL LEVEL, IMPROVES EFFECTIVE DECISION MAKING, ORGANISATIONAL LEARNING AND IMPROVEMENT, IMPLEMENTATION OF NEW PRACTICES AND BETTER ORGANISATIONAL INNOVATION.

EMPLOYEES OFTEN WITHHOLD SUGGESTIONS OR ADVICE WHEN THEY HAVE IDEAS, CONCERNS, OR OPINIONS, UNSURE OF MANAGEMENT'S REACTION AND THE ORGANISATIONAL EXPECTATIONS. EMPLOYEE VOICE REQUIRES HONESTY AND IS A RISKY BEHAVIOUR.

BEHAVIOURAL INTEGRITY IS WHEN LEADERS' ACTIONS ARE ALIGNED WITH THEIR WORDS. WHEN LEADERS HAVE HIGH BEHAVIOURAL INTEGRITY, THEY CREATE TRUST AND COME OFF AS RELIABLE; THIS ENCOURAGES EMPLOYEE VOICE.

EMPLOYEE VOICE IS ENCOURAGED IN A CLIMATE WHERE THE NORM WITHIN A TEAM IS TO FOLLOW THEIR OWN PERSONAL ETHICAL BELIEFS. A SHARED ETHICAL PERCEPTION OF WHAT IS RIGHT OR WRONG HELPS CREATE A TEAM CLIMATE CONDUCIVE TO EMPLOYEE VOICE. THIS INDEPENDENCE CLIMATE ENCOURAGES INDIVIDUALS TO ADHERE TO THEIR PERSONAL INDEPENDENT MORAL JUDGMENTS, AND INCREASE EMPLOYEE VOICE.

CORPORATE ETHICAL VALUES, WHEN HIGHLY EMPHASISES, ALSO ENCOURAGE EMPLOYEE VOICE.

THIS RESEARCH SUGGESTS THAT TO ENCOURAGE EMPLOYEE VOICE, ORGANISATIONS NEED TO RECRUIT EMPLOYEES WITH A HIGHER DEGREE OF BEHAVIOURAL INTEGRITY, SET UP INCENTIVE AND TRAINING SYSTEMS THAT ENCOURAGE BEHAVIOURAL INTEGRITY, AND FOR MANAGERS TO LEAD BY EXAMPLE.

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DO GOOD, DO WELL AND BE SINCERE: THE PATH TOWARDS A HIGH-IMPACT CORPORATE PHILANTHROPY STRATEGY

CSR is more about substance over form than just doing – or doing more: Prof. **Ping-Sheng Koh** of **ESSEC Business School, Asia-Pacific,** shares his research into how firms can effectively create win-win value through their giving.

Ilya R.P. Cuypers, Ping-Sheng Koh, Heli Wang (2016) Sincerity in Corporate Philanthropy, Stakeholder Perceptions and Firm Value. Organization Science 27(1):173-188. http://dx.doi.org/10.1287/orsc.2015.1030

GENEROSITY ONLY GETS YOU SO FAR

TAKE THE TOP 10 corporate givers in 2018-2019. All of them household names. Among them Alphabet (Google), Walmart, Goldman Sachs, Microsoft and – lodged in the middle of the list – 2 petroleum multinationals: Exxon Mobil and Chevron.

Perhaps you are an investor. And if not investor then consumer or simple citizen that you are. How do you feel about that? Truth is, your perception of these two oil giants would most probably lead you to brush their

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generosity aside and veer towards at least skepticism, at most a condemnation of blatant greenwashing. This is exactly what Profs Ping-Sheng Koh of ESSEC Business School, Asia-Pacific and Ilya R.P. Cuypers and Heli Wang of SMU, have found in their research on corporate philanthropy. Giving more is not always better – in fact it can make things worse. As such, they take a step further than previous studies to explore not only the questions of why and how companies give, but also how a firm's value is impacted by how its stakeholders perceive it, the firm's line of business and its lifecycle. This amounts, in many ways, to a best-practice strategy for corporate philanthropy.

WHY GIVE?

For a long time, it was thought that a company's sole reason for being was to create profit and maximize economic efficiency. Philanthropy was seen as diverting valuable firm resources away from a firm's business operations and in doing so reducing shareholder wealth. But recent decades have witnessed the growing influence of businesses in many aspects of social and political life which has led to growing interest in the impact of their actions on employees, communities, society and the environment. Public awareness has given rise to pressure and expectations for firms to engage in philanthropic activities. Moreover, studies have shown that there is a positive relationship between corporate giving and the firm's financial performance.

Today, philanthropy is value. Indeed, customers often perceive firms engaging in corporate philanthropy as having better product quality and customer care and tend to remain loyal while being ready to pay a higher price for their brands' products and services. Investors too, are now increasingly picky when it comes to choosing where they place their money and even governments bring out the carrot and the stick by providing support to firms committed to philanthropy and punishing those that don't by controlling firms' access to credit. As such, it seems in the best interests of a modern firm to give – but there's a catch. They often have different underlying motives for giving, in what they give, and how they give it.

Some, for example, engage in long-term, high-impact philanthropy to genuinely fulfill their shareholders' expectations, while others, to return to the notion of greenwashing, indulge in symbolic actions – mere short-term shots at polishing up their external image.

SINCERITY, SINNERS, SAVIOURS AND STAGES

For Prof Koh, this matters. Moreover, with his fellow researchers he set out to prove, using data from nearly 3,500 US firms and their corporate giving over a 19-year period, that 4 dimensions have a direct impact on the shared value that philanthropy can generate:

• Stakeholder perception and firm value: You can judge a book by its cover

Largely overlooked in previous studies, Prof. Koh and his colleagues integrated the role of a firm's stakeholder (customers, investors, shareholders, the community in which the firm operates) perceptions. He argues that the meaningful impact of a firm's philanthropic actions is not solely determined by the actions themselves, but by how stakeholders perceive them. On the one hand, when actions are perceived as meaningful, corporate philanthropy is likely to be more positively associated with firm value. And on the other, if stakeholders see a firm's actions as symbolic and without substance, then the firm will benefit less from charitable acts. Indeed, how stakeholders perceive and attribute corporate philanthropic activities has been argued to be the key mechanism through which firms can gain positive returns from corporate philanthropy.

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• Generous versus innovative giving: Size isn't everything

Because it's difficult for people to see a firm's motives for engaging in philanthropy, stakeholders must rely on various information to assess whether a firm is providing meaningful or purely symbolic giving. It's here that the difference can be made between generous giving and innovative giving. Donating a healthy million or more may be seen as gaining greater credibility for a firm and thus influence perceptions to believe in the sincerity of the gesture, improve public image and build rapport with stakeholders. On the other hand, innovative giving – that is, when a firm commits effort and resources to carefully design actions aimed at promoting long-term self-sufficiency and social improvement among the recipients (such as training and education or energy autonomy) – earns greater credibility. As such, innovative giving enhances the giving firm's reputation as a genuine and sincere donor in the eyes of its stakeholders. If the two types are compared – generous and innovative – it is the latter that is more likely to be perceived by stakeholders as being meaningful rather than symbolic. Better still – if firms can afford it – mix the two: give generously and make it useful and meaningful.

• Type of firm: Of sin and sincerity

In addition to the quantity and quality of a firm's philanthropic activities, stakeholders also search for cues that can help them assess if a firm is sincere or not. One of these is the firm's activity or product line. Take Philip Morris, for example. When the firm made an annual commitment of $175 million in donations in 1999, most critics dismissed it as an attempt to buy respectability and legitimacy. In people's minds tobacco and its associated undesirable consequences just could not be associated with doing good. Indeed, firms dealing in 'sin' products – tobacco, alcohol and gaming – are subject to even greater scrutiny from stakeholders under which generous giving (i.e., the quantitative aspect) is even more likely to be questioned than innovative giving. Let's return to the opening example in this article of the oil & gas companies featuring in the world's top twenty donors. The $268 m given by Exxon Mobil in 2015 might well spark initial feelings of distrust given the firm's activities and their negative side-effects. But look a little closer and you'll see that Exxon Mobil's money went into education programmes, malaria treatment and economic opportunity for women throughout the world. Have our perceptions changed as a result? In all appearance, the firm is engaged in innovative giving – with meaning and impact – so the answer is most probably yes, if even slightly. To sum up, stakeholders distrust big firms involved in selling sin products who give large amounts of money to philanthropic actions. But if the action is innovative and involves tangible, positive impact and meaning, then they are likely to consider the giving as sincere and, to a degree, 'forgive these firms their sins'. In short, give a lot – and give it substance.

> "Being known for doing good with genuine motives is essential for charitable acts to be truly value-enhancing for both business and society alike."

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• Firm life-cycle: All the world's a stage...

Prof. Ping-Sheng Koh et al added a new dimension to their research in the form of the firm's life-cycle stage, contending that this provides another source of information for how stakeholders may perceive and assess a firm's philanthropic activities. This is bad news for mature companies. Of the three stages considered – growth, mature and shakeout – their study of 3,500 US firms over time points to mature companies' corporate giving being seen as less sincere than the others. Why? Because the latter are often considered cash cows, rich in resources and with limited investment possibilities, ready to spend generous sums in order to give shine to their image. Remember – it's not size that necessarily counts.

On the other hand, perceptions change when firms in their growth phase are considered. Here, firms face intense challenges, requiring large amounts of borrowed capital and effort to gain market share. As such, regardless of whether the giving is generous or innovative in nature, stakeholders see a firm's philanthropic actions at this stage in their life as something of a sacrifice and a sincere commitment in their intention to do good. The same goes for firms in the shakeout phase. Here, firms face difficult challenges to overcome in order to avoid decline. Growth decreases, profits are squeezed and resources, especially financial, become scarcer. Once again, stakeholders tend to view these factors as a convincer when firms at this stage commit to philanthropy. In a nutshell, it is likely that both generous and innovative giving by companies in the growth and shakeout stages of their life-cycle will be considered as having substance, meaning and impact. As a result, these firms are likely to reap the rewards of their giving via improved reputation, customer loyalty and increased investor interest.

THE WAY FORWARD FOR CORPORATE GIVING

Prof. Koh's research points to several important implications for the practice of corporate philanthropy, not least the prerequisite that although it generally pays for firms to engage in corporate giving, managers must keep in mind that not all corporate philanthropy is valued equally. To garner consistent positive capital and add to firm value and financial performance from their philanthropic initiatives, it is sincerity that counts rather than donating to earn smileys among its stakeholders and the wider community. Being known for doing good with genuine motives is essential for charitable acts to be truly value-enhancing for both business and society alike. The research shows that even sin firms, if they are genuine in their philanthropic activities, can do good and be recognised for their efforts. All in all, it is not so much about whether philanthropy in itself adds value to a firm, but how firms can engage in philanthropy and add value in the face of their constraints on resources. Avoiding self-interest, demonstrating sincerity, achieving the delicate balance between economic and social responsibility and being sensitive to one's stakeholder opinion, are key.

KEY *TAKE AWAYS*

THE MEANINGFUL IMPACT OF A FIRM'S PHILANTHROPIC ACTIONS IS DETERMINED BOTH BY THEIR ACTIONS AND BY HOW STAKEHOLDERS PERCEIVE THEM. WHEN ACTIONS ARE PERCEIVED AS MEANINGFUL, CORPORATE PHILANTHROPY IS LIKELY TO BE MORE POSITIVELY ASSOCIATED WITH FIRM VALUE.

A DIFFERENCE CAN BE MADE BETWEEN GENEROUS GIVING AND INNOVATIVE GIVING. INNOVATIVE GIVING ENHANCES THE GIVING FIRM'S REPUTATION AS A GENUINE, MEANINGFUL AND SINCERE DONOR IN THE EYES OF ITS STAKEHOLDERS

MATURE COMPANIES' CORPORATE GIVING IS SEEN AS LESS SINCERE BECAUSE THEY ARE OFTEN CONSIDERED CASH COWS, RICH IN RESOURCES AND WITH LIMITED INVESTMENT POSSIBILITIES, READY TO SPEND GENEROUS SUMS IN ORDER TO EMBELLISH THEIR IMAGE.

IN THE GROWTH STAGE, REGARDLESS OF WHETHER THE GIVING IS GENEROUS OR INNOVATIVE IN NATURE, STAKEHOLDERS SEE A FIRM'S PHILANTHROPIC ACTIONS AS SOMETHING OF A SACRIFICE AND A SINCERE COMMITMENT IN THEIR INTENTION TO DO GOOD.

IN THE SHAKEOUT STAGE, A FIRM'S GROWTH DECREASES, PROFITS ARE SQUEEZED AND RESOURCES, ESPECIALLY FINANCIAL, BECOME SCARCER. THE FIRM'S PHILANTHROPY IS THEREFORE SEEN AS SINCERE.

IT IS NOT SO MUCH ABOUT WHETHER PHILANTHROPY IN ITSELF ADDS VALUE TO A FIRM, BUT HOW FIRMS CAN ENGAGE IN PHILANTHROPY AND ADD VALUE IN THE FACE OF THEIR CONSTRAINTS ON RESOURCES.

AVOIDING SELF-INTEREST, DEMONSTRATING SINCERITY, ACHIEVING THE BALANCE BETWEEN ECONOMIC AND SOCIAL RESPONSIBILITY AND BEING SENSITIVE TO ONE'S STAKEHOLDER OPINION, ARE KEY.

Ping-Sheng Koh

EUROPE IN THE SHADOW OF BREXIT: TIME TO RETHINK COMPANY STRATEGY

Caterina Moschieri and **Daniel Blake,** Associate Professors at **IE Business School** analyse the far-reaching implications of Brexit on organisational structure and strategy.

Based on the paper titled "The organisational implications of Brexit" penned by Caterina Moschieri and Daniel J Blake in the Journal of Organization Design, 8:1.

FROM THE END ofFrom the end of the Second World War through to the early 1970s, the world witnessed growing economic integration facilitated by the creation of international institutional arrangements such as the World Trade Organisation, ASEAN, and the EU. Fast forward a few decades and look around one more time. This time you'll see the Catalan uprising for independence, President Trump's withdrawal from the Trans-Pacific Partnership and Brexit. What do these events have in common? The answer: the rather disquieting, and yet growing, sentiment of anti-globalisation. Let's take Brexit as an example to highlight the unsettling changes on company strategy and organisational structure that inevitably follow a powerful disruption to the institutional foundations of economic integration.

WHEN THE GATEWAY TO EUROPE STARTS CRUMBLING

For many non-European countries around the world, the UK has been the perfect "gateway to Europe." A stable currency, relatively liberal economic policies and strong institutions made the UK an ideal manufacturing hub. The automotive industry, for instance, is an excellent example of a top exporter from the UK to Europe. But, Brexit is going to change the game by, in all likelihood, raising barriers to trade and incentivising UK-based exporters to transfer much of their production process from the UK to countries which are part of the EU.

What is less obvious is that even firms which were producing predominantly for the domestic market will suffer. These firms often rely on raw material imports from the EU for their production. With Brexit looming on the horizon, these firms have to either find local suppliers or vertically integrate more of their value chain domestically. The firms who stand to gain from this transformation are the UK-based manufacturers of substitutes for European imports who can seize this opportunity to strengthen their position in the domestic market. This, however, could be countered by European suppliers who may choose to establish independent operations in England in order to hold on to their markets there.

Unfortunately, tariff barriers and mounting transaction costs constitute only the tip of the iceberg. A major likely outcome of Brexit would be the loss of regulatory harmonisation, which will require firms to ensure compliance with two separate sets of certification procedures for their products – one for the EU and another for the UK. This would cost them not just money, but also a lot of time.

SAY GOODBYE TO 'PASSPORTING'...

Thanks to a process called 'passporting,' London-based financial institutions had the right of automatic access to European financial markets owing to the license they have from the UK government. But once Brexit is finalised, the authorisation by the UK government will cease to be a valid passport to operate in the rest of EU. On top of that, the European Central Bank has restrictions on the extent of operations that European banks can establish in "third party" countries, and this will come into effect for the UK once Brexit renders them a "third party." As such, it's no wonder that many banks have already begun to strengthen their operational presence in other financial hubs such as Paris, Frankfurt and Dublin.

The aviation industry is in a similar position with carriers such as Ryanair and EasyJet facing a potential struggle to maintain licenses to operate between EU destinations. Such firms may look to restructure their ownership to ensure they are minimum 50% EU owned and controlled in order maintain access to the intra-EU travel market. But that is certainly easier said than done.

...AND HELLO TO BRAIN DRAIN

With English being a commonly spoken second language in the EU, the UK has been a popular destination for some of Europe's best talent and consequently, a centre for innovation. But post-Brexit, barriers to immigration are likely to be much more significant given the fact that immigration was a dominant issue in the debate surrounding the Brexit vote. These barriers threaten the supply of skilled and unskilled workers to the UK, and the overall competitiveness of Britain's workforce. A post-Brexit brain drain from Britain may be further exacerbated by the limited access that British universities will have to European funding for research. Once again, firms investing in research activities in the UK may have to start shifting their R&D activities progressively outside the UK. But the good news is that they can relocate to emerging markets since proximity to market is not always critical when it comes to R&D activities.

RE-ORGANISING IN THE FACE OF UNCERTAINTY

Multinational firms operating across Britain and Europe will soon find themselves operating in increasingly distinct jurisdictions. This may trigger them to create a regional structure, similar to EMEA, to account for the proximity, and yet the differences, between the EU and the UK. This would call for a shift towards a multi-domestic or transnational strategic orientation with greater autonomy granted to local units operating in the EU and Britain respectively to enable them to adapt to different local regulatory and institutional demands. Consequently, organisations, in terms of vertical structure, business units, individual roles, and reporting lines will be affected significantly.

It took over two years of wrangling between the EU and the UK to reach a Brexit deal. Moreover, negotiations over the future of the EU-UK economic relationship have only just begun and progress is likely to be delayed due to the region's efforts to contain and manage the COVID-19 pandemic. Under this prolonged cloud of uncertainty, many firms will continue to withhold investments in the UK. They are hedging their bets by setting up operations in mainland Europe while not completely closing down activities in the UK yet. Regardless of the post-Brexit deal that is reached, Britain has lost some of its credibility as a country with a reliable and predictable business environment.

BEARING THE BRUNT OF BREXIT

Brexit will, beyond a vestige of doubt, be accompanied by high adjustment costs. These will include direct increases in transaction costs associated with restriction on cross-border activities as well as the costs associated with re-locating employees and operations. These additional costs will be passed on to shareholders and consumers too, meaning all concerned parties stand to lose.

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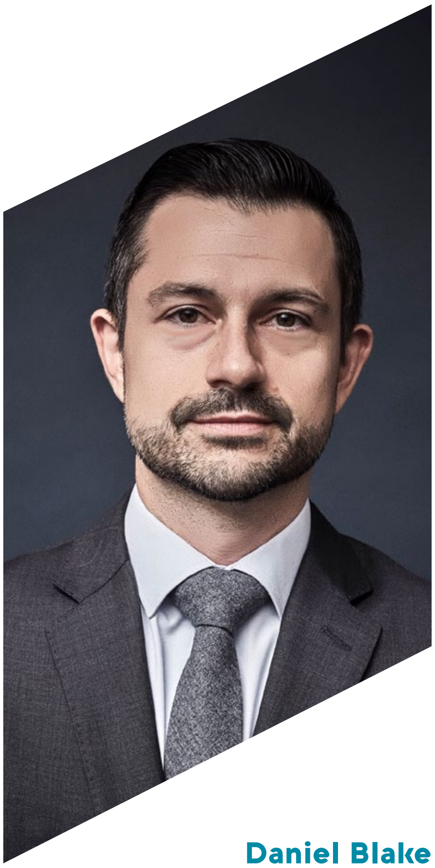
One might assume that domestic firms that are not engaged in cross-border activity will suffer less, but that is not necessarily the case, particularly for British companies. For instance, the British construction industry still currently benefits from easy access to labour and just-in-time supply of raw materials from the EU. A post-Brexit disruption in these two areas will inevitably affect construction firms.

Although we still do not know the final terms that will govern EU-UK economic relations post-Brexit, a difficult and costly period of adjustment beckons. Such is the price of operating in a global business environment where the institutions that guide the global economy are always subject to pressure and change, and where nation-states have the scope to quickly re-establish borders that had become increasingly irrelevant.



Daniel Blake

Caterina Moschieri

KEY *TAKE AWAYS*

BREXIT WILL RAISE BARRIERS TO TRADE AND INCENTIVISE MANUFACTURERS TO TRANSFER THEIR PRODUCTION PROCESS FROM THE UK TO EU COUNTRIES.

LOSS OF REGULATORY HARMONISATION WILL LIKELY OCCUR, REQUIRING FIRMS TO ENSURE COMPLIANCE WITH TWO SEPARATE SETS OF CERTIFICATION PROCEDURES FOR THEIR PRODUCTS – ONE FOR THE EU AND ANOTHER FOR THE UK – COSTING THEM MONEY AND TIME.

THE EUROPEAN CENTRAL BANK HAS RESTRICTIONS ON THE EXTENT OF OPERATIONS THAT EUROPEAN BANKS CAN ESTABLISH IN "THIRD PARTY" COUNTRIES, AND THIS WILL COME INTO EFFECT FOR THE UK ONCE BREXIT RENDERS THEM A "THIRD PARTY."

AS THE SUPPLY OF SKILLED AND UNSKILLED WORKERS TO THE UK WEAKENS, BRITAIN'S WORKFORCE WILL LOSE SOME OF ITS COMPETITIVENESS.

FIRMS INVESTING IN RESEARCH ACTIVITIES IN THE UK MAY HAVE TO START SHIFTING THEIR R&D ACTIVITIES PROGRESSIVELY OUTSIDE THE UK.

MULTINATIONAL FIRMS OPERATING ACROSS BRITAIN AND EUROPE WILL SOON FIND THEMSELVES OPERATING IN INCREASINGLY DISTINCT JURISDICTIONS. THIS MAY TRIGGER THEM TO CREATE A REGIONAL STRUCTURE, SIMILAR TO EMEA, TO ACCOUNT FOR THE PROXIMITY, AND YET THE DIFFERENCES, BETWEEN THE EU AND THE UK.

FIRMS MAY SHIFT TOWARDS A MULTI-DOMESTIC OR TRANSNATIONAL STRATEGIC ORIENTATION WITH GREATER AUTONOMY GRANTED TO LOCAL UNITS OPERATING IN THE EU AND BRITAIN RESPECTIVELY TO ENABLE THEM TO ADAPT TO DIFFERENT LOCAL REGULATORY AND INSTITUTIONAL DEMANDS.

OVERALL, ORGANISATIONS, IN TERMS OF VERTICAL STRUCTURE, BUSINESS UNITS, INDIVIDUAL ROLES, AND REPORTING LINES WILL BE AFFECTED.

BREXIT WILL BE ACCOMPANIED BY HIGH ADJUSTMENT COSTS, INCLUDING DIRECT INCREASES IN TRANSACTION COSTS ASSOCIATED WITH RESTRICTION ON CROSS-BORDER ACTIVITIES AS WELL AS THE COSTS ASSOCIATED WITH RE-LOCATING EMPLOYEES AND OPERATIONS. THESE ADDITIONAL COSTS WILL BE PASSED ON TO SHAREHOLDERS AND CONSUMERS.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EQUALLY OR EQUITABLY— HOW SHOULD MANAGERS TREAT THEIR TEAM MEMBERS?

Paradoxically, both! Signifying that implementing Human Resource Management is a managerial challenge that has to consider the contrasting notions of uniformity and individuality, asserts Prof Na Fu of Trinity Business School at Trinity College Dublin in her article with Prof Patrick Flood of Dublin City University, Professor Denise Rousseau of Carnegie Mellon University, and Professor Tim Morris of University of Oxford.

THE CONTRIBUTION of employees is a key to achieve sustainable competitive organisational advantage. As such, it is important to effectively manage human resources to achieve long-term organisational goals. How this is done can be assessed at three levels of Human Resource Management (HRM). These levels are intended, actual, and perceived HRM.

Intended HRM refers to the HR system(s) or practices that the firm's executives seek to establish in order to increase firm performance. Its importance has been proven by well-established research on the link between HRM systems such as high-performance work systems, high-commitment work practices and firm performance. However, actions speak

> Team members are motivated to demonstrate positive attitudes and behaviours when they perceive that their manager values their contributions.

louder than words—bringing us to witness what really goes on when intended HRM is put into practice—*actual HRM.*

As such, actual HRM is concerned with how managers practically execute HRM in their daily interactions and dealings with their assigns. It begs questions from managers along the lines of which HRM practices they implement and from employees as to whether they believe that their managers treat them fairly.

SETTING THE STAGE

To better evaluate these realities in implementing HRM practices, Prof Na Fu and her fellow researchers partnered with 60 teams of a global consulting firm situated in at least three continents. The researchers studied the impact of reporting managers' HRM implementation in terms of their subordinates' job performance, measured both objectively and subjectively.

So, how are these HRM practices put into effect? What is their effect on individual performance?

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TUG OF WAR

The results were startling. To answer these questions, there are two contradictory notions—consistence or equality and individual responsiveness or equity—that need to be considered. The first deals with the concept of uniformity, similarity, and equal treatment—key elements of procedural justice. As such, it means that managers treat everyone equally in terms of collective needs and concerns.

In order to properly execute this approach, managers need to be consistent with how they actually do things. This consistency should reflect in such activities as personnel recruitment, informational flows about trainings, and provision of developmental feedback. Consistency provides team members with a clear, coherent, and fair message regarding the organisation's values, systems, and expectations. As such, it leads to increased motivation and involvement, and consequently, better performance.

On the other side is the contrasting concept of equity—reflective of the idea of distributive justice—which focuses on the substantive rather than on the procedural. It lays stress on the value of taking a person's contributions into account when giving rewards. In practice, it means a manager is to treat subordinates in a manner that reflects what they bring to the table in order to motivate them and keep them there.

Taking this idea of equity into consideration is important because being different is the one commonality that people share. Not taking these differences into account can cause employees to feel undervalued and bereft of managerial support. The impact of equity on performance is further supported by theory, which proposes that team members are motivated to demonstrate positive attitudes and behaviours when they perceive that their manager values their contributions.

THE BALANCING ACT

Reconciling these two views requires managers to harness the potential of their delegates in a way that takes into account disparities in expectations, capabilities, and contributions that arise out of such basic differences as gender, personality, education and work experience. Moreover, the individual responsiveness approach is beneficial as

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it can consider, within its ambit, the varied responsibilities that different people execute in their daily activities. And the need for different types of support.

Simultaneously, a manager has to ensure that this uniqueness is not singularly practiced – it should be unique in responding to each individual rather than being unique for a select few. As such, individual responsiveness has to be consistently applied to avoid perceptions of favouritism. This perception of fairness that the manager consistently creates in the workspace provides a foundation for viewing individual responsiveness as an acceptable and just system. Considering how important both consistency and individual responsiveness are to improved job performance, managers are faced with a Herculean task—implementing bespoke HRM practices for everyone.

WALK THE TALK

Now that it has been established that the intent of a manager in applying HRM practices has to be 'equally individualistic' in her/his interactions with subordinates, it is imperative to transform this intent into action.

To this end, organisations can establish practices that promote both equality and equity. For example, managers in such organisations could share information about trainings and career advancement opportunities with all members of the team. But, when making a decision as to who attends such trainings, managers could consider individual contributions or how a particular employee may gain from them. Another way is for a manager to solicit everyone's participation in meetings but to give more weightage to contributions of those who have more experience. Moreover, managers could balance consistency and individual responsiveness when they decide criteria for granting such special privileges as flexible working hours based on serious need or individual performance.

As such, organisations first need to improve the effectivity of managers in boosting their junior colleagues' performances. This could be done by providing managers—who are generally recruited for their subject-matter expertise rather than HR acumen—with support from senior executives and HR professionals. By properly managing these contradictory positions of equality and equity, organisations can reap synergetic benefits of both, boost individual performance and simultaneously achieve organisational goals.

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Na Fu

KEY TAKE AWAYS

COMPANIES CAN ACHIEVE SUSTAINABLE COMPETITIVE ORGANISATIONAL ADVANTAGE THROUGH THEIR EMPLOYEES AND EFFECTIVE HR IS KEY. HRM POLICY CAN BE ASSESSED AT 3 LEVELS: INTENDED, ACTUAL, AND PERCEIVED HRM.

INTENDED HRM REFERS TO THE HR SYSTEM(S) OR PRACTICES THAT THE FIRM'S EXECUTIVES SEEK TO ESTABLISH IN ORDER TO INCREASE FIRM PERFORMANCE.

ACTUAL HRM IS CONCERNED WITH HOW MANAGERS PRACTICALLY EXECUTE HRM IN THEIR DAILY INTERACTIONS AND DEALINGS WITH THEIR ASSIGNS.

THIS INVOLVES MANAGERS DECIDING WHICH PRACTICES TO IMPLEMENT AND FOR EMPLOYEES TO GAUGE IF THEIR MANAGERS TREAT THEM FAIRLY.

MANAGERS ARE JUDGED ON CONSISTENCY – PROVIDING TEAM MEMBERS WITH A CLEAR, COHERENT, AND FAIR MESSAGE REGARDING THE ORGANISATION'S VALUES, SYSTEMS, AND EXPECTATIONS – WHICH LEADS TO INCREASED MOTIVATION, INVOLVEMENT BETTER PERFORMANCE.

EQUITY EMPHASISES THE VALUE OF TAKING A PERSON'S CONTRIBUTIONS INTO ACCOUNT BY GIVING REWARDS AS WELL AS ATTENTION. IN PRACTICE, IT MEANS A MANAGER IS TO TREAT SUBORDINATES IN A MANNER THAT REFLECTS WHAT THEY BRING TO THE TABLE IN ORDER TO MOTIVATE THEM AND KEEP THEM THERE.

EQUITY IS IMPORTANT BECAUSE BEING DIFFERENT IS THE ONE COMMONALITY THAT PEOPLE SHARE. NOT TAKING THESE DIFFERENCES INTO ACCOUNT CAN CAUSE EMPLOYEES TO FEEL UNDERVALUED AND BEREFT OF MANAGERIAL SUPPORT.

THE IMPACT OF EQUITY: TEAM MEMBERS ARE MOTIVATED TO DEMONSTRATE POSITIVE ATTITUDES AND BEHAVIOURS WHEN THEY PERCEIVE THAT THEIR MANAGER VALUES THEIR CONTRIBUTIONS.

RECONCILING THE NOTIONS OF CONSISTENCY AND EQUITY REQUIRES MANAGERS TO HARNESS THE POTENTIAL OF THEIR TEAM BY TAKING INTO ACCOUNT DISPARITIES IN EXPECTATIONS, CAPABILITIES, AND CONTRIBUTIONS ARISING FROM DIFFERENCES AS GENDER, PERSONALITY, EDUCATION AND WORK EXPERIENCE.

A MANAGER HAS TO ENSURE THAT SHE/HE SHOULD BE UNIQUE IN RESPONDING TO EACH INDIVIDUAL RATHER THAN BEING UNIQUE FOR A SELECT FEW.

INDIVIDUAL RESPONSIVENESS HAS TO BE CONSISTENTLY APPLIED TO AVOID PERCEPTIONS OF FAVOURITISM.


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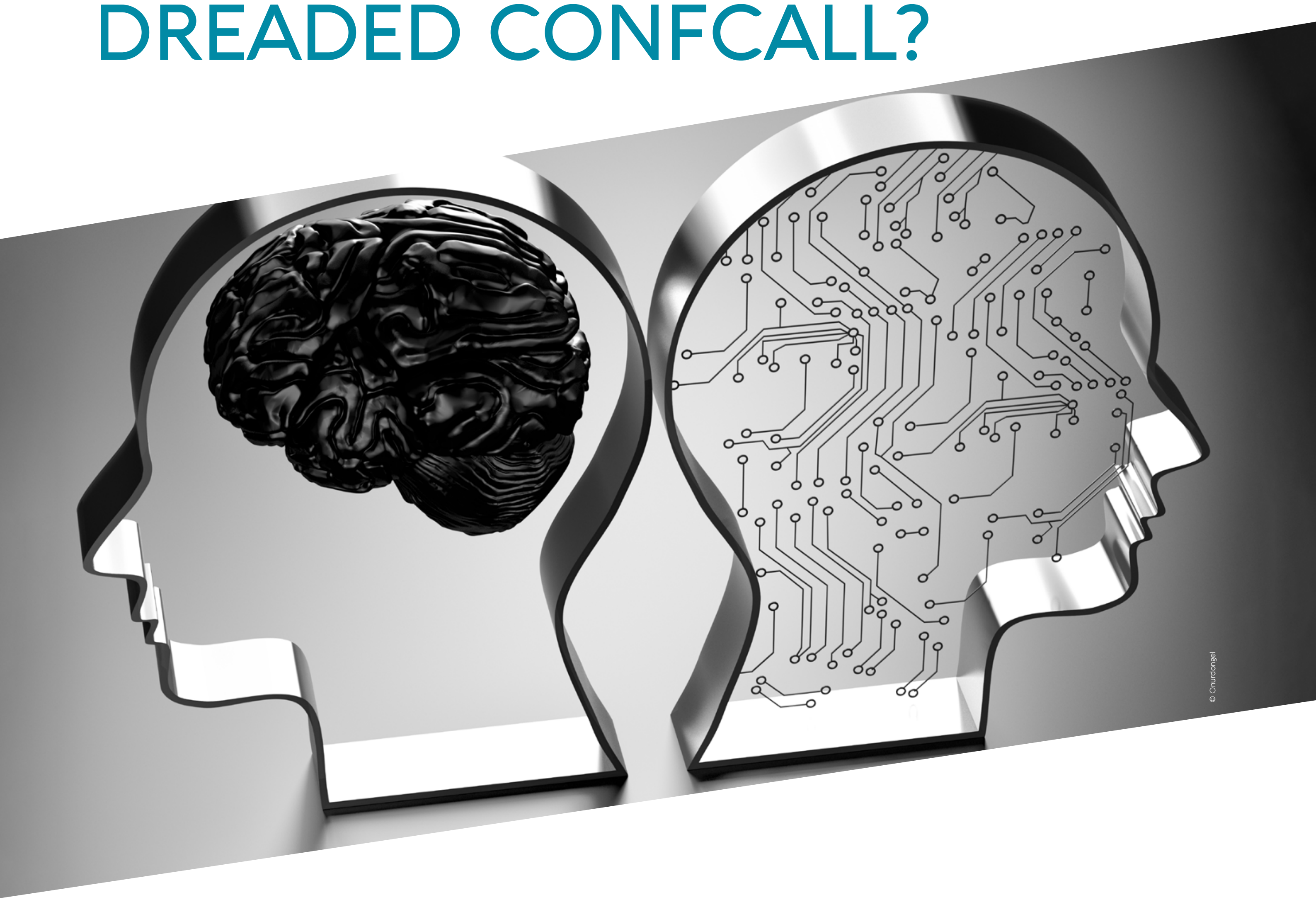
VIRTUAL-WORLD MEETINGS—AN ALTERNATIVE TO THE DREADED CONFCALL?



Xianghua Lu, Professor of Information Management and Information Systems at **School of Management Fudan University,** explores the potential of using virtual worlds for group collaboration

THE UNIVERSE OF VIRTUAL WORLDS has long been ruled by video games. However, this may soon change. With organizations increasingly going global and remote work becoming more common, these simulated environments may provide a solution for collaboration at distance. Nevertheless, questions about the effect of this technology on group interactions have been raised with some positing that people could exhibit different personalities when working through a virtual world. Through her research, Professor Xianghua Lu answers many of these questions and argues how organizations can best employ this technology to maximize its benefits.

FROM SCIENCE-FICTION TO SCIENCE-FACT

Virtual worlds—computer-based simulated environments where users can create personal avatars, explore, participate in activities and communicate with others—have long been used in video games like *Minecraft* and *Grand Theft Auto*. These virtual environments are often designed to mimic reality so that users

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feels immersed in the world and experience a degree of presence. With massive strides made in virtual reality (VR) technology and the appearance of mass-market VR headsets, some have argued that these virtual worlds will one day become indistinguishable from reality.

With organizations more global today than ever before, these recent technological developments provide new opportunities to facilitate group interactions like meetings. Up until now, collaboration at distance has been a challenge due to the nature of human interaction and the constraints imposed by technology. Current solutions such as phone meetings are unpopular and unproductive because people are easily distracted and tend to multitask ineffectively. Virtual worlds, in contrast, are designed to be engaging and focus their users' attention. Combined with the rapid advances in VR technology, virtual worlds could hence become an effective tool for collaboration at distance—if people are willing to use them.

Indeed, it is thought that people may exhibit different personalities in a virtual world than in the real world—in part because of the anonymity that is typically enjoyed in these simulated environments. However, in an organizational setting, people are likely to know the identities of the colleagues with whom they would interact in a group. Hence, they may make an effort to self-regulate and limit the degree of difference in personality that they exhibit in a virtual world. In her research paper *Dr. Jekyll vis-à-vis Mr. Hyde: Personality variation between virtual and real worlds*, Professor Xianghua Lu sets out to uncover whether people would exhibit this difference in personalities when working through a virtual world and whether such a difference would cause people to stop using the technology.

BEING YOUR VIRTUAL SELF

Professor Xianghua Lu decided to use the virtual world service *Second Life* to conduct her experiment. *Second Life*—which has been used in the past by organizations like IBM and Harvard University—offers a three-dimensional environment with visualizations that simulate real-world settings. It allows users to interact with each other through their avatars and engage in problem-solving together in a virtual environment. These constant stimuli engage the user and remind them of the goal of the activity: to solve a set of problems with the group.

Using a fully-equipped custom-made meeting room on *Second Life*, Professor Xianghua Lu was thus able to study the effect of using a virtual world on a group of about 300 undergraduate students. To measure potential personality differences, a survey based on seven pre-selected factors such as creativity and honesty was given before and after the students began participating in their virtual group meetings. The students were also asked to rate their satisfaction using the virtual worlds at the end of the experiment—an indicator of their willingness to continue using the technology.

As expected, the findings demonstrated that the students' had experienced significant differences in their exhibited personalities between the virtual and real worlds. What's more, a statistical analysis of the findings by the researchers also found a negative association between the variation in personality and satisfaction with the virtual worlds—in other words, the more people felt their personality had changed while working on *Second Life*, the more dissatisfied they were with the virtual group meeting. This confirmed the researchers' hypothesis that people who perceived a smaller change in their exhibited personality in the virtual world and acted more like themselves would be more inclined to continue using the technology in the future.

VIRTUAL SOLUTION, REAL ENGAGEMENT

Considering the cost of implementing them, organizations want to be assured of the feasibility of using virtual worlds for group interactions like meetings. By challenging the conventional belief that smaller personality differences in virtual worlds would cause dissatisfaction, Professor Xianghua Lu's research confirmed that these simulated environments can be effectively used in an organizational setting where anonymity is not guaranteed. In addition, qualitative feedback from the students who participated in her experiment suggests that this technology may in fact be better at facilitating group interactions than current alternatives.

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> "The more people felt their personality had changed while working on Second Life, the more dissatisfied they were with the virtual group meeting."

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As one of the students who took part in the virtual-world experiment stated: "We were all in a conference room that looked just like a room we would have gone into in real life. We even had coffee and fruit as well as a projection screen to show slides… It gave all of us the feeling that we were really in the room together and that we were paying much better attention to the meeting." This level of engagement may seem unworldly for organizations used to the usual phone meetings that plague teams collaborating at distance. However, with proper management, these virtual worlds can be powerful tools to help people problem-solve together.

One useful suggestion that Professor Xianghua Lu shares in her paper is that the manager of virtual-world group meetings should make the goal-oriented nature of the sessions clear. The researchers also recommended conducting several familiarization sessions before an actual meeting to reduce the novelty of effect that may distract people from their goal. Nevertheless, because of the limitations of the study, more research may be required to perfect the application of this technology. All things considered, however, Professor Xianghua Lu's findings show that if properly managed, virtual meetings are not only a feasible alternative but can also be more engaging and perhaps even more effective than the current solutions.

TOWARDS A VIRTUAL FUTURE

As organizations increasingly go global there is a need to develop better solutions for collaboration at distance. Although they may have only occupied the realms of science-fiction and video games so far, organizations are showing a growing interest in employing virtual-world technologies to enhance group interactions like meetings. Professor Xianghua Lu's research demonstrates that this technology can be effectively used in an organizational setting. What's more, her findings suggest that if properly managed, virtual meetings may help people become more engaged in problem-solving together. Given the real-world evidence, what's stopping you from organizing a virtual-world meeting?

Xianghua Lu

KEY TAKE AWAYS

WITH VIRTUAL REALITY (VR) TECHNOLOGY AND THE APPEARANCE OF MASS-MARKET VR HEADSETS, SOME SAY THAT VIRTUAL WORLDS WILL ONE DAY BECOME INDISTINGUISHABLE FROM REALITY. FOR COMPANIES, THESE RECENT TECHNOLOGICAL DEVELOPMENTS PROVIDE NEW OPPORTUNITIES TO FACILITATE GROUP INTERACTIONS LIKE MEETINGS.

CURRENT SOLUTIONS SUCH AS PHONE MEETINGS ARE UNPOPULAR AND UNPRODUCTIVE BECAUSE PEOPLE ARE EASILY DISTRACTED AND TEND TO MULTITASK INEFFECTIVELY.

PEOPLE MAY EXHIBIT DIFFERENT PERSONALITIES IN A VIRTUAL WORLD THAN IN THE REAL WORLD—IN PART BECAUSE OF THE ANONYMITY THAT IS ENJOYED IN THESE SIMULATED ENVIRONMENTS.

IN A COMPANY SETTING, PEOPLE ARE LIKELY TO KNOW THE IDENTITIES OF THE COLLEAGUES WITH WHOM THEY WOULD INTERACT IN A GROUP AND AS SUCH MAKE AN EFFORT TO SELF-REGULATE AND LIMIT THE DEGREE OF DIFFERENCE IN PERSONALITY THAT THEY EXHIBIT IN A VIRTUAL WORLD.

STUDENTS TESTING THE EXPERIMENT EXPERIENCED SIGNIFICANT DIFFERENCES IN THEIR EXHIBITED PERSONALITIES BETWEEN THE VIRTUAL AND REAL WORLDS. THE MORE THEY FELT THEIR PERSONALITY HAD CHANGED WHILE WORKING ON *SECOND LIFE*, THE MORE DISSATISFIED THEY WERE WITH THE VIRTUAL GROUP MEETING.

MANAGERS OF VIRTUAL-WORLD GROUP MEETINGS SHOULD MAKE THE GOAL-ORIENTED NATURE OF THE SESSIONS CLEAR AND CONDUCT SEVERAL FAMILIARIZATION SESSIONS BEFORE AN ACTUAL MEETING TO REDUCE THE NOVELTY OF EFFECT THAT MAY DISTRACT PEOPLE FROM THEIR GOAL.

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THE ACHILLES HEEL OF ENVIRONMENTAL ACCOUNTING: SUPPLY CHAINS

As firms scramble to get their emissions under control facing pressure from customers and regulators, Prof. Frederik Dahlmann from Warwick Business School explains what they may be forgetting.

From the article 'When it comes to carbon footprint, supply chains are our Achilles heel' by Professor Frederik Dahlmann, with kind acknowledgements to Warwick Business School.

FORGET SOMETHING?

CLIMATE CHANGE may have little impact on Donald Trump – a staunch believer of climate change being a hoax – but it seems like several firms and organisations have begun cleaning up the carbon trails they leave behind. Although this may seem like a ray of hope in an otherwise seemingly bleak future, Professor Dahlmann claims that it may not necessarily be the case. While firms get busy reducing their carbon emissions, what many are ignoring is the inclusion of their supply chains – something that Prof. Dahlmann considers a key factor. Take for example, the popularity of electric scooters. Users and propagators of the electric scooter claimed for a long time that the electric scooter was an eco-friendly way to cover short distances. However, most manufacturers of these scooters are Chinese firms, the majority of which do not maintain records of their carbon emissions. Moreover, most electric scooters have never lived an Forget Something?

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Climate change may have little impact on Donald Trump – a staunch believer of climate change being a hoax – but it seems like several firms and organisations have begun cleaning up the carbon trails they leave behind. Although this may seem like a ray of hope in an otherwise seemingly bleak future, Professor Dahlmann claims that it may not necessarily be the case. While firms get busy reducing their carbon emissions, what many are ignoring is the inclusion of their supply chains – something that Prof. Dahlmann considers a key factor. Take for example, the popularity of electric scooters. Users and propagators of the electric scooter claimed for a long time that the electric scooter was an eco-friendly way to cover short distances. However, most manufacturers of these scooters are Chinese firms, the majority of which do not maintain records of their carbon emissions. Moreover, most electric scooters have never lived an efficient life-cycle because of their non-durable build. The electric scooter has ridden a wave of popularity thanks to only a single segment of its lifecycle that is easy on emissions – riding it. Research has revealed that after taking into account the emissions from manufacturing, transportation, maintenance, and upkeep, electric dockless scooters do not rank as high on the green-o-meter as companies would have liked us to believe.

HEAVY IS THE HEAD THAT WEARS GREEN

Overlooking supply chains is bad news for the environment. Supply chains bear a heavy weight in determining a firm's carbon footprint, amounting to as much as four times the organisation's own operational emissions. And it seems few organisations are aware of their own. The Carbon Disclosure Project (CDP) – a charity running the global disclosure system on carbon emissions for investors and other interested parties – revealed that a mere 36 percent of companies that responded to its annual survey are actually engaging with their suppliers. Professor Dahlmann explains why this is disturbing on two fronts. Firstly, regulation. Increasingly, regulators around the world are demanding publicly listed companies to cough up their greenhouse gas (GHG) emission numbers and disclose them in their annual reports. One among these countries is the UK, which has gone as far as to introduce the Streamlined Energy & Carbon Reporting (SECR) scheme in 2019, which brings under purview, the entire supply chain. Secondly, with the subject of climate change an increasingly politicised arena thanks to Greta Thunberg's worldwide movement, pressure is building on firms to not just use their carbon-reduction actions as good PR, but more importantly to lead society in the move towards a sustainable future. It is increasingly important firms engage with their supply chain to work collectively to reduce carbon emissions.

THE 3 LEVELS OF HANDLING SUPPLY CHAINS

By analysing the CDP annual survey from 2014 to 2017, Professors Dahlmann from WBS and Roehrich from the University of Bath examined 1,686 listed companies from all over the world that are actively collecting environmental data and engaging with their supply chain i.e. customers on one end and suppliers on the other. Indeed, of those 28 percent only engage with their customers while 21 percent only with their suppliers, while the rest talk to both ends of the chain. Although two thirds of firms are doing neither, the number of firms engaging with some or all of their supply chain has seen an increase of 57 percent between 2014 and 2017. From this data, Professor Dahlmann was able to place firms into three different categories, based on their level of involvement with the supply chain – basic, transactional and collaborative. "It is at the collaborative stage where we see the most comprehensive approach to managing supply chain partners and customers", Professor Dahlmann points out.

The basic level involves an elementary level of interaction, where companies typically send their suppliers a survey to fill in on their emissions data. US software firm Symantec produces an annual report on its suppliers' GHG emissions, while Bank of America has been conducting a CDP supply chain survey since 2009. Firms at the basic level will usually only measure and collate data, engaging only in the first step necessary for the conception of a more comprehensive carbon reduction plan. "Perhaps tellingly", Professor Dahlmann observes, "survey responses from firms engaging in only basic engagement were relatively shorter in length and qualitatively less detailed". On the other hand, more advanced firms – at the transactional and collaborative levels – use this data for more productive means. At the transactional level firms calculate their carbon footprint and identify opportunities for improvements. The more experienced firms of this lot, then, use the data to provide their supply chain with targets and incentives. Virgin Atlantic Airways, for example, aims for reductions in emissions from its supply chain each year, while nuclear power firm Exelon sets goals for its suppliers to reduce energy usage and GHG emissions. What is more is that this data is also being used for the development of key performance indicators (KPIs) which can facilitate supplier selection and the assessment of their performance. Warnings are sent to firms not hitting requisite performance levels and improvements demanded. As a result, the emissions data becomes an integral part of the selection criteria for suppliers making them more accountable. For instance, pharma giant Pfizer reported that the aim of its data collection is "to provide benchmarking to suppliers regarding their GHG emission reduction and water conservation programmes, in order to identify sustainability improvement opportunities".

GOING ALL THE WAY

At the collaborative level, on one end firms and suppliers work together to develop shared goals and values around sustainability: collaboration is more tightly knit. Professor Dahlmann maintains that in order to build mutually beneficial and greener relationships, a deeper involvement and commitment is necessary from firms and suppliers. This means more meetings, seminars on best practice, more personal interactions in the form of phone calls and emails including the establishment of online discussion groups for a mutually beneficial relationship aimed at reducing their overall carbon footprint. Eventually, some firms offer supportive supplier training and development courses, briefings, summits and award ceremonies to identify joint development and innovation projects. On the other end of the chain, firms at the collaborative level also seek to engage customers and consumers, persuading them through marketing and PR of the benefits of new, greener products and how to use them in a way that is less harmful on the environment. Companies bring the collaborative relationship to life in a variety of different ways. Food multinational Kellogg's has created a 'Sustainability Consortium' with its supply chain to "drive scientific research and the development of standards and information technology tools to enhance the ability to understand and address the environmental, social and economic implications of products", while The InterContinental Hotels Group is working with the International Tourism Partnership to reduce the environmental impact of the cotton used in its bed linen. In the B2B sphere, companies employ two-way engagement with customers with a more proactive and strategic approach on show. Partnerships with industry associations and university research teams is the way the French hospitality firm Sodexo has gone. Sodexo is funding the position of the Professor of Sustainable Sourcing at the Euromed School of Management in Marseilles. In other instances, Professor Dahlmann's team also discovered firms which are able to employ transactional and collaborative modes of engagement simultaneously with different suppliers and customers.

All said and done, to calculate the carbon emissions across the lifecycle of a product – which could mean from sourcing raw materials to the final product ending up in a landfill – is no easy task, which is why a collaborative approach is increasingly important. The requirement for companies to report their emissions makes them more accountable in a system where what one does affects the rest. Companies must understand that they are part of a single system that must work together, rather than employ emissions monitoring as another supply chain management tool.

THOSE WHO TECH, CAN

Let's not forget data. Tracking emissions can be incredibly complex especially for the likes of firms like Walmart. The amount of data that would involve is probably why tech companies are leading the way in the reduction of their carbon footprints. Their data analytics skills mean it is natural for them to not only collate data but also to put it to effective use, both up and down the supply chain. Aside from being ahead in the game, tech companies are likely to be in an optimal position and poised to develop emission management platforms and tech that is much in demand given the increasing requirement for emissions accounting.

"Supply chains bear a heavy weight in determining a firm's carbon footprint, amounting to as much as four times the organisation's own operational emissions."

© Ivan Bajic

If tech companies can resolve this complex puzzle and produce a comprehensive software package that does it all – track, record and manage carbon emission across the entire chain effectively – they could see a new market opening to them. Verizon, for example, now sees its Internet of Things products, designed to reduce carbon emissions, as "providing significant revenue opportunities".

It's clear, with the youth of today engaged as never before in the climate change political battle, that sustainability will be the issue of this generation. If businesses are to prosper in this climate they need to include their whole supply chain to claim they are truly on the planet's side and not be accused of creative carbon accounting.

KEY TAKE AWAYS

FIRMS AND ORGANISATIONS OFTEN FORGET TO TAKE INTO ACCOUNT THEIR SUPPLY CHAINS IN THE REDUCTION OF THEIR CARBON EMISSIONS.

REGULATORS AND CUSTOMERS ARE INCREASING THE PRESSURE ON BUSINESSES TO COUGH UP EMISSION NUMBERS AND LEAD THE WAY TO A SUSTAINABLE FUTURE.

BASED ON THE LEVEL OF INVOLVEMENT WITH SUPPLIERS TO REDUCE EMISSIONS THERE ARE THREE DIFFERENT LEVEL OF RELATIONSHIPS: BASIC, WHERE THERE IS ONLY COLLATING AND MEASURING OF DATA; TRANSACTIONAL, WHERE FIRMS USE TO DATA TO SUGGEST IMPROVEMENTS AND GENERATE INSIGHTS; FINALLY, THERE IS THE COLLABORATIVE LEVEL WHERE FIRMS HAVE A DEEPER LEVEL OF INVOLVEMENT WITH SUPPLIERS AND WORK WITH THEM TO COLLECTIVE REDUCE THEIR OVERALL CARBON FOOTPRINT

A COLLABORATIVE APPROACH IS THE WAY TO GO SINCE DATA IS COMPLEX TO GATHER AND BECAUSE IT MAKES FIRMS MORE ACCOUNTABLE; ONE'S ACTIONS AFFECTS THE OTHERS IN THE CHAIN.

TECH COMPANIES, BECAUSE OF THEIR ANALYTICAL ABILITIES ARE AHEAD OF THE GAME IN USING DATA TO REDUCE THEIR CARBON FOOTPRINT. THIS ALSO MAKES THEM POISED TO TAKE ON THE MARKET FOR CARBON ACCOUNTING SOFTWARE AND TECHNOLOGIES.

Fred Dahlmann

FINANCE & ECONOMY

SUSTAINABLE DEVELOPMENT: HOW THE LAW AND THE WORLD OF FINANCE CAN HELP

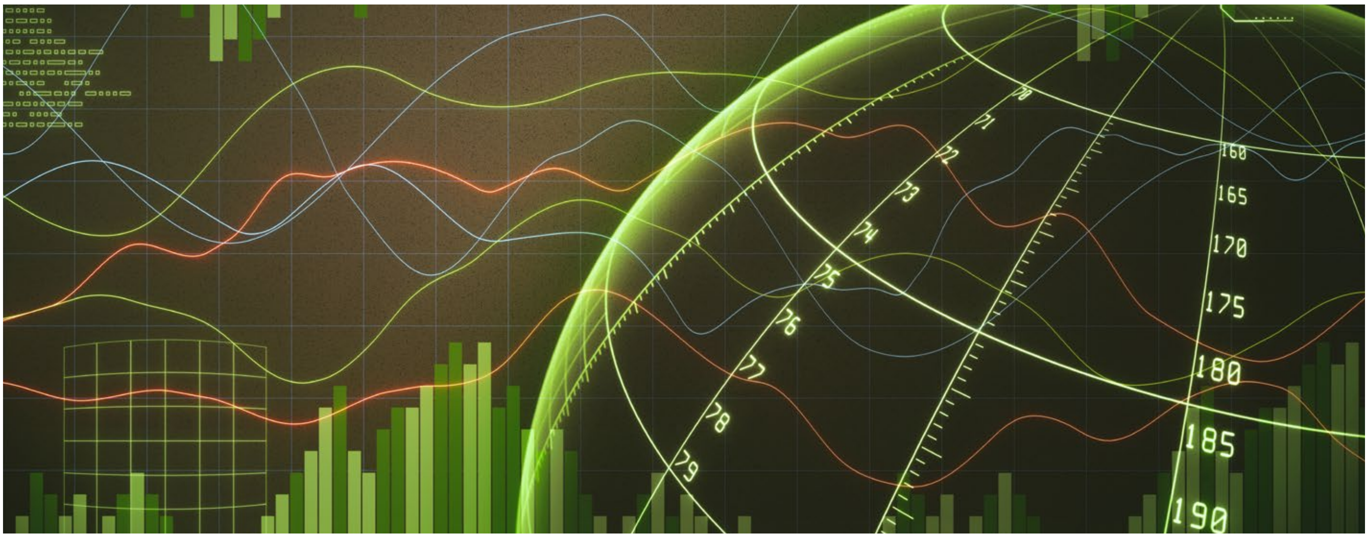
Hugues Bouthinon-Dumas, Professor of Law at **ESSEC Business School,** looks into sustainable finance, how it fits into the notion of sustainable development and how the law can be used to promote it.

From an interview with Prof. Hugues Bouthinon-Dumas following the Sustainable Finance and Law conference held at the Sorbonne on 22nd October 2019 within the framework of the Transnational Network on Banking and Financial Law.

THE BEGINNING OF SOMETHING BIG AND PIVOTAL?

SUSTAINABLE FINANCE is much like a school of thought and a tendency based on older notions such as Sustainable Development, CSR or ESG (Environment-Social-Governance) criteria applied to company audits. Geographically, sustainable finance initiatives have gained impetus in Europe, Canada, and the United States, as well as in Asia – for example in Singapore, where the country is attempting to position itself as a major hub in this field. So, what makes the financial world want to turn green?

The motivation is two-fold – which explains why there is a certain ambiguity attached to the very idea of sustainable finance – firstly to take into account social and climate risks



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in financial decisions and calculations, without necessarily questioning financial logic. Secondly, however, sustainable finance can also be conceived in a wider, more radical perspective, indeed revolutionary, regarding the transformation of the economic system towards sustainable development and by using the means of action proper to the field of finance.

It's still much too soon to say if sustainable finance is just a fad, or the exact opposite – the demonstration of a complete change of paradigm that transforms short-term finance into finance that is concerned by its long-term development.

What is sure, however, is that sustainable finance is a movement that impacts every segment in the field of finance: banks, providers of credit, insurance companies, pension funds, investment funds – including private equity – listed companies, and primary and secondary financial markets as well as all the players orbiting around these: regulators, auditors, rating agencies, financial analysts, and so on.

FINANCIAL MECHANISMS AND SUSTAINABLE DEVELOPMENT

The good news is that there are many mechanisms available – and what's more, they can be combined. The oldest is without doubt socially responsible investment (SRI) where investors seek only to place their money in companies they see as ethically fit. Today, an increasing number of investors are willing to shun activities that they believe go against the values and actions of sustainable development. SRI can also be encouraged by the law makers, certain rules obliging investors to ask themselves the question of whether an investment will be respectful of the planet and its populations. Other regulations oblige those who manage and commercialize savings products such as UCITS, life insurance, and savings accounts to propose green or sustainable investments to their policy holders.

Shareholder activism is another means. Investment funds or NGO's, for example, motivated by the advocacy of a social or environmental cause, can make use of the law and corporate governance to influence how a company is run, requesting green or social impact issues to appear on the agenda of general meetings. And finally, other means and mechanisms include external audit reports, employee representation on boards, eco-labels ad ISO standards, and redefining a company's purpose to include the notion of the common good and sustainable development. In France, for example, the PACTE law was passed and equivalent initiatives have appeared in other countries that support B-corporations. The vast majority of mechanisms are not mandatory by law and regulations are limited in their effectiveness. As such, mechanisms are needed that incentivize rather than coerce.

WHY THE CHANGE?

Without doubt, it is the general awareness in society of the stakes involved – indeed emergency – of the climate issue. After all, players in the financial field do not live on another planet, even if in the past financial rationality did not generally include concerns of this nature. And then there's the pressure exerted by various heavyweights in the field, the most notable case being that of Larry Fink of BlackRock and his open message to CEOs.

But what has radically changed the standpoint of traditional financial players on social and environmental stakes has without doubt been risk assessment even more than the potential of commercial developments in this new niche. The consequences of climate change and social troubles associated with it generally have a negative impact on the assets of financial institutions because a large number of their investments will lose value – for example, not only their assets but also their liabilities will be affected. It is no longer possible today to outsource social and environmental risks and even more so to base one's business model on forms of unethical exploitation or policy that does major harm to the environment. From this moment on, these risks will have to be taken into account as seriously as possible: identify them, measure them and take action to minimise them.

A HANDFUL OF PRETTY GREEN

Finance will play a truly essential role in sustainable development if it manages to provide the green transition with substantial financial means – thousands of billions of euros or dollars – it requires if it is to succeed. The budgets of the States or local authorities are not limitless, if only for the reason that fiscal revenues are today weakened by tax evasion practices made easier by globalisation and the insufficient cooperation between states in this area. So, finance will have to turn to turn to other, sustainable sources such as long-term savings accounts and the capital generated by pension funds or life-insurance policies, as well as green bonds and loans. It's here that the law plays an extremely important role in preventing misappropriation and greenwashing which can completely undermine sustainable finance by discrediting it. Vigilance with regard to sustainable finance is therefore necessary and the stuff of both the regulators and other watchdogs such as NGOs in areas such as providing investors with a clearer idea of the extra-financial qualities of investments that claim to be ethical in nature.

MOTIVATING PROSPECTS FOR REGULATORS AND LEGAL PRACTITIONERS

Legal practitioners have commonplace challenges to deal with, but these will – if sustainable finance endures – change the nature of the legal practitioner's lot. For example, green bonds are in essence bonds, green loans are first and foremost loans – but in each case, the elements that justify their qualification as being sustainable have to be taken into account.

Certain professional bodies such as the International Capital Market Association (ICMA) are also driven to developing new models of financing contracts. Another example is that rules of responsibility must without doubt be adapted in case an issuer fails to keep to his promise to commit to an environmentally-friendly policy he has drawn up – because the existence of prejudice, in its usual sense, can count as default. In the context of common law, sustainable finance begs the question of whether fiduciary obligation should be redefined – should fiduciary contracts still seek maximum yield in the sole interest of their beneficiaries without taking into account any other consideration? It has been shown that the information communicated by issuers within the framework of extra-financial reporting is today both of a very varying quality and interest. As such, this information should be standardized or in any case presented in a way that it can truly be used by stakeholders.

Certain topics linked to sustainable finance raise theoretical questions that are extremely interesting for legal practitioners. One of these is the question of the nature of financial instruments when what is traded on a market – that very much resembles a financial market – is not a financial product like a transferable security or a derivative, but a right to emit greenhouse gases. Another example: legal practitioners are being pushed to redefine the purpose of a company from the moment companies are considered set up not only to earn money for their shareholders, but also to play a social role. As a final example, the interest in acting liability against a company that adopts a non-compliant behaviour towards sustainable development: can shareholders raise a red flag? Can stakeholders other than shareholders file a law suit against the firm?

Sustainable finance also poses legal practitioners the daunting question of knowing how to develop effective standards to meet the requirements of stakes that are both global and that affect the planet – something that favours international norms or transnational mechanisms of coordination – whereas the authorities possessing the power to create and apply norms are essentially national authorities. Sustainable finance obliges legal practitioners to be skilled and creative in order for them to carry out their mission in a difficult context. Often, states use optional, indicative or non-binding rules such as soft law, good practice and self-regulation that precede their adoption and general use. A kind of virtuous market dynamic foreruns and prepares regulations. Let's observe, nevertheless, that this can only happen as such if the market conditions and the dispositions of the actors involved allow it to. Within a very competitive and tense environment where every extra cost causes the short-term bankruptcy of a company, or indeed if the players are strictly motivated by the unbridled search for profit, this ethical dynamic cannot be implemented without external constraint and credible sanctions.

WHAT ROLE WILL REGULATORS PLAY IN SUSTAINABLE FINANCE?

Regulators' traditional mission consists in protecting savings and savers, keeping a watch over the proper functioning of the markets, financing systems and payment, and ensuring that the financial system isn't destabilized to the detriment of the economy. However, it seems that regulators are indeed sensitive

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to the issues and expectations of society as well as impetus provided by governments. Everywhere in the past few months, we can see the regulators tackling the question of sustainable finance. They are launching individual – for example, the AMF (French financial markets authority) partnership with the ACPR (French Prudential Supervision and Resolution Authority) – or global initiatives, such as the creation of the NGFS (Network for Greening the Financial System) network.

The role of regulators is both one of catalyzing the reflection on sustainable finance and keeping an eye out so that the actors in financial systems don't divert the new tools that see the light of day from their end-goals – notably through green washing or other opportunistic behaviours. Ill-intentioned speculators might impact the performance and integrity of the markets dealing with green products through manipulations and insider operations. In a nutshell, regulators must essentially remain vigilant.

Hugues Bouthinon-Dumas

KEY TAKE AWAYS

SUSTAINABLE FINANCE (SF) CAN BE DEFINED AS FINANCE THAT HAS A CONCERN FOR LONG-TERM CONCILIATION BETWEEN ECONOMIC, SOCIAL AND ENVIRONMENTAL INTERESTS.

THE MOTIVATIONS BEHIND SF ARE TWOFOLD: 1) THE TAKING INTO ACCOUNT OF SOCIAL AND CLIMATE RISK IN FINANCIAL DECISIONS AND CALCULATIONS 2) THE WIDER, PURPOSEFUL TRANSFORMATION OF THE ECONOMIC SYSTEM TOWARDS SUSTAINABLE DEVELOPMENT.

SF IMPACTS EVERY SEGMENT IN THE FIELD OF FINANCE (BANKS, INSURANCE COMPANIES, PENSION FUNDS, ETC.) AS WELL AS REGULATORS, AUDITORS, RATING AGENCIES, FINANCIAL ANALYSTS, ETC.

THE VAST MAJORITY OF MECHANISMS ARE NOT MANDATORY BY LAW AND REGULATIONS ARE LIMITED IN THEIR EFFECTIVENESS. AS SUCH, MECHANISMS ARE NEEDED THAT INCENTIVIZE RATHER THAN COERCE.

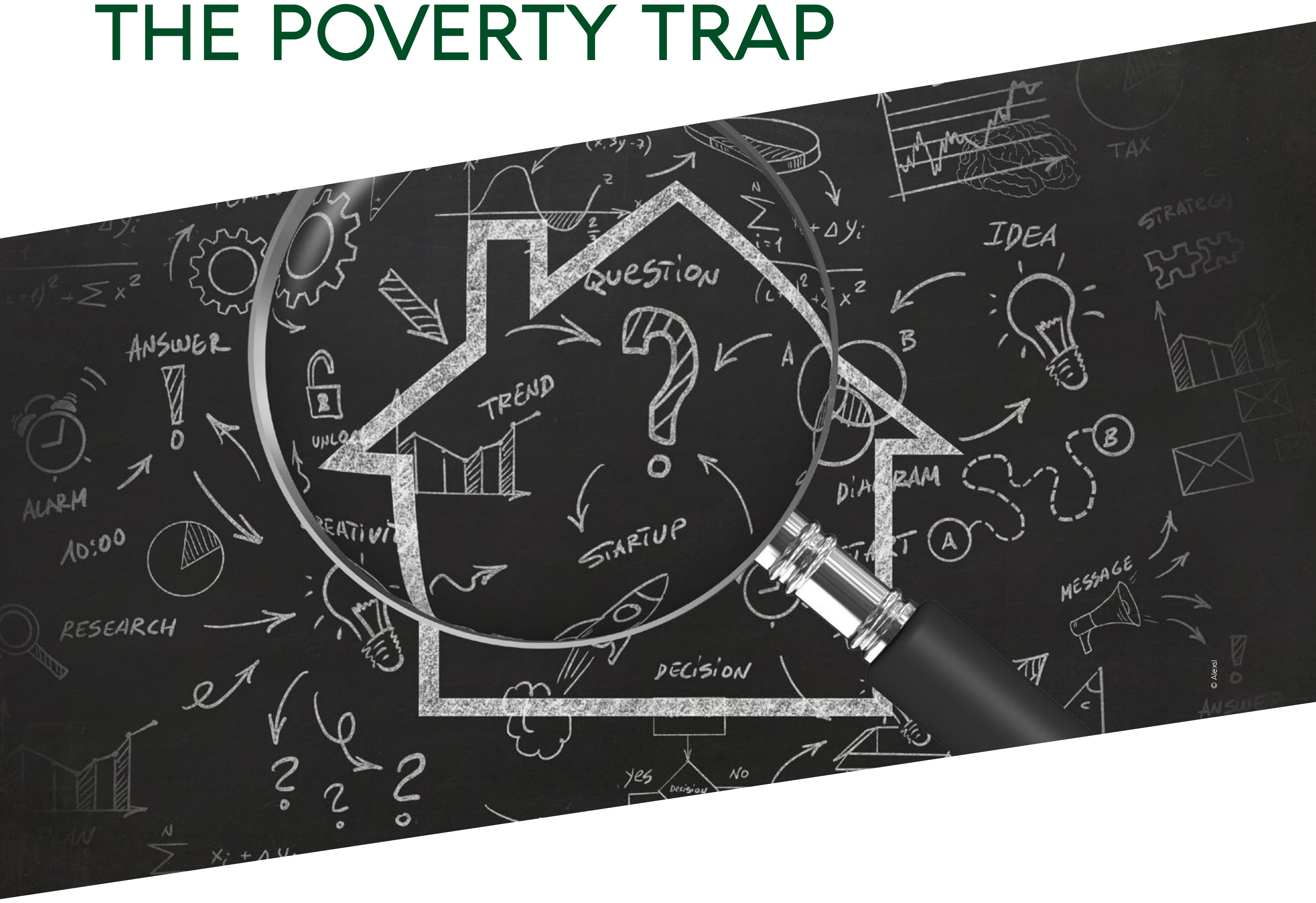
IT IS RISK ASSESSMENT THAT HAS RADICALLY CHANGED THE STANDPOINT OF TRADITIONAL FINANCIAL PLAYERS ON SOCIAL AND ENVIRONMENTAL STAKES.

THE CONSEQUENCES OF CLIMATE CHANGE AND ASSOCIATED SOCIAL TROUBLES HAVE A NEGATIVE IMPACT ON THE ASSETS OF FINANCIAL INSTITUTIONS – A LARGE NUMBER OF THEIR INVESTMENTS WILL LOSE VALUE.

LEGAL PRACTITIONERS ARE SEEING THEIR PROFESSION EVOLVE: FOR EXAMPLE, THEY ARE BEING PUSHED TO REDEFINE THE PURPOSE OF A COMPANY FROM THE MOMENT COMPANIES ARE CONSIDERED SET UP NOT ONLY TO EARN MONEY FOR THEIR SHAREHOLDERS, BUT ALSO TO PLAY A SOCIAL ROLE.

THE ROLE OF REGULATORS IS BOTH ONE OF CATALYZING THE REFLECTION ON SUSTAINABLE FINANCE AND MONITORING ANY MISCONDUCT.

HOW MICROFINANCE CAN HELP ENTREPRENEURS BEAT THE POVERTY TRAP



Through her research, **Giorgia Barboni,** Professor of Finance at **Warwick Business School,** provides compelling evidence in favour of affording entrepreneurs more flexible microfinancing options, highlighting the potential benefits for developing economies around the world.

IN 1976, Muhammad Yunus, a young economics professor, lent $27 to a group of 42 women living in a forgotten Bangladeshi village named Jobra. He couldn't have known at the time, but with this small act of goodwill, Mr Yunus had sown the seeds of what would blossom into a global microfinance industry. Billions of dollars have since been disbursed to impoverished borrowers, financing small entrepreneurial ventures around the world. However, as the aspirations of these micro-loan recipients have evolved, the microfinance industry has not always evolved along with them. Today, highly rigid repayment structures can often inhibit the growth and even sustainability of borrowers' businesses. Through a partnership with a microfinance institution in India, Professor Giorgia Barboni of Warwick Business School tests the viability of affording entrepreneurs more flexible micro-loans.

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FROM HUMBLE BEGINNINGS

Following his first $27 loan, Mr Yunus founded Grameen Bank in 1983 and pioneered the microfinance industry—earning a Nobel Prize in the process. The organization has since disbursed more than $29 billion to impoverished borrowers while its microfinancing methods have spread around the globe. As one early recipient of a Grameen micro-loan once noted: "My parents gave me birth, but Grameen Bank gave me a life". At the time, Mr Yunus' intention was to provide immediate relief for the hunger and poverty he saw around him in Bangladesh. He sought to help people "get through another day with a little more ease". In doing so, he empowered women, entrusting them with loans that, until then, had only been obtainable through informal moneylenders, along with the responsibilities that accompanied formal financing arrangements. However, what borrowers initially saw as assistance to survive, often sparked a desire to create economic prosperity for themselves through entrepreneurial ventures.

In many developing countries, the economic transformation from agriculture to industry has created new business opportunities. However, many small entrepreneurs need flexible funding options to bring their ideas to life but often lack sufficient collateral to obtain it. At present, microfinance institutions allow them to borrow small sums of money on a highly rigid repayment structure which entails frequent repayments starting immediately after the loan is disbursed. But these types of contracts do not offer these micro-entrepreneurs enough liquidity to grow and sustain their businesses. According to Professor Barboni, one of the reasons for this is because lenders are worried that providing a suitably flexible contract to micro-entrepreneurs will lead to greater default rates. Moreover, it is often difficult for lenders to gauge a borrower's suitability for riskier, more flexible loans. What little research has been conducted on the issue seems to validate these concerns. A study that put forth a standard loan contract with a flexible one found that, although the flexible contract increased the borrowers' revenues, it also raised default rates. This contributes to explain why no microfinance institution in India incorporated any sort of flexibility into their microfinance contracts.

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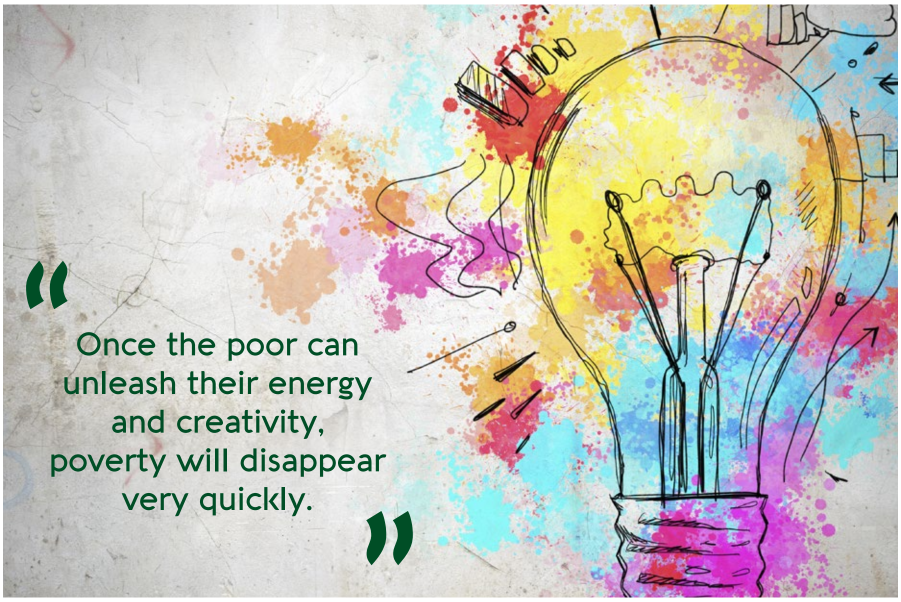
A FLEXIBLE SOLUTION

However, theory predicts that it is possible to devise a flexible contract structure that attracts "good" borrowers. These contracts would have to be given to micro-entrepreneurs that were no more likely to default with a flexible loan than with a standard contract. Professor Barboni argues that offering a more flexible contract at a higher rate of interest than the standard contract would trigger a positive self-selection mechanism that would filter out risky borrowers. Indeed, the flexible element and additional cost of the loans would discourage borrowers that needed to be tied to a rigid repayment schedule while attracting micro-entrepreneurs with the potential to create greater expected returns on capital to compensate for the additional costs. Therefore, the additional interest rate would allow to disclose borrower's characteristics and create a sustainable product for microfinance institutions.

To test this theory in the field, Professor Barboni and her research team partnered with Sonata Microfinance, a micro-loan provider based in India. They designed their flexible contract with an interest rate priced two percentage points higher than the regular loans. The new contract allowed borrowers to take a three-month payment break, whenever needed, adjusting the repayment amount upwards accordingly once payments resumed. A randomised contract trial was organized in Uttar Pradesh, India, involving 28 of Sonata's bank branches. Half of the branches offered customers a choice between the flexible and standard contracts while customers at the other branches were only offered the standard contract. Nearly 800 borrowers were included in the study. They had all previously borrowed from Sonata and had successfully repaid at least one loan. This made them eligible for slightly larger individual loans worth an average of approximately $500. According to Professor Barboni, as previous customers, the existing element of trust between borrower and bank may have helped overcome any reluctance to enter into a flexible contract.

RETURNS ON INVESTMENT

Professor Barboni's study provides encouraging findings for micro-entrepreneurs, microfinance institutions, as well as for poli-



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cymakers interested in promoting entrepreneurship and economic growth. The data across the 24-month loan cycle showed that the repayment rates were not statistically different across the flexible and standard contracts. This indicates that microfinance institutions can offer a flexible type of micro-loan and increase revenues without incurring higher debt default rates. Furthermore—and of particular interest to policymakers—based on self-reported sales figures, borrowers under the flexible contract reported on average approximately 20 percent higher sales. They also reported that they incurred smaller losses than their standard loan counterparts and were less likely to request a "loan top-up" from Sonata. This suggests that the additional liquidity provided to micro-entrepreneurs by the flexible contracts benefits their business with no additional cost to the lenders.

Moreover, interviews Professor Barboni conducted with some of the micro-entrepreneurs in question revealed the opportunities provided by the repayment holidays. The borrowers reported using the repayment holiday in anticipation of periods where there is a downturn in business and below-average revenues. Borrowers added that they used the repayment holiday also to capitalise on opportunities to earn above-average revenues during periods of high demand such as during India's festival season. Having demonstrated a proof of concept, Professor Barboni argues microfinance institutions and policymakers should promote flexible micro-loans, if only due to competitive forces.

UNLEASHING ENERGY AND CREATIVITY

The new micro-loans Professor Barboni and her team offered in their pilot study provided the cash-flow flexibility for only a few hundred micro-entrepreneurs. But if scaled, flexible micro-loans have the potential to give millions of micro-entrepreneurs the freedom they need to grow their businesses sustainably and, in doing so, benefit developing economies around the world. As Mr Yunus noted in his 2006 Nobel Lecture, "all [the world] needs to get the poor people out of poverty is for us to create an enabling environment for them. Once the poor can unleash their energy and creativity, poverty will disappear very quickly." According to Professor Barboni, flexible micro-loans can help create that enabling environment.

KEY TAKE AWAYS

THE EMERGENCE OF MICROFINANCE HAS ENABLED COUNTLESS PEOPLE TO BEAT THE POVERTY TRAP THROUGH SMALL, ENTREPRENEURIAL VENTURES.

AS THE ASPIRATIONS OF MICRO-LOAN RECIPIENTS HAVE EVOLVED, THE MICROFINANCE INDUSTRY HAS NOT ALWAYS EVOLVED ALONG WITH THEM.

HIGHLY RIGID REPAYMENT STRUCTURES WHICH ENTAIL FREQUENT REPAYMENTS STARTING IMMEDIATELY AFTER THE LOAN IS DISBURSED DO NOT OFFER MICRO-ENTREPRENEURS THE LIQUIDITY NEEDED TO GROW AND SUSTAIN THEIR BUSINESSES.

BY OFFERING MORE FLEXIBLE MICRO-LOAN CONTRACTS WITH HIGHER INTEREST RATES, MICROFINANCE INSTITUTIONS CAN EMPOWER THE RIGHT BORROWERS WHILE AVOIDING THE RISK OF INCREASED LOAN DEFAULT RATES.

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Giorgia Barboni

THE MISSING MIDDLE IN MICROFINANCE

Savita Shankar, Associate Professor at **Keio Business School,** Japan, shares her research on how to address the needs of millions of micro entrepreneurs who form the 'missing middle' as their financing needs are met by neither microfinance institutions nor commercial banks.

THE MISSING MIDDLE

ANIKA, BABAR, AND SABA met during a festival organised by their village community hall and hit it off straight away. All three had a dream to start their own business selling local snacks and specialties to the business people and merchants of the area. They had no capital, only their passion and expertise in cooking, and the motivation to offer their snacks to people in the village and beyond. Luckily, they had heard of a micro-finance bank in the nearest big town some seventy miles away and, after convincing the lender that their business idea was worth it, they became the happy beneficiaries of an initial Rs25,000 ($384) loan – enough to set them up in a stall near the market place and pay for the ingredients for their first snacks. Business boomed and Anika, Babar and Saba, naturally encouraged by the signs, wanted to grow and add an area in front of their stall where customers could sit and eat their snacks and engage in conversation.

So they returned to the micro-financer and obtained another loan – this time for Rs50,000 ($768). The stall grew, and the quality of their snacks and passion for service spread by word-of-mouth further and further afield until they realised that the opportunity for yet another venture was there to be explored – a food truck. So once again they returned to the micro-finance banker who, very pleased with the regular repayments and slight margin he gained from the youngsters' business success, announced that he was ready to accord them a grand Rs100,000 loan, equivalent to $1,536. Now this might have been enough to purchase a very old van, but certainly not a reliable and newer van as well as all the outlay required for ingredients, petrol and wages for the two people they wished to hire as driver-sellers of their famous snacks. But when they mentioned this, the lender sadly shook his head – he could no longer help them because his type of bank could not lend over the limit of Rs100,000. It was the law. Thanking the lender for the help already given, undeterred and believing in their dream, Anika, Babar, and Saba decided to go and see a commercial bank in the city for a bigger loan. The commercial banker listened with interest to their story and congratulated them on their success and entrepreneurial spirit. But then, when they had finished explaining their case and fell silent for the banker to make them an offer, all she did was sadly shake her head – she could not, unfortunately, grant them a loan. No – the smallest amount she was allowed to grant was Rs1 million – and that was for targeting small-to-medium enterprises, not informal start-ups. Anika, Babar, and Saba looked at each other in disbelief. Little did they know, but they had just become victims of what might be called the *microfinance graduate syndrome* or *missing middle*.

THE CONTEXT AND ISSUES

Savita Shankar, professor at Keio Business School, Japan, decided to research the phenomenon of the *missing middle* in three key countries for micro-finance – India, Bangladesh, and Pakistan. The term *missing middle* is generally used to describe the disproportionately small number of SMEs in relation to the number of micro or large enterprises in developing countries. In her research, Prof. Shankar uses the term more specifically to refer to the lack of financing options for enterprises whose needs fall in between the typical loan sizes offered by micro-finance institutions and commercial banks – exactly the case of our young heroes Anika, Babar, and Saba. They were successful 'graduates' in their entrepreneurial venture but capped on the amount of micro-financing required to grow further, and too small to benefit from the size of loans offered to SMEs by the commercial banks: almost like striding across a series of stepping stones only to find, mid-river, several of them missing and the other side of the river heart-achingly out of reach. This problem creates something of a conundrum for millions of fledgling entrepreneurs in developing countries. But there is hope.

FINANCIAL EXCLUSION AND THE GROWTH OF MICRO-FINANCE

'In recent times, financial inclusion has been on the policy agenda of many developing countries, states Prof. Savita Shankar. This implies availability of a continuum of financial services for all income groups, the idea of an inclusive financial system being to 'provide credit to all bankable individuals and firms, insurance to all insurable individuals and firms, and savings and payment services for everyone,' she continues, quoting the United Nations definition of financial inclusion.

The figures speak for themselves. In India, Bangladesh and Pakistan – the three countries analysed in Prof. Shankar's research – financial exclusion is widespread. According to the World Bank's Global Findex database (2014), only 56.3%, 35% and 13% respectively of individuals in those countries above the age of 25 years possessed a bank account while only 8.8%, 13% and 2% respectively had a formal borrowing account.

However, spurred by the UN, the willingness to promote financial inclusion helped pioneers such as the Grameen Bank in Bangladesh and hundreds of others who followed to grow. The result today, is that the microfinance sector, having reached maturity, sees the need for successful micro-financed entrepreneurs to aim for higher loans that don't actually exist. Hence, the 'missing middle' – those whose needs are neither met by microfinance institutions nor commercial banks. Indeed, India, Bangladesh and Pakistan have sizable missing middle segments with considerable employment potential. 'And as employment generation is an important goal for all three countries,' she asserts, 'catering to the missing middle is a priority. This means that it is firmly on the policy agenda.'

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> Catering to the financing needs of missing middle firms has great potential to invigorate South Asian economies – making them more inclusive and dynamic.

MICROFINANCE AND THE CHALLENGES

Prof. Shankar based her research on interviews with key personnel from the microfinance and banking sectors in each of the three countries. Thirty-two interviews were conducted in all, with at least ten interviews conducted in each country, mostly with chief executive officers of microfinance institutions and banks including stars such as BRAC, Grameen Bank and the Basix Group.

She found that the biggest challenge faced in lending to the 'missing middle' firms in the three countries is the high degree of informality of their operations. In India, a large urban-based NBFC-MFI, Janalakshmi Financial Services, surveyed 13,177 potential missing middle customers with surprising results: 90% of them had never filed an income tax return, 67% had not maintained a book of accounts, and 65% had no enterprise registration of any form. 'This informality,' states Savita Shankar, 'is a primary reason for their financial exclusion, as banks typically ask for various documents and records before lending.'

These entrepreneurs also miss out on finance for another reason: they are unable to offer collateral – security pledged for the payment of a loan – to lending institutions. 'And even if they do have property,' explains Prof. Shankar, 'often the accompanying papers and documents may not be complete, making it hard for lenders to create a title and mortgage it.' As a result, lending to them has to be based on an assessment of their cash flows. But this isn't easy. Try gaining a clear picture of a small company's accounts and transactions when most of their business is cash-based. It makes it tough for financial institutions to obtain a clear picture of their volumes.

HIGH-TOUCH AND HAND-HOLDING: WHERE THE SOLUTIONS LIE

So how can these challenges be overcome? The top ingredients for success are highlighted in Prof. Shankar's research results, successful models in all three countries having two features in common. First, credit appraisal of potential borrowers must involve a specially designated lending officer who spends considerable time observing the business, interviewing the owners, cross-checking the records, analyzing the business model and assessing suppliers and customers. Altogether, it is a very high-touch and hand-holding experience and it is often the case that these officers themselves draw up cash flow statements for the potential borrowers. The second essential feature often involves training the potential borrowers in financial accounting practices – either formally or informally.

In addition, other in-the-field factors have an important impact. The issue of collateral can be circumnavigated by banks accepting notional security such as original land documents or identity cards. Pragmatically, microfinance banks can also develop in-house model cash flow statements for specific sectors that are commonly financed. And on another level – that of eliminating bias – banks can offer a more objective treatment of potential missing middle companies by separating the credit function from the sales function within their organisation.

'The problem is that these strategies call for upfront investment in employee time before obtaining any financial returns from the enterprise,' states Prof. Shankar. 'But if microfinance institutions manage to build a robust lending model, in the long term the benefits of this strategy can pay off by way of potential repeat business as well as savings in recovery and loan write-off costs.'

STEPPING UP A LEVEL

On a more macro level, Prof. Shankar's interviews and analysis pinpointed other measures that could help increase the availability of funds to missing middle enterprises. For example, in India, Bangladesh and Pakistan it has now become easier for microenterprises to open and operate bank accounts due to the availability of mobile-based digital finance and debit cards. 'So it should be possible for them', argues Prof. Shankar, 'to switch to account-based transactions.' However, this will take time – their entire ecosystem, including suppliers and customers, needs to change. And this is where Intervention from NGOs and government may be required to nudge things forward through policy, technical help, funding and training initiatives.

Other recommendations include developing new, customized financial products to address entrepreneurs' specific needs and constraints – one criticism being that microfinance banks tend to offer a one-size-fits-all model. Another way is what is termed value chain financing: microfinance providers can analyse the value chains of small enterprises and finance the various participants with a view to improving the overall efficiency of the chain. 'This would involve assessing the enterprise's suppliers and customers,' explains Savita Shankar, 'and financing all of them as a cluster so as to reduce overall risk for the lender.'

And finally, other areas for hope include the role of credit bureaus. In India and Pakistan at least, most large microfinance providers now report to them. This means that if individuals have borrowed from these institutions in the past, their credit histories will now be available – a way to both check a small enterprise's legitimacy for a bigger loan and also reduce risk for the bank. Moreover, the payment history for utility and telephone bills of potential borrowers can also be scrutinized to check creditworthiness. Not to mention the fact that specialized credit rating agencies focusing on small firms may soon develop.

STEPS AT THE MICRO LEVEL

'In India, the infrastructure to cater to this segment is being put in place,' says Prof. Shankar, something that can be seen in the launch of a public sector financial institution, the Micro Units Development and Refinance Agency, known as MUDRA. Its job is to assist micro-finance banks – which report to credit bureaus – with a hefty Rs200 billion available for onlending and Rs30 billion for provision of credit guarantees.

'Bangladesh, the earliest microfinance market, has also been the first to observe and address the needs of microfinance graduates,' states Shankar. Larger MFIs dominate the segment as smaller ones are constrained by availability of funds. 'However,' she continues, 'the lack of a credit bureau increases risk levels considerably and is a significant drawback in the Bangladesh microfinance sector.' This high risk reduces the incentive for lenders to provide larger-value loans and Prof. Shankar stresses the importance for regulatory action to address this lacuna. The prevailing uncertain political climate in Bangladesh also increases the riskiness of microenterprise loans, as small businesses are often adversely affected by shutdowns and at times even sustain damage during political disturbances.

In Pakistan, microfinance banks providing microenterprise loans have met with success and two banks are in the process of scaling up the product to cater for the missing middle. 'As the loan sizes and number of loans increases,' asserts Prof. Shankar, 'the availability of a credit bureau in the country should help lenders. An area for concern,' she adds, 'is that the overall penetration of the microfinance sector in the country is low, though the recent efforts being made to increase funding for MFIs may be helpful in this regard.' Prof. Shankar points to the fact, however, that the political disturbances in the country and prevailing shortage of electricity are risk factors that could affect the performance of microenterprise loans.

'In all three countries, governments need to support lenders with funding options, make reporting to credit bureaus compulsory, fund financial literacy campaigns targeted at microenterprises, introduce measures to reduce use of cash-based transactions, and make registration of enterprises easy and universal,' concludes Prof. Savita Shankar. 'Catering to the financing needs of missing middle firms has great potential to invigorate South Asian economies – making them more inclusive and dynamic.'

KEY TAKE AWAYS

IN EMERGING ASIAN ECONOMIES, ENTREPRENEURIAL VENTURES ARE CAPPED ON THE AMOUNT OF MICRO-FINANCING REQUIRED TO GROW FURTHER, AND TOO SMALL TO BENEFIT FROM THE SIZE OF LOANS OFFERED TO SMES BY THE COMMERCIAL BANKS.

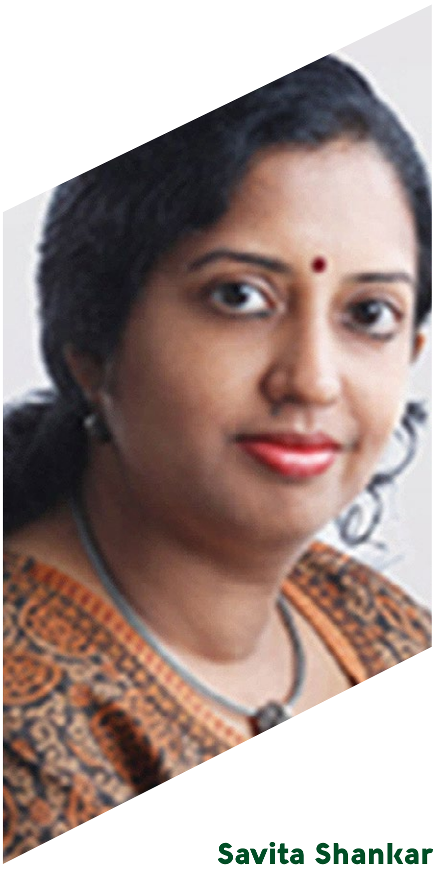
THE MICROFINANCE SECTOR, HAVING REACHED MATURITY, SEES THE NEED FOR SUCCESSFUL MICRO-FINANCED ENTREPRENEURS TO AIM FOR HIGHER LOANS THAT DON'T ACTUALLY EXIST.

CREDIT APPRAISAL OF POTENTIAL BORROWERS MUST INVOLVE A SPECIALLY DESIGNATED LENDING OFFICER TO OBSERVE, DISCUSS, CROSS-CHECK AND ANALYSE THE BUSINESS MODEL.

MICROFINANCE PROVIDERS CAN ANALYSE THE VALUE CHAINS OF SMALL ENTERPRISES AND FINANCE THE VARIOUS PARTICIPANTS WITH A VIEW TO IMPROVING THE OVERALL EFFICIENCY OF THE CHAIN.

IF INDIVIDUALS HAVE BORROWED FROM CREDIT BUREAUS IN THE PAST, THEIR CREDIT HISTORIES WILL NOW BE AVAILABLE – A WAY TO BOTH CHECK A SMALL ENTERPRISE'S LEGITIMACY FOR A BIGGER LOAN AND ALSO REDUCE RISK FOR THE BANK.

GOVERNMENTS NEED TO SUPPORT LENDERS WITH FUNDING OPTIONS, MAKE REPORTING TO CREDIT BUREAUS COMPULSORY, FUND FINANCIAL LITERACY CAMPAIGNS TARGETED AT MICROENTERPRISES, INTRODUCE MEASURES TO REDUCE USE OF CASH-BASED TRANSACTIONS, AND MAKE REGISTRATION OF ENTERPRISES EASY AND UNIVERSAL.



Savita Shankar

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CHINESE FIRMS AND CORPORATE MALFEASANCE ON THE HONG KONG STOCK EXCHANGE

Through their research on the Hong Kong Stock Exchange, Profs **Daphne Lui** and **Andrei Filip** of **ESSEC Business School** uncover evidence of corporate malfeasance by publicly listed Chinese firms, exposing the cross-jurisdictional challenges faced by regulators.

From the paper Cross-listing and corporate malfeasance: Evidence from P-chip firms; Andrei Filip, Zhongwei Huang, Daphne Lui.

AS THUNDERING POLITICAL demonstrations shook Hong Kong last summer, China's continued dependence on the former British colony for access to global capital markets tempered Beijing's response. For years, the Chinese private sector's thirst for external sources of capital has been quenched by the US$3.9 trillion Hong Kong Stock Exchange (HKSE). However, research by Professors Daphne Lui and Andrei Filip of ESSEC Business School has uncovered evidence of rampant corporate malfeasance by Chinese firms listed in Hong Kong. Cross-jurisdictional challenges between the special administrative region and the mainland, they argue, have left investors vulnerable to expropriation and other misconduct by firms' controlling shareholders and executives.


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FINANCING RAGS TO RICHES

Following its market-oriented reforms in 1978, China's economy experienced exponential growth, rising to become the second-largest economy in the world. According to Profs Lui and Filip, this market-oriented growth was "initially fueled by the partial privatization of state-owned enterprises". In recent years, however, "the economic power released by the phenomenal growth of the private sector has dominated the scene". The demand for external sources of capital has surged as Chinese private sector firms have sought financing to pursue further expansion. From London to Singapore, the world has witnessed an influx of applications by these firms for listings on their stock exchanges, but most are concentrated in Hong Kong. This has made the special administrative region the "de facto hub for hosting initial public offerings (IPOs) of mainland Chinese private sector firms". However, although Hong Kong and other popular overseas listing destinations have high-quality securities regulatory environments, Profs Lui and Filip assert that "there have been mounting concerns" that overseas-listed private-sector Chinese firms have not met the more stringent listing, disclosure, and corporate governance requirements that ensure better investment protection. Instead, numerous financial scandals associated with Chinese firms have broken in recent years, often subjecting investors to significant financial losses.

In order to study these recurrent cases of corporate malfeasance, Lui and Filip analysed a large sample of Chinese firms listed on the HKSE commonly known as P-chips. These firms are particular as their operations are located in mainland China but they are incorporated in tax havens such as the Cayman Islands. Despite their suspect corporate structures, P-chips have proliferated since their first listing at the turn of the 21^{st} century. At present, they are the largest group of Chinese firms listed on the HKSE, representing 20.3% of the stock exchange's total market capitalisation. In their research of their misconduct, Profs Lui and Filip focused on aggressive earnings management—a financial reporting practice that could involve the diversion of financial resources. Using discretionary accruals as a proxy for this earnings management, they analysed over 3,200 HKSE-listed firms' accounting and financial data. In addition to higher total assets and net income, the researchers found statistically significant evidence that P-chip firms have higher levels of discretionary accruals than other HKSE-listed firms, contributing to their estimated US$10.5 million high profits than non-P-chips. In addition, non-P-chip firms' financial statements are more prone to material accounting misstatements and they are more likely to tunnel corporate resources out of the companies to their controlling shareholders. However, they can engage in these corporate malfeasances with relative impunity by exploiting the cross-jurisdictional challenges faced by Hong Kong's regulatory authorities.

FINDING THE SHERIFF

Although Hong Kong was returned to China in 1997, as a former British colony, the special administrative region follows a common law tradition. Consequently, the securities regulations and their enforcement in Hong Kong and mainland China differ significantly. According to literature cited by Professors Lui and Filip, the special administrative region "has a stronger legal system with regard to shareholder and debtholder protection relative to mainland China". Moreover, the World Bank consistently scores Hong Kong far above mainland China in its regulatory quality index. Along with its effective enforcement environment and the rule of law, these qualities have enabled Hong Kong to become Asia's leading financial centre in spite of its small size. However, the special administrative region's regulatory reach is limited. On the mainland, the Beijing-based China Securities Regulatory Commission (CSRC) is responsible for the oversight of all securities activities. While the CSRC has cooperated with Hong Kong's Securities and Futures Commission (SFC) in the past, according to Lui and Filip, "Hong Kong securities regulators have repeatedly voiced concerns about mainland authorities rejecting their requests for information to investigate Hong Kong-listed companies and businessmen from mainland China". As such, although Hong Kong has high regulatory standards for listed firms, in the presence of cross-jurisdictional enforcement difficulty, managers of P-chip firms perceive lower risks of misbehaviour and thus have stronger incentives to engage in opportunistic behaviours to extract private benefit at the expense of minority shareholders.

From investigating P-chip firms' alleged financial irregularities and bringing their key managers to face justice to seizing their assets, without the support of local authorities such as provincial governments and courts, Hong Kong securities regulators are often powerless to enforce minority shareholders' rights. This was the case in 2008 when First Natural Foods (FNF), a Bermuda-incorporated food manufacturing and trading company operating in mainland China and listed on the HKSE since 2002, was arbitrarily shut down by its chairman and filed for bankruptcy. Soon thereafter, Hong Kong regulators uncovered a few irregularities. In addition to an RMB705 million difference between the company's audited financial statements

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and its actual cash deposits, an investigation revealed that its chairman had embezzled HK$85 million from the company. However, multiple attempts to seek help from local mainland authorities failed. Although anecdotal, the story of the expropriation of FNF's investors is not unique. Indeed, having become aware of the cross-jurisdictional challenges faced by Hong Kong regulators, investors have started to account for P-chip firms' corporate malfeasance. Lui and Filip's analysis demonstrates that the market discounts P-chip earnings surprises, understanding that they are often the result of manipulations. This provides evidence that P-chip firms engage in earnings management activities against the benefits of minority shareholders but that the market anticipates their misbehaviour.

ACTING WITH IMPUNITY

Through their research, Profs Lui and Filip provide evidence that P-chip firms, the largest and most representative group of Chinese private sector firms listed overseas, manipulate their accounts and engage in corporate malfeasance. Although Hong Kong has a higher-quality regulatory environment than mainland China, cross-jurisdictional challenges and enforcement difficulties enable P-chip firms to engage in this misbehaviour with relative impunity. Subject to expropriation by their controlling shareholders and executives, minority investors have started to anticipate these P-chip firms' corporate malfeasance through the market, highlighting the need for greater regulatory cooperation on both sides of the Sham Chun River.

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Daphne Lui

Andrei Filip

KEY TAKE AWAYS

THE DEMAND FOR EXTERNAL SOURCES OF CAPITAL HAS SURGED AS CHINESE PRIVATE SECTOR FIRMS HAVE SOUGHT FINANCING TO PURSUE FURTHER EXPANSION.

HONG KONG HAS BECOME THE DE FACTO HUB FOR HOSTING INITIAL PUBLIC OFFERINGS (IPOS) OF MAINLAND CHINESE PRIVATE SECTOR FIRMS.

NUMEROUS FINANCIAL SCANDALS ASSOCIATED WITH CHINESE FIRMS HAVE BROKEN IN RECENT YEARS, OFTEN SUBJECTING INVESTORS TO SIGNIFICANT FINANCIAL LOSSES.

RESEARCH HAS FOCUSED ON P-CHIP COMPANIES: FIRMS WHOSE OPERATIONS ARE LOCATED IN MAINLAND CHINA BUT WHICH ARE INCORPORATED IN TAX HAVENS SUCH AS THE CAYMAN ISLANDS. THEY ARE THE LARGEST GROUP OF CHINESE FIRMS LISTED ON THE HKSE, REPRESENTING 20.3% OF THE STOCK EXCHANGE'S TOTAL MARKET CAPITALISATION.

P-CHIPS REPORT AN ESTIMATED US$10.5 MILLION ON AVERAGE MORE IN PROFITS THAN NON-P-CHIPS.

AGGRESSIVE EARNINGS MANAGEMENT IS A FINANCIAL REPORTING PRACTICE THAT COULD THE DIVERSION OF FINANCIAL RESOURCES.

HONG KONG HAS HIGH REGULATORY STANDARDS FOR LISTED FIRMS, BUT CROSS-JURISDICTIONAL ENFORCEMENT DIFFICULTY WITH MAINLAND CHINA MEANS THAT MANAGERS OF P-CHIP FIRMS PERCEIVE LOWER RISKS OF MISBEHAVIOUR AND THUS HAVE STRONGER INCENTIVES TO ENGAGE IN OPPORTUNISTIC BEHAVIOURS TO EXTRACT PRIVATE BENEFIT AT THE EXPENSE OF MINORITY SHAREHOLDERS.

WITHOUT THE SUPPORT OF LOCAL AUTHORITIES SUCH AS PROVINCIAL GOVERNMENTS AND COURTS, HONG KONG SECURITIES REGULATORS ARE OFTEN POWERLESS TO ENFORCE MINORITY SHAREHOLDERS' RIGHTS.

THROUGH RESEARCH, EVIDENCE HAS BEEN FOUND THAT P-CHIP FIRMS MANIPULATE THEIR ACCOUNTS AND ENGAGE IN CORPORATE MALFEASANCE.

SUBJECT TO EXPROPRIATION BY THEIR CONTROLLING SHAREHOLDERS AND EXECUTIVES, MINORITY INVESTORS HAVE STARTED TO ANTICIPATE THESE P-CHIP FIRMS' CORPORATE MALFEASANCE THROUGH THE MARKET, HIGHLIGHTING THE NEED FOR GREATER REGULATORY COOPERATION.

THE UNAVOIDABLE COST OF GOING GREEN: MOVING FROM DEMAGOGY TO EFFICIENT ACTION

Marc Guyot and **Radu Vranceanu,** Professors of Economics at **ESSEC Business School,** take a pragmatic look at the global warming debate and call upon stakeholders to accept a no-pain-no-gain approach.

FUELLING THE ANGST

IT IS WIDELY agreed today that the major political, economic and technological challenge to come for humanity is climate change. Inevitably, this all-too-real challenge triggered the media machine into motion, hammering home an apocalyptic message meant to incite passions and provoke all sorts of reactions through accusing the wicked perpetrators behind it. Anxiety linked to a forthcoming end of the world is taking root, upsetting the minds of the young and not-so-young alike, and is prompting? companies and governments to undertake action that seems more aimed at calming this angst and bringing new business into the fold than taking effective decisions.

This nervousness is all the more distressing given that the diagnostic is indeed damning. The last two centuries of growth based on the use of fossil fuels – coal, petrol and natural gas – have resulted in an accumulation of CO^2 in the atmosphere, which sends the sun's rays back towards Earth, warming it at an alarming rate. While in 1750 the concentration in CO^2 (or carbon) was 280 ppm, it was 413 ppm in 2018, and, if nothing changes, it is set to reach 700-900 ppm in 2100, bringing with it a 3°-5°C rise in temperatures in relation to the pre-industrial era. This should have truly dramatic consequences for life as we know it.

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FUELLING THE ANGST

It is widely agreed today that the major political, economic and technological challenge to come for humanity is climate change. Inevitably, this all-too-real challenge triggered the media machine into motion, hammering home an apocalyptic message meant to incite passions and provoke all sorts of reactions through accusing the wicked perpetrators behind it. Anxiety linked to a forthcoming end of the world is taking root, upsetting the minds of the young and not-so-young alike, and is prompting? companies and governments to undertake action that seems more aimed at calming this angst and bringing new business into the fold than taking effective decisions.

This nervousness is all the more distressing given that the diagnostic is indeed damning. The last two centuries of growth based on the use of fossil fuels – coal, petrol and natural gas – have resulted in an accumulation of CO^2 in the atmosphere, which sends the sun's rays back towards Earth, warming it at an alarming rate. While in 1750 the concentration in CO^2 (or carbon) was 280 ppm, it was 413 ppm in 2018, and, if nothing changes, it is set to reach 700-900 ppm in 2100, bringing with it a 3°-5°C rise in temperatures in relation to the pre-industrial era. This should have truly dramatic consequences for life as we know it.

OF FOSSILS AND GREEN POPULISM

Insofar as carbon capture technologies are not yet fully developed, at this date in time there seems to be no other serious solution possible than the diminishing of CO^2 emissions by a drastic reduction in the use of fossil fuels for the production of energy. As much as there is large consensus on this vital necessity, its tangible implementation remains extremely difficult. In effect, how can we decide on a common amount of reduction in their use? What power stations should be closed? In which countries? And from now onwards should fossil fuel-driven engines be banned? The absence of an answer from policymakers to these core questions are to the delight of the activists who strive to take on the role of saviour by proposing reductions that are as poorly well-grounded as unachievable. It also provides support to a new form of green populism. Accusations of climate indifference on the social networks leads to governments sidestepping the issue by highlighting a patchwork of spectacular, yet conflicting and ineffective measures.

> "To date, there is no viable solution other than massively taxing carbon and accepting the strong increases in costs that come as a result."

It is not the market economy itself that is responsible for pollution and carbon emissions. It is a consequence of the methods of industrial production – whether this production takes place within the framework of a planned economy or that of a market-driven economy. However, a market economy offers a possibility of bringing necessary adaptation from the simple principle of the so-called law of supply and demand: the more expensive the product, the less it will be in demand and therefore the less it will be produced. As such, the hidden cost of a ton of carbon must be set – and those producing it made to pay. A while ago, A.C. Pigou (1920) indicated that a tax on pollution would enable governments to effectively correct – via price mechanisms – this form of negative externality. Applied to the present issue, this would mean a tax on every ton of carbon produced. This is the principle of the "carbon tax".

A MULTI-DISCIPLINARY LIGHT ON THE MATTER

To measure the feasibility and the cost of the transition towards an economy that limits its carbon emissions, experts use integrated evaluation models (IMAs), in large part developed by Professor William Nordhaus, Nobel Prize for Economics 2018 [cf. Barrage, 2019], building on the early work of Tjalling Koopmans. A model of this type enables the integration of economic, demographic and physical mechanisms – the use of energy for production and how that production is used; and physical mechanisms – how production generates carbon, how technology contributed to higher efficiency use of energy over time, what the carbon cycle is, what share is absorbed and what share accumulated, and how the accumulation of carbon modifies the sea temperature and level – to be represented. The model then represents how in turn these changes impact the economy (floods, storms, acidification of the ocean, decrease in agricultural productivity, etc.). A model of this type presents many "loops" – or situations where A influences B, B influences C, and C has an impact on A.


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Existing integrated models of evaluation can be relatively compact, with twenty or so key relationships, and delve into the details of the process taking into account hundreds of relationships and hundreds of thousands of variables. What sets this model apart is that (1) its dynamic optimization framework, and (2) its interactive character consumption and carbon emissions – are interconnected. Such models allow us to simulate future developments by using scenarios for population growth, revenue growth, and productivity. And, most importantly, they enable us to simulate how public policy can modify the trajectory of consumption and GDP, carbon emissions and temperatures.

However, IAMs are not infallible tools in as much as the impact on climate and policy costs depends on hypotheses linked to parameters and mechanisms such as productivity growth rate, demographic growth rate or even the discount rate for the future generations well-being. Moreover, there are also uncertainties regarding the relationships themselves and the "tipping points" because global warming can trigger catastrophes and irreversible crises. But the debate on their sources and margins of error (see Gillingham et al., 2018) is in itself useful for improving policies. For example, thanks to integrated evaluation models, we now realise that the objective to limit the rise in temperatures to a 2°C maximum by 2100 is almost unreachable; whether an unachievable goal is useful for its signaling effect or not, it is open to debate. On the other hand, an objective of 2.5°C would be quite realistic.

A TERRIBLE DILEMMA: THE NOW OR THE FUTURE

The integrated evaluation model, through its construction – constrained inter-temporal optimisation (in general with an infinite horizon) – enables us to assess in a rigorous way the "social cost" of an extra ton of carbon released in the atmosphere. Today, an additional ton of carbon is linked to more consumption in the present, thus higher benefit for the current generation. However, it also carries costs on the future generations having to compensate for the harmful effects, by consuming less than they could in their time. In the case of a massive increase in temperatures, these costs can be very high. The social cost of carbon can be seen as the total costs imposed on humanity of today from letting out an extra ton of carbon into the atmosphere. Obviously, the more importance we give to the future generations, the larger this discounted cost of a ton of carbon and inversely. The importance to us of the consumption of future generations is modelled by a discount factor equal to one (or a zero discount rate) if the future counts as much as the present, or less than one if it counts for less. The debate on the correct discount rate is far from settled.

Turning back to the rationale by Pigou (1920) a tax on carbon emissions would increase the cost of fossil energy and would create the incentive to reduce its use. The IAMs allow an "appropriate" carbon tax to be determined. Indeed, a carbon tax identical to the social cost of carbon as determined within the IAMs framework should set economic growth on a path in line with the objectives of reducing emissions and controlling the rise in temperatures.

According to William Nordhaus, who published a summary of the most recent IAMs results in the American Economic Review in 2019 (Nordhaus, 2019), if we make the hypothesis that the discount factor of the future generation consumption is very close to one and we accept the target of limiting the increase in temperature to 2°C maximum, most integrated models reach a carbon social cost in a range of $500 per ton to $900 per ton, which is obviously a very significant figure. We should keep in mind fo instance that today a Paris-NYC flight generates approximately one ton of carbon per traveler, or that a Big-Mag generates some 3 kg of CO^2 emissions. With discounted factors closer to those of private investment and a more realistic objective set at a 2.5°C rise in temperatures, the social cost of carbon would be around $200 per ton. In its latest report, the World Bank (2019) is more optimistic – it estimates that a tax at around $100 per ton towards 2030 would be enough to reach the COP21 objective.

It is worrying to see that today governments are very far from this optimal level. In 2019, out of the thirty or so countries which implemented such a tax, its amount rarely surpassed $30 per ton – with the notable exception of

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Sweden ($129 per ton) and Switzerland ($96 per ton). However, even in these "virtuous" countries, carbon tax covers less than 50% of CO^2 emissions – which is also the case for most other countries. In France, in 2019 the government gave way when faced with the "yellow vests" movement and renounced on the increase in carbon tax it wanted to implement at €44.6 per ton (the French tax being already "hidden" in an older tax on fuels). Implementing too low a carbon tax with only partial cover of emissions virtually means trying to put out a fire with a single drop of water.

The alternative to carbon tax, implemented in thirty or so other countries (sometimes in parallel to the carbon tax) is the setting up of a market for carbon permits, associated with regulations limiting the total amount of the emissions per country in line with the planned reduction in emissions. The price of carbon on this market would be equal to the social cost of carbon. As such, carbon market or carbon tax amount to being equivalent instruments, the second providing the advantage of being less prone to manipulation by lobbies and less sensitive to electoral cycles.

It seems, then, that while there is a possible solution to act on climate change via the carbon tax, governments and the public are not ready to assume the cost of this effective action. Their problem evidently comes from political fear at the idea of announcing to their citizens the level of cost that society should have to bear today and the way in which this cost will be distributed. Whether governments choose a tax or restrictions on emissions, it would push up the price massively for every good that is intensive in carbon – transport, heating, air conditioning – but also, all those goods whose production requires energy would see their price increase. And this would then spread rapidly to the goods that use them as intermediary inputs. While this could set emissions on a sustainable path, today's consumption loss will be significant. Yet, there is no "miracle" solution, where the goals could be achieved only by changing consumption habits at the margin.

THE BOTTOM LINE

The slowness of government action coupled with media pressure focusing on reproaches and accusations rather than on carbon tax make some companies communicate on their plans to become carbon-neutral. Unsurprisingly, these are especially companies selling mass market consumer goods (and therefore dependent on the positive image they provide) whose technical characteristics make them use low levels of energy. Their green strategy is more of a communication tool, while the impact on carbon emissions is small. Companies in the energy or steel sector are technologically unable of presenting such plans, which is easy to understand. This does not mean that we do not need steel or energy and we must shut down these firms. The application of a carbon tax would however have an extremely strong sectorial effect on the price of electricity and steel, yet this cost rise will be transmitted to energy users proportional to their use of energy.

Governments are not only slow but also inconsistent with what they say and what they do. When French authorities focused on limiting particle pollution in the cities, they purely and simply forget climate change and instead incited drivers to change from diesel-driven cars to petrol-driven cars – although the latter produce more CO^2 per kilometer than diesel cars. A country like China has given itself an objective to become the leading producer worldwide of electric cars to reduce urban pollution, but it is also the principal country to use coal to produce electricity. The transition towards electric vehicles will aggravate climate change if coal remains to be used as a source of electric energy.

To date, and in the actual state of technological progress, there is no viable solution other than massively taxing carbon and accepting the strong increases in costs that come as a result. This observation and this way forwards does not seem to be on any government's agenda, and still less that of voters. In the meantime, however, the climate issue will not be solved by one more Sunday market organised by green vests, by one more plate of vegetables, or by a handful of small, daily eco-gestures.

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KEY TAKE AWAYS

THERE SEEMS TO BE NO OTHER SERIOUS SOLUTION POSSIBLE THAN THE DIMINISHING OF CO^2 EMISSIONS BY A DRASTIC REDUCTION IN THE USE OF FOSSIL FUELS FOR THE PRODUCTION OF ENERGY. ITS TANGIBLE IMPLEMENTATION REMAINS EXTREMELY DIFFICULT.

TO MEASURE THE FEASIBILITY AND THE COST OF THE TRANSITION TOWARDS AN ECONOMY THAT LIMITS ITS CARBON EMISSIONS, EXPERTS USE INTEGRATED EVALUATION MODELS (IMAS).

THIS MODEL ENABLES THE INTEGRATION OF ECONOMIC, DEMOGRAPHIC AND PHYSICAL MECHANISMS TO BE REPRESENTED AND SHOWS HOW THESE CHANGES IMPACT THE ECONOMY.

IAMS ALLOW AN "APPROPRIATE" CARBON TAX TO BE DETERMINED. BUT IN 2019, AMONG 30 COUNTRIES WITH SUCH A TAX, ITS AMOUNT RARELY SURPASSED $30 PER TON. EVEN IN "VIRTUOUS" COUNTRIES (SWEDEN, SWITZERLAND), CARBON TAX COVERS LESS THAN 50% OF CO^2 EMISSIONS – WHICH IS ALSO THE CASE FOR MOST OTHER COUNTRIES.

THE ALTERNATIVE/PARALLEL SOLUTION TO CARBON TAX IS SETTING UP RESTRICTIONS ON CARBON EMISSIONS BUT GOVERNMENTS AND THE PUBLIC ARE NOT READY TO ASSUME THE COST OF THIS EFFECTIVE ACTION.

WHETHER GOVERNMENTS CHOOSE A TAX OR RESTRICTIONS ON EMISSIONS, IT WOULD PUSH UP THE PRICE MASSIVELY FOR EVERY GOOD THAT IS INTENSIVE IN CARBON.

TO DATE, THERE IS NO VIABLE SOLUTION OTHER THAN MASSIVELY TAXING CARBON AND ACCEPTING THE STRONG INCREASES IN COSTS THAT COME AS A RESULT.

READER'S NOTES

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COBS READER COMMENTS

This is one of the best sites [for articles] I have ever visited. We all need to support women entrepreneurs in every aspect. The content is very informative. Thank you for sharing it.
Ashwin

These articles or blog posts are genuinely wonderful and I routinely move them on to my college students who're facing/struggling with exams and research competencies – they listen to you in a very way they really don't to me!
Moinc

Thanks for sharing this stuff, teaching innovation is one of the best points I found here, keep up the good work. Best Regards.
Fek

This is inspiring and thought-provoking. As businessmen, we indeed need to learn to live with sustainability and mind and we should also learn how to respond to environmental emergencies.
Chelsea L

Hi, I like your articles everyweek. Your writing style is witty, keep up the good work!
Anon

It's a pity you don't have a donate button! I'd most certainly donate to this fantastic blog! I suppose for now I'll settle for bookmarking and adding your RSS feed to my Google account. I look forward to new updates and will talk about this blog with my Facebook group. Chat soon!
Alena Vayon

Thanks for a marvelous posting! I really enjoyed reading it, you happen to be a great author. I will remember to bookmark your blog and definitely will come back later on. I want to encourage you to continue your great work, have a nice morning!
Lanny Battaglino

I blog often and I genuinely thank you for your information. This article has really peaked my interest. I'm going to take a note of your website and keep checking for new information about once per week. I opted in for your Feed as well.
Baten

I absolutely love your blog and find a lot of your posts to be what precisely I'm looking for. I wouldn't mind publishing a post or elaborating on a lot of the subjects you write regarding here. Again, awesome blog!
Rudolphe H

I love the advice for students about fostering intellectual curiosity. It seems like this can lead to a love and passion for almost anything, especially the energy sector. My brother in law is very interested in futures trading. He's looking into energy market reports.
Jake G

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