



2004 Corporate Public Affairs Oration
An initiative of the Centre for Corporate Public Affairs

**Governance and the Stakeholder Corporation:
New challenges for Global Business**

**Delivered by Professor James E. Post
Boston University**

**Melbourne, Australia
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Foreword

The Centre for Corporate Public Affairs annual Oration has two objectives:

- to extend knowledge about public affairs management. It seeks to do this by providing a forum for those who have made a distinguished contribution in related areas to reflect on their experience and thus contribute to understanding of the function; and
- to focus attention on the nature of the social and political environment. The Oration seeks to illustrate why and how successful management includes in its vision and practice constructive engagement with its communities.

Through the wide distribution of the Oration and through the other activities of the Centre for Corporate Public Affairs we seek to further these goals.

The 2004 Oration was delivered by Professor James E. Post from Boston University at a Centre dinner held in Melbourne on 24 June 2004.

This is the eleventh Corporate Public Affairs Oration. Previous Orations in the series have been:

1994 The Hon John Dawkins, former Federal Treasurer, *Business-Government Relations: a decade of economic reform and the role of business*

1995 Mr John Prescott, Managing Director and Chief Executive Officer, BHP Company Limited, *Business in its Community: forging a new partnership*

1996 Mr John Ralph, AO, Chairman, Forster's Brewing Group Limited, *A corporate social responsibility?*

1997 Mr W Frank Blount, CEO Telstra Corporation, *Convergence or Collision? Emerging complexities at the business/community interface*

1998 Mr M A (Tim) Besley, AO, *End of Millennium Challenges for Business, Government and Society*

1999 The Hon. John Howard, MP, Prime Minister, *Corporate Community Involvement*

2000 Mr S D M Wallis, AO, Chairman AMCOR, Coles Myer, and AMP, *Corporate Governance - Conformance or Performance*

2001 Mr Richard Humphry, AO, Managing Director & CEO, Australian Stock Exchange, *Globalisation of Capital Markets: Implications for the Australian Community*

2002 Mr Leon Davis, Chairman, Westpac, Deputy Chairman, Rio Tinto, *Business and Society*

2003 Mr Graeme Samuel, AC, Chairman, Australian Competition and Consumer Commission, *Industry regulation – can voluntary self-regulation ever be effective?*

About the Centre for Corporate Public Affairs, Australia

"Public Affairs is the management function responsible for interpreting the future political, social and regulatory environment of an organisation, continuously integrating these assessments into the strategic planning process, and undertaking and supporting consequent organisational action."

The Centre for Corporate Public Affairs was established in 1990 in response to demand from corporate and public affairs professionals for a support organisation for their activities.

The Centre now has more than 100 members from the ranks of corporate Australia, industry associations and government business enterprises.

The Centre aims to provide mutual exchange within the profession's leadership, excellent professional development programs and information resources that allow senior public affairs practitioners, senior executives and line managers to:

- Better interpret their social, political and economic environment,
- Contribute significantly to the way their organisation relates to its internal/external stakeholders; and
- Strengthen the role of corporate affairs staff as key advisers to management.

These aims are achieved by providing:

- Professional development and training;
- Research and information resources;
- International affiliations; and
- Peer group dialogue and mutual learning.

For further information about the Centre please visit <http://www.accpa.com.au>

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2004 CORPORATE PUBLIC AFFAIRS ORATION

Governance and the Stakeholder Corporation: New challenges for Global Business

Thank you for that generous introduction. It makes me feel a bit like David Roderick, the former chairman of a steel company, who was once introduced to an audience as the most gifted businessman in the country, evidenced by the fact that *he “had made a million dollars in California oil.”*

When he came to the podium, Roderick was a bit embarrassed. Those facts, he said, were essentially accurate, but it wasn't oil, it was coal.

And, it wasn't California, it was Pennsylvania.

And it wasn't a million, it was one hundred thousand.

And it wasn't he, it was his brother.

And he didn't make it, he lost it!”

So, Geoff, thank you for introducing my brother.

When Geoff invited me to deliver the 2004 Oration, I readily agreed. Then I realized that I needed to be clear about the expectations for an Oration. I needed to better understand ... “What is an Oration?”

This is what I learned. In a class or a workshop, the perspective is that of an “on-the-ground” discussion – what are the trees in the forest.

In a lecture, the perspective is that of just above the tree tops; we learn to distinguish between the forest and the trees.

In an address, the perspective is at least 10,000 feet.

In an oration, the perspective is at 30,000 feet ... and climbing!
So, that is the perspective I bring to this Oration tonight.

Introduction

It is nearly 15 years since Geoff (Allen) and I first communicated about the newly formed Centre for Corporate Public Affairs and his idea of an “Institute” where public affairs practitioners could learn from one another and from international experts. Geoff's goal was to broaden and deepen the knowledge base of Australian public affairs practitioners. The progress that has been made in creating one of the world's most dynamic centers of public affairs thinking is simply remarkable.

Geoff and I share the conviction that corporate public affairs is probably the most exciting function in modern business. Those who awake each day to the public affairs and communications challenges facing Australian organizations are among the luckiest people in the Lucky Country.

You share the excitement of dealing with problems that matter to both “company and country;” problems that defy the word “routine.” And you do this in the company of some of the smartest, most imaginative business, media, and political thinkers in the world.

When the Institute began, the most pressing issues facing the policy makers in our respective nations involved national defense, economic stimulation, and the creation of economic opportunity for more citizens. The deregulation of key industries was high on the policy agenda in both nations. Global trade was also important, but few imagined the great changes we would witness in the decade to follow.

The first Institute meeting gave Geoff an opportunity to organize a few collateral activities. One of our meetings involved 25 business leaders from the automobile, energy, mining, and financial services industries. For three or four hours, a few Americans (including Chuck McKittrick of IBM) and these corporate affairs leaders from Australia discussed the state of the field, including lessons learned from the U.S. experiment with deregulation. One topic of discussion was how the Hawke government, or a future successor, could be persuaded to maintain a commitment to such a public policy course in Australia.

During the meeting, I experienced one of those “flashes of light” when a truth is suddenly revealed. The five automobile manufacturers operating in Australia [General Motors (Holden), Ford, Toyota, Nissan, and Mitsubishi] were trying to capture a market that was the size of my home state of New York – with its 17 million residents. I knew that no company could make money in such a situation. The fixed costs of plant and equipment were too high, the customer base too small, and there was too little incentive for costly innovation. The economic logic did not -- could not -- work. Politics had forced an extremely uneconomic regime on a nation whose consumers wanted safe and attractive vehicles, at an affordable price.

Our conversation didn’t produce an economic manifesto, but it affirmed the importance of international trade, the nation’s need to reduce trade barriers, and the stake that every Australian had in a more open, competitive economy. In the years since that meeting, I have watched Australia’s business and political community exercise leadership in economic policy and take long strides in the direction of economic freedom.

Australian Public Affairs Profession

The recent state funeral of former U.S. president Ronald Reagan brings to mind a story. On one occasion President Reagan was speaking to a group of college students. One student was saying that Reagan couldn’t possibly understand their situation because the world was so different from the time of his youth. After all, the student continued, in a somewhat critical tone, Reagan’s generation didn’t have computers, supersonic aircraft, and so on. Reagan looked at the young man and replied, “You’re right, we didn’t have those things. We *invented* them.”

Many of the people in this room tonight helped “invent” the corporate public affairs profession in this part of the world. Many of you have contributed vital ideas -- and the wisdom of “best practice”-- to the hundreds of men and women who practice the government relations, public relations, community affairs, and communications professions.

Many of you have also helped shape the way government leaders think about the business-government-society relationship. It has made a difference. For all of the day-to-day problems that afflict you, consider the accomplishments:

- Today, there is a competitive automobile market in Australia.
- Today, there is a deregulated financial services sector.
- Today, there are globally competitive mining, energy, and agricultural industries.
- Today, Australia (and New Zealand) have become the home for entrepreneurial ventures in biotechnology, entertainment, telecommunications and filmmaking.

Over the past two decades, Australia has shaken the bonds of old-fashioned protectionism, moved through an era of wrenching industrial modernization, and created jobs in new sectors and industries that are building a promising economic future. It has been hard work, but it has helped secure a promising future. You have helped create one of the most dynamic and modern political economies in the Southern hemisphere and the world.

These significant accomplishments could not have happened without dynamic public affairs practice. Sound government policies don't "just happen." Nor do sound business policies "just happen." Both are the product of a system that encourages freedom and democratic capitalism.

Dialogue, advocacy, and openness to new ideas are the hallmark of a politically vibrant society. Public affairs professionals help make that vision a reality.

The Stakeholder Corporation

To an extent you may not fully appreciate, Australia has helped create the working model of the "stakeholder corporation."

Australian business leaders and public affairs professionals have been among the world's leaders in developing a robust understanding of the interdependencies amongst customers, employees, investors, and communities. Senior managers in many of your companies have learned how to walk the tightrope between shareholder returns and socially responsible business practices, and they understand why it is so important to do so. The language of stakeholder management is being joined by the practice of stakeholder management.

There have been some notable business failures, and more than a few crises, along the way to be sure. But there have been many business successes as well. You have learned lessons from both the failures and the successes. These lessons have been incorporated as part of the "living history" of business-government-community relations in Australia today.

The stakeholder corporation is characterized by leaders who understand the need to balance, prioritize, and adjust to the needs of all constituencies. Today, we understand the different forms of risk facing an enterprise if it fails to recognize the importance of those who benefit from the firm's success and those who are injured by its activities. Employees, customers, shareholders, and communities all have something to gain, and something to lose, from the success or failure of a corporation. The business challenge is one of developing new ways to create economic and social value, and better ways to manage economic and social risk.

Through the years, Australian businesses have provided important examples of how to recognize and respond to stakeholder considerations.

- Workplace reforms have changed how companies and trade unions operate. Moreover, a new relationship has been shaped between employers, employees and trade unions – featuring more dialogue, information sharing, and consultation.

- In the community, public concerns for community health, safety, and environmental risk have led to community stewardship programs, consultation processes, and right to know agreements.
- In the capital markets, Australian companies have become more open and friendly to foreign investors. And Australian companies, and Australian business values, are becoming known in global capital markets as well.

These actions speak louder than words, but powerful words have been spoken as well. Throughout the past 15 years, Australian business and political leaders have contributed to our broad understanding of stakeholder capitalism. John Prescott, John Ralph, Frank Blount, Stan Wallis, and Leon Davis and others have, through this Oration, addressed aspects of the social contract between business, government, and Australian society.

Governance

In recent years, these Orations have drawn attention to the important connection between corporate governance and the roles of business and government. Richard Humphrey of the Australian Stock Exchange made governance a central theme in his Oration.

A corporation that aspires to sound corporate governance, must be concerned with all of its stakeholders. And a corporation that is concerned about its' stakeholders, must aspire to a system of sound corporate governance. The relationship between a corporation that recognizes and responds to its stakeholders, and a corporation that pursues sound governance exists is fundamental.

As one chief executive said, *"I have no doubt that success in the economic marketplace as well as the marketplace of ideas will increasingly be granted only to those who earn and protect the public trust."*

He went on to say, *"In the future, lower prices, flashy commercials, dazzling rhetoric, grand promises will not be sufficient strategies for success in a society that will value honesty and integrity above all else."* (A. Thomas Young, President, Martin Marietta Corporation, at The Conference Board, May 5, 1992)

He did not foresee the scandals that would sweep over the business community in the next decade. But he understood a basic rule of the public affairs profession: Success in the economic marketplace, the political marketplace, and the marketplace of ideas, will be granted only to those who earn and protect the public trust ... and it will be withheld from those that do not.

Today, we see the public consequences that flow from failures of corporate governance. As events of the past three years have made clear, global markets place an economic value on honesty and integrity. Global markets simply cannot function efficiently, and effectively, without high standards of truth and integrity.

Good governance is both a "public good" from which we all benefit, and a "private good" from which the organization benefits. Markets exist in the context of public policy and the public confidence that is built on honesty and integrity. That is why the public trust matters so greatly.

My purpose is not to deliver another speech on ethics. But there is no doubt that such speeches remind us – one person at a time, one idea at a time – of the nature of our responsibilities to our business, our country, and our family.

If we require such sermons from time to time, we surely need humor as well. While visiting Sydney, the great humorist and poker player, Mark Twain, was asked to define an ethical businessman. He quipped, “(An ethical businessman is) ... a Christian holding four aces!

The serious point, of course, is that corporate governance, ethics, and stakeholders are fundamentally entwined. Simply stated, we cannot have good governance unless we have individuals who believe in the value good governance and are prepared to act in ethical ways to ensure it flourishes.

Redefining the Corporation

[You will be interested to know that the exciting title of this year’s Oration was selected by a committee of Centre staff ... we rejected all the uninspiring titles! This is a tribute to teamwork. As we take stock of these trends –from 30,000 feet!—what does it mean?]

In our recent book, *Redefining the Corporation: Stakeholder Management and Organizational Wealth*,¹ Lee Preston, Sybille Sachs and I have argued that the modern corporation is being redefined by stakeholder practices that business leaders find necessary and useful to creating wealth in the current climate.

All three of us are academics who have spent most of the past five years immersed in companies on three continents. Our views seem well-grounded in business reality. I will say a few words about the book since that is the topic I was invited to discuss this evening.

A few quick points:

The modern corporation is being redefined by the stakeholder practices that business leaders find necessary and useful to creating wealth in the current climate. The normal evolution of business practice has reached a watershed regarding stakeholders. They matter for many reasons, but most of all, because they are the key to organizational wealth and success.

Our core argument is this: Organizational wealth is increasingly attributable to “soft forms” of capital – reputation, trust, credibility, good will, image, relationships. The “hard forms” of capital – natural resources, plant, equipment, manufactured goods—are still important, but relatively less so in relationship to a company’s overall wealth.

To the extent that tangible forms of capital are plentiful, their value is commoditized. And, since pricing power is still the key to above-average returns on investment, we are learning that it is the ability to command a premium in the market –the price premium flows from the firm’s intangible assets- that enables above-average returns to be earned.

¹ James E. Post, Lee E. Preston, and Sybille Sachs, *Redefining the Corporation: Stakeholder Management and Organizational Wealth*, Palo Alto, CA: Stanford University Press, 2002.

Some experts call this as “relational wealth.” Others prefer to call these “intangibles.” *The Economist* magazine offered this visually compelling definition of intangibles: “An intangible is anything in a firm that generates value that you can’t drop on your foot.”

Or, as Patricia Seeman, CEO of Sphere Inc. in New York said, “Simply put, it means people, brand, perception, image, reputation; the ability to innovate and learn; and the relationships with customers; the confidence investors have in your strategy and your ability to deliver on it.”

The analysts at the Accenture Consultancy recently added support to this practical theory of intangible assets. In a survey of business leaders, 96% of executives polled said that intangibles are important to their company. 50% think they are among top three issues the firm faces. But 95% of the executives also said that they had no deliberate management systems to deal with them.

Intangibles cannot be the “left-overs” after everything else of importance is done. We were once taught to think of corporate “goodwill” as a residual value on the corporate balance sheet. But today’s intangible assets are too critical to the modern enterprise to be treated as an after-thought or as an accounting residual.

Image, customer loyalty, reputation, and intellectual property are enormously important to many businesses. Consider intellectual property for example. Intellectual property is no longer confined to a few knowledge-based industries that are seeking patents for new inventions. We all operate in IP-rich environments these days; knowledge is the key to innovation, productivity, and economic success ... in every industry and business.

By several estimates, 30 to 60% of a publicly listed company’s value now lies in its intangibles. Share price behavior, for example, is one highly sensitive indicator of the power of intangibles. Stock prices rise and fall on leadership changes, reputation failures and recoveries, and relationships between a company and its critical stakeholders.

Businesses cannot lose sight of value-creation and risk management. The importance of intangibles, in both financial and non-financial sense, makes the clear case for managing and governing intangibles as rigorously as tangibles.

Experts urge four essential steps to managing intangibles well:

1. The firm must have a track record of keeping its promises;
2. The firm must have a compelling strategy that stakeholders understand and have faith in;
3. The firm must invest clearly and rigorously in line with that strategy;
4. The firm must focus on building those capabilities that enable it to deliver the strategy.

But there is an important fifth step. To manage intangibles well, the firm must manage its public issues and its reputation with the sophistication, skill, and clear purpose of public affairs management.

Intangible assets are intrinsically connected to an organization’s stakeholders. Respect the stakeholders and you protect your assets. Disrespect your stakeholders, and your intangible assets are placed at risk (in harm’s way).

As part of the research for our book, we interviewed Robert Galvin, son of the founder of Motorola, and the distinguished chief executive officer who led that company for nearly four decades. We were talking about the importance of business relationships, and Mr. Galvin spontaneously said, “*Every business is a stakeholder company.*” To him, it was unthinkable that a leader could think of a business as anything other than a network of human relationships.

Perhaps this is why Motorola enjoyed significant success in China well ahead of many other western business enterprises. The company eschewed more familiar “transaction-only” thinking and insisted on relationship building. It took a decade or more, but China truly became Motorola’s “second home.”

Some would say this was simply good business. I would say, “*Exactly so!*” It is good business and it is good stakeholder management.

Motorola understood that relational wealth, although invisible and hard to measure, was being created by its investments in China’s schools and students, by its creation of new housing, through the establishment of an electronics museum, and by the job training and language development it was investing millions of dollars to establish. Today, every aspect of Motorola’s investment in these intangible relationships is contributing to their market position as a leader in Chinese telecommunications.

Global Business Challenges

In bringing these remarks to a close, I will comment briefly on three global business challenges ---trade, terrorism, and trust--- that frame the public affairs agenda each of you will confront in the near future.

Even as we are building commercial relationships around the world, we are forced to recognize that some individuals and organizations are determined to sever and disrupt the stability of those relations.

The threat of violence toward individuals and property is on the minds of business leaders everywhere. Security spending has been rising in companies around the globe, in both direct and indirect forms. Procedures and practices to identify and respond to risks have intensified. For many companies, including those in natural resources, petrochemicals, manufacturing, and financial services, these efforts are extensions of security measures that have long focused on minimizing the risk of sabotage. For companies in other, less violence-prone sectors, however, the past few years have forced a costly adjustment to a new reality.

Many companies are radically reexamining and re-thinking their strategic approach to security issues. Many are using stakeholder analysis as a vital tool in the process. Military organizations are now integrating sophisticated scenario planning with sophisticated stakeholder analysis and mapping. Terrorism has underscored the need for better intelligence and risk management. Public affairs practitioners are at the center of these efforts in many companies and government agencies.

Terrorism also undermines trust.

National and global political leadership is vulnerable to the “trust gap.” After the Madrid bombings, the cover page of *The Economist* highlighted the faces of four national leaders: President Aznar of Spain; President Bush; Prime Minister Tony Blair; and Prime Minister John Howard. An “X” covered Aznar’s face and the title read, “*One Down. Three to Go.*” The defeat of Aznar’s party in Spain was directly tied to public confidence in his explanation of who was responsible for the bombings. Within the

next year, we may see other faces join the ranks of the new century's political leadership.

Agendas (economic and political) are changing and we must wonder again, as in the past, what this means for our nations, our economies, and our businesses. Progress in public affairs is often hard-fought and hard-won. But it can be easily lost. Australia's economic and political landscape has changed dramatically since the first Institute program. Amidst such global challenges, dramatic shifts are possible again. They may not all be so salutary.

The Era of Corporate Accountability

Two words capture the spirit of the time – transparency and accountability.

Citizenship requires a global view. Adaptation to local conditions is essential, of course, but we are operating in a world where global norms and standards are increasingly relevant to the business. It is now impossible for manufacturers to immunize themselves from public criticism by creating networks of suppliers – contractors and subcontractors. Buffers are more difficult than ever to create and maintain.

Transparency has become the norm, even among those who wish it would go away. As in the marketing arena, if you make it, ship it, sell it, or profit from it, you *own* responsibility for it!

Accountability in all sectors

The recent resignation of the Anglican Archbishop of Adelaide for covering up more than 200 cases of child abuse points to one final element to the picture of stakeholder accountability. The controversy surrounding the administration and governance of modern organizations is not confined to the commercial sector alone – it is a multi-sector and worldwide phenomenon. Government departments, NGOs, and even churches are called on to govern and manage within a network of stakeholder relationships.

I have learned a good deal about this challenge in the past two years. In Boston, we lived through the terrible disclosure of hundreds of cases of clergy sexual abuse in the Catholic Church. Under the unrelenting pressure of lay Catholic groups -- including a group which I helped found that now has more than 35,000 members²— Church leaders were moved to respond.

In February 2004, the Church's own investigation showed that more than 4,300 priests were alleged to have abused more than 10,600 children over a fifty-year time span. More than \$570 million were spent to settle and resolve the cases. All of the data are believed to be under-stated, yet all of these figures are substantially higher than had ever before been documented.

Once again, accountability and transparency are the key words of this era for organizations in all sectors.

² Voice of the Faithful can be found at www.votf.org

Conclusion

As we venture further into the global economy of the 21st century, millions of shareholders are providing applause for executives who lead the way. Our leaders are filled with optimism; the risks don't trouble them, but we know risk can get the best of them – and us.

It is in the treacherous landscape of global competition, political misfortune, and loss of integrity that we face the greatest risks. We need a compass that still points toward a moral “true north,” a compass that points us toward sound policy and political practice, a compass that points toward creating value for customers, efficiency in all we do, and the importance of intangibles.

At the end of our book, Professors Preston, Sachs and I close with this thought: *“Although the corporate system is currently expanding throughout the world, its future is by no means assured. To maintain its status as the preeminent institutional arrangement for the creation of wealth, the corporation must earn its “license to operate,” both locally and globally, by demonstrating its respect for people and its contribution to building a better world.”*

And then we say, *“The wealth of the corporation is not merely the property it owns, the financial resources it accumulates, or even the intellectual property it develops. The corporation’s most important asset –and the only one it cannot create or replace on its own – is its acceptance within society as a legitimate institution.”* (p. 256)

This idea echoes that of Sir Arvi Parbo who, at the founding of CCPA, said: *“We can do our sums, be great at production and marketing, fine tune our cash flows, manage people – we can do all those things well but fail badly if we haven’t managed the social and political issues.”*

That was sound advice in 1990; it is sound advice today.

Without the support of a society that understands its value, the corporation simply has no license to operate, and there is no sustainable path to the future.

Well, that is the view from 30,000 feet. It has been a privilege to address you tonight.

Thank you.