Flagship Report:

The Networked Corporation

Introducing two new tools to help companies make the business case for improved stakeholder relations through shareholder engagement

- We propose a roadmap to help companies integrate social and environmental issues into business strategy, using shareholder dialogue as a means of corporate learning about stakeholder concerns.

- We introduce the Shareholder Alignment Frontier™, a method for identifying public issues that are relevant for corporate performance through ongoing dialogue between management and long-term shareholders.

- Our BRAVE Matrix™ (Business Relationship Analytics for Value Enhancement) proposes a generalized business case for addressing social and environmental issues. The academic research has identified six discrete business drivers affected by non-financial stakeholder relationships. We consider how relationships with supply, demand and contextual stakeholders individually may affect each of the six business drivers, positively or negatively.
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Executive summary: Creating value through networks

The modern corporation is a network whose value arises from the relationships among its various stakeholders. Stakeholders create value, derive benefit, and may also suffer harm through their interactions with the corporation. Companies achieve excellence by responding appropriately to stakeholder concerns, which mitigates risk and opens up potential opportunities. The ability to do this consistently requires identifying key stakeholders; understanding their concerns; and evaluating how these concerns may impact the business.

This report outlines a method for developing specific and holistic business cases for corporate excellence in stakeholder relations by understanding both (1) how these stakeholder relationships may affect company financial performance and (2) which stakeholder issues are salient at any point in time. Our method entails thoughtful and ongoing engagement with shareholders, using the following three analytical tools.

1. The “Shareholder Alignment Frontier™”

Companies may struggle to make sense of a cacophony of conflicting stakeholder demands, or they may assume that a lack of explicit stakeholder criticism signals universal support. They may succumb to “group-think” and minimize the relevance of stakeholder demands until it is too late, or they may overreact to loud but ultimately ineffectual gadflies.

Among stakeholders, the interests of shareholders are most closely aligned with those of companies. We introduce the Shareholder Alignment Frontier™, a method for identifying public issues that are relevant for corporate performance through ongoing dialogue between management and long-term shareholders.

Engaging with shareholders is an indispensable tool of corporate governance. Shareholder dialogue serves several functions, including:

- **Framing** external public issues for companies and **sensitizing** management to the importance of these issues;
- Encouraging companies to **integrate** public issues into **internal** company discussions;
- Enabling management to **explore solutions** to public issues in a neutral and safe environment; and
- Providing **external assessment** of company responses.
Corporate stakeholder relations are dynamic, and issues may evolve alongside technology, scientific knowledge, cultural attitudes, and politics, as well as company strategies and operations. The correct response to stakeholder issues depends in part on where in its lifecycle the issue resides.

We adapted our **Issue Lifecycle Model** for a financial perspective from a tool developed by Novo Nordisk to measure the maturity of issues from a societal perspective (summarized in a classic article by Simon Zadek of AccountAbility¹). The stages are:

- **non-financial** (of importance to neither companies nor stakeholders);
- **pre-financial** (of concern to stakeholders but not companies);
- **transitional** (of strategic importance to both companies and stakeholders); and
- **financial** (of operational importance to companies, but no longer a priority for stakeholders).

2. **The BRAVE Matrix™**

The academic research has identified six discrete business drivers affected by non-financial stakeholder relationships: Cost, Risk, Sales and Pricing Power, Reputation, Attractiveness as an Employer, and Capacity to Innovate. We consider how relationships with supply, demand and contextual stakeholders individually may affect each of the six business drivers, positively or negatively. A holistic examination of each of 18 potential business value drivers can help companies identify where their priorities should lie.

Readers will note we have peppered this report with real-life examples of “shareholder engagement in action.” These stories are true, but we have changed identifying details to maintain confidentiality.

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Introduction: Times have changed

Henry Ford and Steve Jobs, active a century apart, dominated their firms and came to personify for many people the innovative spirit of their eras.

In 1915, Henry Ford began to purchase land in Dearborn, Michigan, for the River Rouge Plant, the first step toward realizing his vision of 20th century manufacturing. Ford hoped the plant would achieve complete self-sufficiency by allowing him to control all of the resources that went into the production of automobiles, with “raw materials coming in on one end of the Rouge plant and the finished cars going out the other end.”

The River Rouge plant, fully operational in 1927, exemplifies an early 20th century business model of centralized management control, standardized production processes, and limited product lines. The plant enabled Henry Ford to realize his vision of bringing affordable transportation to the mass market. Although his authoritarian style would eventually put the company at risk, Ford’s achievement solidified his reputation as one of the most important management innovators of the early 20th century.

The 21st century corporation: all about relationships

Fast-forward 100 years. Apple Computer is the largest company by market capitalization and for many people the icon of 21st century innovation. Apple owns few manufacturing plants, controls no natural resources, and offers a sprawling product line that ranges from watches and TV systems to an online media “store” that also connects to other businesses that will recommend movies, help you to find long-lost friends, or tell you how to fix your kitchen sink.

Apple is the product (and in many ways the creator) of an information revolution. Instantaneous and basically free global communication reduces the benefits of hierarchy and centralized control and enables the evolution of corporate structures and business models. While physical assets made up much of the value of Ford Motor Company in 1915, investors in 2015 are willing to pay 6-7 times Apple’s book value even though most of that value is intangible: the skills and knowledge of its workforce; its brand; its supplier relationships; and even its customer value proposition, which is not so much specific products or services as comprehensive solutions connecting consumers to the information that they want.

2 http://www.pbs.org/wgbh/amERICANEXPERIENCE/features/timeline/henryford/
One trait that Apple did share with the early Ford Motor Company — until recently — was its leadership style. Just as Henry Ford controlled his namesake company for much of its early history, Steve Jobs dominated the governance and management of Apple and rarely allowed his decisions to be influenced by outside voices. Jobs’s successor, Tim Cook, has slowly begun to adopt a different tone with outside stakeholders. In the past few years, the company has:

- Agreed to heed activist investor calls by buying back a total of $200 billion in shares by 2017;
- Yielded to shareholder calls to adopt corporate governance reforms that open management to greater accountability, such as electing directors by majority vote;
- Responded to concerns about working conditions at its Chinese contract suppliers by developing policies and practices to protect employees of these companies;
- Reportedly fired a top executive for refusing to publicly apologize for the company’s widely criticized Maps program, a gesture that would have been unlikely under Steve Jobs.

Few governance experts would consider Apple Inc. to have consistently embraced best practices for accountable governance. However, these examples demonstrate how even the most successful and internally directed companies have recognized the need to become more open to external voices.

Figure 1: The evolution of the quintessential corporation

<table>
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<tr>
<td>Capital-intensive investment in…</td>
<td>Innovative workforce located…</td>
<td>Intangible assets comprise 80% of corporate value</td>
</tr>
<tr>
<td>Dearborn, MI to operate…</td>
<td>All over the world, relying upon…</td>
<td>Globalization of finance, production, research, marketing and distribution</td>
</tr>
<tr>
<td>One vertically integrated factory that produced…</td>
<td>Partnership with contract suppliers to produce…</td>
<td>Vertical dis-integration and re-engagement of supply chains</td>
</tr>
<tr>
<td>Model T’s, managed by…</td>
<td>Diversified, but integrated, solutions connecting customers to the information they need…</td>
<td>Horizontal integration of complementary product lines focused on creating customer solutions</td>
</tr>
<tr>
<td>Communication though personal interaction and management hierarchy that was…</td>
<td>Produced in public view, resulting in the company becoming increasingly responsive to…</td>
<td>High degree of public scrutiny and engagement</td>
</tr>
<tr>
<td>Dominated by one man.</td>
<td>Pressure for reform from shareholders.</td>
<td>Broad and assertive shareholder base</td>
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</table>

Source: Cornerstone Capital Group
Just as Ford Motor Company was the archetypal 20th century company, Apple today is the embodiment of the 21st century company. It is the quintessential networked corporation, whose value proposition lies not in physical assets, particular products or even specific skills, but in the quality of its relationships.

**From “machine” to “network”**

Whereas at one time corporations could be compared to machines, today they are better understood as networks. Companies create value not solely through individual effort, but rather through the interactions of network members — their stakeholders. Company behavior is not dictated from an omnipotent “top,” but results from the individual decisions of all stakeholders, which have both self-interested and social motivations. Understanding how these interactions influence company financial and operating performance can yield important strategic insights for companies and investors.

Traditionally, stakeholder relations have been understood as the static result of arms-length negotiation, codified into contracts and enforced by laws and regulations. In an efficient market, these negotiations would guarantee the fair representation of each stakeholder’s interests, the resolution of all conflicts in advance, and expectations of each participant to be made clear.

While this approach works well overall, the market is not perfectly efficient. Short-term thinking may obscure long-term interests; groups not included in agreements may nevertheless experience harm or benefit from corporate activities (“externalities”); certain stakeholders may consider an outcome unfair because of a perceived or actual power imbalance (e.g., seemingly undue influence over government policy); some stakeholders may engage in “rent-seeking” behavior (i.e., aiming to increase one’s share of existing wealth without creating new wealth); circumstances may change so that previous agreements are no longer perceived to be reasonable; or governments may be unable or unwilling to enforce agreements.

In short, the “rational” market fails to fully capture the dynamics of the long-term, informal relationship between a company and its stakeholders, which can have significant financial implications. A holistic understanding of how stakeholder relations impact a company’s unique circumstances can help to build a comprehensive and multi-faceted business case for systemically integrating stakeholder welfare concerns into business planning.
We adapt the categories established by prominent investment manager and sustainable finance scholar Lloyd Kurtz\(^3\) to help map key stakeholder relationships (see Figure 2). We address those relationships later in this report.

**Figure 2: Key stakeholder relationships**

![Key stakeholder relationships diagram]

Source: Cornerstone Capital Group

### Financial stakeholders

While most people assume that the primary function of the financial markets is to supply capital for business investment, this is mostly untrue in practice, at least for large listed companies. For the past several years, U.S. companies have been net buyers of their own shares, while business investment has lagged cash inflows net of dividends and new debt has slightly exceeded net buybacks of shares. In other words, while earnings are sufficient to fund business investment, increase retained earnings and pay dividends, companies have issued new (cheap) debt primarily to purchase their own shares. (Financial capital remains an important source of business investment and liquidity for new and small businesses, however.)

Shareholders’ primary role has become the oversight of corporate boards and management both through the price discovery function of the equity markets and through direct monitoring via proxy voting.\(^4\) Many investors that engage in


Shareholder engagement in action:

A large energy company reaches out to one of its biggest shareholders to better understand why more than half of shareholders voted against the CEO’s pay package. After implementing the shareholder’s recommendations, the company receives a vote of over 90% in favor of its compensation plan at the next annual meeting.

Despite these complexities, long-term shareholders as a whole have a common interest in promoting corporate governance that aligns company decision-making with long-term financial performance, regardless of the interests of the control group. Because shareholders lack direct access to board decision-making, they rely on company disclosures and direct engagement with management and boards to evaluate the quality of firm corporate governance. Corporate financial disclosures provide insights into how corporations make strategic decisions and on whose behalf these decisions are made. Sustainability reporting sheds light on how thoughtfully the company considers the link between its relationships with stakeholders and the long-term interests of the firm. Beyond public disclosures, the quality of the firm’s engagement with shareholders and other stakeholders can provide additional information about firm governance.

Shareholder alignment frontier™

While shareholders differ in time horizon and risk tolerance, and numerous agency conflicts exist within the investment value chain, companies tend to have a shareholder base that broadly aligns with their overall corporate strategy; companies with long-term strategic goals tend to attract shareholders with long-term investment horizons.

Recognizing that shareholders will vary in their motivations, capabilities and expertise, companies will derive optimal benefit by engaging with a diverse group of shareholders. The ideal shareholder dialogue group will, in aggregate,
have a relatively large and long-term stake in the company (though it may include some individually small investors); represent a diversity of perspectives, including “mainstream” investors and “thought leaders;” will respect the roles of shareholders, boards, and management; and will approach dialogue with professionalism and a spirit of cooperation.

Shareholders should not seek to dictate policy to management or to micro-manage corporations, which would be impractical for diversified investors and undermine the separation of ownership and control. Instead, dialogue should be perceived as a mutual and ongoing learning process for shareholders and companies.

While the perspectives of management and shareholders might initially differ, it is reasonable to expect that honest and open dialogue would eventually produce an agreement about priority issues and strategies for addressing them. We refer to this convergence as the “Shareholder Alignment Frontier™.” A consistent failure of shareholder and company perspectives to converge over time might signal concerns about company strategy or governance.

In contrast to the topics typical of analyst calls, which emphasize specific business decisions or financial results, shareholder dialogue is concerned with fundamental questions about corporate governance, which we define as the relationships among stakeholders used to determine and control the strategic direction of the company. Below we outline the major topics for shareholder dialogue.

<table>
<thead>
<tr>
<th>Fundamental corporate governance questions</th>
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<tr>
<td>1. Do board policies, as well as the qualifications and diversity of its members, provide confidence that the board of directors is not just formally independent of management, but can also exercise objective, independent judgment?</td>
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<tr>
<td>2. Do compensation disclosures demonstrate a clear understanding of how executive compensation will establish the incentives of top managers? Does compensation align management interests with the long-term interests of shareholders? Does the plan provide appropriate incentives to consider the reasonable interests of stakeholders?</td>
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<tr>
<td>3. Do shareholders have meaningful avenues of input into company governance? Do governance policies provide reasonable opportunities to remove underperforming directors, or effect a change of control? Does the company engage in dialogue with shareholders on a regular basis? Are board members in contact with shareholders?</td>
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<tr>
<td>4. Does the company have a strategic approach to addressing sustainability issues? What do company disclosures indicate about the importance of stakeholder relationships to that strategy? Which stakeholders are most important?</td>
</tr>
<tr>
<td>5. Are company disclosures clear, meaningful and accurate? Does the company have systems in place that inspire confidence in its reporting?</td>
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Adapted from “Corporate Governance: Why it matters for strategy and ethics,” By Harry Van Buren III, Anderson School of Management, University of New Mexico, (unpublished presentation, available http://tinyurl.com/ogmzrk2).
Dialogue with long-term investors also contrasts with shareholder activism. Activist investors target companies with shareholding and proxy vote pressure to drive major strategic or leadership change, hoping to generate higher returns for their investments in these companies. HFR, a firm that tracks the industry, says that the activist investment strategy is growing in popularity with investors, with total assets now at nearly $130 billion\(^8\), an amount that signals their growing influence in board rooms and at annual general meetings.

Activists can force change at companies only when they can rally the support of other shareholders and win their support on proxy ballots or trading decisions. Companies that cultivate relationships with their long-term shareholders will find a more open audience during defenses against activism. Moreover, ongoing dialogue with shareholders and other stakeholders may help management to avoid the kinds of issues that attract activists in the first place.

The benefits of shareholder dialogue for companies can be identified as follows:\(^9\)

**Framing and sensitizing.** Any organization is vulnerable to cognitive biases and “groupthink.” Closed corporate cultures that fail to incorporate outside perspectives may be exposed to “blind spots” about stakeholder risks and opportunities. Shareholders can help to ensure that the company understands how stakeholders define and frame issues and can provide a credible, unbiased and independent assessment of the salience of societal issues to outside stakeholders. Effective shareholder dialogue can provide an “early warning system” to companies regarding these concerns.

**Integrating internally.** External dialogue encourages companies to incorporate shareholder and stakeholder perspectives into internal business planning discussions. This is important because many potential internal advocates within companies may be less hesitant to speak up if they have the implicit support of the company’s shareholders. Shareholders also provide important framing questions for internal debate.

**Exploring solutions.** By respecting confidentiality and emphasizing the natural alignment of their interests, shareholders and companies can establish trust that enables a frank exchange of views. Shareholder dialogue can be a venue for company management to explore possible solutions to stakeholder concerns and receive shareholder feedback without fear of reprisal or other negative consequences.

**Assessing externally.** Successful implementation of a stakeholder strategy should include periodic review to determine whether company efforts have had

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\(^8\) Barron’s, “Activist Hedge Funds Draw Big Inflows and Some Worries,” May 22, 2015.

\(^9\) For a similar and more detailed perspective, see “Understanding Voice: Mechanisms of Influence in Shareholder Engagement,” by Fabrizio Ferraro, IESE Business School and Daniel Beunza, London School of Economics, January 24, 2013.
the desired result. Shareholders will test the company's strategies and internal processes to address societal issues. A particular focus of dialogue at this stage is the quality and effectiveness of corporate transparency and disclosure regarding its policies, practices and performance.

Shareholder engagement in action:

By the 1990s, many footwear and apparel companies were outsourcing most of their production to developing countries. The companies assigned full responsibility for production to their contract suppliers in order to allow the brands to focus on their own core competencies, namely design and marketing. At first, the managements of the brand companies were unprepared for activism regarding the labor rights of those making their products, which they regarded as the responsibility of the contract supplier.

Shareholders reframed the issue, to help managements understand that many stakeholders, particularly customers, believe that brands remain ethically responsible throughout the product lifecycle for products bearing their names.

Shareholder dialogue also helped to sensitize managements to the importance of potential violations of labor rights to many of their customers. Some managers assumed that concerns about “sweatshops” were driven primarily by anger in the U.S. over foreign competition for manufacturing jobs. Shareholders stressed that many labor advocates welcomed the economic development benefits of these factories, but had strong concerns about the working conditions and safety.

Continued engagement, including through the mechanism of shareholder proposals, encouraged companies to integrate the issue into internal company discussions. In initial dialogues with shareholders, companies often struggled to provide responses to shareholder questions. Companies initiated internal conversations about these issues, if only to have better answers. Eventually, internal advocates within companies pointed to shareholder concerns as a rationale for the need to address the issue.

As companies began to recognize the need for action, shareholders served as a confidential and trusted sounding board for management as they explored possible solutions. For example, shareholders provided feedback about what entities would be the most credible monitors of factory compliance.

Over time, companies developed systems to address labor rights concerns. Continued dialogue with shareholders has served as a valuable external assessment tool, in some cases leading companies to adapt and change their strategies in response to shareholder feedback. Finally, in discussions assessing their solutions with shareholders, many companies came to acknowledge that their solutions were not always effective, and restarted the exploration process.
**Prioritizing stakeholder issues: the lifecycle model**

Which issues matter? Which stakeholder relationships matter? How should companies prioritize the competing demands of stakeholders?

Companies need to carefully consider which stakeholder issues will be a priority for policy and action, since not all issues that may be of concern for some stakeholders will matter for the company’s financial or operating performance.

Many leading companies map issues according to their importance to stakeholders and their importance to management. Those that are important to both stakeholders and the company become the priority issues for strategic consideration. The map may look something like Figure 3.

While this approach is useful, it implies that stakeholder views are considered important, but that company interests are separate and independent of outside stakeholders. However, issues that are serious concerns for stakeholders often become business issues eventually, especially if those issues affect the relationship between a company and its key stakeholders.

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**Figure 3: Prioritizing stakeholder issues**

**Figure 4: Introducing the “Shareholder Alignment Frontier™”**

Source: Cornerstone Capital Group
A comprehensive approach for understanding of the dynamic between stakeholders and companies would also include:

- An explanation of how stakeholder views influence company priorities.
- A procedure for identifying priority issues.
- Appropriate guidelines for addressing issues that are not priorities for stakeholders and companies simultaneously.
- Insights into how priorities can change over time.

Companies may interpret disagreement with stakeholders as reflective of their differing interests or lack of mutual understanding, but persistent disagreement can also help to identify an emerging risk or opportunity that the company may not have identified otherwise.

Shareholders can serve as a useful resource in such a process, because they are independent of the company while having an interest in long-term performance which aligns with the companies’ goals. By incorporating the “Shareholder Alignment Frontier™” into the stakeholder map (Figure 4), over time companies and shareholders should come to agree about whether issues are important or not because of their common interest in long-term financial value.

Issues and stakeholder groups may emerge and fade over time, as companies adapt strategy and operations to evolving business contexts. The influence of an issue on the stakeholder-company relationship will differ at each point in its evolving lifecycle.

For companies, issues become important, demanding strategic attention from the board and management, when evolving norms and expectations have created a business case for action, but there is not yet an accepted procedure for managing the issue. For stakeholders, issues are important to the extent that they believe a company’s behavior is affecting them in some way and that the company has the power to address their concerns. It is important not to confuse issues that are meaningful for society (marriage equality or public education policy) with issues that strategically impact companies (such as labor conditions).

Our lifecycle model is influenced by a tool developed by Novo Nordisk to measure the maturity of issues from a societal perspective, summarized in a classic article by Simon Zadek of AccountAbility. The stages of our issue lifecycle are shown in Figure 5.

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Shareholder alignment through the issue lifecycle

Companies depend on key stakeholders for success, and their potential opposition is a source of risk. Companies that regularly engage key stakeholders will likely be more aware of emerging issues, find more openness to their own perspectives on issues, and create trust that can be drawn upon in times of crisis, especially in support of the company against more hostile stakeholders.

Numerous organizations, including the Sustainability Accounting Standards Board (SASB), Global Reporting Initiative and the International Integrated Reporting Council, have developed lists of issues of concern for particular sectors. While these resources are useful, ultimately each company must determine how particular issues affect its business strategy and operations.

Over time, successful stakeholder dialogue will lead companies and stakeholders to converge somewhat in their understanding of which issues matter to companies. Stakeholders and companies will never be perfectly aligned in their understanding of issues, because stakeholders have different interests than...

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Please see important disclosures at the end of this report.
companies and because stakeholders themselves may be in conflict (e.g., U.S. workers compete with foreign contractors for jobs). However, companies with good stakeholder relations will find that the relative importance of different issues is similar for stakeholders and companies.

Figure 6 illustrates how over time, issues may evolve in importance from non-financial to financial. Each issue is plotted according to its relative importance to stakeholders and companies. Issues reside inside the red band when companies and stakeholders largely agree on the importance of the issue, indicating that engagement has been successful. Where issues reside outside of the red band, companies are out of alignment with stakeholders, indicating that more dialogue is needed. The red band is wide to indicate that stakeholders and companies may never fully agree on the issue.

**Figure 6: Completing the “Shareholder Alignment Frontier™”**

The “Shareholder Alignment Frontier™” represents areas of agreement (more or less) between stakeholders and companies.

Shareholders (i.e., financial stakeholders) can help companies make sense of this conflicting information. While managers and boards have the best information about their specific business circumstances, investors may have a clearer perspective on the macroeconomic reality, as well as societal trends, by virtue of their investment in a broad portfolio.

This does not imply that companies should merely follow the lead of their shareholders. Thoughtful shareholders listen to the companies and prefer to defer to companies’ expertise. Their role is to evaluate, and when necessary
challenges management thinking about stakeholder concerns. While companies and shareholders may start out at very different positions regarding issues, successful ongoing dialogue between these two points of view can help both sides converge on a more complete shared understanding of the relevant issues and how to resolve them than either could achieve alone.

Deviation from the shareholder alignment frontier may indicate a need for continuing dialogue to resolve emerging issues (above and to the left), or it may be the sign of an agency conflict or poor corporate governance (below and to the right). For shareholders, a primary metric for alignment will be the quality of company disclosures. Agreement between shareholders and companies on the need for action (on the line) may identify areas of potential collaboration.

**Managing issues: the example of climate change**

Following is a discussion of how leading companies might address issues at each point in their life cycle, using the issue of climate change as an example.

**Non-financial issues**

Throughout the 1980s, as the science of climate change began to take shape, Congressional hearings began to shed light for the most engaged members of the public on this emerging, but still inconclusive scientific phenomenon. For companies and their shareholders, this issue failed to rise to a level of concern. Nevertheless, some far-sighted investors began to wonder what the long-term impact of the issue might be.

Devoting significant resources to addressing non-financial issues is probably a waste of company resources. However, monitoring these issues and occasionally checking in with opinion leaders can help to avoid surprises.

**Pre-financial issues**

In the 1990s, companies began receiving shareholder proposals on climate change. The proposals received limited support from mainstream shareholders, and most companies resisted taking decisive action on the issue. To the extent that companies engaged with shareholders, they usually preferred to debate the science rather than discuss the business implications.

At the time, the scientific consensus regarding greenhouse gases (GHGs) was beginning to solidify. Moreover, it had become clear that large corporations, both in the energy sector and elsewhere, were responsible for a significant share of emissions. The policy environment was shifting with the adoption of the Kyoto Protocol, but despite all of this, for many companies the issue did not yet rise to the level of a strategic concern.
At this stage, shareholders were *framing and sensitizing* management to the importance of the issue. While some corporations preferred to delay action until absolute proof could be established (and funded front groups to cast doubt on the science), shareholders proposed that management adopt a precautionary approach. They encouraged companies to engage in internal dialogue (*integrating internally*) on the issue, and to engage in scenario planning to anticipate potential business impacts, if only to understand how eventual climate policy may ultimately impact their businesses.

By the end of the 1990s, most non-energy companies had ceased denying the science of climate change, leading companies began to actively engage with coalitions (such as CERES), and a growing number of companies began collecting and reporting on operational GHG emissions.

From a shareholder perspective, companies should anticipate *pre-financial* issues and be ready to respond if and when they become relevant for shareholder value. Shareholders will examine company disclosure of *pre-financial* issues to evaluate the company’s understanding of the issues, and whether the company appears to be gathering information that may help it analyze the potential long-term performance impact, if any. Shareholders raise awareness and focus management attention on key issues. Where company disclosures are lacking, shareholders might pose directed questions to better understand management’s perspective and address any information gaps. For laggards, shareholders may use shareholder proposals to ask for disclosures of data about these issues.

Through dialogue, shareholders and companies may determine that an emerging issue lacks resonance (return to *non-financial*) or that it requires greater strategic attention (move to *transitional*).

**Transitional**

By the 2000s, the business case for addressing climate change had grown clearer for many industries. The Kyoto Protocol to reduce emissions had come into force in many countries (though not the U.S.), and companies began to anticipate greater public expectations for action to mitigate climate change over the long term. Though many companies expressed concern about the potential costs and feasibility of reducing greenhouse gases, technological advances had boosted the business case for resource efficiency as a cost-saving measure.

The key subject of shareholder proposals on climate change was that companies disclose their GHG emissions. Reporting standards, such as the World Resources Institute Greenhouse Gas Protocol, began to emerge, providing companies with a standardized means of disclosure. Shareholder dialogue often centered on technical issues, such as whether to report on an intensity or absolute basis.
As the decade progressed, activism on the issue became increasingly assertive, culminating in the current campus divestment campaign. Companies began to set GHG reduction targets at the urging of shareholders. Others began to explore business opportunities based on the issue, such as trading carbon credits or developing products to enable others to reduce emissions.

At this point, the role of shareholders was a combination of exploring solutions and integrating internally, as companies began to experiment with climate change mitigation strategies that were also consistent with overall business strategy. Companies exhibited a great diversity in responses, from outright denial to creative solutions that engaged employees, customers and shareholders.

Transitional issues are somewhat fraught for shareholders and companies, but offer opportunities as well. Transitional issues are ones for which the business risk or opportunity is being developed and better understood, but norms and expectations for companies are not yet fully accepted. Therefore, some companies may see business opportunity in taking a leadership position, while laggards may be unaware of risks that they face.

Shareholders will be interested to know whether companies are fully aware of the business case for addressing transitional issues, whether risks and opportunities are actually relevant for the company’s situation, and whether the company is a leader or laggard in developing solutions. Shareholders will serve as sounding boards for company plans to manage the issue and will be a source of feedback for the company regarding stakeholder expectations and what peer companies are doing. Shareholder proposals may address company plans to resolve concerns, and forward-thinking investment managers may reward leaders with higher valuations.

Financial issues

It would not be correct to say in 2015 that climate change has fully emerged as a financial issue, since a global climate reduction regime is not in force. However, companies are forced to contend with the emergence of a sprawling array of local, regional and international rules and norms surrounding climate change.

Many firms have established strategic business cases for addressing climate change. These diverge significantly according to industry: stranded asset risk for the extractives; smart grids and distributed energy for utilities; fuel economy requirements, electric vehicles and fuel cells for automotive; energy efficiency and green building for real estate; and so on.

12 See http://350.org for example.
In 2015, shareholders continue to play the roles of framing and sensitizing (when necessary), and exploring solutions and integrating internally for companies that are struggling to adapt to quickly evolving public expectations. Increasingly, companies are relying on shareholders for external assessment, to provide feedback on company strategies as they evolve. As carbon regulations continue to come into force, shareholders will emphasize the need for companies to innovate in response to public policy initiatives, not simply to oppose all new regulation.

Financial issues should no longer be strategic issues for the company because they should now be embedded in business planning and operations. At this stage, investors will expect that company disclosures include policies, descriptions of process, and performance measures and goals. The role of shareholders regarding these issues is to monitor performance for any concerns. For significant laggards, shareholders may use the proxy ballot to effect governance changes, including withholding support for compensation plans and director nominations. Valuations may be impacted by a failure to implement effective business plans to address these issues, particularly if the result is a significant legal or regulatory sanction.

Corporate relationships and corporate performance: The “BRAVE Matrix™”

The strength of the business case determines whether and how quickly an issue moves through the stages of its lifecycle. Leaders derive value from anticipating, and in some cases assisting, the emergence of these business cases. Leading companies create competitive advantage through an understanding of how relationships with specific stakeholders drive shareholder value.

Figure 7 summarizes our analytical method for evaluating the business risks and opportunities related to stakeholder relations. We consider how the company’s relationships with demand, supply, and contextual stakeholders might influence six common drivers of financial performance. The resulting matrix provides a comprehensive rationale for action on stakeholder concerns. Please note that the matrix is intended as a method of inquiry, not an exhaustive list of possible business cases.

Below, we discuss each of the six business drivers, the three stakeholder groups (Demand [customer], Supply [labor and other], and Contextual [communities, etc.], and provide an example of how the matrix can be used.
Figure 7: BRAVE Matrix™

<table>
<thead>
<tr>
<th>Business Value Drivers</th>
<th>Demand Stakeholders</th>
<th>Supply Stakeholders</th>
<th>Contextual Stakeholders</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost/cost reduction</td>
<td>Retention vs. churn</td>
<td>Turnover vs. productivity</td>
<td>Operational efficiencies vs. cost of</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>compliance</td>
</tr>
<tr>
<td>Risk/risk reduction</td>
<td>Liability, emergence of substitutes</td>
<td>Work continuity vs. stoppages; supply</td>
<td>Resource availability; accidents</td>
</tr>
<tr>
<td></td>
<td></td>
<td>constraints</td>
<td></td>
</tr>
<tr>
<td>Sales and pricing power</td>
<td>Premium pricing</td>
<td>Motivated sales force</td>
<td>Regulatory burden, speed to market</td>
</tr>
<tr>
<td>Reputation/brand equity</td>
<td>Boycotts vs. identity marketing</td>
<td>Ongoing labor relations</td>
<td>Social license to operate</td>
</tr>
<tr>
<td>Attractiveness as employer</td>
<td>Attract, retain and motivate talent by enabling</td>
<td>Attract, retain and motivate talent</td>
<td>Attract retain and motivate talent by</td>
</tr>
<tr>
<td></td>
<td>meaningful work</td>
<td>by establishing trust and loyalty</td>
<td>aligning with personal values</td>
</tr>
<tr>
<td>Capacity for innovation</td>
<td>Anticipate evolving customer needs</td>
<td>Operational learnings, entrepreneurial</td>
<td>Organizational learning; early warning</td>
</tr>
<tr>
<td></td>
<td></td>
<td>culture</td>
<td>system</td>
</tr>
</tbody>
</table>

Source: Cornerstone Capital Group

Business value drivers

Reviewing the business literature, sustainability expert Stefan Schaltegger and his co-authors find that all of the “business cases” fall into six categories. We discuss them here, listing them from most tangible to least tangible (Figure 8) and providing examples.

Figure 8: Summary of business value drivers

<table>
<thead>
<tr>
<th>Business value driver</th>
<th>Relevance to business case</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost/ cost reduction</td>
<td>By improving the efficiency and productivity of the use of human and natural capital, companies can sustainably lower costs.</td>
</tr>
<tr>
<td>Risk/ risk reduction</td>
<td>Very often the pressure to cut costs in the short-term increases risk. Risk may be technical, political, market, or societal.</td>
</tr>
<tr>
<td>Sales and pricing power</td>
<td>Investments in human capital and sustainable inputs may result in higher quality products (and the perception thereof), which can help improve sales and margins.</td>
</tr>
<tr>
<td>Reputation/brand equity</td>
<td>While reputation is usually associated with the strength of consumer brands, in fact companies may have different reputations with different stakeholders. Each can have a profound impact on the company’s ability to form productive relationships both with its employees and with external stakeholders.</td>
</tr>
<tr>
<td>Attractiveness as employer</td>
<td>Companies that offer opportunities for advancement, that demonstrate a commitment to employees' well-being, that provide meaningful work opportunities, and that are perceived to benefit society as a whole have an advantage in attracting and motivating talent.</td>
</tr>
<tr>
<td>Capacity for innovation</td>
<td>Sustainability challenges present entrepreneurial opportunities for companies who are aware of them. Moreover, creating a business culture of sustainability can also drive innovation within a firm.</td>
</tr>
</tbody>
</table>

Source: Cornerstone Capital Group

Cost

Over the last several years, real estate companies have embraced energy efficiency and “green building.” While these programs provide many benefits, the most tangible benefit is an increase in cost efficiency. However, until pressed by shareholders, tenants and municipalities to manage their environmental impact, many real estate companies failed to take advantage of these opportunities. The reason was an absence of management systems, including, in some cases, the ability to capture cost savings in return-on-investment calculations.

At its most tangible level, unsustainable business practices are wasteful of both human and natural capital. By improving the efficiency and productivity of their resource use, companies can sustainably lower costs.

Risk

Extractive industries have long faced conflicts with local communities over environmental impact, working conditions and cultural differences. Beginning in 2011, the United Nations and Harvard University undertook a study on the financial impact of these conflicts on extractive companies, and found that the total financial impact was material for financial performance. Some companies were unaware of this materiality because the accounting for these costs were often spread across different business units (legal, operations, security, lost revenues etc.) and never aggregated until the question about the cost of conflict was posed by outsiders. Since that time, many companies have begun to mitigate risk by investing in conflict resolution before entering communities.14

Very often the pressure to cut costs in the short-term results in an increase in risk. For example, failing to invest in safety may reduce expenses in the short-term while increasing the likelihood of catastrophe later on. Risks may be technical, political, market, or societal in nature. Note the distinction between a strategic focus on cost efficiency and reactive, formulaic cost-cutting during downturns.

Sales and Pricing Power

In a March 2015 report, (“The Economics of Automation: Quick Serve Restaurant Industry”) Cornerstone Capital Group analysts Michael Shavel and Andy Zheng15 demonstrated that restaurant companies that invest in human capital through higher wages enjoy higher revenues and margins even though costs are higher, and may be better positioned to take advantage of emerging opportunities to automate the ordering process. Many of these companies also source their

ingredients sustainably as well, which is perceived positively by affluent consumers.

Investments in human capital and sustainable products may result in higher quality products (and the perception of higher quality products) that can help improve sales and margins.

**Reputation:**

Corporate reputation is not a simple concept. Wal-Mart has long been known for its innovative use of technology, a frugal culture, and above all for offering affordable products to low-income consumers. More recently, it has become known as a leader in environmental performance.

At the same time, Wal-Mart’s recent well-publicized wage increase is its latest effort to address its longstanding reputational problems relating to workforce and suppliers, following on its significant environmental program as well as earlier improvements in workforce diversity.

Reputation may be an intangible asset, but for Wal-Mart its impact is not unmeasurable: A 2005 study indicated that 2-8% of consumers would not shop at Wal-Mart because of “the negative press they have read”; the company continues to experience difficulty opening new stores in the U.S. because of community opposition; and even as early as the 1990s, it faced a class-action suit from its own employees over gender discrimination. As of June 2015, Wal-Mart reports that it has experienced lower turnover since the wage increase took effect.

The perception of a company’s relations with stakeholders may have implications for its ability to do business. While reputation is usually associated with the strength of consumer brands, in fact companies may have different reputations with different stakeholders. Each set of stakeholders can have a profound impact on the company’s ability to form productive relationships both with its employees and with other stakeholders.

**Attractiveness as employer**

Motivating and retaining employees is a core strategy at Starbucks. The company does so by combining ongoing team-building programs and a strong customer service ethic with generous employee benefits. The company also considers its social responsibility efforts, including both cause-based marketing and responsible sourcing, to be part of its personnel management strategy. The strategy may appear counterintuitive, because its primary beneficiaries are “baristas” who serve food and drink to customers, often considered a low-skill, low-status and high-turnover occupation. Starbucks, however, has invested in

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**Shareholder engagement in action:**

After receiving high votes on shareholder proposals relating to predatory lending, a bank collaborates with its shareholders to develop policies and procedures to ensure fair lending practices for its sub-prime mortgage lending business. Although overall the bank is battered in the 2008 financial crisis, its mortgage lending operations produce few “toxic loans” and remain relatively healthy.
their baristas because they are the public face of the company, and therefore essential to creating and maintaining the company brand.

Companies compete on talent, most obviously at the professional and executive levels but, as in the case of Starbucks, at every level of the corporation. People are only partly motivated by money. Research consistently demonstrates that companies which offer opportunities for advancement, demonstrate a commitment to employees’ well-being, provide meaningful work opportunities, and are perceived to benefit society as a whole have an advantage in attracting and motivating talent.

**Capacity to innovate:**

Nike’s efforts to improve the working conditions in its suppliers’ factories have historical roots in activist claims that the company was running “sweatshops.” But today, increased engagement in its supply chain is an integral part of the product and materials innovation strategy for its apparel business. Nike recognizes that its high-tech vision for its clothing line requires modern, well-managed production facilities capable of working with advanced materials. These operations are well within the capabilities of manufacturers in developing countries with the right level of support and resources, and they require engagement with a skilled workforce, who may themselves drive key innovations. This kind of employee relationship is incompatible with the maltreatment of workers.

Sustainability challenges present entrepreneurial opportunities for companies who are aware of them. Moreover, creating a business culture of sustainability can also drive innovation within a firm.

**Stakeholders**

The first step in stakeholder management is to identify the key stakeholders and understand how these relationships affect business value. We adapt the categories established by Lloyd Kurtz, found in Figure 9, to help map key stakeholder relationships.

In a purely transactional relationship, each party may seek to negotiate the best possible outcome for itself at the lowest possible cost, with little explicit concern for the welfare of the other stakeholders. In long-term relationships, win-win solutions (e.g. innovation) may result when both sides understand the interests of the other and seek to maximize total welfare, while lose-lose results (e.g. industrial accidents) may accompany systematic exclusion of some stakeholder.

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Opposition from key stakeholders can impede a company's progress

Concerns. Long-term organizational relationships require awareness and anticipation of how business decisions impact the welfare of affected parties.

Engaged and supportive stakeholders are essential for companies, while opposition from key stakeholders can impede a company's progress toward achieving its strategic goals. Each company needs to identify its key stakeholders according to its own particular situation, but all company operations are interactions between those who supply the company's products and services, those who demand those products and services, those who finance company operations, and groups that provide the operating context for the company.

Figure 9: Key stakeholder relationships

<table>
<thead>
<tr>
<th>Demand Stakeholders</th>
<th>Financial Stakeholders</th>
</tr>
</thead>
<tbody>
<tr>
<td>Consumers</td>
<td>Shareholders</td>
</tr>
<tr>
<td>Distributors</td>
<td>Bondholders, etc.</td>
</tr>
<tr>
<td>Franchisees</td>
<td></td>
</tr>
<tr>
<td>Users of free internet, etc.</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Supply Stakeholders</th>
<th>Contextual Stakeholders</th>
</tr>
</thead>
<tbody>
<tr>
<td>Employees</td>
<td>Government</td>
</tr>
<tr>
<td>Suppliers</td>
<td>Media</td>
</tr>
<tr>
<td>Contractors, etc.</td>
<td>Activists</td>
</tr>
<tr>
<td></td>
<td>Communities</td>
</tr>
<tr>
<td></td>
<td>Analysts</td>
</tr>
<tr>
<td></td>
<td>Environmental Ratings</td>
</tr>
<tr>
<td></td>
<td>Agencies, etc.</td>
</tr>
</tbody>
</table>

Who are they?

- Consumers of the firm's products, including individuals or institutional purchasers of final goods and services;
- Distributors;
- Franchisees; and
- End users who are not technically customers because they do not pay directly for services (particularly for media, internet or "sharing economy" companies).

Why does the relationship matter?

The quality of customer relationships has greater significance for company performance than the immediate purchase decision. Customers may decide to:
Promote the company brand (or boycott it);
Consider new products from the company (or seek substitutes);
Share personal information (or demand greater privacy protections);
Fulfill the terms of purchase agreements (or lack the capacity or willingness to do so); or
Remain loyal during crises (or join the opposition).

Moreover, social media and sharing economy companies are evolving new ways of relating to users and customers that are more dependent on customer trust and loyalty. (See our report, “Dissecting the Sharing Economy,” June 9, 2015.)

Among the stakeholder groups, customers are the best understood by most companies, at least in terms of the drivers of a purchase decision. Most companies perform extensive research on customer preferences and patterns of demand. Nevertheless, companies differ in their understanding and reaction to longer-term drivers of customer relationships. Investors can gain insight into long-term company performance by distinguishing immediate measures of customer demand, such as sales figures, from the ongoing relationships that companies are creating with their demand-side stakeholders.

- Does the customer consider all interactions with the company to be voluntary and consensual?
- What hidden costs, risks or benefits for the consumer are revealed over time?
- Since people often identify with brands whose products and services they consume, what is the impact of the brand on the customers’ perception of themselves?
- How does association with the brand impact customers’ relationships with others?

**Supply stakeholders**

Supply stakeholders include everyone who plays a role in producing goods and services, from board members, executives and other employees, to raw material suppliers. For purposes of our analysis, we divide the group into employees and non-employees.

**Employees**

Employees are the source of a company’s core competencies. Simply put, the more productive and innovative employees are, the more successful companies will be. As companies outsource non-core operations, they become increasingly levered to the employees that they retain. For example, the consumer electronics
company Vizio earns revenues of over $30 billion per year with a workforce of only a few hundred who oversee outsourced operations employing tens of thousands of manufacturing employees.

While job growth in the U.S. has fallen below the level of population growth over the last several years, the number of jobs considered “non-routine cognitive” — meaning, those that require talent — has doubled in the last three decades and continues to rise. However, as discussed earlier in the case of Starbucks, any employee can be considered strategically important.

Employees, in turn, are highly levered to companies. The employment relationship is mostly non-diversifiable, and opportunity costs in terms of forgone leisure or other employment opportunities may be significant. Employment is a source of both economic and non-economic benefits. The employees’ perception of these benefits may help to determine their engagement, which numerous studies show is a determinant of long-term company performance.

At a time when employee engagement is more important to companies than ever, the employment relationship grows more tenuous. Lifetime employment expectations disappeared decades ago, and other benefits that tie individuals to companies, such as health care and retirement benefits, are on the decline. New business models, such as those embodied by Uber and Lyft, which provide services through semiautonomous “driver-partners,” challenge traditional notions of the employee-employer relationship.

At the same time, the emerging cohort of workers expects non-monetary (non-transactional) benefits in addition to financial (transactional) compensation. Of the three top benefits younger workers value from employers, the top two are training and flexible work hours, with cash bonuses coming in third place. When asked what the most important factor indicating career success, only one in four identified high pay. More than half listed “meaningful work” or a “sense of accomplishment.”

We submit that companies known to provide exceptional products and services to customers, take care of their employees and maintain good relationships with all stakeholders will be better positioned to offer meaningful work and a sense of accomplishment to talented and motivated employees.

Why is the relationship important?

What do companies and investors need to know?

- How does the company evaluate the safety of its operations?
- How does the company measure the motivation, commitment to ethical behavior, and engagement of employees?

17 Data in this section is sourced from a presentation at the Internet Trends 2015 – Code Conference, by Mary Meeker, KPCB, May 27, 2015, pp. 94-114.  

Please see important disclosures at the end of this report.
Non-employee suppliers

Who are they?
Non-employee suppliers provide all of the services companies need outside of core competencies. They may include traditional supply chains, but also contract and contingent workers, security, logistics, back-office support, legal assistance and many others. The employees of some newer, lean companies may be responsible primarily for managing outsourced operations, as in the case of Vizio. Our discussion focuses on such labor-oriented suppliers.

Why is the relationship important?
The business case for outsourced and offshored supply chains is relative to other means of producing goods, either through home country outsourcing, insourcing, or automation.

Many companies, for example in the “fast fashion” industry, evaluate supplier relationships entirely according to short-term criteria including price, speed and reliability of shipment, and adherence to product standards. This approach has helped to bring down prices of certain items for consumers and create jobs in the developing world. However, as opposed to other options, including developing long-term supplier relationships and producing closer to developed country markets, this strategy entails risks including:

- Loss of manufacturing expertise that leads to new product and process innovation;
- Time-to-market lags in cases of operational disruption;
- Information costs;
- Infrastructure, labor and political risks; and
- Public criticism for “exporting” jobs.

Companies in many industries have argued that the reduced costs of supply more than compensate for these disadvantages. However, a growing awareness of the benefits of closer supplier relationships, improvements in automation technology, and some high-profile industrial catastrophes are changing the incentive structure for many companies.

Understanding supplier relationships can shed light on whether companies are actually deriving long-term benefits from their outsourcing decisions.

Please see important disclosures at the end of this report.
### What do companies and investors need to know?

- Do contract suppliers have access to the financial and non-financial resources and the incentives to operate in a manner consistent with the company’s business principles?
- How transparent is the company with respect to its suppliers’ operations?
- How stable, and conducive to sustainable practices, are the business environments in which the supply chain operates?
- How do the company’s supplier relationships fit into its overall business strategy?

#### Contextual stakeholders

Contextual stakeholders may be the largest group of stakeholders, and potentially the most difficult to deal with, because they have no formal relationship with the company. Instead, these stakeholders set the business operating environment, and may or may not have a specific interest in the success of the company.

<table>
<thead>
<tr>
<th>Who are they?</th>
</tr>
</thead>
<tbody>
<tr>
<td>Governments, including legislators, regulators, and multilaterals;</td>
</tr>
<tr>
<td>Civil society, which includes non-governmental organizations, media, religious groups, academics, rating agencies, investment analysts (who may also be financial stakeholders) and other professional influencers;</td>
</tr>
<tr>
<td>Communities, especially those bordering a firm’s facilities, ethnic minorities, and indigenous communities;</td>
</tr>
<tr>
<td>The natural environment and associated advocates; and</td>
</tr>
<tr>
<td>Peer companies, particularly those that may be disrupted by corporate activity.</td>
</tr>
</tbody>
</table>

#### Why is the relationship important?

The importance of contextual relationships varies significantly by company and industry. In general, the influence of each stakeholder group will depend on both the circumstances of the company and the stakeholders.

For companies, these circumstances might include:

- The size and geographical placement of the company;
- The company's industry and market position within its industry;
- The public prominence of the company's brand;
- The company's capacity and history of public engagement;
- The perceived “sphere of influence” of the company, which may include the scope of its supply chain, the reach and interconnectedness of the company’s products, the size of its workforce, etc.; and
The potential for conflicting stakeholder demands.

For stakeholders, key factors are:\textsuperscript{18}

- The degree to which the stakeholder has \textit{power} over the company, meaning the ability to impose its will on the company. Power may be \textit{coercive} (e.g. the government imposing mandates), \textit{utilitarian} (e.g. the media’s ability to cast the company in a negative light), or \textit{normative} or \textit{moral} (e.g. a religious figure making a moral plea).

- The stakeholder’s perceived \textit{legitimacy}, or right to a voice regarding company affairs. Governments, for example, are usually considered to have a legitimate right to influence corporate behavior. In some cases, a stakeholder may be considered legitimate to some and not others. For example, workers, but not management, may see labor activists as legitimate.

- The \textit{urgency} of the stakeholder’s claim on management, meaning that it has a significant and time-sensitive concern about the company’s behavior.

In the early 2000s, activists accused The Coca-Cola Company of complicity in the murder of a trade unionist in Colombia. These stakeholders may not have been \textit{legitimate} in the eyes of Coca-Cola directors or executives, but they did have legitimacy in the eyes of some university students and faculty members. Although they owned no stock and controlled no significant relationships with the company, the activists obtained \textit{power} over Coca-Cola by persuading several universities to sever their relationships with the company based on these allegations. Their power at the universities was \textit{normative}; their power with Coca-Cola was \textit{utilitarian} or perhaps \textit{coercive}.

The courts eventually found a lack of evidence that Coca-Cola had any responsibility for the specific murder cited in the case. Yet, activist claims gained \textit{urgency} because the company lacked a corporate policy to respect human rights globally, despite having operations in some of the most challenging environments in the world. Without any effort to insure the safety of the workers who distributed their product, the company found a blind spot that limited its ability to credibly defend itself against accusations of complicity.

This gap became the basis of a shareholder campaign, as well as internal advocacy at the company, that eventually resulted in the company adopting a

\begin{quote}
\textbf{Shareholder engagement in action:}

Several years after the conclusion of dialogue on contentious environmental and social topics, a former executive at a major ag-tech company tells an active shareholder, “you had a lot of influence on us...we just didn’t want you to know that.”
\end{quote}

global human rights policy and set of practices. Today, Coca-Cola is known as a leader among corporations for its efforts to respect human rights.

- Who are the key contextual stakeholders upon whose support the company relies? Which contextual stakeholders may have the power to disrupt company strategies?
- How does the company measure the lifecycle ecological impacts of its products and operations?
- What processes does the company have to engage its contextual stakeholders and respond to their concerns?
- Is the company’s approach to addressing contextual stakeholder issues consistent across business functions?

For a greater understanding of how issue alignment (or misalignment) affects corporate stakeholder relations, we recommend “Legitimacy in the Banking Sector,” by Cornerstone Capital’s Michael Shavel, in collaboration with Robert D. Lamb, Ph.D., and Diane Glossman, CFA. Although the report pertains specifically to the financial services industry, the approach can be adapted to any industry.
Applying the BRAVE Matrix™: Green real estate

Beginning around 2009, shareholders began to engage real estate companies regarding their strategies for energy and water consumption. At the time, few companies had comprehensive “green” strategies, but academic evidence had begun to identify a link between environmental performance and company financial performance in the real estate industry. At first, companies lacked the systems to evaluate, capture or account for these benefits. Over the next few years, in part because of the urging of shareholders, companies began systematically exploring the potential of energy and water efficiency to save costs, improve tenants’ experience, and enhance their relations with local governments, who were beginning to develop municipal climate change policies.

Today, “green” strategies and marketing are common for real estate companies and other firms that occupy large amounts of real estate. The division of responsibility between owners, tenants and building managers complicates this analysis, but some benefits of sustainable building are available to each of these parties.

Below we use our BRAVE Matrix™ to illustrate how a company might make the case for green real estate. Note that in general, as in the example, one does not need to fill in every cell of the matrix, only those that are relevant.

Figure 10: The business case for “green” real estate

<table>
<thead>
<tr>
<th>Business Value Drivers</th>
<th>Demand Stakeholders</th>
<th>Supply Stakeholders</th>
<th>Contextual Stakeholders</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost/ Cost Reduction</td>
<td>Reduce energy and water costs; reduce vacancies</td>
<td>Reduced healthcare costs (tenants)</td>
<td>Reduced compliance costs or fines</td>
</tr>
<tr>
<td>Risk/Risk Reduction</td>
<td>Reduced risk of building obsolescence, reduced stock price volatility (REITS)</td>
<td></td>
<td>Reduced Regulatory risk through proactive local government engagement</td>
</tr>
<tr>
<td>Sales and Pricing Power</td>
<td>Increased rents, higher asset valuation, preferred for certain tenants. For retail tenants, green building may improving shopping experience.</td>
<td>Green buildings contribute to greater tenant worker productivity (tenants)</td>
<td></td>
</tr>
<tr>
<td>Reputation/ Brand Equity</td>
<td>Owners can enhance relationship with tenants by educating about efficiency opportunities</td>
<td></td>
<td>LEED Certification/Energy Star may offer mission alignment (e.g. for universities or local government offices)</td>
</tr>
<tr>
<td>Attractiveness as Employer</td>
<td>Use energy efficiency programs to motivate employees</td>
<td>Greater employee engagement and well-being (tenants); some evidence of improved ability to attract and retain</td>
<td></td>
</tr>
<tr>
<td>Capacity for Innovation</td>
<td>Green building standards leads to design innovation</td>
<td>Opportunity to develop employee networks within firms to share knowledge</td>
<td>Participate in local government climate adaptation efforts</td>
</tr>
</tbody>
</table>

Source: Cornerstone Capital Group
Conclusion

Henry Ford’s famous decision to pay his workers $5 per day (about double the prevailing wage at the time) was seen as an act of charity by some and an act of anti-American socialism by others. In fact, it was a cost-saving measure.

Ford’s assembly workers, many of whom were accustomed to the variety and pace of agricultural employment, barely tolerated the dull and repetitive tasks assigned to them. Turnover was high, and the need to train new employees was a substantial expense as well as a management headache. Increasing wages reduced turnover and defused interest in a nascent unionization drive. As has often been told, it turned workers into customers as well. Finally, giving everyone a raise had a salutatory impact on Henry Ford’s reputation and that of his company.

A holistic understanding of stakeholder motivations and relationships can help to uncover the value of strategies that may initially appear unrelated or even harmful to corporate performance. This was true in Henry Ford’s time as it is today. But the complexity of the modern, globalized, hyper-connected market favors those companies that can understand and respond accordingly to stakeholder concerns. Companies that engage in ongoing and productive dialogue with long-term shareholders will gain valuable insights that will allow them to integrate stakeholder relations into business strategy for competitive advantage.
John K.S. Wilson is the Head of Corporate Governance, Engagement & Research at Cornerstone Capital Group. John has over 17 years of experience in socially responsible investing and corporate governance. He was Director of Corporate Governance for TIAA-CREF, the largest private pension system in the United States with assets under management of over $500 billion. In this role, he oversaw the voting of proxies at CREF’s 8,000 portfolio companies and engaged in dialogue with corporate boards and management to promote sustainability and good corporate governance. He also writes and presents widely about the relevance of social responsibility to investment performance for academic, corporate and investor audiences. Prior to joining TIAA-CREF in early 2008, John served as Director of Socially Responsible Investing for Christian Brothers Investment Services, an investment advisor to Catholic institutions.

An Adjunct Assistant Professor at Columbia Business School, John is also a member of the Advisory Council to the Sustainability Accounting Standards Board. He is a past Vice-Chair of the Interfaith Center on Corporate Responsibility and was a founding advisory committee member of the International SRI Working Group, a think tank serving social investing professionals. John has also served on the Global Reporting Initiative’s Human Rights Working Group and the UN Principles for Responsible Investment Clearinghouse Steering Committee. He has an MBA and a Master of International Affairs from Columbia University and a BA in English from Georgetown University.

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Erika Karp is the Founder and CEO of Cornerstone Capital Inc. The mission of the firm is to apply the principles of sustainable finance across the capital markets, enhancing transparency and collaboration. In offering investment banking, investment management and strategic consulting services, Cornerstone works with both corporations and financial institutions, promoting new research in the field of ESG (Environmental, Social and Governance) analysis, and facilitating capital introductions for companies around the world engaged in sustainable business practices. Prior to launching Cornerstone, Erika was Managing Director and Head of Global Sector Research at UBS Investment Bank, where she chaired the UBS Global Investment Review Committee. Erika served on the UBS Securities Research Executive Committee and the UBS Group Executive Board’s Environmental and Human Rights Committee.

Erika is a founding Board member of the Sustainability Accounting Standards Board, a member of the World Economic Forum Global Agenda Council on Financing and Capital, and serves as an Advisor to the Clinton Global Initiative Market-Based Approaches Track initiative. She sits on the Program Design Advisory Council for Harvard Business School’s Executive Education Program on Innovating for Sustainability, and serves as an Ambassador for the International Integrated Reporting Council. Erika speaks at events including those of the OECD, the UN Global Compact and PRI, Oxford University, The Forum for Sustainable and Responsible Investing, Ceres, The Aspen Institute, and the White House. She holds an MBA in Finance from Columbia University and a BS in Economics from the Wharton School.

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