Leadership Reimagined: Strategies for Stakeholder Engagement and Long-Term Success

By: Alexandra Khart, Audrey Yu May 2024

Introduction

What is considered effective corporate leadership has changed substantially over time. Thirty years ago, best practices encouraged business leadership to be predominantly autocratic, and to make decisions without input from other stakeholders. However, over the past few decades, there has been a growing emphasis on responsive and collaborative leadership. This shift has come with a new generation of leaders, employees, and consumers who hold different priorities and expectations than their predecessors. Corporations have begun facing pressure to consider stakeholders beyond just shareholders, and to consider social and environmental issues in balance with wealth-maximization.

However, these goals often find themselves at odds, and it can be very challenging for leadership to adapt to these new expectations while still addressing existing company needs. With this whitepaper, we intend to identify key strategies and initiatives that leadership can utilize to maintain the careful equilibrium necessary to effectively meet ever evolving expectations.

Shareholders vs. Stakeholders

Historically, corporations have been led according to the theory of shareholder primacy. Shareholder primacy is a shareholder-centric form of corporate governance purely focused on maximizing shareholder wealth. Within the last twenty years, shareholder primacy has faced increased criticism, with critics citing the theory's tendency to lead to short-term profit-seeking decisions with disregard to the long-term welfare of the company and other stakeholders. This phenomenon has been dubbed 'short-termism' and has become increasingly prominent in media as several high-profile cases have brought the issue into the spotlight.

Case Study: Boeing

Aircraft manufacturer Boeing presents a clear example of the potential dangers of short-termism. Boeing's 737 Max suffered two fatal crashes in 2018 and 2019, killing 346 people. During the development of the 737 Max, Boeing was largely focused on cost-cutting and producing the cheapest possible plane. This effort to quickly increase profits led to the negligence of safety standards. The resulting crashes cost the company tens of billions, including a $200MM penalty to settle the SEC's charges. Boeing's focus on maximizing profit – in keeping with the principles on shareholder primacy – ended up costing the company financially and costing 346 people their lives.

Figure 1 Ethiopian Airlines Flight 302 Crash

Case Study: Nokia

Nokia became a prime example of how chasing quarterly profit margins could hurt a business in the long-term. In 2007, just before the release of the first smartphone, Nokia held nearly 50% of the cell phone market. However, when smartphones came out and became highly utilized, Nokia refused to update either hardware or software, because investing in R&D would hurt its quarterly performance. Due to the lack of innovation, Nokia rapidly lost market share, until they held just 3% in 2013. In 2021, the cell phone market was valued at $457B. Nokia's focus

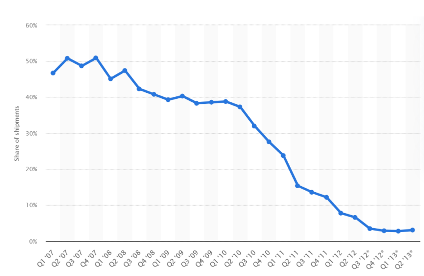

Figure 2 Nokia Market Share 2007-2013

on maximizing short-term profitability had cost the company billions in market share over the longer term.

A Radical Approach: Lessons from Indigenous Governance

In the present day, legal shareholder rights are such that an individual, or single entity, may purchase as many common shares of a corporation as they choose, and exercise the voting rights on those shares immediately after purchase. These laws have made it common for corporations to be controlled by large investors who have little interest in stakeholders beyond those who own voting shares. In essence, shareholders become the only stakeholders with voting power. Combined with the short-termism of shareholder primacy, it becomes all too easy for leadership to focus on short term profit, neglect other stakeholders, and in doing so sacrifice long term growth for short term gains.

One approach to addressing these issues involves legal changes by government entities. This rather radical approach finds its origins in the corporate governance models of Indigenous Corporations such as Alaska Native Corporations and Māori Corporations. Most of these potential changes have the same goal in mind: to align as much as possible the interests of shareholders with those of other stakeholders.

Shareholder Voting Rights Laws

Laws related to shareholder voting rights could be altered to encourage leaders to provide greater consideration to stakeholder interests. For example, rather than allowing shares of common stock to provide immediate voting power, shares can include voting rights that come into effect only after a certain amount of time. This ensures that voting shareholders have witnessed the company's decisions over time and have actively chosen to keep their shares, making them more likely to vote with long-term goals in mind.

Additionally, shares with variable voting rights can be issued, meaning that a share may or may not contain voting rights depending on the number of shares already owned. Putting a legal limit on the voting power of individual shareholders will allow for more diverse annual meeting attendance, leading to the election of board members that will advocate for a wider range of stakeholders and promote long term thinking.

Figure 3 Sample timeline for deferred voting rights

Share Ownership Laws

Another potential legal change reframes the idea of corporate share ownership itself. More precisely, mandating that stakeholders such as employees and community members have ownership in the company will ensure that interests in better working conditions as well as community and environmental awareness are heard and properly accounted for when leaders make decisions. Although not legally obligated to allocate share ownership to all stakeholders, several countries in the EU require that corporations designate seats on their Board of Directors for employees or representatives of worker interests. Adopting similar models worldwide through legal changes will necessitate that leaders become more responsive to all stakeholders.

Adopting Voluntary Changes: Minimizing Short-termism

Drastic legal changes to shareholder voting and ownership rules are not necessary to kick off long-term thinking for corporations. Leaders can begin to adopt some of these principles within the existing legal structure to engage stakeholders and help their companies look to the long term. The key to making these changes within existing shareholder-centric systems is the same as the principle behind the legal changes: to align shareholder and stakeholder interests.

Encouraging Long-term Thinking Through Investment and Compensation

Leaders can grant stock options to investors instead of direct stock. Stock options give the owner the right to purchase a specific number of shares at a pre-set price. Stock ownership is granted after a fixed vesting period. Until then, owners do not have voting rights, ensuring that voting shareholders support more long-term growth. In addition, implementing stock option compensation throughout the company instead of RSUs encourages employees at all levels to work towards the long-term growth of the company.

In the same vein, weighing management compensation more towards long-term goals and integrating metrics that track the impact of their decisions on all stakeholders can help align management and stakeholder interests. Some examples include compensation metrics based on the company's environmental impact (in this case, the environment is considered the stakeholder), or the company's direct impact on their local communities. In addition, taking the pressure off management to produce spectacular earnings at every quarterly call will encourage investment in long-term projects that benefit all stakeholders more than quick cash grabs.

Leading From the Ground Up

As mentioned previously, another voluntary change that can be implemented is the representation of employee interests on the Board of Directors. This initiative is complementary to employee stock option programs as described above because it engages and retains employees, and benefits employees in return, because they have a voice in strategic decision making. The employees selected for the board would be those with significant tenure at the company and can lend their wisdom based on substantial experience. In addition, because employees will typically reside in the area where the company is based, these initiatives will also help involve other stakeholders such as the community and the environment in decision making.

Final Thoughts

Whether leaders make changes related to altering share structures or introducing new models and programs, adaptability is key to addressing the needs of stakeholders and promoting long-term thinking. The implementation of these changes does not necessarily need to be rigid and all-encompassing; leaders should adjust their decisions based on their company's specific size, location, industry, vision, and culture. Each change, though on its own small, brings us one step forwards to the future of leadership that ensures flourishing environments for all of society.

The Black Box Institute is a unique boutique advisory firm and think tank that brings purposeful and thoughtful advice and guidance to clients. We specialize in complex business, transactional and organizational challenges. Our problem-solving techniques are a blend of traditional strategy and financial advisory capabilities and incorporate creative design thinking.

The Black Box Institute

For more information, please contact:

Janet McLeod
PO Box 52025
Oakville, ON, Canada, L6J 7N5
T: 416.862.5487
F: 416.861.9268

www.theblackboxinstitute.com
/the-black-box-institute

References

Ahmed, M. A. (2021, September 8). *4 Ways a Business Can Create a Positive Social Impact*. LinkedIn. https://www.linkedin.com/pulse/4-ways-business-can-create-positive-social-impact-aitzaz-ahmed/

Balancing sustainability and profitability. (2022). IBM. https://www.ibm.com/thought-leadership/institute-business-value/en-us/report/2022-sustainability-consumer-research

Bennard, I. (2022, March 4). *How Leadership Has Changed Today from 5 Years Ago*. Training Magazine. https://trainingmag.com/how-leadership-has-changed-today-from-5-years-ago/

Boeing will pay $200 million to settle SEC charges over 737 Max crashes. (2022, September 22). NPR. https://www.npr.org/2022/09/22/1124617261/boeing-will-pay-200-million-to-settle-sec-charges-over-737-max-crashes#:~:text=Boeing%20has%20agreed%20to%20pay,and%202019%2C%20killing%20346%20people

Burlington Coat Drive: Keeping Your Community Warm. (2022). Delivering Good. https://www.delivering-good.org/our-impact/campaigns/burlington-coat-drive/

CFI Team. (2023, January 11). *Shareholder Primacy*. Corporate Finance Institute. https://corporatefinanceinstitute.com/resources/equities/what-is-shareholder-primacy/

Christensen, G. (2021). Indigenous Perspectives on Corporate Governance. *University of Pennsylvania Journal of Business Law*, *23*(4), 902-954.

Creary, S. (2022, May 10). *Why More Companies Are Standing Up on Social Issues*. The Wharton School. https://knowledge.wharton.upenn.edu/article/why-more-companies-are-standing-up-on-social-issues/

Do ESG Ratings Impact Stock Price Volatility? (2022, July 11). ISS Insights. https://insights.issgovernance.com/posts/do-esg-ratings-impact-stock-price-volatility/

EHS Today Staff. (2022, April 12). *Workforce Trends Leaders Need to Understand*. EHS Today. https://www.ehstoday.com/ehs-outloud-blog/article/21238529/workforce-trends-leaders-need-to-understand

Fine, M. (2022, August 29). *The Leadership Of The Future*. Forbes. https://www.forbes.com/sites/melaniefine/2022/08/29/the-leadership-of-the-future/?sh=543430f57ed2

4 Reasons to Invest in Leadership Development. (2022). Center for Creative Leadership. https://www.ccl.org/articles/leading-effectively-articles/why-leadership-development-is-important-4-reasons-to-invest/

The Future of Leadership in 2030: 6 New Disruptive Trends. (2022, August 5). Quantic. https://quantic.edu/blog/2022/08/05/the-future-of-leadership-in-2030-6-new-disruptive-trends/

Gassmann, P., & Jackson-Moore, W. (2022, December 6). *The CEO's ESG dilemma*. PwC. https://www.pwc.com/CEO-ESG-dilemma?WT.mc_id=CT1-PL50-DM2-TR2-LS4-ND30-TTA9-CN_CEOESGDilemma-LI

Gratton, L. (2021, May). *How to Do Hybrid Right*. Harvard Business Review. https://hbr.org/2021/05/how-to-do-hybrid-right

Harwell, D. (2022, November 14). *A fake tweet sparked panic at Eli Lilly and may have cost Twitter millions*. The Washington Post. https://www.washingtonpost.com/technology/2022/11/14/twitter-fake-eli-lilly/

Herman, C. (2022). *How much does the public care about ESG?* PwC. https://www.pwc.com/gx/en/services/sustainability/publications/cop26/how-much-does-the-public-care-about-esg-pwc-cop26.html

How far is sustainability embedded into your corporate strategy? (2023). The Economist. https://impact.economist.com/projects/real-world-strategy/esgstrategy/1/

Jaffe, D. (2021, February 24). *From Shareholder Primacy To Stakeholder Primacy: How Family Businesses Lead The Way*. Forbes. https://www.forbes.com/sites/dennisjaffe/2021/02/24/from-shareholder-primacy-to-stakeholder-primacy-how-family-businesses-lead-the-way/?sh=419c4c4d21ed

Kelly, E., & Girzadas, J. (2022). *The future of business leadership*. Deloitte. https://www2.deloitte.com/us/en/pages/about-deloitte/articles/future-of-business-leadership.html

King, D. (2022, August 10). *How companies can balance people and profit when engaging in social issues*. Accenture. https://www.accenture.com/us-en/blogs/accenture-research/how-companies-can-balance-people-and-profit-when-engaging-in-social-issues

Long-term Thinking Is Your Best Short-term Strategy. (2018, August). The Wharton School. https://executiveeducation.wharton.upenn.edu/thought-leadership/wharton-at-work/2018/08/long-term-thinking/

Marsh, E. (2020, January 22). *How leadership has changed: 2000 versus 2020*. T-Three. https://www.t-three.com/thinking-space/blog/leadership-2000-2020

Passengers in fatal Boeing 737 MAX crashes are 'crime victims,' US judge says. (2022, October 23). CNN. https://www.cnn.com/2022/10/22/business/boeing-737-max-crime-victims/index.html

Picardo, E. (2022, October 12). *Employee Stock Options (ESOs): A Complete Guide*. Corporate Finance Institute. https://www.investopedia.com/terms/e/eso.asp

Posner, C. (2019, August 22). *So Long to Shareholder Primacy*. Harvard Law School. https://corpgov.law.harvard.edu/2019/08/22/so-long-to-shareholder-primacy/

Recent Study Reveals More Than a Third of Global Consumers Are Willing to Pay More for Sustainability as Demand Grows for Environmentally-Friendly Alternatives. (2021, October 14). BusinessWire. https://www.businesswire.com/news/home/20211014005090/en/Recent-Study-Reveals-More-Than-a-Third-of-Global-Consumers-Are-Willing-to-Pay-More-for-Sustainability-as-Demand-Grows-for-Environmentally-Friendly-Alternatives

Reducing Environmental Impact Is Now A Business Imperative. (2020, January 22). Forbes. https://www.forbes.com/sites/deloitte/2020/01/22/reducing-environmental-impact-is-now-a-business-imperative/?sh=78eea2766cc6

Robison, P. (2019, May 9). *Former Boeing Engineers Say Relentless Cost-Cutting Sacrificed Safety*. Bloomberg. https://www.bloomberg.com/news/features/2019-05-09/former-boeing-engineers-say-relentless-cost-cutting-sacrificed-safety

Serafeim, G., & Yoon, A. (2021, August 2). *Does Positive ESG News Help a Company's Stock Price?* Kellogg School of Management at Northwestern University. https://insight.kellogg.northwestern.edu/article/esg-news-market-reaction

Sethi, B., Brown, P., & Zhao, Y. (2022, October 31). *Younger workers want training, flexibility, and transparency*. Strategy&. https://www.strategy-business.com/article/Younger-workers-want-training-flexibility-and-transparency

Upskilling, career growth and job security among top expectations of young workers, new survey finds. (2022, May 24). Nestle. https://www.nestle.com/media/news/career-growth-security-young-workers-study

Wigert, B., & White, J. (2022, September 14). *The Advantages and Challenges of Hybrid Work*. Gallup. https://www.gallup.com/workplace/398135/advantages-challenges-hybrid-work.aspx