

Manager Update

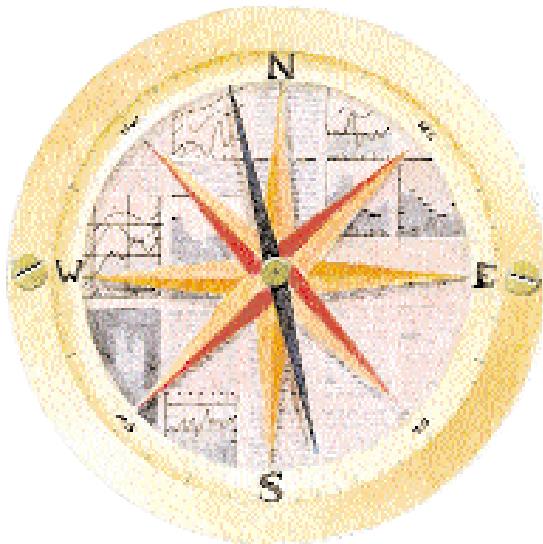
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A quarterly summary of topical management ideas, focusing on four key issues.



**Faculty of Finance
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Manager Update

... is produced in parallel with the Braybrooke Press publication of the same name.

Manager Update helps the general manager keep abreast of the latest articles in specialist management journals. The most useful ideas in the fields of strategy and organisation, marketing, accounting and finance, and human resources management are carefully selected from a wide range of publications with the busy general manager in mind.

Experts in each field explain and discuss the relevance, practicality and usefulness of the key new concepts and ideas, thus enabling the senior executive to keep really up-to-date.

The articles represent the personal views of the authors and not necessarily those of their organisations or of the Faculty. The nature of some subjects will preclude the articles from being definitive or mandatory. Being general in nature, the points made in **Manager Update** may not be relevant to specific circumstances.

The Faculty committee intends that **Manager Update** will act as an aide-memoire for members, provide new ideas, and encourage good practice, but cannot accept responsibility for their accuracy or completeness. Responses from the membership will be a very important part of the successful development of the series.

Manager Update was compiled and edited by the late Professor Keith MacMillan, director of the Centre for Organisational Reputation and Relationships at Henley Management College (see box, right).

Comments and suggestions should be addressed to Chris Jackson BA FCA, Head of Faculty, telephone 020 7920 8486, e-mail chris.jackson@icaew.co.uk, or write to:

The Faculty of Finance and Management,
The Institute of Chartered Accountants
in England and Wales,
Chartered Accountants' Hall,
PO Box 433, Moorgate Place,
London EC2P 2BJ

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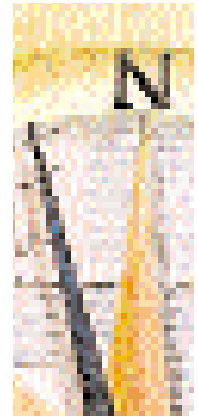
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We learned with great sadness of the death early last month from cancer of Professor Keith MacMillan, director of the Centre for Organisational Reputation and Relationships at Henley Management College. Keith had compiled and edited *Manager Update* for many years with great skill. We offer his family our deepest sympathy.

Is VBM past its prime?



Value based management (VBM) puts shareholder value at the centre of company philosophy. It is often used as a generic name for a range of performance measures and techniques sold by expensive consultants, each claiming to be the best. This can be confusing for top management. Here, **Roger Mills** reviews research that categorises the different approaches and identifies whether the outcomes are also different. He wonders whether VBM may be past its prime.

Value based management (VBM) remains a topical business management issue. For many, it has been a significant means of driving business performance, while lately others view it with more caution, arguing that we should develop more substantial theoretical underpinnings for it or simply move on to other approaches.

What is VBM?

One of VBM's distinguishing characteristics is its focus upon the principles of shareholder value. As defined by KPMG, VBM is: "... a management approach which puts shareholder value creation at the centre of the company philosophy. The maximisation of shareholder value directs company strategy, structure, and processes, it governs executive remuneration and dictates what measures are used to monitor performance".¹

That it should be seen as a continuous process that requires much energy to sustain the momentum is clear from a recent review article of VBM by Samuel Weaver and Fred Weston, together with its process implications: "... VBM is a continuous process. It begins with strategic planning to achieve competitive advantages which produce superior growth in economic profits and returns to shareholders. Strategic planning guides the firm's choice of a product-market scope and its resource requirements. The economic nature of the industry or industries in which the firm operates determines the patterns of its financial statements reflected in traditional financial ratio analysis.

Based on a business economic analysis of the industry and the firm's competitive position, projections of financial relationships provide a basis for valuation estimates. Since these are subject to error and change, further analysis based on identification of the key drivers of value are made. This facilitates study of the impact of operating performance on the value driver levels and the resulting valuations. Intrinsic value estimates are related to alternative performance measurements. Compensation systems should be linked to performance metrics. Periodic reviews lead to strategy revisions as well as to changes in policies and operations".²

Yet, as Weaver and Weston point out, the value based management literature contains many unsettled issues, particularly alternative performance measurement theories (Martin and Petty, 2000; Rappaport, 1998; Stewart, 1991; Young and O'Byrne, 2001; Copeland et al, 2000).³ This issue of different underlying theories is critical. VBM is driven by the principles of shareholder value and the approach is built upon the basic underlying principle that management's goal should be to maximise the market value of the shareholders' stake in a company.⁴

But what is meant by value creation? Externally, it typically refers to total shareholder returns, ie increases in share price over time plus dividends. Internally, this is often translated into proxy measures, like the need to produce returns on capital greater than the cost of capital. Interpreted as such, a management's task is to create value by earning

VBM is a management approach which puts shareholder value creation at the centre of company philosophy

VBM aims to give a strategic perspective... necessary for sustained competitive performance

returns on the capital which exceed its costs. VBM is seen as a process of achieving this target by managing the elements – both tangible and intangible – that create a company's economic value. It aims to give a strategic perspective by providing a balance between short-term performance factors and the longer-term factors necessary for sustained competitive performance.

Which VBM performance measure to use?

Yet, although the principles underpinning value creation seem to be straightforward, multiple methods of performance measurement are widely used in the literature. Which, therefore, should we use?

Weston and Weaver attempt to answer this question by testing the relationships of the following four, alternative financial accounting performance metrics versus market metrics on historical and prospective bases:

- intrinsic value analysis/discounted cash flow valuation;
- returns to shareholders;
- economic profit; and
- market to book ratio.

They used data from Hershey Foods to compare the strengths and limitations of each performance measure. Hershey was used to relate and extend the analysis to the major reference text on the subject by Tom Copeland et al, in which data from the company were used. Although illustrative calculations for different companies for different measures are acknowledged as valuable, Weston and Weaver argue that by using one company, alternative performance measures can be more directly compared.⁵

Intrinsic value analysis

Two-stage discounted cash analysis was applied to Hershey Foods for the period 1994 to 2000. Stage 1 was an assumed period of competitive advantage during which the firm had favourable growth and profitability rates. Stage 2 was the terminal period beginning at the end of Stage 1 and running to infinity with lower growth rates and profitability. The enterprise operating value (present value of free cash flows for the 10 year forecast time period, plus the present value of the residual value) obtained from this analysis of Hershey was \$9,430 million.

Returns to shareholders

Returns to shareholders (RTS) are typically measured by calculating annual capital gains plus dividend yields. RTS is applied by using appropriate benchmarks, groups of firms, or indexes and, as a performance metric, it compares the economic returns to investors in a firm relative to alternative benchmark investments.

Using this approach, Weston and Weaver argue that the use of the RTS measure permitted them to make a reasonably firm conclusion, ie that Hershey's performance was comparable to the broader industry segment of which it is a part and was superior to the broader S&P 500 index. They recognise that it would be useful to make a similar comparison with four or five firms with products more closely comparable to Hershey's, but there are no other major public chocolate and confectionery companies in the US.

Economic profit measures

Economic profit can best be distinguished from accounting measures of net income because, in its calculation, a charge for the use of capital invested is deducted. The consulting firm, Stern Stewart, has employed the concept in a measure called economic value added which makes adjustments to net operating profit after tax (NOPAT) that also affect the measurement of the invested capital base. Adjustments to NOPAT seek to capitalise expenses such as research and development (R&D) and advertising over the estimated lives during which they contribute to revenues.

Weaver and Weston prepared a valuation of Hershey Foods using discounted economic profit as well as discounted cash flows. The model used for this calculation was similar to the DCF calculation in that an explicit 10-year period was used, but they did not capitalise year 11's cash flow as a perpetual residual value. By all accounts, they extended the financial strategic plan into the future as far as 250 years! The resulting value is consistent with the enterprise operating value from DCF analysis, ie \$9,430 million.

Market valuation ratios

The q (or Tobin's q) ratio has been widely used to analyse the sources of differential firm efficiency related to variables such as

Multiple methods of performance measurement are widely used

diversification, percentage of equity ownership by top management, etc. In theory, the q ratio is defined as the market values of equity and debt divided by the current replacement value of assets. In practice, though, the denominator is difficult to calculate and, as a consequence, Weston and Weaver used more than one M/B (Market/Book) measure, including the Tom Whited (2001) approach that measures Tobin's q as the ratio of the market value of assets divided by the book value of assets.⁶ This is equivalent to adding to the book value of assets the difference between the market and book value of equity and the denominator is therefore equivalent to the book values of equity plus debt.*

Using the q ratio, as measured by Whited, and the M/B ratio for the data obtained from the Hershey financial statements for 1980-2000 resulted in both ratios generally moving upward over the 20 year period.

In summary, Weston and Weaver found that the four alternative financial performance metrics – intrinsic value analysis/discounted cash flow valuation, returns to shareholders, economic profit, and the market to book ratio (equivalently, the q ratio and market value added [MVA]) are highly correlated. They also found that the results from standard financial ratio analysis, as expressed in the DuPont formulation, are also significantly related to market performance metrics and in the implementation of VBM.

Weston and Weaver argue that each of the performance measures has something to contribute, but recognise that each also has limitations. Their data for Hershey show that each provides information useful for increasing shareholder value and, while some accounting measures are useful vehicles since they underlie the intrinsic valuation of the firm, the ultimate tests are market-based.

If each performance measure provides useful information but also has limitations, the question might be posed, 'since none of the measures is perfect what would you recommend as the performance metric of choice?' Their answer is to employ a multiple of performance measures to obtain a more complete and reliable assessment of performance.

Weston and Weaver recognise that, in theory, the four alternative approaches to VBM that they analyse are somewhat different.

However, their argument is that, in practice, the implementations drawing upon their use have had similarities in methodology and coverage insofar as they all centre on strategic financial planning and 'appear to make valuable contributions to performance improvement and to value creation'.

The conclusion by Weston and Weaver is that: "The empirical evidence argues for an eclectic approach to value based management. Intrinsic value DCF analysis, returns to shareholders or the shareholder scoreboard, economic value added, and the market-to-book analysis have all enhanced value. Each could contribute to effective information planning and control processes."

VBM shortcomings?

In addition to the case made for a better understanding of the theoretical underpinnings of VBM, views have been expressed that a much more radical rethink of the whole issue is required. For example, Bernard Von Mutius argues for: "...a broader understanding of strategy and management that devotes greater attention to intangible values and quality factors, moving beyond the rigid, outdated separation of corporate accounting and business development. I intend to show how it is becoming possible to integrate the orientation towards corporate value and corporate values – in defining a company's purpose, strategic orientation and design of management systems".⁷

Von Mutius put his view in a nutshell by saying that a strict management concept geared solely towards corporate value has probably passed its prime. He argues that its theoretical foundations are crumbling, and it is increasingly being eroded by external influences and what he refers to as its own innate contradictions. He acknowledges that the shareholder value model has had an impressive career but that more recently, dissenting views have gained in number and weight, criticising its strategic narrow-mindedness, challenging its absolutist claims, and questioning its feasibility.

Von Mutius does not contest that the fundamental objective of business is creating value (or increasing the share of equity in corporate value). Instead, he focuses on what he sees as one-sidedness and a lack of realism of a perspective that do not do justice to the

The empirical evidence argues for an eclectic approach to VBM

Von Mutius argues that its theoretical foundations are crumbling

Is it meaningful to squeeze a complex organisation into a shareholder value model?

multidimensional requirements of modern business management. In particular, he questions whether it is meaningful to squeeze a complex organisation into a sub-complex (shareholder value) model. He argues for a deliberate combination of material 'value orientation' with intangible 'values orientation' – in defining corporate purpose and strategic orientation, and in designing management systems. He considers that it is high time to rethink the relationship between corporate value and corporate values in the context of what he refers to as 'balanced values management'.

In effect, Von Mutius makes the case for what he refers to as thinking 'the other.' He does not advocate the development of an entirely new model, but rather starting from existing insights and experiences to combine them in a new way on the level of strategic business management.

Hybrid VBM

Von Mutius raises some very valid points that would doubtless strike a chord with those who have been involved with VBM implementations. However, from the perspective of the company that has embarked on a VBM programme and for which there is an ongoing need to develop and work within this programme, a reasonable question would be, 'what evidence or practical insights are available to help me along the journey?' In this regard, a study by James Wallace might be of particular interest.⁸

The paper by Wallace discusses VBM, stakeholder theory, and a hybrid form of VBM called 'enlightened value maximisation'. This hybrid he attributes to Michael Jensen and argues that it blends the performance measurement attributes of traditional VBM with the strategic philosophy of stakeholder theory.⁹

Wallace begins by identifying a key issue relating to the fundamental purpose of the organisation. He recognises the existence of two main views on what should constitute the primary goal of the firm. Those falling into the ranks of what we might call 'economists' tend to endorse value maximisation and the precepts of what was discussed earlier with reference to VBM. The primary challenge to this is stakeholder theory, for which the underlying rationale is that the corporation exists to benefit not just investors, but

all its major constituencies – employers, customers, suppliers, the local community, and the government, as well as shareholders. In simple terms, the success of the company following the VBM approach would be assessed simply by its long-run return to shareholders, whereas under stakeholder theory a company's success would be judged by taking into account the contribution to all of its stakeholders.

Wallace reviews both of these approaches together with Jensen's hybrid theory of enlightened value maximisation. Most importantly, he uses statistical analysis to investigate whether a broader focus on multiple stakeholders is necessarily inconsistent with the pursuit of long-term shareholder value.

Wallace recognises the existence of a major challenge in undertaking such analysis. Whilst determining whether a company has provided value for its shareholders is fairly straightforward, measuring the corporate contributions to other stakeholders, and the effect of such contributions on the company's market value, is much more difficult. He identifies reputation as being a good indicator of commitment to its stakeholders and illustrates that what evidence there is supports the view that financial success and value creation are not incompatible with stakeholder prosperity. That said, he identifies a straightforward causality issue, ie 'is it a company's reputation for treating stakeholders well that helps drive its market value to higher levels, or is it the financial success and value creation of the company that give it the wherewithal to invest in its stakeholder relationships?'

To disentangle the relationship between value creation and stakeholder benefits, Wallace sought to answer two questions from his study:

1. How are stakeholder benefits affected by changes in shareholder value? and
2. How do changes in stakeholder benefits in turn affect shareholder value?

Wallace used the annual Fortune ranking of 'America's most admired companies' over the period 1996 to 2000 as a proxy for stakeholder benefits, and Standard & Poor's Compustat database to compute market value added (MVA). His analysis of over 400 companies suggests that creating value is a prerequisite to enhancing stakeholder bene-

'Enlightened value maximisation' blends the performance measurement attributes of traditional VBM with the strategic philosophy of stakeholder theory

fits. Quite simply, companies that fail to add value to their shareholders generally end up failing to provide for other stakeholders. Moreover, for those companies that have clearly under-invested in stakeholder relationships, further investment is likely to be a value-adding proposition. Wallace's final words summarise our experience from substantial involvement in trying to help organisations improve their performance: "...companies generally do well by doing good – but at the same time, they must do well to be able to do good."

New avenues for VBM

VBM has the principles of shareholder value at its core. Typically, these principles are applied at the corporate or business unit level to show the potential for value creating strategies to improve performance and returns. Interestingly, these principles have recently been applied to the area of purchasing. Typical views on purchasing are that it is a relatively insignificant backwater that warrants relatively little attention. Yet a report by Crichton et al for the Future Purchasing Alliance goes a long way towards dispelling this myth.¹⁰

The report gives insight into the profound impact that purchasing/procurement decisions can have on the value of the business. It argues that purchasing and supplier management can be deployed as a strategic lever capable of maximising shareholder value. This is quite different from the tradition in purchasing which has typically seen it omitted from the value agenda. As such, the authors argue the full potential of supplier contribution and the complete range of programmes for purchasing performance improvement have not been properly evaluated.

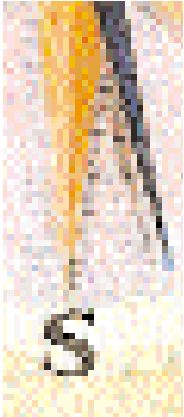
The report by Crichton et al is the conclusion of the first phase of a four-year research programme examining ways in which business-wide initiatives with third party suppliers can be properly aligned to maximise shareholder value. It provides a good illustration that the principles that underpin VBM have much to offer and are in a robust state. [MU](#)

The principles that underpin VBM have much to offer and are in a robust state

** The rationale for using the Whited definition of the q ratio is that it is highly correlated with the other measures of q and does not require the complex estimates of the current replacement costs of investments.*

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Reviewing the value of loyalty

Many organisations invest in customer loyalty programmes, often at great cost. These include loyalty cards, frequent flyer programmes and a wide variety of membership schemes. But are they bringing the business real value for money? For this it is necessary to focus on high value customers and discourage those who are less valuable. But who are these high value customers? Do they really want a closer relationship with the business? **Susan Foreman** explores the issues.

Loyalty programmes are designed to increase traffic through retail outlets and develop brand loyalty

The increasing sophistication of relationship marketing and the development of relationship-management systems have led to several approaches aimed at capturing business and developing long-term customer loyalty. Loyalty programmes are a long-established approach that are designed to increase traffic through retail outlets and develop brand loyalty. The impact of these marketing strategies can be intangible, such as perceptions of value, or more tangible financial returns which have, however, historically been difficult to measure. This article considers a range of issues managers grapple with when designing programmes that aim to pull the customer closer to the organisation, to develop metrics to help value marketing's contribution, and to assess the effect of these strategies in developing long-term value for the organisation. The paper ends with a note of caution – that the search for customer 'proximity' can sometimes be at the expense of the broader vision that is really needed for future success.

Getting close and developing loyalty

Loyalty programmes have been one approach to developing brand loyalty and understanding customers' perceptions of value. Many organisations have, in fact, seized on these as the answer to developing long-term relationships with profitable customer segments. And, for many, they have indeed been a successful means of differentiation and a way to increase the value of their offering to key customer groups. Supporters of loyalty pro-

grammes highlight the positive impact on the brand, the creation of switching barriers, the balancing of supply and demand, and reductions in price sensitivity. Yet some authors, such as Youjae Yi and Hoseong Jeon,¹ building on conceptual work by Grahame Dowling and Mark Uncles,² think that although the loyalty programme can be useful to reach long-term strategy goals, it can be an inappropriate response to short-term competitive challenges. It can, they say, be an expensive approach if merely used for developing price-promotion strategies.

Yi and Jeon outline two perspectives on loyalty. First, they describe the attitudes of loyal customers, and draw attention to the strength of customer preferences and the level of commitment to products and services that customers are prepared to purchase repeatedly. Second, they consider the implications of loyal customer behaviour for retailers and manufacturers. Here, for example, they emphasise the positive impact on a brand's market share of frequency of purchase (per customer), of repeat purchase patterns and, of those who purchase one brand and those who switch between brands. In return for 'loyalty' to the brand, customers can be 'rewarded' in various ways. Yi and Jeon group rewards in two ways, for example whether they are direct and allocated immediately (eg scratch cards), delayed over time (eg frequent flyer schemes), indirect and allocated immediately (eg membership schemes), or delayed over time (eg multi-product incentives). The key to success, the authors say, is recognising that customer groups like to be

The key to their success... is recognising that customer groups like to be rewarded differently

rewarded differently. Yet, matching these different preferences to achieve the desired corporate outcomes requires, of course, careful consideration.

Opponents, however, draw attention to the costs of developing and maintaining loyalty programmes and argue there is often little evidence to show they affect customer behaviour changes or increase market share. From Yi and Jeon's research, it seems that closeness to and involvement with products and services is an important factor in the link between loyalty programmes, customer loyalty and the determination of effective rewards. In theory, when customers are highly involved and interested in a product, they will gather information about the nature of the reward and value those rewards that are directly related to the products. For those less interested in the product, the timing of the reward is more important and they value immediate rather than delayed rewards. If borne out in their investigation, this will give useful guidance when designing programmes and reward schemes for specific customer segments.

According to the authors' research, a loyalty scheme is most likely to be successful when it focuses on 'high-involvement' customers. This segment values rewards that are related directly to purchases and where timing is less important. Interestingly, for some customers the programme itself has value. This is particularly important for customers with low involvement with products and services. These customers only like ongoing links or relationships with basic products like washing detergent because the rewards are immediate and thus the loyalty scheme adds value for them.

As Yi and Jeon state, 'to be successful a loyalty programme must target a valuable customer segment and discourage those customers who are less valuable'. Thus brand managers need to be clear about which aspects of the schemes are perceived to add value and allocate rewards accordingly. Marketers also need to think about the competitive position – some loyalty-reward schemes may be easy for rivals to copy – while others will give a more sustainable advantage.

Hedging customers

As any marketing manager knows, customers can be unpredictable and capricious. This causes problems when planning how to

achieve the optimum financial return from large numbers of customers. Ravi Dhar and Rashi Glazer³ have researched how companies manage customers whose spending patterns are varied and irregular and highlight attempts to develop 'portfolios' of customers, in addition to product portfolios. By comparing customers to stocks and shares in an investment portfolio, they say, managers can see how they can best 'mix' customers, envisage the returns they can achieve and see what level of risk they can tolerate.

Thus, the customer is thought of as an asset and can be classified into different groups, such as 'risky but lucrative,' while others that are lower in value, but 'consistent performers.' According to Dhar and Glazer, the key balance is that between the risk and rewards of 'collective behaviour', which need to be measured and calculated.

There are several methods for calculating the lifetime value of relationships with customers to achieve a balanced and profitable 'portfolio.' Each, of course, has their pros and cons. In general, they incorporate projected cash flows or expected returns, establish present values and, in addition, some factor in the recency, frequency and value of spend. Dhar and Glazer, though, note that these calculations could be more extensive since they fail to take into account the cost of acquisition, ongoing service and retention of customers. Nor, they say, do such methods acknowledge recent customers' behaviour, or how customers' spending can vary with changes in environmental and economic conditions.

The portfolio approach proposed here suggests that customer selection needs to go beyond meeting customers' needs with the appropriate products and services. The company needs to look at the customer to see whether there is a match with the other customers in the portfolio. Customers need to be monitored closely so that fluctuations in spending and the mood and behaviour of the markets are highlighted. Increasingly, sophisticated marketing intelligence and data management techniques facilitate this. In this scenario, the company assesses the customer's contribution to the success of the portfolio, accompanied by an appraisal of their risks. The balance now, the authors say, is between 'volatility and predictability'.

Dhar and Glazer's approach asserts that, 'a base of customers selected for their risk-

Opponents, draw attention to the costs of developing and maintaining loyalty programmes

Customers need to be monitored closely so that fluctuations in spending and mood and behaviour of the markets are highlighted

By using statistical techniques, customers can be selected on the basis of contributions as well as cash flow

adjusted lifetime values should generate higher returns for a given level of risk than one assembled without regard to the constituents and their effect on the resulting portfolio'. In doing this, the authors marry the disciplines of marketing and finance. A beta measure for assessing 'variability' – similar to that used in assessing stocks and shares – is used to assess the risk and returns of accepting customers into the portfolio. By using statistical techniques, segments and clusters are developed, a risk adjusted lifetime value is assessed and, customers can be selected on the basis of their contributions as well as on cash flow. This improves planning and focuses on long-term goals, in turn smoothing out the volatility created by short-term fluctuations in customer behaviour and helping achieve optimum performance.

Using information to develop partnerships

Developing loyalty and assessing its value requires information exchange between organisations and their customers. However, with the rise of relationship management, and increasingly e-business, other issues including trust, equity and honesty have emerged. Both parties need to learn about each other to promote a spirit of partnership. This, of course, requires mutual respect and access to information from individuals and about segments to assess the viability of relationships. Keith Fletcher⁴ notes, for example, that although many companies say they advocate 'relationship management', in practice this can be 'manipulative' and follows closely the marketing mix approach. In Fletcher's view, the misuse of relationship marketing and concerns of customer's surrounding privacy may hinder what he terms 'information-led' marketing.

For instance, some customers will not share personal information because they have heard about companies gathering information without permission, are concerned about privacy and, also, are unsure the information exchange will benefit them. Often, for example, customers perceive a disparity in the value of the information they provide and what the company is prepared to 'pay'. Fletcher has indicated that people's attitude to information sharing depends on their relationship to the company and levels of trust. He identified four customer segments, according to their knowledge and attitudes to privacy:

- the 'sleepers' have a negative outlook and low levels of trust. They need careful handling and regulation may be needed to safeguard this group;
- the 'silent majority' is not particularly knowledgeable but has higher levels of trust. According to Fletcher they are more prepared to share information as they can see the returns. It is important that these customers' experiences are positive, since they are likely to be vocal in their criticism if they are not;
- activists' are knowledgeable, but also have privacy concerns. They are sceptical of the company's promises. Fletcher also refers to this group as 'fundamentalists'; and
- 'partners' are, as the name suggests, more interested in a relationship with the company and believe they will benefit from it. They will expect openness and access to information collected but they are selective, and will not be forthcoming with all companies.

In any relationship strategy, the first task is to build customer loyalty and trust so that customers can be converted into profitable partners. Gaining customers' permission to use information and safeguarding privacy is a key confidence-building task. Failure to do so can also lead to increasing costs, such as for data protection. A reduction in company trust can also impact business performance and company reputation. In addition, failing to respect privacy may lead to increased regulation or litigation.

For Fletcher, relationship marketing is a two-way affair – a balance is needed so that each party enjoys the benefits and advantage of the relationship. Mutuality, he argues, is thus the key to closeness and longevity of the client-business bond.

Getting close to the customer whilst staying flexible

At the heart of Ajay Kohli and Bernard Jaworski⁵ and John Narver and Stanley Slater's⁶ seminal and award-winning work on market orientation in the early 1990s was the need for companies to get close to the customer. Yet, as Erwin Danneels⁷ says, there are pitfalls to this strategy. Despite Kohli and Jaworski's focus on current and future customers, the strategy in practice has often tended to concentrate on current customers about whom there is often detailed information on spending behaviour, preferences and

Research by Fletcher indicated that people's attitude to information sharing depends on their relationship to the company and levels of trust

expectations. This is not, however, often the case for prospective customers. A company can therefore be left open to the accusation of short-termism, since it may not be receptive to changes in the environment, discover emergent markets or be at the forefront of innovation. As Danneels states 'the same processes that enable a firm to develop efficient transactions with its market restricts, environmental enquiry and limits the available options'. Thus, he calls for a balanced approach.

Danneels uses two concepts from process and organisation theory to help unravel and investigate this paradox; the notion of 'enactment' and 'tight' and 'loose' coupling, a measure of closeness to the customer. He combines these concepts and uses them to investigate how being close to the customer can be both 'beneficial and detrimental'. The enactment process, for example, is a type of information-processing model, which shows how information gained from the environment is interpreted internally and is used to facilitate decision-making and develop future strategies. The enactment is a key part in cre-

ating tight coupling. However, he warns against this, arguing that relationships that are too close can lead to restricted vision in the organisation. Implementing a market orientation and strong focus on current customers leads to tight coupling whilst loose coupling enables organisations to be open to change, to monitor turbulent markets, assess the competition, appreciate technological shifts, be responsive to current and future customer needs and learn about segments served by rivals.

Whilst some may disagree, Danneels states that market orientation occurs as part of everyday working life, whereas loose coupling needs more deliberate planning and action. He states that organisations can do both of these things – a strong basis in developing long-term and close relationships can be married with a flexible approach to future opportunities by matching the tight coupling that market orientation brings with the insights of loose coupling. This, according to Danneels, is something at which organisations need to work harder to increase their strategic options. MU

Organisations need to work harder to increase their strategic options

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Improving assessment centres

The assessment centre has become a standard way of evaluating the potential of managers, particularly senior managers, for promotion or selection. The tests and exercises used tend to cover skills such as leadership, communication, decision-making and problem-solving. Experience has, though, indicated problems such as flaws in the exercises themselves and biases of the assessors. **Richard McBain** reviews the research, highlights the problems and suggests ways of putting them right.

ACs have become increasingly popular for making selection and promotion decisions

Assessment centres (ACs) have become increasingly popular for making selection and promotion decisions. Typically, an AC will last between one and three days and involve psychometric tests, presentations, mock interviews, leaderless group discussions and in-tray exercises intended to simulate a future role. The controlled conditions and rating of participants by trained assessors distinguish ACs from other assessment approaches, such as '360-degree feedback,' which gathers information 'on-the-job' through questionnaires from an employees' managers and colleagues.

ACs are, however, expensive and involve a significant investment in resources, such as in the case where assessors are senior managers. Yet they may be worth it. According to an IDS' survey, ACs offer objectivity, consistency and a 'well-rounded picture of a person's capability,' that often accurately predicts future performance. This 'criterion validity' of ACs has helped underpin their popularity.

Yet, AC measurements still arouse concerns. While reported criterion validity ratings tend to be high, this is not the case for construct-related validity, another type of validity. Put simply, the issue here is the clarity of what exactly ACs are measuring and their effectiveness in doing so. Construct-related validity in AC measurement involves two aspects. First, when assessors rate a candidate on the same dimension (say interpersonal skills) in different activities (such as a leaderless discussion group and the in-tray exercise) the

ratings tend not to be as highly correlated as expected. In other words, they exhibit low 'convergent' validity. Second, when assessors rate different characteristics or dimensions (such as interpersonal skills and problem solving) in the same exercise (such as a leaderless discussion group) the ratings between the different dimensions are more highly correlated than expected – they show low 'discriminant' validity.

This article focuses on recent research that suggests ways of improving this construct-related validity and on research into the underlying dimensions that ACs assess, which may help to improve the criterion or predictive validity of ACs.

What factors underpin the predictive ability of assessment centres?

Although the criterion-related validity of ACs seems to be well established, questions remain about their predictive ability. In an analysis of 34 published research projects, Arthur Winfred et al² sought to identify the dimensions ACs actually purported to assess, which are most important for performance and career success, and whether the use of an overall assessment centre rating (OAR) is helpful.

They first identified 168 different dimensions reported as being used in ACs and grouped them into a set of six dimensions that were then used to calculate criterion-related validities:

However, questions remain about their predictive ability

- *consideration/awareness of others* – consideration for the feelings and needs of others and an awareness of the impact and implication of decisions made;
- *communication* – conveying oral and written information and responding to questions and challenges;
- *drive* – originating and maintaining a high activity level, setting and maintaining high performance standards and expressing the desire to advance to higher functions;
- *influencing others* – persuading others to do something or adopt a point of view and taking action primarily on the basis of one's own convictions;
- *organising and planning* – systematically arranging one's own and others' work and resources efficiently, and anticipating and preparing for the future; and
- *problem solving* – gathering and understanding information, effectively analysing data and information, selecting courses of action for problems and situations, using available resources in new ways, and generating and recognising imaginative solutions.

The researchers found that criterion-related validities for the six dimensions in terms of future performance – or the correlations between the predictor and predicted variables – ranged between 0.25 and 0.39. More interestingly, perhaps, just four of these dimensions accounted for the criterion-related validity of AC ratings and explained 20% of the variance in future performance – a higher figure than in earlier estimates. 'Problem solving', alone, accounted for 15% of the variability in future performance. The three other significant predictors were 'influencing others', 'organising and planning' and 'communication'. Thus, according to these findings, 'drive' and 'consideration/awareness' of others may not be significant predictors.

This research also suggests that too many dimensions may be used for assessment in ACs, and that it is important to discriminate clearly between the dimensions in the assessment process, both in terms of definition and measurement. In addition, the use of OARs – which do not 'separate out' the impact of the different dimensions – may not only under-estimate the criterion-related validity of ACs but also reduce the level of construct-related information. Where composite scores are used, consideration should be given to weighting the importance of different dimensions in the final score.

Strategic and interpersonal management styles

Kenneth Craik et al³ provide another approach to identifying the factors underlying management performance and AC validity. Rather than adopting the usual 'exercise-dimension' approach, which involves rating particular dimensions after each exercise, they rated participants at the end of the assessment programme. Unusually, their research combined managerial and personality assessment programmes. Two independent groups of assessors separately rated performance on agreed managerial and personality dimensions from the same exercises. This allowed the researchers to examine any links between managerial and personality assessment measures.

119 participants undertook managerial assessment procedures that included an in-basket exercise, a leaderless group discussion and a GMAT test. Personality assessment procedures included a life-history interview and a leaderless group discussion. Fourteen managerial performance ratings, or dimensions, were used and a key finding was that these dimensions could be grouped into two managerial stylistic dimensions, both of which were related to judgements of overall management potential and to personality characteristics:

- *strategic managerial style (SMS)* – comprising decision-making, fact-finding, delegation, analytic approach, written communication, planning and organisation; and
- *interpersonal managerial style (IMS)* – oral communication, initiative, energy, leadership, creativity and stress tolerance.

Scores on SMS and IMS correlated with consensus ratings of overall management potential to similar high levels – so, a high management performance rating required high scores in both SMS and IMS. However, different activities seemed to be linked to one or other dimension. Thus, for example, SMS was linked in particular to the in-basket exercise that required cognitive skills while IMS was best assessed by the leaderless group discussion that depended on good social skills. In terms of the relationship between these styles and personality, SMS is related to 'conscientiousness' and 'openness to experience'. IMS was related to these personal traits as well as to 'extraversion' and 'agreeableness'. Another inter-

It is important to discriminate clearly between the dimensions in the assessment process

There are two managerial stylistic dimensions

esting finding was that only the personality factor 'openness to experience' was a common predictor of SMS, IMS and managerial potential. This suggests that the role of innovation and creativity in career outcomes may be worthy of further investigation

- while the level of convergent and discriminant validity for training/development centres was higher than for selection/promotion purposes, it was not significantly so.

Construct validity and trait activation theory

One issue not touched upon in the previous study, however, was how appropriate an activity was for rating a particular dimension. As Stephanie Haaland and Neil Christiansen⁵ note, the rationale for ACs is that they can measure a behavioural dimension – and any underpinning personality traits – over various activities with a high degree of consistency. This assumption, however, may ignore the impact of the characteristics of the different activities on the amount of consistency that can be observed. The authors sought to explore if the lack of convergence of AC ratings on the same dimension in different exercises was related to the extent to which behaviour relevant to personality traits can be observed in the different activities.

'Trait-activation potential' (TAP) refers to the capacity to observe differences in trait-related behaviours in a given situation. The potential depends on a number of factors. For example, trait-related behaviour varies more in 'ambiguous' than in prescribed behaviour situations. Trait-related behaviour is also more likely where circumstances provide cues for that behaviour. Thus, for example, an individual's leadership traits are more likely to be observed in situations where leadership is a relevant issue and where the individual can act at their discretion. A trait-activation perspective suggests that the level of correlations in ratings of the same trait in different exercises will depend on the trait activation potential of the exercises and the degree to which successful performance will demand a competency related to the trait in question.

The researchers collected data over a six-year period involving 14 ACs and 79 police officers. Five exercises looked to assess five dimensions: sensitivity, counselling, problem solving, stress-tolerance and organisational ability. The 16-PF test measured personality traits. The authors found that the average correlation between ratings from those exercises high in activation potential for a given trait was twice as large as the average correlation where the chance to observe trait rele-

Improving the construct-related validity of assessment centre ratings

David Woehr and Arthur Winfred⁴ identify two possible explanations for the 'validity paradox' of AC ratings. ACs, they say, may be measuring dimensions different from those originally specified or, alternatively, they could have design, implementation or methodological shortcomings that lead to measurement errors. Their meta-analysis of 32 studies spanning 35 years (1966-2001) reported results for 48 separate assessment centres and considered the impact of the following factors:

- number of dimensions employed;
- participants-to-assessor ratio;
- rating approach;
- type of assessor;
- assessor training; and
- assessment centre purpose.

The study suggests that ACs are not an inherently flawed measuring tool. Rather, certain design factors influence the convergent and discriminant validity of AC ratings. These design factors, they argue, all relate to the 'information load' placed on assessors and their ability to deal accurately with the information-processing task of rating participants. The main findings were that:

- the use of fewer dimensions was associated with higher convergent and discriminant validity;
- differences in the participant-to-assessor ratio seemed to have little effect;
- convergent and discriminant validity is improved by rating 'across exercises' (ie evaluation after all the exercises are completed and, usually, with the same raters assessing the same assessee on multiple exercises) as opposed to 'within exercises' (ie evaluation on each dimension after every exercise);
- construct validity was higher when the assessor is a trained psychologist rather than a manager or supervisor;
- the more extensive training provided, the greater the convergent/discriminant validity; and

The rationale for ACs is that they can measure a behavioural dimension

Trait-related behaviour is more likely where circumstances provide cues for it

vant behaviour was limited. However, the average correlation between different dimensions within the same exercises was still larger (at 0.50) than the average correlation in the same dimension across different exercises (at 0.30) even among the high TAP exercises. This research, therefore, suggests not only a means of narrowing the construct validity gap but of removing it altogether. A trait-activation approach should therefore be used alongside other useful design features to increase cross-situational consistency. Exercises could be designed according to the underpinning personality traits they are intended to evoke and, observation of a particular trait should be limited to those exercises that allow expression of behaviour related to that personality trait.

Enhancing construct validity through frame of reference training

We highlighted earlier the importance of assessor training, but research into the effectiveness of alternative training designed to improve AC validity seems limited. Schleicher et al,⁶ however, have researched frame-of-reference (FOR) training. FOR training was originally developed to improve trait judgements in the performance-appraisal context by attempting to give raters a common frame of reference. To its advocates, it holds out the promise of addressing a number of explanations for ACs' validity problems:

- limited information-processing capacity of assessors;
- lack of clarity in dimension definitions; and
- coding behaviours based on the exercises rather than dimensions.

The research involved 58 assesseees (for whom performance data over a four-year period was available), and 122 assessors, all of whom were psychology students. The AC comprised three exercises: a presentation, a leaderless discussion group and a mock-hiring interview. Three dimensions were assessed: leadership, decision-making and communication skills. Assessors were given either FOR training or control-group training of 90 minutes. Although both groups received typical assessor training, the FOR assessors also received additional elements. Common to both were descriptions of the exercises and a video demonstration, definitions of the dimensions to be rated, together

with discussion of the behaviours pertaining to the dimensions and practice in the use of the rating scales. While the control group took longer over this training, the FOR group shared ratings within the group after each exercise. In addition, the trainer clarified discrepancies and provided feedback on the effectiveness of assesseees.

Key findings from the research were that:

- FOR ratings were consistently more reliable than control ratings (0.82 to 0.70);
- control assessors did not discriminate between dimensions as effectively as FOR assessors;
- ratings from FOR-trained assessors were consistently more accurate than those made by control assessors; and
- FOR ratings were significantly more predictive of future performance than the control ratings (0.32 to 0.21), probably due to the increased accuracy of rating.

FOR training, it seems, increases assessor effectiveness through a sharper understanding of the different dimensions and, happily, is no more expensive or longer than traditional training. Importantly, it focuses on the accuracy of impressions formed on performance definitions unlike traditional training, which focuses on the accuracy of observation and recall of behaviour. FOR training is, therefore, a trait-based rather than a behaviour-based approach.

The impact of assessee consistency of behaviour

Finally, we should consider the assessee as well as the assessor. Filip Lievens⁷ tested the impact of both the information processing capabilities and experience of the assessors and the variability in performance of the assesseees in determining convergent and discriminant validity.

His study involved 73 assessors in three samples (psychologists, managers and students). Assessors received a two-hour training session covering items typically included in established training practice. The performance of candidates was videotaped and their performances were designed to demonstrate differences in consistency across exercises and within dimensions. Small teams of assessors observed the performances and independently rated the candidates. They then shared their observations in their teams, discussed their ratings and wrote assessee reports.

Frame-of-reference training, increases assessor effectiveness

Research found the consistency of candidate performance was the critical factor

ACs have rightly become important tools but some key lessons could enhance their effectiveness

Lievens found that the consistency of candidate performance was the critical factor in terms of establishing convergent and discriminant validity. Convergent validity requires candidates to perform consistently across exercises, and discriminant validity requires candidates to perform differently. The type of assessor also plays a role, although to a lesser degree. Convergent and discriminant validity was higher for the psychologists than for either managers or students. Accordingly, the choice of assessors – and the level of their experience – are important factors. In addition, assessor reliability can be improved by a number of means: allowing them to rate candidates on all exercises or dimensions; by limiting the number of dimensions being rated; or, by the use of behavioural checklists. However, assessor selection and reliability are not sufficient. After all, the paradox of validity may be due in part to candidate performance rather than the accuracy of rating!

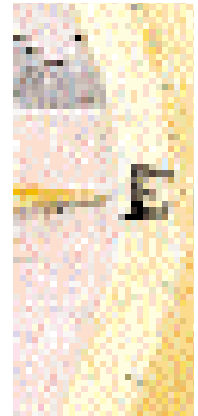
Concluding comments

ACs have rightly become important tools for making selection decisions. Yet, some key lessons could enhance their effectiveness. These lessons, moreover, apply to all HR assessment activities. The designers of assessments must pay attention especially to the number of different dimensions or competences being assessed, as well as to their definition and the ability to recognise and differentiate between them. There is significant evidence that only a limited number of key dimensions need assessing and that imposing a greater burden on assessors can limit the validity of their judgments. In addition, the training of assessors is a vital aspect of AC effectiveness and the FOR approach is an example of a straightforward strategy that may have significant benefits. This is particularly important where the assessors are not HR professionals or trained psychologists. MU

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Corporate governance in the spotlight



Following recent business scandals, corporate governance has become a big issue for publicly-listed companies around the world. Does it make a difference to performance, whether the company is shareholder-controlled or management-controlled? Does 'shareholder activism' have any effect? And will the various reforms in company law, either already enacted or proposed, make a difference? **Ian Turner** reviews a number of these suggestions to see where corporate governance is heading.

The issue of corporate governance has become highly topical due to well-publicised business scandals on both sides of the Atlantic. Many commentators have spoken of a 'crisis of capitalism', calling on governments to introduce more regulation, improve the transparency and accountability of corporations, and prevent more egregious examples of business fraud and abuse.

The roots of the crisis

So where did it all go wrong? The origins of the issue are certainly deep-rooted. As long ago as the 18th century, Adam Smith pointed out that the divergence of interests between the owners of capital and the managers of corporations was problematic and predicted the end of limited liability companies. In fact, were it not for the wide-reaching changes in financial markets and equity ownership that took place in the 1980s, many believe corporate governance would probably have remained an arcane legal and financial issue.

During the 1980s, according to Bernard Taylor who has studied corporate governance over many years, governments in the US and the UK stimulated a 'share-owning democracy', where private citizens were encouraged to invest their personal savings in the stock market in the belief they would reap high returns for minimal risk. Then, in the 1990s, the 'dot com bubble' of overvalued internet and technology companies led to a dramatic crash in the stock market. The opportunities for quickly making (and los-

ing) immense fortunes at this time posed temptations that would try even the most, well-developed systems of corporate governance.

The level and pervasiveness of the problem only became apparent after the collapse, when several large technology-based companies were revealed to have engaged in fraudulent activities. As Warren Buffet said at the time, 'it is only when the tide goes out that you get to see who's been swimming with their trunks off'.¹ Another factor that pushed corporate governance to the top of the agenda, Taylor says, were the high-risk strategies pursued by some major companies who in the rush to transform themselves into technology or media companies succeeded only in wiping billions of dollars off their market capitalisation. Consequently, the reputation of the corporate world and public trust in large companies is at an all time low and investors in many countries have turned their backs on stock markets in disgust.

Why boards fail the test

Yet, for long-standing critics of corporate accountability, the crisis was predictable. Robert Monks, a well-known US promoter of shareholder activism, argued in a recent article that company boards remain destined to fail in crisis situations when the company and its shareholders need them most. 'Boards work adequately so long as the demands are predictable and slender; it is this orderly process with which so much of the literature is concerned'.² For him, the

The issue of corporate governance has become highly topical due to well-publicised business scandals

Public trust in large companies is at an all time low

The pattern of 'negligent oversight'... was exacerbated in the US by the practice of also making the CEO chairman of the board of directors

involvement of board directors is often so slight and narrow in its function that they have easily been able to absolve themselves of responsibility for corporate failures. The pattern of 'negligent oversight' – where some boards failed to involve themselves adequately in management decision-making – was exacerbated in the US by the practice of also making the chief executive officer chairman of the board of directors. The failure of auditing firms to maintain their independence and give a true picture of the company's financial situation – or to insist on greater financial transparency – means that, in most cases, public companies are only notionally accountable to their shareholders, Monks says.

The case for the defence

Executive compensation packages and the transfer of wealth at some large corporations (including successful companies like IBM and General Electric), certainly seems to indicate the plunder of some corporations by their chief executives. Monks refers to the situation in the US as 'an atrocity' and the 'greatest peaceful transfer of wealth in recorded history'.³ Some, however, have taken a more measured position. Bengt Holmstrom and Steven Kaplan,⁴ for example, say that despite the criticisms the performance of US Inc compared with its international competitors remains strong. Just look, they say, at the stock market returns for US companies compared with Britain, France, Germany and Japan over several periods from 1982 until 2001. Even in the period since 2001 when equity returns have been negative, they say, the US performance compares favourably with international benchmarks. They also point out that shareholders of US companies earned better returns, even after management remuneration, suggesting that neither executive pay nor corporate governance are designed less efficiently than in other countries.

For many, the key to effective corporate governance is to increase the proportion of independent directors

While Holmstrom and Kaplan are not uncritical observers of US corporate behaviour, they believe that developments since the leveraged buy-out movement of the 1980s and subsequent increased focus on shareholder value have improved corporate accountability. The trend towards decentralisation on the one hand and outsourcing on the other has also tended to align corporate incentives more closely with shareholder interests. 'While corporate managers still re-allocate vast amounts of resources through internal capital and

labour markets, the boundary between markets and managers appears to have shifted. As managers have ceded authority to the markets, the scope and independence of the decision-making have narrowed'.⁵

They also caution against drawing general conclusions based upon the worst examples of corporate abuse. Of course, they say, there have been egregious examples of option packages awarded to chief executives but they claim changes made by the Securities and Exchange Commission since the early 1990s have allowed shareholders to challenge management teams more effectively: the fact that there has been a marked increase in the number of forced CEO departures and the recruitment of new chief executives from outside the company suggests, they argue, greater corporate accountability for poor performance, not less.

Controlling chief executive power

For many, the key to effective corporate governance is to increase the proportion of independent directors. In the UK, for example, this suggestion formed part of the recent Higgs report recommendations. But, as Henry Tosi et al have pointed out,⁶ some of the worst recent abuses of corporate power have occurred in companies with a majority of outside directors. These boards, they claim, 'often act like they are members of the emperor's court, either approving the CEOs actions or not being terribly interested in what the CEOs do, so long as they are able to hold onto their board status'.⁷ The problem, the authors believe, is two-fold. The first is the clear danger of conflict of interest when CEOs pursue their own interests at the expense of shareholders. Second, there is the problem of 'information asymmetry,' when the CEO may withhold important information from the shareholders and other board members.

Tosi et al also make an important distinction between management-controlled firms, where no individual shareholder has more than 5% of the stock, owner-controlled firms, where equity holders have large shareholdings and a say in the management, and owner-managed undertakings where one or more members of the management holds more than 5% of the shares. In management-controlled firms, shareholdings are often dispersed amongst large institutional investors, many of which have no more than 2% of the company's total equity. As a result, their involvement in man-

agement direction of the company is often limited. In such firms, in particular, chief executives have been able to obtain and secure power in a number of ways. First, they are able to negotiate favourable employment contracts with compensation which is both higher and less risky, since it is less linked to their own performance. Second, they are able to exert more control in setting their own compensation as well as over the appointment of nominees to boards of directors. Third, they are able to implement diversification strategies which enable them to minimise the risk of corporate failure while simultaneously weakening their accountability for poor performance.

Having achieved appointment, chief executives are then able to manipulate the constitution of the board of directors by appointing individuals who share their views or who come from similar professional backgrounds and are less likely to challenge their views. In such companies, the authors' research shows that compensation of chief executives is generally far more closely related to the size of the company than the company's financial performance. In such situations, it is easier for CEOs to claim that poor performance is attributable to external factors beyond their control while claiming, conversely, that strong performance can be linked directly to their leadership.

Corporate governance – the theory behind the practice

Catherine Daily, Dan Dalton and Albert Cannella have carried out extensive research into corporate governance and recently surveyed the state of research in this area.⁸ The dominant theoretical approach in corporate governance, they say, has been agency theory, which assumes – like Adam Smith – a divergence of interests between shareholders and managers. This requires a corporation to have greater alignment between shareholder and management interests. As Daily et al point out, agency theory has had a profound influence over the dominant orthodoxy in corporate governance though it is by no means the only theoretical perspective possible.

Many of the reforms advocated by shareholder activists are based on agency theory principles. The authors, however, when considering the evidence, concluded that independent governance structures do not correlate strongly with corporate financial performance.

There appears, for example, to be no correlation between executive compensation and shareholder value – nor between board independence and corporate financial performance. In fact, they conclude that the oversight function of directors stressed in agency theory has probably been over-emphasised at the expense of the so-called boundary spanning functions of board directors, ie, their role in providing external advice, contacts and expertise to the CEO and the business.

Nor are Daily et al particularly impressed with the potential of shareholder activism. Based on the evidence of the research, they argue, institutional investors probably aren't becoming more active. Since actively participating in corporate governance is likely to be more costly and time-consuming than divesting a firm's stock or simply relying on passive investment strategies like indexing, they believe that there are limitations to what can be expected from active shareholders' influence. Interestingly, however, the research does suggest that independent corporate governance mechanisms can help when a company is in crisis, because effective independent boards may be more willing – or able – to remove ineffective management. Yet, as they point out, if a company is spiralling towards disaster, it may become less responsive to shareholders' needs because other stakeholders, notably banks, take priority.

What is to be done?

New legislation has been enacted to try and correct the worst corporate excesses. In the US, the 2002 Sarbanes-Oxley Act affects areas such as executive compensation, shareholder monitoring and board monitoring. In particular, the Act increases the independence of audit committees, mandates more transparent accounting practices and imposes stricter obligations upon boards and chief executives for financial reporting.

Beyond these, there is no shortage of suggestions for how corporate governance can be improved. Many writers – including those reviewed here – believe that the period for which chief executives hold share options should be extended to encourage closer CEO identification with the corporation's long-term success. Others, such as Monks and Tosi et al, emphasise the importance of shareholder representatives on the board of directors as a counter-weight to the power of the chief executive.

Independent boards may be more willing – or able – to remove ineffective management

Chief executives could hold share options longer to encourage identification with the corporation's long-term success

Boards must
be more
transparent
and
professional

In the UK, meanwhile, the revised Combined Code has been published, which requires boards to report regularly on their activities and encourage directors to be better trained and competent in their roles.

These initiatives are all laudable – boards must be more transparent and professional.

But do we expect too much of boards and their directors? Is it really realistic for non-executive directors to comprehend the operations of large complex organisations and exercise effective scrutiny, let alone active leadership? Indeed, the proof will be whether recent reforms can prevent such abuses and failures in the future. **MU**

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Tel: 020 7928 7770;
fax: 020 7928 7780; contact: Alex Murray or Gabrielle Liggett.

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The Faculty of Finance and Management,
The Institute of Chartered Accountants
in England and Wales,
Chartered Accountants' Hall,
PO Box 433,
Moorgate Place,
London EC2P 2BJ

Telephone: 020 7920 8486
Fax: 020 7920 8784

