MSc Marketing Management

Pre-course Fall 2007

Corporate Management

Session 3.
Maximizing shareholders value. Managing stakeholders expectations

Firm's Objective *Shareholder Value Approach*

Firm's objective is the maximization of shareholders' value (returns), both through dividends and capital gain – Rappaport 1986, Grant 2002

Shareholders are a particular stakeholder sub-group:

- Those who provide equity receive what remains after all other stakeholders are remunerated
- Return on investment should be higher than the opportunity cost for the investor

There is an agency problem between shareholders and management, which interests are often conflicting

Firm's Objective *Shareholder Value Approach*

The social responsibility of a firm is to generate profit - Milton Firedman 1970

- only human beings have a moral responsibility for their actions
- it is managers' responsibility to act only in the interest of shareholders
- social issues and problems are the proper province of the state rather then corporate managers

Firm's Objective *Shareholder Value Approach*

Equity is what shareholders have invested at current values

Given that the benefits produced by firm in its activity will be all distributed to shareholders through dividends, Equity value is the actualized sum of future dividends (and other receivables)

$$W = \sum_{t=1}^{\infty} \frac{D_t}{(1+k_E)^t}$$

Equity value is: rational, measurable, understandable, widely accepted, stimulating

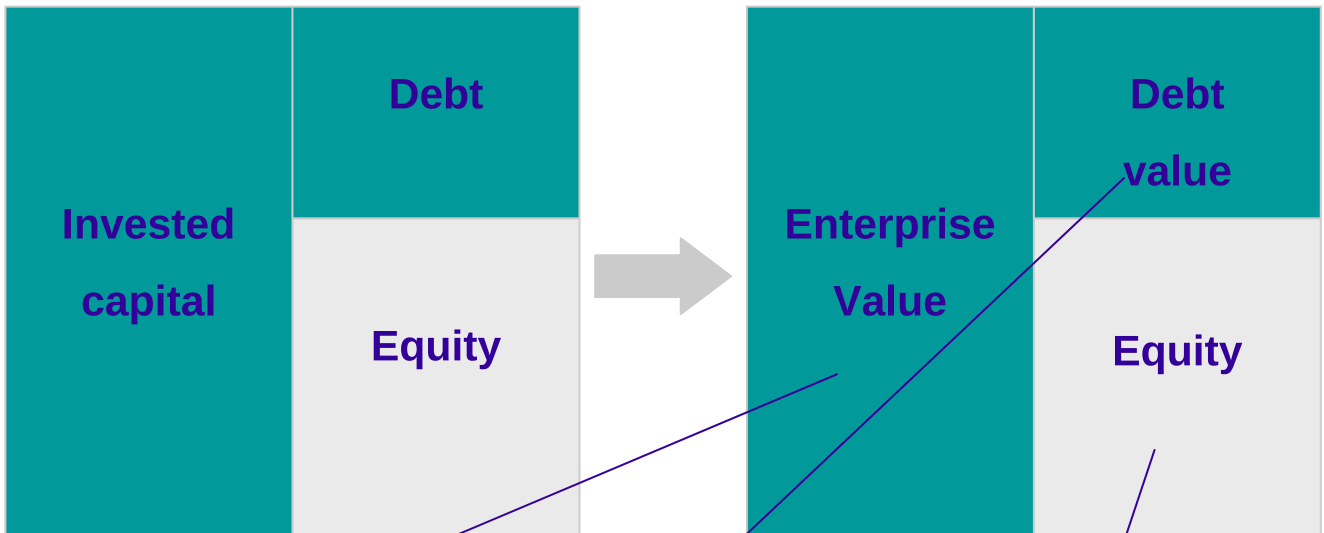
It also makes people look forward

Firm's Objective *Shareholder Value Approach*

Traditional Accounting system

Asset & Liabilities

Value oriented sysyem



Free cash flow from operations

Market value of net financial debts

Free cash flow to equity

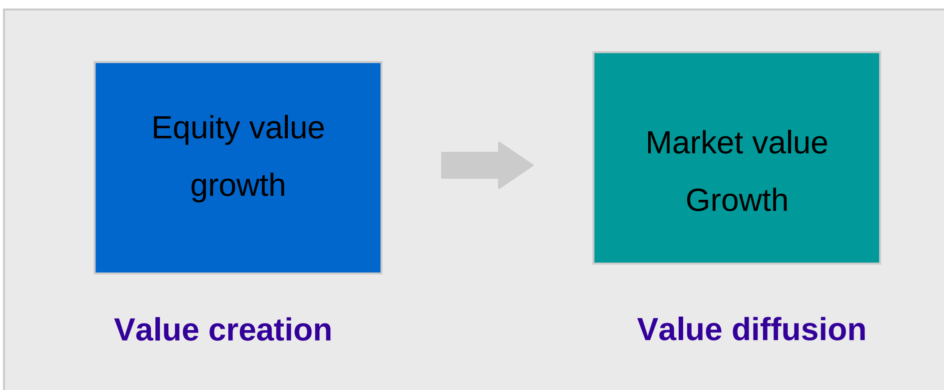
$$\sum_{t=1}^{\infty}\frac{FCFO_t}{(1+k)^t} - \sum_{t=1}^{\infty}\frac{F_t}{(1+k_D)^t} \Rightarrow \mathbf{W} = \sum_{t=1}^{\infty}\frac{FCFE_t}{(1+k_E)^t}$$

Firm’s Objective *Shareholder Value Approach*

Equity value is often different from Market value, due to:

- Speculation activity of some investors
- Market transparency
- Market dimension
- Cyclical trends
- Expectations effect

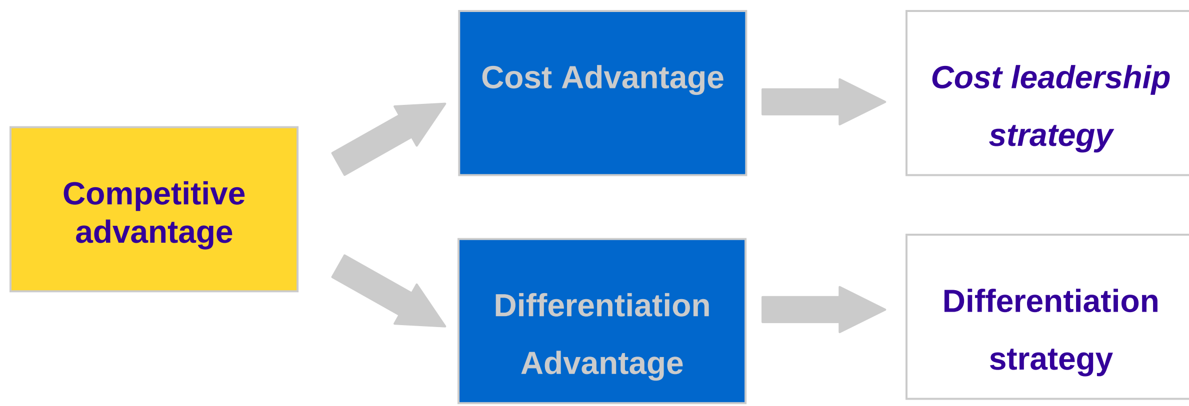
So a key issue is the dffusion of value, managing the alignement between “theoric” Equity value and Market value (stock prices)



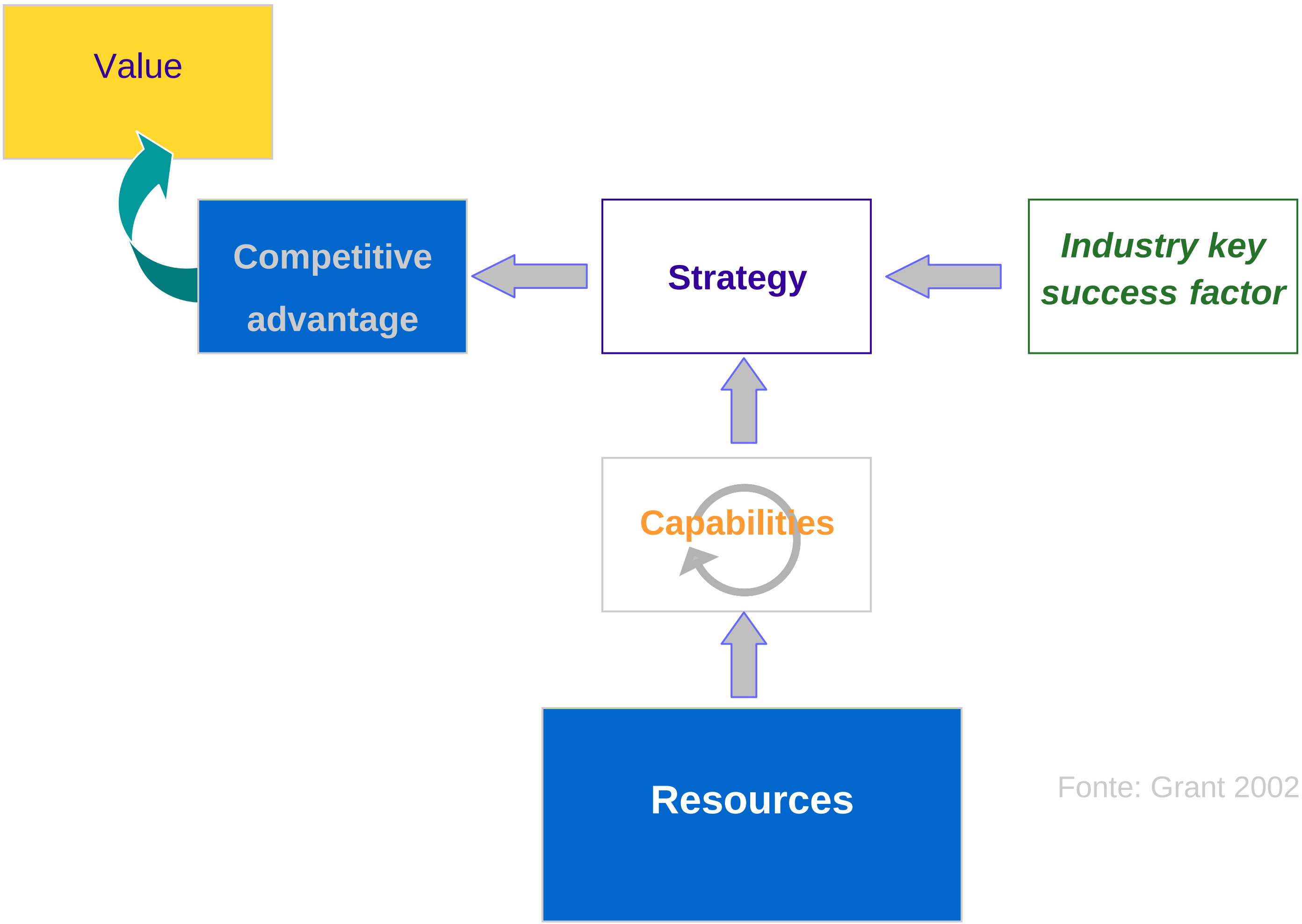
Firm's Objective *Shareholder Value Approach*

Shareholder value theory:

- Grounded on a sustainable competitive advantage
- Value can be distributed to shareholders



Firm’s Objective *Shareholder Value Approach*



Fonte: Grant 2002

Stakeholders of a Firm

Inside Claimants	Outside Claimants
Executives	Customers
Board of Directors	Suppliers
Shareholders	Governments
Employees	Competitors
	Local Communities
	General Public

Definition and Importance of the Stakeholder Concept

A stakeholder is

- "Any group or individual who can affect or is affected by the achievement of the organization's objectives" (Freeman, 1984)

Stakeholder theory is important because it addresses

- "The principle of who or what really counts" for the organisation (Freeman, 1994)

Why Managers Need to Understand Their Stakeholders

Managers responsible for returning shareholder value/profit maximisation

However, also responsible for "reconciling divergent interests" (Hill & Jones)

- Growth of awareness of Corporate Social Responsibility & governance issues
- Increased stakeholder activism
- Growth of ICT

Challenge the 'Business of Business is Business' concept

Traditional Focus of Stakeholder Management

‘Business of Business’ Concept

- To meet the claims of those with ‘power’
- Offers support for the shareholder view of the firm
- A product of resource dependency approach
- Power accrues to the individuals, groups or coalitions with access to critical resources

Therefore a narrow interpretation of the question of ‘who or what really counts’

Shareholder Matrix

B820 focus upon Winstanley et al (1995)

- Criteria Power
- Operational Power

A traditional, narrow, approach

- Favours stakeholders who possess ‘resources’ the organisation needs
- But has difficulty explaining why stakeholders with no ‘power’ often are important to organisations

Monsanto and ‘Frankenstein Foods’

Monsanto attempted to introduce genetically modified foods to Europe

Developed strategy which satisfied its key stakeholders holding criteria and operational power

- Farmers, Regulatory Authorities, Shareholders, Supermarkets/Retailers

But misjudged the attitude of other key stakeholders who seemingly had limited power

- Customers, Environmentalists

Monsanto and ‘Frankenstein Foods’

So what happened?

- Resistance by stakeholders with limited Criteria or Operational Power (Greenpeace and Customers)
- Influenced other stakeholders (Retailers) who had power
- Who used that power to undermine Monsanto’s strategy

A narrow interpretation of stakeholder management would be unlikely to predict this outcome

What Do We Mean By Salience?

- **“The degree to which managers give priority to conflicting stakeholder claims”**
- **Theory suggests Salience is positively related to cumulative number of stakeholder attributes**
  - Power
  - Legitimacy
  - Urgency
- **Salience suggests a broader interpretation of the question of ‘who or what really counts’**

Components of Salience

Power

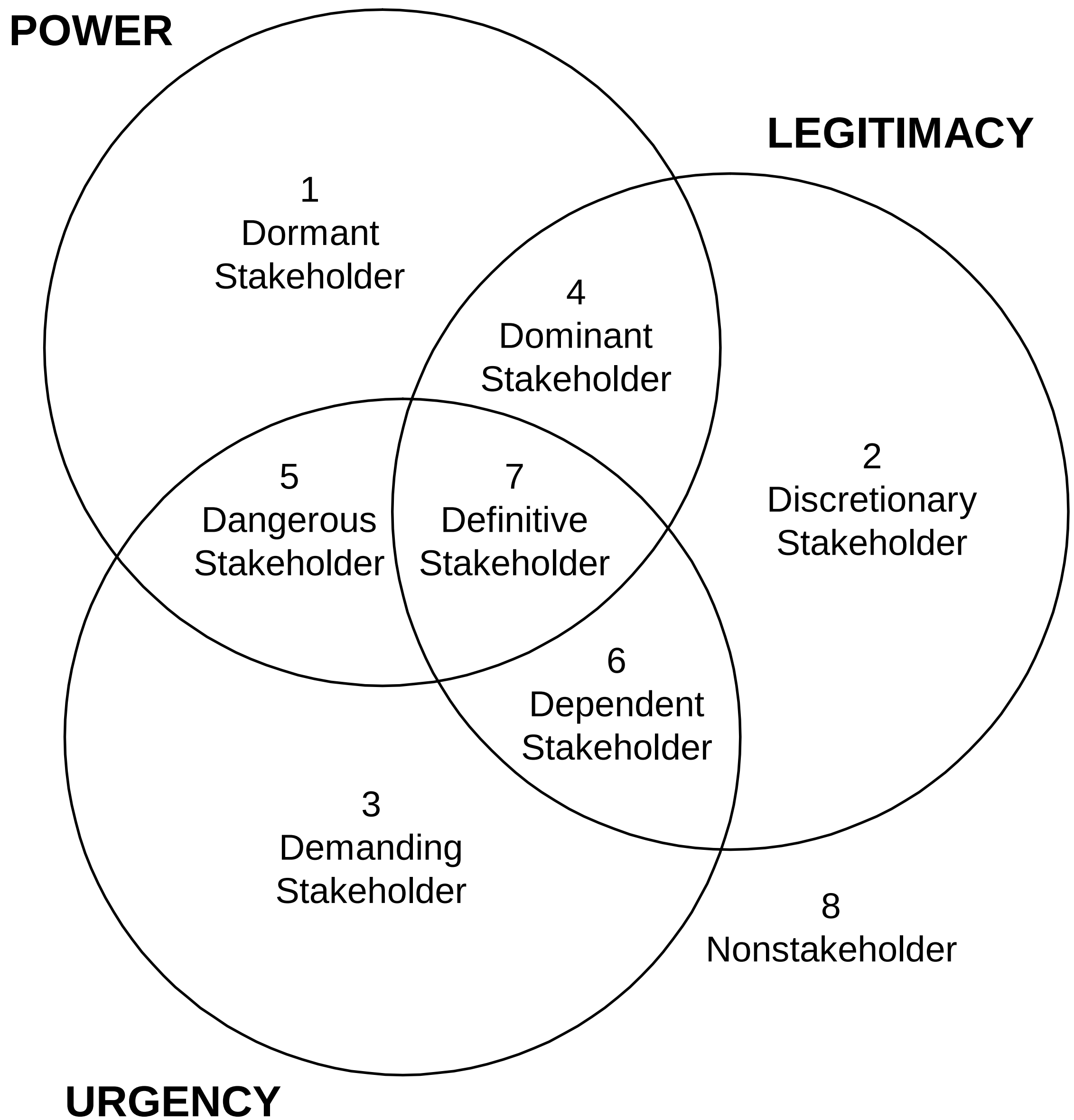
- Where ‘A’ can get ‘B’ to do something ‘B’ would not otherwise have done (Weber, 1947)

Legitimacy

- Contract, Exchange, Legal Title, legal Right, Moral Right, At-Risk Status, Moral Interest

Urgency

- The extent to which the stakeholders claim calls for immediate attention
- Or when not paying attention to a stakeholders claim is unacceptable


POWER
LEGITIMACY
URGENCY
1 Dormant Stakeholder
4 Dominant Stakeholder
2 Discretionary Stakeholder
5 Dangerous Stakeholder
7 Definitive Stakeholder
6 Dependent Stakeholder
3 Demanding Stakeholder
8 Nonstakeholder

Stakeholder Classes

Latent Stakeholders: **Dormant, Discretionary and Demanding**

- Low Salience Stakeholders
- Possessing only one attribute

Expectant Stakeholders: **Dominant, Dependent and Dangerous**

- Moderate Salience Stakeholders
- Possessing two attributes

Definitive Stakeholders

- Highly Salience Stakeholders
- Possessing all three attributes

Implications for Managers

Most organisations understand need to meet claims of DEFINITIVE Stakeholders

- Basis of Shareholder Theory of the Firm

However, key requirement to appropriately manage EXPECTANT stakeholders

- Dominant Stakeholders
- Dependent Stakeholders
- Dangerous Stakeholders

Dominant Stakeholders

Both Powerful and Legitimate

Influence assured – these people matter

Organisations require formal mechanisms to interact with these stakeholders, and understand their interests

May include owners, significant creditors, community leaders et cetera

- Tend to be served by Investor Relations, Public Affairs departments

May become 'Definitive' quickly

Dependent Stakeholders

Lack Power, but have Urgent Legitimate claims

Depend upon other stakeholders, with Power, to become Definitive

Managers need to be aware of the possibility of alliances between Dependent and Dominant or Dormant stakeholders and develop contingencies

- E.g. Greenpeace in the Monsanto case were able to enlist retailers to achieve their aims

Dangerous Stakeholders

- Possess Power and Urgency but lack Legitimacy
- Dangerous because of their ability to influence Dominant or Dependent stakeholders
- Weapons include unofficial strike action, mass protest, violence
- Organisations need to develop contingencies to countermand their potential impact

Points to Note

- **Empirical testing of stakeholder salience theory found that 'narrower' stakeholders had greater salience than 'broader' stakeholders**
  - Predictable
  - But broader view may be of value incorporating within an organisations strategic analysis activity
- **Concept of Legitimacy is perceptual, based on social norms**
- **Managers values key to question of stakeholder salience**

Other Applications

Stakeholder Salience of particular importance in marketised former public service industries

Who are Definitive stakeholders?

Difficulties exist because there is conflict between

- dominant stakeholders (owners) and
- dependent stakeholders (service users) who depend upon
- dormant stakeholders (regulators) to obtain power

Conclusions

All organizations need to understand

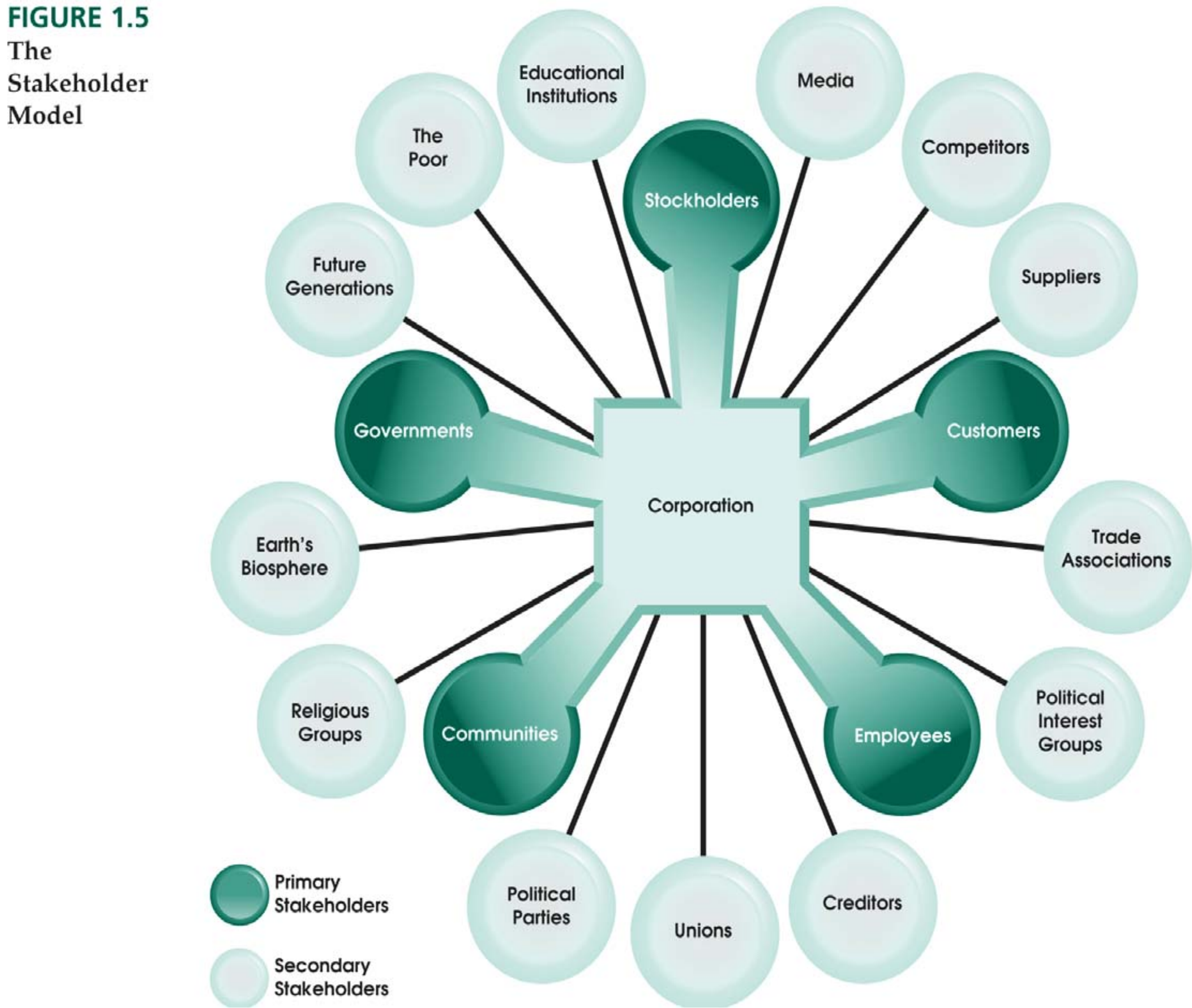
- who their stakeholders are,
- what they want, and
- how they can affect an organization's ability to achieve its objectives

Salience theory may help managers to better understand their stakeholders and prioritise meeting of their claims

In particular, managers need to understand the effects of dependent stakeholders that obtain any degree of power

Bocconi

The Stakeholder Model



Stakeholder Mapping

Stakeholder Mapping is an important part of Strategy Formulation. It consists of making judgements on three issues:

How likely each stakeholder group is to impress its expectations on the firm.

Whether they have the means to do so - **power of the stakeholder group**.

The likely impact that stakeholder expectations will have on future strategies

Stakeholder Mapping -Power/Dynamism Matrix

PREDICABILITY

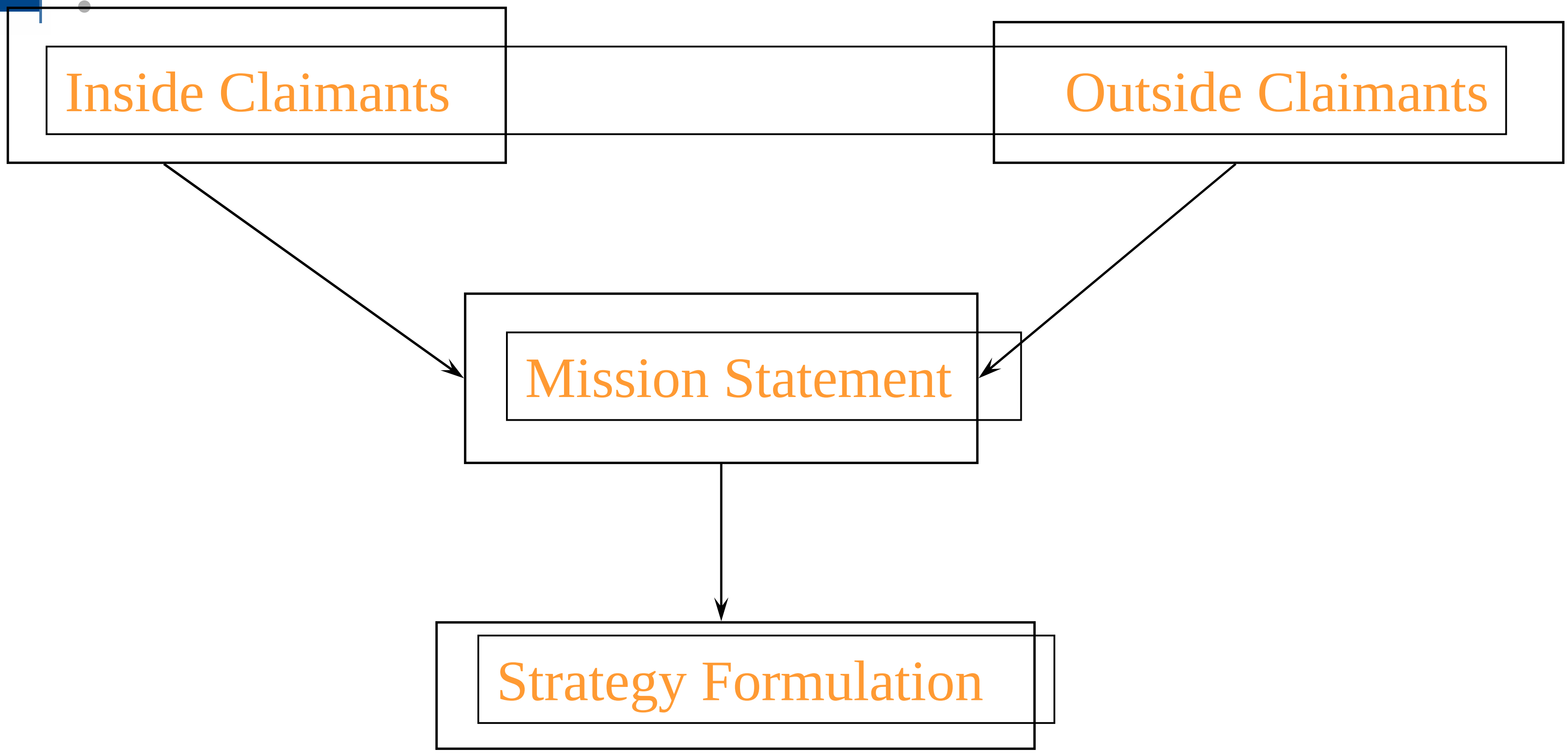
POWER	High	Low
Low	**A** Few Problems	**B** Unpredictable but Manageable
High	**C** Powerful but Predictable	**D** Greatest Danger or Opportunities

Stakeholder Mapping -Power/Interest Matrix

LEVEL OF INTEREST

POWER	Low	High
Low	**A** Minimal Effort	**B** Keep Informed
High	**C** Keep Satisfied	**D** Key Players

Mission, Stakeholders & Strategy



Customer Groups

Customer Needs

Who is being satisfied ?

What is being satisfied ?

Definition of the Business

How are Customer Needs being Satisfied ?

Distinctive Competencies

Nokia Example

In 1992 Nokia's strategic intent was expressed in four criteria

- Focused
- Global
- Telecommunications-orientated
- High value-added

Its vision was the *voice will go wireless*

In 1997 the strategic intent was articulated in terms of *a mobile information society* and *bring the internet to everyone's pocket*

Nokia 2

The Nokia vision in 1992 led to the company divesting a broad range of businesses that contributed some 90 percent of its revenues and to focus on the manufacture of handsets and network equipment

The leaders set a further goal of doubling market share by the end of the decade. This achieved by 1997 and by 1999 Nokia had overtaken Motorola as market leader.

The 1997 vision further consolidated Nokia's market position and led to the development of the picture phone and the mobile internet etc.

Nokia's website

Nokia 3

The company's 2006 Mission is about 'the awesome potential in connecting people'

Wherever, whenever, we believe in
communicating, sharing
and in the awesome potential of
connecting the 2 billion who do,
with the 4 billion who don't.

Mission Statement & its Role

Sense of Purpose & Aspiration

Company Image

Statement of Company Values, Culture and Ethics

Role as a Guide for the Strategy Process

What is in a Mission Statement ?

Philosophy and Self Concept

Desired Public Image

Concern for Different Stakeholders :

- Customers
- Employees
- Shareholders

Quality, Product and Service Aspirations