Boards of Directors and Corporate Strategy in an Uncertain Context

2021 IESE-ECGI Corporate Governance Conference

October 4-5, 2021

Prepared by **Giacomo Marchesini** and **Alexis Yong**
(PhD candidates, IESE Business School)

Organizers:

Center for Corporate Governance

european corporate governance institute

Sponsored by:

Social Trends Institute

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Introduction

Corporate strategy is considered to be a central driver of a firm's long-term orientation and a key influencer in corporate financial performance. Corporate governance suggests that boards of directors have the duty to govern a firm and help develop it sustainably for the long term. Hence, boards are supposed to discuss corporate strategy and make relevant decisions in that regard. More recently, large institutional investors such as BlackRock, State Street and Vanguard, among others, have explained that they expect boards of directors to understand and discuss business strategy with their CEOs. Boards need to make sure that strategy and strategic decisions will help the company create sustainable economic value. This perspective offered by asset managers today is consistent with what leading families in business, private equity and venture capital firms have been doing over the past two decades. As investors sitting on boards of directors, they are very active in working on strategy with the CEOs of the firms in which they invest. Boards' work on corporate strategy can have a profound impact on companies.

A good corporate strategy will help companies face their overall responsibilities, invest for the long term, create jobs, develop innovative products and services, and make an overall positive impact on society. Boards face a complex task when dealing with strategy. The board of directors must have an in-depth understanding of the company's businesses and sectors, as well as the main issues involved in complex strategic decisions, such as digital transformation, decarbonization, acquisitions, mergers, spin-offs and corporate restructuring. The core issue of a specific strategic decision—such as a strategic investment, acquisition, or merger—is very important and requires specific knowledge and skills. Some areas involve not one, but a sequence of strategic decisions, which may involve adopting a notion of purpose for the firm, leading a corporate transformation, shaping the firm's culture, or committing to a sustainable business model. Finally, the context and process by which the board makes the final strategic decision are also highly relevant and may influence the outcome of the decision.

Introduction

There are many forces shaping this process, such as board dynamics, the tone at the top, the interaction between the board and the CEO, relations between the board and key shareholders or among the different board members. The responsibility of the boards of directors for strategy and strategic decisions is clear. The degree of strategic uncertainties faced by companies and their boards is also on the increase. In this context, boards need to develop and implement a series of criteria and frameworks to tackle those strategic challenges and make decisions, especially in contexts of high uncertainty. They should also be organized to make this type of decision. In the first place, they need to understand strategy. In the second, they need to develop certain skills, such as discussing strategy and strategic decisions, following up on the execution of these decisions and monitoring senior management. They need to learn how to work on strategy with the CEO and top management. Thus, boards need to develop strategic decision-making skills.

Conference Agenda

The conference took place on two separate days, Monday October 4th and Tuesday October 5th 2021. The IESE-ECGI corporate governance conference series traditionally blends theory and practice, a combination that is primarily reflected in the structure of the sessions. There were three purely academic sessions, three completely practitioner-oriented sessions and two sessions with a mixture of academics and practitioners.

Monday, October 4, 2021

WELCOME AND CONFERENCE INTRODUCTION

- **Marco Becht**, ECGI and Université libre de Bruxelles
- **Jordi Canals**, IESE Business School
- **Carlos Cavallé**, Social Trends Institute, President
- **Franz Heukamp**, IESE Business School, Dean

SESSION 1

Boards, Activist Investors and Strategic Decision-Making

- **Margarethe F. Wiersema**, University of California, Irvine
- *Discussant:* **Gaizka Ormazabal**, IESE Business School
- *Chair:* **Colin Mayer**, University of Oxford

SESSION 2

Distinguished Lecture: Corporate Governance, Boards of Directors and Corporate Strategy

- **Bengt Holmstrom**, MIT Professor and Nobel Laureate in Economics
- *Discussant:* **Sophie L' Helias**, LeaderXXchange, President
- *Chair:* **Marta Elvira**, IESE Business School

SESSION 3

Sustainability Strategy

- **Ioannis Ioannou**, London Business School
- *Discussant:* **Fabrizio Ferraro**, IESE Business School
- *Chair:* **Pascual Berrone**, IESE Business School

SESSION 4

CEO Roundtable: Boards of Directors and Corporate Strategy

- **Denise Kingsmill**, Inditex, Board Member
- **Tobías Martínez**, Cellnex, CEO
- **Risto Siilasmaa**, Investor and former Chairman of Nokia
- *Moderator:* **Jordi Canals**, IESE Business School

WRAP-UP

- **Marco Becht**, ECGI and Université libre de Bruxelles
- **Jordi Canals**, IESE Business School

The first day of the conference presented a set of interesting empirical findings, which illustrate the broad picture of novel topics on boards of directors and corporate governance. Session 1 on Boards, Activist Investors and Strategic Decision-Making was presented by Professor Margarethe F. Wiersema (University of California, Irvine) who showed a summary of her research on activist investors, and was discussed by Professors Colin Mayer (University of Oxford) and Gaizka Ormazabal (IESE Business School). Session 2, The Distinguished Lecture on Corporate Governance, Board of Directors and Corporate Strategy, followed, in which Nobel Laureate in Economics Professor Bengt Holmstrom (MIT) discussed the future risk of corporate strategy, with especial emphasis on the impact of digitalization and platforms. Comments were presented by Sophie L'Helias (President of LeaderXXchange) and Professor Marta Elvira (IESE Business School). Next, in Session 3 on Sustainability Strategy, Professors Ioannis Ioannou (London Business School), Fabrizio Ferraro (IESE Business School) and Pascual Berrone (IESE Business School) discussed interesting findings on sustainable actions and imitation dynamics. Finally, in Session 4, CEO Roundtable, Professor Jordi Canals (IESE Business School) chaired the CEO Roundtable, with participation from Denise Kingsmill (Board member of Inditex), Tobias Martinez (CEO of Cellnex) and Risto Siilasmaa (investor and former Chairman of Nokia).

Conference Agenda

Tuesday, October 5, 2021

INTRODUCTION - DAY 2

- **Marco Becht**, ECGI and Université libre de Bruxelles
- **Jordi Canals**, IESE Business School

SESSION 5

Boards of Directors and Governance during the Pandemic

- **Renée Adams**, University of Oxford
- *Discussant:* **Francisco Reynés**, Naturgy, Chairman
- *Chair:* **Mireia Giné**, IESE Business School

SESSION 6

Strategy, Sustainability and Transformation: A Dialogue

- **Jean-Pascal Tricoire**, Schneider Electric, Chairman
- *Moderator:* **Jordi Canals**, IESE Business School

SESSION 7

Boards and Strategy: Managing Conflicts Among Stakeholders

- **Jay B. Barney**, University of Utah
- *Discussant:* **Joan Enric Ricart**, IESE Business School
- *Chair:* **Africa Ariño**, IESE Business School

SESSION 8

CEO Roundtable: Strategy and Sustainability. A Board Perspective

- **Sophie L' Helias,** LeaderXXchange, President
- **Juvencio Maeztu**, Ingka Ikea, Deputy CEO and CFO
- *Moderator:* **Jordi Gual**, IESE Business School

WRAP-UP

- **Marco Becht**, ECGI and Université libre de Bruxelles
- **Jordi Canals**, IESE Business School

On the second day, the discussion centered on the role of boards in dealing with crises, managing different stakeholders, and pursuing and embracing sustainable business models. In Session 5, Boards of Directors and Governance during the Pandemic, Professor Renee Adams (University of Oxford), together with Francisco Reynes (Chairman and CEO of Naturgy), discussed how the board of directors as a team can lead companies through turbulent times and necessary transformations in times of disruptive change. In Session 6 Strategy, Sustainability and Transformation, Jean-Pascal Tricoire (Chairman and CEO of Schneider Electric) shared the compelling story of how his company has been implementing three critical transformations—sustainability, digitalization and globalization—and the board's role during these processes. For Session 7, Boards and Strategy Managing Conflicts Among Stakeholders, Professors Jay Barney (University of Utah) and Joan Enric Ricart (IESE Business School) delved into the dilemma of how boards can manage the variability of stakeholders, dealing with sometimes contrasting requests. Finally, in Session 8, CEO Roundtable, Sophie L'Helias and Juvencio Maeztu (deputy CEO and CFO of Ingka IKEA) explored the challenges that companies face in embracing a sustainable transition.

At the end of each day of the conference, Professor Marco Becht (Université libre de Bruxelles and ECGI) summarized the main contributions and takeaways emerging from all conference sessions.

The 2021 IESE-ECGI Corporate Governance Conference discussed the aforementioned issues from the specific perspective of the board of directors as the top decision-making body of the company as well as findings from the research of leading scholars in the fields of corporate strategy, corporate finance, and organizational economics. Over 100 people attended the conference on campus, with 1,500 participating remotely.

SESSION 1

Boards, Activist Investors and Strategic Decision-Making

Margarethe F. Wiersema,
University of California, Irvine

Discussant: **Gaizka Ormazabal**,
IESE Business School

Chair: **Colin Mayer**,
University of Oxford

INTRODUCTION

Activist investors have become a major concern for boards, as their campaigns have shown to have major implications for companies' strategic decision making. Margarethe F. Wiersema, Professor of Strategic Management at The Paul Merage School of Business, University of California Irvine, Colin Mayer, Professor at Saïd Business School, University of Oxford, as chair of the session, and Gaizka Ormazabal, Professor of Accounting at IESE Business School, as discussant, present and discuss the latest research on this novel and interesting phenomenon.

Presentation (**Margarethe Wiersema**, University of California, Irvine)

Hedge fund activism, although initially a US phenomenon, is now global as activist investors are finding investment opportunities across the globe. Hedge fund activism represents one of the biggest challenges facing firms and boards.

Like other institutional investors, Activist Hedge Funds are sophisticated financial organizations that manage a portfolio of investments. But unlike other institutional investors, a hedge fund portfolio does not need to be diversified, and fund managers typically put their own wealth into the fund. A particular characteristic of hedge funds is the nature of the compensation: 2% management fee and 20% of the overall excess return of the fund. Over the past two decades, hedge funds have seen immense growth, consistently outperforming the market. For this reason, many pension funds and other institutional investors have been attracted to these types of investments and have put their money into hedge funds as part of their overall diversification strategy.

Activist Hedge Funds comprise a small fraction of the hedge fund sector (around 5%). Activist Hedge Funds are not passive investors, but instead seek to "actively" engage with the firms they take a stake in to enhance shareholder value. Activist investors typically perform extensive due diligence before targeting a firm, which is reported in "white papers". In their campaigns, activist investors issue demands to improve shareholder value. There demands may include selling the company, divesting business units or breaking up the company, scuttling a merger, as well as financial demands such as share buybacks or issuing dividends. In addition, they often ask for board seats. Evidence shows that activist hedge funds tend to be successful, with settlements being reached 66% of the time.

Professor Wiersema's research presents a framework for understanding the context of activist campaigns and the various constituents involved. The initiation of an activist campaign creates uncertainty for the targeted firm. Management and the board must decide whether to negotiate with the activist investor and how best to respond to the activist's demands. There is considerable uncertainty as to the validity and merits of the activist investor's demands and whether they will enhance shareholder value, as suggested. Professor Wiersema in her paper published in the Strategic Management Journal finds that boards and management respond to activist campaigns based on the reputation of the activist investor. Activists that have a reputation for being hostile, based on engaging in proxy fights in their early campaigns, are more successful in their campaigns. This may be a defensive response on the part of the firm in order to avoid the potential adverse consequences of a hostile campaign.

Prof. Wiersema also examines the consequences of activist campaigns on CEO dismissal and finds that certain factors increase the likelihood that the CEO of a firm targeted by activist investors is likely to be fired. Her research also examines what happens when activist investors gain board representation. Demand for a board seat is the number one activist demand and they have gained significant board representation. Once on the board, an activist appointed director can influence other board members since they are likely to be equipped with research conducted by the activist investor and thus are knowledgeable.

In summary, the phenomenon of hedge fund activism is a wake-up call for boards. Activists initiate campaigns against firms where boards tend to be complacent. In this sense, Professor Wiersema recommended that to avoid being targeted by activist investors, that boards be more proactive regarding corporate strategy. There may be serious concerns with regard to governance and strategy, especially in the case of boards of directors that are not looking after stakeholders' interests. One suggestion from Professor Wiersema when it comes to improving adaptation and preparing for the appearance of an activist investor is to examine the company from the activist perspective, and asking "hard questions" regarding the firm's business portfolio. As a final message, boards must be more proactive in setting corporate strategy.

Discussion (**Colin Mayer**, University of Oxford)

Professor Wiersema's central argument throughout her papers is that management academics need to pay greater attention to activist hedge funds, which hitherto have remained primarily in the domain of law and finance scholars. Both areas offer a complimentary perspective on the subject of the market for corporate control in both its main guises: hostile takeovers and hedge fund activism. From the point of view of management theory, the discussion focuses on topics such as strategy, culture integration and due diligence. From the point of view of law and finance, there are discussions of asset management, valuation and regulation. The former is really about how to realize the objective of the corporation through strategy formulation and implementation, while the latter is about maximizing the value of the corporation, subject to the rules of the game. As long as the objective of the firm is to maximize shareholder value, then the two are essentially mirror images of one another. However, when the objectives of the shareholders change, the strategy implementation carried out by management and what is expected by global capital markets may diverge rather than converge. This confrontation of objectives among different groups of shareholders can lead to tensions that might lead to activist campaigns.

In this sense, Professor Wiersema's paper on the role of reputation argues that the greatest success of confrontation engagements by aggressive activists may reflect target management's unwillingness to accept the adverse reputational consequences that come from resisting aggressive activists. This may be context-sensitive and culturally dependent. For example, a number of other authors have collected evidence on Japanese activism, which suggests that in many cases, quieter constructivism may be more successful than high-profile confrontation. In another paper by Professor Wiersema, she argues that hedge fund activism can be a source of enhanced efficiency and financial value by addressing agency problems and aligning the interests of management for shareholders. However, she also acknowledges that it can be a cause of conflict between controlling and other stockholders, between short- and long-term value creation, and between shareholders and other stakeholders.

Recently, there have been several pertinent instances of this: most notably, the intervention of the two hedge fund activists Artisan & Partners and Bluebell Capital Partners in the case of the French company Danone, forcing the move of CEO Emmanuel Faber from the position of chair and then his removal altogether. This is regarded by some as an indicative of the conflict between activism and the corporate purpose beyond short-term shareholder value maximization. To others, it is simply a reflection of stock market underperformance by Danone of 40% over the previous five years, relative to its peers. Neither Bluebell nor Artisan appear to be activist hedge funds in search of short-term gains at the expense of long-term profits. Both are signatories to the principles of responsible investment; both emphasize sustainability and commitment to long-term investing. Bluebell states: "As active long-term investors, we are naturally focused on material environmental, social and governance (ESG) factors which can impact the performance of the companies in which we invest and the responsible stewardship of our investments."

In contrast, and against all the odds, the little activist fund Engine N1 was able to overturn the mighty Exxon Mobil with just a $40 million stake, representing less than 0.02% of Exxon Mobil's value. It successfully elected three new members of the board, arguing that it would serve "to better position the company for long-term sustainable value creation." In other words, Exxon Mobil's predisposition to fossil fuels was not only damaging for the environment, but also for the company's long-term financial performance and resilience. This brings out an important point, which is the change in activism. Since the success of activist campaigns is dependent on the support of other institutional investors, the activist's objectives must be consistent with those of the rest of the investment community. As investors embrace ESG factors, so too must activists. Indeed, new activist funds are emerging, such as Jeff Ubben and Lynn Forrester de Rothschilds' Inclusive Capital Partners, which explicitly seek to promote a greater focus on inclusion and sustainability in corporate objectives.

All this would seem to help align the management and finance perspectives on activism. However, it is important to recognize the limitations of this. Even if investors and activists universally adopt "enlightened shareholder value" and recognize the importance of stakeholder interest and long-term value creation, that does not resolve the divide between management and law and finance perspectives on activism. It is still shareholder primacy disguised in stakeholder theory claims. It pushes the recognition of other party interests only insofar as they contribute to shareholder value creation. Then, and only then, will activists intervene where stakeholder interests diverge from those of shareholders in relation, for example, to the environment; then it is shareholder interests that will prevail.

The success of the Engine N1 campaign was based not on concerns about climate change per se, but the consequences of it for the financial performance and resilience of Exxon Mobil shares. Hedge funds' understanding of the term activism remains very different from that of NGOs, environmentalists and social campaigners. But so long as it is investors who retain authority over the appointment, removal and remuneration of directors, it is almost certain that management will mean little more than money. Management that seeks to go beyond that by addressing global problems can expect to enjoy the rot of even the most enlightened activists. In this sense, Professor Wiersema's thesis on the significance of activism for management, as well as for finance academics, will remain profoundly important.

Discussion (**Gaizka Ormazabal**, IESE Business School)
Hedge fund activism in on the rise and here to stay. Although it is controversial, it has several advocates because it leads to improvements in the target firm's governance and efficiency. Pressure on management to improve operations and performance can have a positive effect on the firm's value. Most negative arguments are related to controversial practices such as insider trading, "wolf pack" attacks, and short selling and derivative contract control through "empty voting" and "hidden ownership." The hedge fund activism phenomenon arose in the early 2000s as a convergence of several factors: on the one hand, improved methods in efficiency in the allocation of resources from the finance industry. Starting in the late 1970s and throughout the 1980s, hostile takeovers were a common method of reorganizing large enterprises and extracting abnormal returns from a more efficient allocation of resources. Something similar happened with the wave of activism of institutional investors in the 1990s. However, the latter was not so effective, since institutional investors tend to be well diversified and, therefore, lacked the incentives to monitor the ongoing investments. In this sense, there was a perceived opportunity to drive value through activism as staggered boards declined, proxy advisors' power increased, and proxy contests and proxy access costs dropped because of deregulation. All of this empowered investors and made hedge fund activism easier through the support of institutional investors.

Along those lines, with the announcement of an activist campaign, the stock market reaction of targeted firms tends to improve, signaling a beneficial effect for shareholder wealth. These abnormal returns come from acquisitions, as activists play an important role in monitoring M&As. Nevertheless, this return pattern is not unique to hedge funds. Other investors taking a position in the firm, including financial institutions, insiders and other investors with more than 10% of shares exhibit the same distribution of returns. This pattern may reflect a general effect for blockholders, agents that have a strong incentive to monitor the firm and have a medium-/long-term investment perspective. Moreover, this pattern is not only a US phenomenon since it is reflected in Asia, in Europe and across North America. Some other potential benefits to activism not captured by firm value are related to the disciplining effect on related firms, the governance role on managers and employees, and the disciplining effect on other stakeholders through the restructuring of previous supplier and client relationships. Evidence also shows that hedge funds usually dispose of their shares within one year. During this time, investment decreases, especially in R&D, but there is an observed increase in innovation. This could signal the decrease in overinvestment as activists push towards more efficient levels of investment. In this vein, it seems that returns for shareholders happen at the expense of other stakeholders. Following the announcement of an activist campaign, debt holders see a decrease in the bond returns, employees experience greater underfunding and firms exhibit greater tax avoidance. This evidence signals a redistribution effect among the target firm's stakeholders, with a clear negative effect on other stakeholders in relation to current shareholders.

In summary, hedge fund activism exerts a positive effect on shareholder wealth, at least in the short term. Although this effect is concentrated in a small number of firms and is connected to specific tactics, a clear strategy in wealth redistribution can be observed. Long-term consequences are still inconclusive as it is difficult to establish causality relationships in the long term.

SESSION 2

Distinguished Lecture: Corporate Governance, Boards of Directors and Corporate Strategy

Bengt Holmstrom,
MIT Professor and Nobel Laureate in Economics

Discussant: **Sophie L' Helias**,
LeaderXXchange, President

Chair: **Marta Elvira**,
IESE Business School

INTRODUCTION

The distinguished lecture presented by Bengt Holmstrom, Emeritus Paul A. Samuelson Professor of Economics at MIT and Nobel Laureate in Economics, examined the role of corporate governance in the formulation of the corporate strategy by board members. Special emphasis was placed on the major changes in the strategy landscape and challenges that lay in the future. The discussion was led by the chair, Marta Elvira, Professor of Strategic Management and Managing People in Organizations, IESE Business School; and Sophie L'Helias, President at LeaderXXchange, who discussed the main points of professor Holmstrom's lecture and related it to the way board, management and investors interact with each other.

Presentation (**Bengt Holmstrom**, MIT and Nobel Laureate in Economics)

Corporate governance is an extremely important topic, not only for academics but for society as a whole, as it involves what corporations should and should not do. There is also a historical view of the evolution of corporate governance throughout the 1980s and 1990s with the popularity of hostile takeovers as a way to break things down and move the market to get into new opportunities. There was also an economic purpose behind it: the reallocation of resources. However, there are differences between Europe and the US in what regards resource allocation. In Europe, the reallocation of resources happens through inter-industry migration. Nokia is a good example as they started off with rubber boots and ended up with mobile phones. Europe is much more tolerant; it doesn't have the market mechanism of the US. Although the market mechanism allows for experimentation with new organizational forms, this process has also led to scandals, like the ones we observed in the 2000s. Looking ahead of the game, we see the opportunities that digitalization is presenting to us today—and digital platforms in particular, constituting as they do a major discontinuity, a major change in the strategic landscape. The appearance of platforms in the competitive landscape is a disruption for companies that boards should take into consideration.

Current technological developments suggest that the future of corporate strategy and an efficient allocation of resources will come in relation to platforms. At its core, corporate strategy is about coordination among different agents to organize the reallocation of resources, and this process will be challenged by platforms. Platforms generate enormous social value, which, given today's market structure, is captured by just a few players. Data and digital tools are the most important resources. Many things are changing as a result, such as the conceptualization of the proximity of industries, which will make it more difficult to identify a company's closest competitor.

One particular characteristic of data is that it is non-rival. The supply of data is not affected by its use, in the sense that data can be used several times without fear of its depletion. Moreover, the marginal costs of spreading information have come down to zero, reducing distances and enhancing connectivity. This has opened up opportunities in isolated regions and geographical areas whose populations lacked access to certain kinds of services that were only typically available given close contact. Another characteristic that generates a huge benefit is the scalability of platforms, as it can be leveraged by many different technologies. We are beginning to see the intersection of artificial intelligence (AI), blockchain, and cloud computing, which allows platforms to achieve new scalability as more people are able to use their assets. In the end, it is the platforms' participants who generate value.

The success of platforms depends on the replacement of inefficient intermediaries. Algorithms are becoming the new middlemen, and information the new collateral. What does this imply for board members and corporate strategy? First, boards need to pay more attention to strategy. Second, there is a trend of opening up, giving other platform participants access to tools, data and resources. Wherever the flow and generation of data is involved, AI plays a critical role.

In summary, boards need to adapt and adopt a massive mindset. It is important to get everybody on board and, in that regard, it is crucial to pay attention to the human side. Most threats to a company's business will come from outside their current industry, and most likely they will come from the digital side in a platform ecosystem. There is a trend towards opening up, providing access to data and tools so that users can complement the assets they provide and generate value. It is essential to really understand these innovations.

Discussion (**Sophie L'Helias**, President of LeaderXXChange)

The availability and ease of access to information today is the basis of a social tsunami. It puts pressure on boards of directors and investors to change their mindset. In particular, it requires the capacity to gather insights to enhance decision making and the ability to provide tools that people can use to invest. In this regard, three ideas arise:

The first is the notion of strategy, the board, and how to engage with management. On the corporate side, this implies alignment of skills. Talking about corporate strategy is not a question of a single-session conversation; rather, there needs to be an iterative process until the idea can be communicated internally and externally. At root is the purpose; then the strategy follows, and next it will be deployed throughout the organization and with external partners. The next question is whether the board has the right skills, not only for now but also for the future. You might want to upscale your board—maybe find some external partners that can support you, as sparring partners who can help to polish the strategy. This whole idea that strategy is just something up there, very esoteric, is very distant from the operational strategy we need. Today, markets want to see three drivers in sustainable business models: governance, environmental, social, and financial factors, since they will guide everything to be deployed.

The second idea has to do with how management engages with investors, financial partners and the broader investor community. The latest technological developments have accelerated interaction among different stakeholders. The availability of information is a major change in the landscape. It is imperative to give investors the information they are looking for, because otherwise they will find it elsewhere. They will then be building an analysis or an understanding of the company's strategy with information not provided by the company. That creates a gap and, in turn, uncertainty, which is inconsistent with building trust over the long term. And trust is not formed in engagements based solely on financial considerations; it is built on the transmission of information that offers a broader and deeper understanding of the culture of both the company and its board. The more you share, the more they understand how you operate and how you engage with the board. This builds trust.

Finally, there is the idea of how the board engages with investors. In the past, the relationship was generally focused on compensation issues, as that was the main interest of investors. Today there has been a major shift in the discussion at the board level, touching on diversity, the environment and other ESG issues. This has been amplified by COVID-19. The board no longer does basic oversight; the new context demands that directors understand the company and the strategy. Questions from investors may be very specific, aimed at finding out whether the board is engaging in enough oversight on certain issues. In this evolving context, we are seeing a change of mindset, not just with the competition, but also with investors. It affects employees, who are expecting major changes in how companies operate, their engagement and the promises they make for the future. It is also changing for society. So, clearly, the role of the board of directors is not changing, but its involvement is. This requires a change in mindset and the inclusion of employees and society in the decision making. As the board represents a diverse group of investors, it is its duty to engage in oversight, define the topics to be discussed, and follow up in terms of accountability.

SESSION 3

Sustainability Strategy

Ioannis Ioannou,
London Business School

Discussant: **Fabrizio Ferraro**,
IESE Business School

Chair: **Pascual Berrone**,
IESE Business School

INTRODUCTION

Can sustainability-based differentiation strategies help maintain competitive advantage? In this session on Sustainability Strategy, Ioannis Ioannou, Associate Professor at London Business School (LBS), presented novel findings on how unique sustainability actions are positively correlated with firms' performance. Although firms operate in an environment with strong imitation forces, unique sustainable actions can enhance a firm's competitiveness. The discussion was led by the chair Pascual Berrone, Professor of Professor of Strategic Management and holder of the Schneider Electric Chair of Sustainability and Business Strategy at IESE Business School, and Fabrizio Ferraro, Professor and Head of the Strategic Management Department at IESE Business School, who discussed the main points and caveats of Professor Ioannou's research. Special emphasis was placed on the contributions to the strategic management literature and the managerial implications of corporate sustainability as key elements in a firm's competitive advantage.

Presentation (**Ioannis Ioannou**, London Business School)

In recent years, sustainability actions have become an important element of a company's strategy, as they try to address different stakeholder expectations regarding environmental, social and governance (ESG) criteria, which help them to build a differentiation advantage over their competition. However, if that advantage is profitable, competitors will be likely to imitate it, thereby reducing the initial advantage, as well as the profits, of the pioneer.

Previous studies have found that value creation can be materialized through different channels associated with sustainability-based differentiation, such as: superior access to finance, more and better innovation outcomes, enhanced access to human capital and employee engagement, improved reputation and increased sales, favorable access to international markets, employee and customer satisfaction, and pre-emption of regulatory intervention.

Although this body of research brings to light evidence that companies can establish a competitive advantage through sustainability, the literature has not explored the conditions under which companies are able to maintain such an advantage—in particular, when faced with imitation pressures: for example, which actions are most likely to diffuse via imitation, and which are more valuable in the long term. The analysis of these questions can provide a deeper understanding of the variety of sustainability actions in a given industry, with special emphasis on the ones that exhibit persistent performance.

The adoption of sustainability actions can be understood in two ways, which describe the tension in the dynamics of imitation. First, sustainability can be viewed as a "common practice", an investment necessary to achieve the same production structure as industry peers. In this sense, the imitation of a practice is likely to eliminate unique attributes and differentiation, and to homogenize profits. Second, sustainability actions can be used to position a company in an unexploited market position. Some sustainability measures can be part of a unique and difficult-to-imitate strategy that can lead to successful differentiation which is difficult for competitors to match. High levels of variation across industries can lead to different market responses, since a particular sustainability action may have different results in different industries.

The study being presented uses data from the MSCI ESG Ratings from 2012–2019, taking into consideration 2,095 firms. The MSCI ESG data has the purpose of helping investors understand ESG risks and opportunities by providing a quantitative assessment of experts' opinions on 37 key ESG issues in 10 macro themes: climate change, natural capital, pollution and waste, environmental opportunities, human capital, product liability, stakeholder opposition, social opportunities, corporate governance, and corporate behavior. The MSCI aggregates information based on materiality taking into consideration company-specific actions, with macro data relevant to a company's geographies of operation and business segments.

The study has three main findings: first, that in most industries, there is intra-industry convergence, meaning that firms undertake an increasing set of sustainability actions during the sample period. In particular, the rate of convergence in a given industry is associated with the relative importance of environmental and social issues relative to governance and the level of stakeholder scrutiny that the industry is facing. The higher the level of social scrutiny, determined by the tone and volume of coverage in the media, the higher the rate of convergence. Second, sustainability practices are replicated in environments of low regulatory uncertainty. Third, novel sustainability actions are less likely to be imitated, as they require higher corporate capabilities. Finally, such unique sustainability actions are associated with higher performance and market valuations, while common sustainability actions are not associated with any key performance measurement.

In summary, the study asks: Under what conditions are companies able to maintain their sustainability-based differentiation advantage when faced with imitation pressure from industry peers? The main findings suggest that: (1) imitation happens, given that we observe an intra-industry convergence; (2) sustainability actions diffuse rapidly via imitation; and (3) there is a significant inter-industry heterogeneity in the rate of convergence.

Discussion (**Fabrizio Ferraro**, IESE Business School)

This paper provides important empirical insights that help us to move beyond the “doing good, doing well” fallacy that has plagued the field of sustainability and ESG in recent decades. The empirical results help us understand that sustainability actions face trade-offs. The key in this study is to understand under what conditions strategic decisions on sustainability actions can be brought together to be effective in a competitive strategy.

The article presents very interesting results. First, it shows a rapid intra-industry convergence of sustainability actions. Second, inter-industry heterogeneity is driven by the materiality of environmental and social issues and the level and tone of stakeholder attention. Third, sustainability practices in areas driven by regulation are more likely to be imitated, while higher novelties are less likely to be imitated, which is very important for strategy. Finally, unique sustainability actions are associated with higher financial and accounting performance measures. These findings raise new questions concerning how we should think about firms’ sustainability actions.

Notwithstanding the important contributions to the strategic management literature, there are some unresolved questions. First, to an extent, we are inferring actions from ratings. Sustainability actions and practices are being inferred from ratings provided by firms, in which the categorization relies on opinions. In particular, rating agencies and companies considered the risk exposure in a given industry, which could be independent of what companies are doing. It would be more interesting to look at the risk on the management side. Moreover, there have been some experiences of rescoring in certain rating companies. The fact the past scores have been changed is not a major issue for the majority of investors, since most of them use the information in forward-looking way, but it could be a big problem for researchers, who rely heavily on historical records.

Another set of questions focuses on the drivers of sustainability actions. These actions can either be a strategic reaction to competitors or the result of pure pressure from regulations. The data shows some evidence that entire industry differences are being driven by the materiality of the category, as well as the level and tone of the stakeholders. For instance, one key driver during the examined period has been the role of the investor. The growth of ESG funds and the global number of PRI signatories in the last decade, in terms of investors and assets under management, is evidence of that. So maybe the reaction of the company is one of compliance following stakeholder pressure, rather than being really strategic, as the paper argues.

Finally, some implications for practice and policy regulation. Throughout this conference, it has been asserted that sustainability should be a board responsibility. However, that is not really the case in most companies. Moreover, the chief sustainability officer who oversees ESG actions typically does not report directly to the CEO. So it is not obvious how these issues can become strategic if they are analyzed ex-post. In a non-compliance approach, more focus should be put on material ESG issues to avoid the temptation of choosing convenient issues as material. Ultimately, there are some consequences for regulation and common sustainability practices, since the study finds that common sustainability practices, while not providing any competitive advantage, might nevertheless provide material benefits for the planet and society. So, it is a good exercise to identify those ESG areas where everyone is better off, by leveling the field and regulating them, so that firms do not have to worry about strategic actions coming from that direction and do not take part in the competitive game.

SESSION 4

CEO Roundtable: Boards of Directors and Corporate Strategy

Denise Kingsmill,
Inditex, Board Member

Tobías Martínez,
Cellnex, CEO

Risto Siilasmaa,
Investor and former
Chairman of Nokia

Moderator: **Jordi Canals**,
IESE Business School

INTRODUCTION

Taking part in the CEO Roundtable were Denise Kingsmill, Board Member at Inditex, Tobias Martinez, CEO at Cellnex, and Risto Siilasmaa, investor and former Chairman of Nokia. The session was moderated by Jordi Canals, professor of strategic management and holder of the Fundación IESE Chair in Corporate Governance. The discussion focused on the interaction between the board of directors and the management team, the role of trust in an organization, and a glance into the future by discussing which will be the most important issues for boards of directors over the next 5 years.

Roundtable Discussion

JORDI CANALS (JC): How can the board of directors become more effective in dealing with strategy and working with the CEO and the top management team on long-term strategy issues?

DENISE KINGSMILL (DK): The board of directors is there not to set the strategy, but to ensure that a sustainable strategy is set—to ensure that there is a strategy which is consistent with the long-term sustainability of the business. For this, the board must ensure that the right people are in office and that they have a clear understanding of sustainability, particularly in relation to their business. Once the objectives of the company are clear, the board should ensure that these are compatible with the overall aim of the company, which is to further the interests of shareholders and other stakeholders and ensure that the business does well. Because at the end of the day, you have to have a high-performing company that meets the needs of its shareholders, its people and, above all, the consumer. They are the ones who, ultimately, will ensure the long-term sustainability and economic logic of the company.

So what you have to do is to fulfill all the stakeholders' needs and recognize different requirements from every actor. We must recognize the different requirements of each of these stakeholders and find a way to communicate with them. It is important to be acutely aware of the different environments—political environment and legal environment—in which the company is working.

In summary, five ideas arise as key responsibilities of the board: to ensure that the strategy is set; that it is robust; that it meets the needs of the company itself; that it's sustainable; and that it is well thought out and appropriate for all the markets and all the challenges which the company faces now.

TOBIAS MARTINEZ (TB): There is no doubt that strategy is one of the main duties of the board of directors. However, the role of the board should be active. And active means that the board should interact with senior management and should set an iterative process, to confirm that the company is in the correct process. The interaction serves also to fine tune the current strategy and ensure that nothing is missing, whether that be a significant risk or a massive growth opportunity. This on-going conversation between management and the board should help to better understand the evolution of the context in which the company is about to operate, to understand, for instance, the impact of disruptive technologies or digital platforms.

The role of the board is to work as a team as part of the executive management, and the executive management's role is to trust the board. If we align objectives and understand the complexity, we can understand the disagreements. And if we understand the disagreements, at the end of the day, we can reach an agreement. This is especially important now that complexity is becoming ever greater, along with volatility and the number of variables. With no crystal ball at hand, we can only rely on interaction and trust to reach agreements at all levels in the firm. And to create trust, there must be full transparency.

RISTO SIILASMAA (RS): Three comments arise from my part: First, rebranding corporate governance; second, building common ground between researchers and practitioners in management science; and third, rethinking the continuity of the board and the value each member brings to the table.

First, we need to rebrand corporate governance. When I ask how entrepreneurs understand corporate governance, most of them answer that it is what they should do when they take the company public—basically, talking about ESG and compensation. The same goes for institutional investors, who also see corporate governance as no more than ESG and compensation, disconnected from the strategy of the firm. So, we should re-think corporate governance, what it really means, and how corporate governance fits into the overall corporate strategy.

Second, there is distance between top management and academic discoveries. CEOs don't read management journals. They ought to be more interested in management strategy journals, like doctors reading about novel developments in medical and scientific journals. Researchers and practitioners in management science don't really work together. In any other field, such as medical health and aerospace, doctors and engineers actually read science journals and find it hugely valuable. But CEOs don't read management science journals.

Finally, regarding the strategy of the board there is a challenge with continuity. We should stop for a moment to think about each board's principles. We should reevaluate those that the board really stands for and that define the way in which they do their job. For example, if the board is data driven, it would be interesting to see how many hours it spends discussing competition, strategy, technology or various functions. And we might then ponder whether this is the right split, considering the environment, competition and dynamics of the industry, and based on this evidence, critically rethink the value each board member brings to the discussion.

One interesting anecdote happened at Nokia in 2012, when we signed a strategic alliance with Microsoft. At some point, Microsoft announced that they would become a devices company, and that was a scary thought for Nokia. What if they became our competitor? What if they launch their own smartphones, and our main supplier became our competitor? So, we did some scenario planning. What if it did happen? How would we know in advance, what data might indicate that they were actually moving down that path, how might we act to prevent it right now? Not tomorrow, but today. Or if they moved down that path, how could we mitigate the worst consequences? What would happen if they did it? How could we react? To respond to this question, we established two subcommittees for the board—the Microsoft dynamics and the Industry Dynamics—and it was a wonderful experience with the management team.
And this idea connects with something previous speakers have talked about: trust. The relationship between the management team and the board has to be based on trust. And how do you build trust? You explain how you operate and then you will walk the talk. And you will work together, you'll spend time together. If you don't spend time together, you won't establish trust.

JC: Thank you very much for your insightful reflections and experiences. A common thread that is relevant for both the practice of the board of directors and for academic research is that interaction between the board and the top management team is indispensable. For this collaboration to work, there is the issue of trust, because, at the end of the day, both board and top management are groups of people who have to work together, trying to take the company to the next level. And this is something that doesn't happen spontaneously. So, I would like to ask how this relationship of trust can be built? And also, could you talk about the time allocation to some specific issues in the agenda of the board?

DK: There is nothing like a crisis to bring the board together. In some circumstances there can be tremendous splits, but in a good board that is prepared to face the crisis together and work as a team, it is something which builds trust. Take the example of the merger between Iberia and British Airways. There were two different boards of directors, people who had completely different viewpoints as to what corporate governance meant. And there was a crisis in the sense of making sense of the merger and making it work. And this space of working together, having dinners and lunches together, really generated an increase in familiarity and trust. In the end, people actually liked each other.

And I absolutely agree with the idea that strategy is an evolving issue. It is not only changing, but evolving. At each single board meeting there must be something that grows. And it is something you will be dealing with at every single board meeting. It will be very useful to be doing it off site as well, away from the traditional boardroom. Somewhere where you can relax together and talk constructively.

TM: Interaction is key. After COVID, this is quite difficult, but it is important to meet again in person. Trust is about individuals, behavior and tone. Earlier we saw that the tone of the activist investor is key to performance and the outcome of the campaign. We don't like it very much if you are questioning us like a teacher, trying to teach us by force. But if you feel that the tone is constructive, challenging, asking smart questions, then you can create an atmosphere of trust.

Regarding the technicality of the agenda, I think it is very important to set up planning for the full year in different structures of the agenda. There are some common items at every board meeting, but you have to be sure that you are covering the entire 360-degree view of the company over the whole year. It always helps to be humble, transparent with the rest of the board members and share your ideas with a good attitude. When this happens, it is easier to reach the objective. In a way, you have to be sensitive, because it is ultimately about individuals.

RS: Crises bring people together. To do this, you really have to spend time together as well. If you are isolated, then disagreements typically emerge. For example, we had a really tough situation at Nokia. We had been one of the most valuable companies in the world and the poster child for technology. And then, suddenly, we were in a situation where our revenues were dropping by 25–30% per year. We were deeply in the red. We had constant lay-offs—nearly 80,000 people in just a few years. The whole environment was very negative; it was just bad news all the time.

So how do you bring the team together so that it feels energized, united and has confidence in the future? The key tool for us was scenario planning. You identify the worst possible outcomes, but also the best possible ones. The worst-case scenarios are important in the sense that it takes fear away when you acknowledge the worst that could possibly happen. Then you plan what you can do to prevent that from happening. Or if it still happens, you plan how you should react and take action right away, or you look at ways to identify the track that you are taking as early as possible if the company is heading that way. And then, of course, there are the best-case scenarios. Those are the ones you want to happen, so you put more of your efforts there, but not exclusively.

All this process was a really intense experience that brought the management team and the board together. And I really felt that it was one of the best times in my time as CEO-chair because of the intensity the united feeling we had as a team.

QUESTIONS FROM THE PUBLIC (QP): In the case of Nokia, you had what we would call a burning platform—a situation which forced the board to get involved in major strategic decisions that ultimately support the survival of the company. So do you have any words of advice for companies that are not on a burning platform and what boards can do to be more engaged with the issue of strategy?

RS: I believe we are heading towards very complex times. And my definition of complexity here is a combination of things getting more complicated (large technology issues) and more unpredictable (surprises are becoming more common), while speed is increasing. So, the combination of unpredictability, complicatedness and speed creates a very difficult environment. And the challenge for traditional business or non-tech business is that it isn't enough to know your own business. You can't just train your board and your management team in your own industry. You need them to be knowledgeable enough about digital technology as well because the surprise might come from that direction. Or it might come from a very different direction, not even from digitalization. So you need to prepare for that, you need to have your ears open to contrarian thoughts from all sources and researchers.

QP: We have heard a lot about the interaction between the management and the board of directors in setting strategy. So, what is the role of open strategy, by which I mean involving other stakeholders, such as staff members, customers, suppliers and so on in helping to set the course for the company. Do any of the panelists use open strategy approaches or take into account the views of other stakeholders?

TM: Let me be disruptive on that. The ownership has to be clear. This is about a duty. It isn't an open responsibility. It is a board duty. It is a CEO and management duty. You have to take into consideration core shareholders, investors, analysts and stakeholders. When you ask for agreement on a subject you have to be very clear about the accountability. And strategy is a very attractive subject to talk about, to discuss, but then, in the end, nothing happens.

Again, the key issue is accountability. Every quarter you have to disclose information to the market, attract new investors and define new goals. You have to be accountable. If you don't perform well, you have to be fired. And we accept that responsibility, so we are accountable for it. If open strategy means that we have to integrate the opinions of stakeholders more, then I fully agree. But I think we have to be prudent.

DK: I disagree with that. I think that the formation of strategy is not something which takes place simply within the boardroom. I think that you have to be aware of what your people are thinking, because otherwise you are not going to get a strategy that is acceptable. You have to ensure that the people who work for you understand, and that they accept it and believe strongly that it works.

Certainly, in a number of industries as well, particularly in the fashion industry at the present, you have to take into account what the NGOs are thinking. They are a powerful influence. And they often have a point of view which is correct, and that you need to incorporate into your strategy. It is part of opening up your sense of strategic direction to those sorts of influences.

I think there is hardware and software; you have to take account of the legal and political environment in which you are operating, because if you don't, you will come up hard against huge difficulties as far as your strategy is concerned. In formulating your strategy, you have to take into account all of these viewpoints and be responsive to some of them to ensure that you do have a sustainable business.

RS: I strongly agree with both of you. I think we are experiencing

this strategy-elephant situation again, where one of us holding the elephant's foot in a dark room and the other one is holding the trunk and we are trying to describe the animal. One thing that we can be sure of is that strategy formulation is an iterative process. So, it requires us to have lots of discussions with lots of stakeholders, and every time we learn something new that will bring about a small shift in the course, and sometimes it will force us to recalculate a completely new course.

Regarding open strategy, I think it is a bit of a definition issue. If it's a question of the formulation of core objectives, that's something we don't necessarily talk about with suppliers. We may ask their opinion on a lot of things, and that may influence our core objectives, but we're talking about the actions. As far as how we move towards the chosen objectives, those are definitely things we discuss with our partners and we ask for their opinions and their support and help, since they may have much better ideas for us to implement. Collaborators can have a very good idea of how to implement a given strategy.

JC: Thank you! I would like to ask just one final question: What are the major concerns or most important themes that should be on the board of directors' agenda over the next five years?

DK: I think one of the most important themes is going to be the recognition of their contribution to global emissions. The reduction to net zero must be an objective of all boards. The climate issue is going to influence people more and more in the years to come. Second, I think, will be recognizing that boards need to be more diverse. There is still a majority of men, still a majority of white men sitting on boards, and even more, a majority of middle-aged white men sitting on boards. I think there needs to be an increasing amount of diversity in the boardroom.

RS: Let's first make sure that our children will have a world to live in. If we fail in that, nothing else really matters. One concept that

sorts of helps in this is to think about the net impact of the company we work for. So, it isn't only the negative things we cause in the world around us, but also the positive things that our products and services bring about. Actually, there is a very interesting business called Upright Project which has created a machine learning model that tries to calculate the net impact of all the businesses for which there is enough information and scientific research available on the Internet. So, please take a look at the project. Just google it; it's highly interesting. The second thing I want to talk about is complexity. It provides a huge opportunity for those that have the foresight or insight to understand something fundamental a little bit earlier than others. For example, in 2008 most of us knew enough about technology and could have predicted the birth of an industry that now has a turnover of US$350–400 billion a year, but which didn't exist at all just 12 years ago. This huge industry is the cloud services industry. Actually, the technology drivers for cloud services are, in hindsight, completely obvious, but I didn't think of them back then. But there is something like that happening right now as well. And, in hindsight, I am afraid that it will feel equally obvious. I hope that I, and all of us, will be smarter this time.

TM: I fully agree with my colleagues. Building on what they said earlier, I would try to be sure to include the concept of purpose. We are conveying it internally and externally. The company is not just about serving customers. It isn't just about providing value to shareholders. It is about society. The second issue is about people. It's about a team of people, because we are realizing more and more that the real competitive advantage has to do with people. It is our team—that is the real and non-replicable competitive advantage. We have to integrate younger people, to understand the new kind of jobs. As a company serving society, we need to emphasize those concerns.

JC: Thank you very much! Thank you so much for this process of sharing your experiences, your wisdom, your reflections on what makes a board of directors a truly effective organ of governance. We've looked at how to think holistically for the long term, how also to think in terms of the wider impact of a company on society, how to protect our investments in people, making sure that your own people are actually integrated, motivated and committed to taking the company to the next level. We should stop here. Thank you once more. Please join me in thanking them for their outstanding performance.

Wrap-Up

Marco Becht,
Université libre de Bruxelles and
ECGI

At the end of this first day of avid discussions on Boards of Directors and Corporate Strategy in an Uncertain Context, four lessons emerged. The first relates to the idea and definition of corporate governance as it relates to institutional design. Corporate governance originally meant the government of corporations, the delegation of power to somebody. Which is of course the main reason why we have boards. At an early stage it might not be important for a firm, but once it reaches a certain size, it will need a structure that delegates and makes decisions in a context of uncertainty. And this relates to the hedge fund activists, since they do the job of the board. First, they formulate strategy and present strategic demands to management. Second, they delegate responsibility by nominating people to the board of directors. The second lesson from Bengt's lecture is that platforms are the big disrupter. And this disruption entails an important contradiction: information is the new collateral. Which leads us to think of information in many other ways, even at an individual level. As Bengt pointed out, people should not own their own data. This is a complex statement since it is in complete contradiction to everything the European Parliament and the European Commission are doing. The third lesson of the day came from sustainability strategy. Now we are aware of what companies are doing and who they are listening to thanks to the MSCI ESG ratings. Although it is good to hear that firms are paying more attention to ESG factors, it is quiet problematic that big decision may be being made based on nothing more than the opinions reflected in the MSCI ESG ratings. Finally, the panel provided fascinating and important thoughts on the job boards must do. There is a reason why corporations delegate responsibilities to the board. It is not only a way to organize decision making in uncertain contexts, but also because boards think about things in a more fundamental way. As each industry and each market setting has very different challenges, boards have a role to play in understanding and reducing complexity.

SESSION 5

Boards of Directors and Governance during the Pandemic

Renée Adams,
University of Oxford

Discussant: **Francisco Reynés**,
Naturgy, Chairman

Chair: **Mireia Giné**,
IESE Business School

INTRODUCTION

COVID-19 has been an unexpected shock with massive implications that have accelerated multiple changes in businesses, including digitalization. The pandemic has forced some companies to lean into the transformation and embrace it. The crucial question becomes how boards of directors can lead through the turbulence and guide the needed transformations in times of disruptive change. Professor Renée Adams from Oxford University and Francisco Reynes, CEO and chair of Naturgy discuss these topics in a session moderated by Professor Mireia Giné of IESE Business School.

Presentation (**Renée Adams**, University of Oxford)

Professor Renée Adams from Oxford University is a specialist in board dynamics and the study of boards as a team. She is currently studying how boards of directors have behaved in response to the pandemic. During most crises, boards tend to suffer serious image problems. On the one hand, they are described as "pawns" and viewed as very passive. On the other hand, they are considered "potentates," extremely aggressive and in conflict with the CEO. As Professor Adams points out, these images arise because it is challenging to really observe boards' behavior and compile reliable data to study them. "It suggests that boards are passive, but they are not. It's just that we don't observe the action." To better understand how boards react to crises, Professor Adams investigated boards meetings of major UK when the pandemic crisis broke out. By collecting the publicly available transcripts of the board meetings and analyzing their contents, she and her colleagues were able to explore how the internal dynamics changed during moments of turbulence.

Since hospitals must disclose their board meetings on their websites, it is possible to observe attendance behavior and thus the level of independence of each meeting. Moreover, analyzing the text makes it possible to attribute the content to a particular speaker. What emerges from these analyses is that the pandemic crisis induced the average independence of board meetings to increase, since the average attendance of non-executive directors increased while the executives stopped attending. The reason for this is that the executives are clinical personnel, such as medical directors, chief nurses, etc. Given the extreme contingencies, their attention had to be focused on running hospital operations, so there was just not enough time to attend board meetings. Hence, the non-executive directors are the ones that take on crucial positions in the board during crisis moments. Moreover, measuring the board's oversight and questioning behavior by looking at the percentage of questioning words during each meeting leads to the observation that boards are more active but do

not oversee more. The main explanation seems to be related to the fact that they cannot engage in oversight because they do not have enough information, since executives are not showing up. On top of that, CEOs and chairs gain a greater voice. By counting all the words attributed to the CEO or chair, it is possible to observe an increase in their share of the discussion during the crisis. Interestingly, the study also finds that directors tend to speak less during online meetings.

In terms of performance implications, the study reveals that those hospitals where the attendance of executive directors is particularly low during the crisis are also the ones that present a better recovery, reverting more quickly to the pre-pandemic number of diagnostic tests. These results highlight the tension between managing operations and governing during a crisis. Overall, what emerges is that, in times of crisis, the best boards leave executives to do their job and begin listening more to the CEO and chair.

Discussion (**Francisco Reynés**, Chairman of Naturgy)

According to Francisco Reynes, CEO and chair of Naturgy, board directors should have a good understanding of the industry and its competitive dynamics. "Having sat on many different boards, argues the Chairman of Naturgy, my experience is that a board is like a family. The relationships depend on who the parents are, the children, the aunts and uncles and the grandparents. The attitude depends on how everyone feels about being engaged." Since boards are human, directors have to be understood with all their differences and peculiarities. "Independent directors should be chosen well." The selection and appointment of an independent board member, identifying the right person for the right board, is highly critical. "A person who has proven to be a leader on one board may fail on a different board if they don't share the objectives, vision, and strategy of that specific company," explains Francisco. The ability to react to a crisis should also reflect the peculiarities of each particular company and each team.

During the pandemic, boards had to deal with a unique situation without knowing how long it would last and what consequences it would bring. "We took a solid decision: board meetings once a week and executive committee once a day," says Francisco. Having frequent meetings at the beginning of a crisis, when the turbulence kicks in, is crucial to raising awareness of the uncertainty. Boards need to start gathering information while removing ambiguity as much as possible in an environment where circumstances change daily. Francisco explains that "in regular meetings boards supervise the strategy, but not during the pandemic. We could not know where we were going. The attention was devoted deeply to governance, finding ways to motivate employees, while monitoring receivables and investments." As the circumstances become clearer, and the uncertainty is reduced, the frequency of meetings should be progressively reduced in favor of efficiency.

Another important aspect is the commitment and involvement of board members during times of crisis. “Everyone has a very high level of commitment. No one avoided attending the board meetings, although attendance was not mandatory.” Francisco explains how boards need to be approached to allow them to contribute best. “If you want a board to just carry out the formal approval of the strategy, the thing to do is to send a large amount of paper. And after three or four hours, everyone will say ‘yes’ because no one will be able to understand the amount of information they have received.” However, Francisco believes that, to the extent that governance adds value to a company, and that the board members are the right ones for their roles, managers have to create the opportunity for the board to express its value. “Managers need to ask the right questions.” Board members have to be provoked, and to do so, the agenda has to be meant for discussion and not for presentations. The correct information needs to be provided on time, proposals should include clear decisions to be discussed, and everyone should be given time to say their piece.

Provided that the board members act as partners, the directors are the right persons, and the managers can provoke valuable discussion, then crisis moments can have positive repercussions for the board’s image. A crisis such as the pandemic can help a company to move quicker in directions that might have been difficult to imagine before. The consequence of this approach to crisis—together with complete transparency—is the improvement of how managers perceive boards. Again, according to Francisco, “Managers shouldn’t feel isolated in a crisis; they need to feel backed up by the ultimate decision-makers.” A board that is well perceived during a time of crisis can be crucial in helping to maintain the company’s values through the management team. Moreover, once the crisis passes, this leaves a legacy, “The board was there when needed,” concludes Francisco.

SESSION 6

Strategy, Sustainability and Transformation: A Dialogue

Jean-Pascal Tricoire,
Schneider Electric, Chairman

Moderator: **Jordi Canals**,
IESE Business School

INTRODUCTION

Jean-Pascal Tricoire, Chairman and CEO of Schneider Electric since 2006, interviewed by Professor Jordi Canals of IESE Business School. discusses the significant transformations that Schneider Electric has been conducting and the role of the board during these processes. Schneider Electric has been carrying out three critical changes. The first is the sustainability transformation, which is connected to and driven by the second: the digital transformation. Schneider Electric is leading an incredible effort to fight climate change and achieve zero emissions. The third necessary transformation addresses the disruption occurring in the global value chain and involves the shift from being an international company to a global one.

The Pillars of Schneider Electric's Transformation

JORDI CANALS (JC): I would like to start this conversation by asking you to reflect on how you engaged the Board in the very relevant transformation processes that you have been leading in Schneider Electric.

JEAN-PASCAL TRICOIRE (JPT): Schneider Electric's transformation is linked to and strongly dependent on a profound transformation of the board. It is important having well-defined governance with the right people to support and guide the transformation efforts. In every human activity, the most important thing is the choice of the people. The board of Schneider Electric became a fully global board, digitally informed and forward-thinking, with an in-depth understanding of the company's long-term objectives. The value added to the board of Schneider Electric is helping the executives put together a strategy for a successful transformation by bringing together different points of view. To achieve this, a board must be well informed, competent, cohesive, and passionate about the future of the company. Moreover, to improve the chances of success and reduce the risk of getting stuck and losing track of the transformation, it is necessary to create a solid alignment between the company, the managers, the board, and the stakeholders around the long-term vision and strategy. To accomplish this, in Schneider Electric we adopted a "multi-stakeholder responsibility perspective" by creating a stakeholder committee to check whether the company is fulfilling its mission while offering innovative ideas to contribute to different areas of society.

JC: I would like to ask you a little bit more on sustainability. Can you share with us some of the issues you encountered in pushing forward the ambitious sustainability objectives at Schneider Electric.

JPT: We believe that great people make a great company, and to have and attract the best people, you need a strong sustainability agenda. Opposing sustainable change is like swimming against the waves. Directors, chairs, or CEOs who don't support sustainable change put themselves in an uncomfortable position on their teams, at the risk of demotivating and losing valuable people. Even more importantly, the Schneider Electric industry is deeply related to sustainability. Therefore, Schneider Electric is in the position of leading the sustainable transition, adopting those critical technologies that are the game-changers: electrification and digitalization. While they were already leaders in electrification, they had to concentrate on a profound digital transformation. This started a long journey of acquisitions, driving Schneider Electric to eventually have 50% of its activities linked to digitalization, with a complete software portfolio for managing efficiency and sustainability. Sustainability is not a flower in the window; sustainability has to be embedded in your strategy. It is a marathon without a finish line.

As a result, sustainability is linked to performance. Jean-Pascal clarifies that "sustainability goes together with efficiency and savings. The payback of sustainability is like quitting smoking. It isn't just people's health that see a difference, it's also their pockets." However, to achieve this, it has to be a team effort. Companies must work together with all the actors in their supply chain. For instance, at Schneider Electric, 90% of the carbon footprint is with its suppliers. For this reason, they had to implicate their entire ecosystem in the change, becoming a role model, and guiding a much broader sustainable transition.

JC: Finally, I would like to ask you to reflect on the current geopolitical situation, the trade war and how these topics are discussed at board level.

JPT: The Western system no longer dominates the world. Other geographies are getting richer and entering the scene, contributing new and different value systems and worldviews. The vision of the future evolves from a thousand different perspectives. The crucial dynamic consists of the fact that, while the world will be more global, regions will be more different from one another. To embrace this new diverse system of values, Schneider Electric has adopted a board with a very international composition. To have a global company, you need a global board. They have engineered a mode of governance called a "multi-hub," in which every region must be embedded in the local ecosystem and stakeholders, with executive committees spread worldwide. It is great to have a diverse board to direct. If you pick the right people and you are interested in differences, it can become a unique place to create a network of knowledge.

SESSION 7

Boards and Strategy: Managing Conflicts Among Stakeholders

Jay B. Barney,
University of Utah

Discussant: **Joan Enric Ricart**,
IESE Business School

Chair: **Africa Ariño**,
IESE Business School

INTRODUCTION

A stakeholder perspective is an economically valuable approach that can guarantee companies' strategies to generate economic value. However, adopting a stakeholder-oriented perspective is not straightforward and gives rise to different problems: How does a board decide which actions to take? Jay Barney, Professor of Strategic Management at the University of Utah, and Joan Enric Ricart, Professor of Strategic Management at IESE Business School, try to navigate this dilemma. The session was moderated by Professor Africa Ariño of IESE Business School.

Presentation (**Jay Barney**, University of Utah)

The standard model of economic value generation, arguing about the existence of shareholder supremacy, has dominated board practice since at least the 1970s. According to this model, maximizing shareholders' wealth is supposed to be a company's only concern and objective. Thus, the purpose of the board is to ensure that the firm accomplishes this purpose. However, the standard model misses a crucial part of the story: understanding where this value comes from. Companies need to create opportunities for financial profit. They do so by assembling resources and capabilities from different sources. Stakeholders provide these resources and capabilities through co-specialized investment. The role of management is to facilitate these investments, generating more value than if they were kept separate. Profit generation is a "team sport": together, a team of co-specialized individuals can do things that a collection of non-specialized individuals cannot.

The problem stems from the fact that a "shareholder supremacy" model asks stakeholders to make co-specialized investments, exposing themselves to possible post-contractual opportunism, for the purpose of generating financial value that occurs for the exclusive benefit of shareholders. "Why would any rational stakeholder agree to make such co-specialized investments?" asks Jay Barney provocatively.

The ability to generate financial profits requires recognizing that stakeholders have to be compensated for making those efforts. Companies know this, and shareholders know that this is a necessary condition for generating financial value. However, a movement towards stakeholders creates complications for boards. What is less well understood is that stakeholders do not always agree on their requests in exchange for their efforts, or on how they would like to see a firm managed. Stakeholders differ in age group and gender. They may be employees with firm-specific investments or with no specific investments. They may be suppliers who have customized their products, or many others. Pleasing one stakeholder typically displeases another. Trying to address all stakeholders at once does not offer results, and creates no value.

How can a company reduce inter-stakeholder conflict? The first solution is to become closely held, reducing the number and variety of equity owners, while attracting employees who prefer to work at a closely held firm. Alternatively, a company can also become a "mission-oriented firm" by declaring one stakeholder more critical than others. Examples include Patagonia supporting the environmental cause or Cotopaxi fighting for poverty alleviation. This will attract stakeholders who have an affinity with the mission. Another solution is to emphasize and cooperate with stakeholders whose co-specialized investments are significant for financial value creation. However, Professor Barney concludes that, despite their attempts, companies will never eliminate stakeholder conflicts. The ultimate goal should be to focus on certain stakeholders while keeping others "barely satisfied."

Discussion (**Joan Enric Ricart**, IESE Business School)

Today's relevant stakeholder governance involves arrangements of ownership rights, identification, prioritization of strategic stakeholders (coalition building), bargaining, and incomplete contracts to harmonize the expected conflicts of interests among the diverse parts. To derive an agenda for a change in corporate governance, Professor Ricart proposes four different situations with varying levels of difficulty.

The first can be labeled the "It pays to be green" scenario. In this case, there are limited tradeoffs and few conflicts among critical stakeholders. While, theoretically, shareholder value maximization should coincide with "value-based competition," in practice, the "It pays to be green" scenario runs up against frictions, a lack of information, and pervasive incentive limitations in management.

The business model focused on innovation represents the second potential solution. A business model should not be seen as static but as a possible object of innovative efforts, with the opportunity to involve strategic stakeholders. In this solution, “trustee-based governance” can use the corporate purpose to lead the process of value co-creation. A third option is called the “shared values business model.” In this scenario, “trustee-based governance” with a corporate purpose can lead to the identification of the right coalition of stakeholders, able to co-create a “shared values business model.” In this case, different ownership structures (privately held), different legal forms (mission-oriented), and more flexibility are needed. To achieve this, it is necessary to change the agenda for corporate governance and promote business model innovation to deploy the company’s purpose. Corporate governance by trustees should work to identify the right coalition of stakeholders to collaborate and develop real “shared-values business models.” Finally, there is the “grand challenges” option. “Grand challenges” are the most difficult, but essential problems of society, which can be solved only with the coordinated efforts of multiple organizations, companies, and individuals. They involve shared resources or public goods, making the problem of governance even broader and requiring systemic changes and new institutions. With the diffuse use of “shared values business models” in the presence of shared resources, corporate governance can become crucial to building broader collaborations and shaping the changes required in the institutional framework to solve the most important challenges of today’s society.

SESSION 8

CEO Roundtable: Strategy and Sustainability. A Board Perspective

Sophie L' Helias,
LeaderXXchange, President

Juvencio Maeztu,
Ingka Ikea, Deputy CEO and CFO

Moderator: **Jordi Gual**,
IESE Business School

INTRODUCTION

The panel discussion brings together Sophie L'Helias, president of LeaderXXchange, and Juvencio Maeztu, deputy CFO and CEO of Ingka IKEA. Together with Jordi Gual of IESE Business School and moderator of the discussion, the round table explores the challenges that companies face when embracing a sustainable transition and how to deal with the various dilemmas and tradeoffs.

JORDI GUAL (JG): There are many businesses in which it is not easy to take actions that are compatible with the ESG metrics. Especially if it is not common practice among competitors, undertaking and integrating ESG factors can put a company at risk of losing market share. How can firms deal with these tradeoffs?

SOPHIE L'HELIAS (SH): I don't see ESG as a strategy. As I see it, we must have a sustainable business model, and the sustainable business model is value creation. Depending on the extent to which a company has a sustainable business model, the ESG drivers become natural. According to Sophie, the ESG metrics are not something you would either pursue or not pursue. By adopting a sustainable business model, the tradeoff disappears because you are creating value for both shareholders and stakeholders. The question should then be, "Do you have a sustainable business model?" That is how today's investors are looking at companies, investigating whether they will survive the competitive challenges of their environment. Integrating ESG is not an option for companies that wish to adopt a sustainable business model. Not integrating ESG and not thinking about how their business will grow in the future will increase the risk of losing competitive advantages.

JUVENCIO MAEZTU (JM): The crucial issue is that satisfying stakeholders is about managing dilemmas. Although a company cannot satisfy all its stakeholders, finding a merging point is necessary. We are at the beginning of a new age of humankind. No one wants to destroy the planet, but we are lost. There are three significant dilemmas that companies are faced with in this path towards a sustainable future. The first relates to the fact that sustainability must be about business, not charity. Our products are selling 30% more than comparable non-sustainable products. In that sense, a sustainable business model must be profitable and cannot renounce financial value. The second dilemma relates to the widespread conviction that sustainability is complex and should be left to experts. However, this is not the case. Leaders are crucial to

driving the change and coordinating efforts and knowledge. They must find solutions in conjunction with the experts, who can help them integrate the solutions into the company. Experts should not be left alone and detached from the rest of the activities. The third and final dilemma is the idea that sustainability is a luxury. Sustainable transitions must be affordable for everyone. Sometimes we phase-out our top selling product because of sustainable reasons, but cutting out consumption is not the solution; the problem is bad consumption. In other words, companies must be able to educate consumers and guide the demand for sustainable products, in order to increase the scale and make them more affordable.

JG: Is it really possible, in the public market, to run a strategy that "barely" satisfies stakeholders but is losing ground against competitors?

SH: Yes, it is possible. Sustainability doesn't replace performance; it is a business. Thus, it should be considered and approached in the same way as running a business. Sustainability is about developing innovative ways to drive growth. If sustainability results in poor performance, most of the time it is the business strategy that is the reason. Investors incorporate ESG into their parameters and investment decision-making processes, either selecting or excluding companies or persuading companies to change. Moreover, competition for talented personnel is very intense and sustainability is crucial to attract, retain and involve them, since this can be vital for a company's future success.

JM: It is essential to consider what performance looks like. Sustainability does not have to be charity or the enemy of profitability. Thus, to be consistent in their decision-making, companies need to re-clarify what performance means for them. For instance, in IKEA, performance is about creating better homes for consumers. It is about a better life for people, a better planet for everyone, and a better company for the long term. If a company can make profits following these performance objectives, it will keep adding value to the other dimensions.

JG: How can we measure the ESG performance? How can someone calculate the return on ESG? How can we know if one company is doing better than another?

SH: If a company starts with a purpose and develops its strategy, it is possible to identify the different metrics for each area according to the purpose and the strategy combined. To do so, companies need a governance system to collect information, verify the data, and make the information consistent and meaningful. Having too many metrics is not so relevant. The crucial point is to build a monitor and reporting system to bring all this information to the board in a timely fashion. It needs to be transversal and interdisciplinary. Metrics must then be validated in conjunction with the company's stakeholders.

JM: Boards and CEOs need to have an in-depth understanding of their company's sustainability model. They must be familiar with the forecasts for their footprint in 10 to 20-year time in order to build standards and objectives that are fitted and tailored. They need to have the right knowledge and information to answer the question, if my company were to disappear today, would the world be a better or worse place?

JG: Developing a single standard for evaluating companies can kill specific business models that do not work well with a particular standard. How will the ecosystem of ratings, analysts, and consultant evaluating companies evolve?

SH: Companies stepped up during the COVID-19 crisis for the safety of employees, increasing the number of board meetings and engaging in outreach with many stakeholders. Companies opened up and aimed to be fully transparent during the crisis. This suggests that, despite the creation of common core standards for specific metrics, companies are increasingly disclosing more on these topics voluntarily. It is difficult to hide information. It follows that companies are able to communicate their corporate culture to investors and financial communities, which goes beyond just numbers and financial statements. Being able to share the corporate culture is much more powerful because it builds trust.

JM: Rigid standards cannot drive the destiny of our companies. Society demands that companies be involved in more social issues, putting them at risk of not knowing what they can and cannot do, what they can and cannot say. The answers can be found by going back to each company's comfort zone, represented by its core principles and values. During the pandemic, we didn't have a roadmap. When it comes to making decisions in these contexts, an organization can only rely on its core values. A time of crisis is when everyone in an organization connects on a more personal level. If the core values are deeply understood, a company in crisis can "move by itself."

JG: What should the role of the board be?

JM: The board must be clear on the core values. The board's role is to challenge the CEO. I'm expecting the supervisory board to challenge me as to whether this is enough. I'm expecting the board to put the tough questions on the table.

SH: Boards should systematically bring decisions back to the company's core purpose and strategy, guaranteeing their alignment. To do so,it is vital to have the right people, the right processes and the right information.

Wrap-Up

Marco Becht,
Université libre de Bruxelles and ECGI

At the end of this day of interesting discussions, some important conclusions emerged. The first relates to the relevance of today's unprecedented degree of uncertainty, in a world constantly exposed not only to "Black Swans", but also to "Green Swans". The second is related to how central a role boards play in formulating strategy. However, formulating strategy is not simple because it must be done in conjunction with investors, managers, and stakeholders. Moreover, the idea of "doing well by doing good" has been discussed, as well as the difficulties related with this statement. It has been recognized that there it embodies a fallacy, especially in a global market where not all actors are doing the same thing or are working within the same timeframe for achieving the sustainable development goals. This involves being honest about the tradeoffs and sacrifices that must be made. Finally, this leads us to consider the role of governments in helping to create rules for everybody and to reduce the negative externalities. Business should push not for more but for better global regulations.