The Era of Stakeholder Capitalism

Mark Weinberger

FORMER GLOBAL CHAIRMAN & CEO OF EY AND SENIOR ADVISOR, TENEO

In this interview, Mark Weinberger reflects on the stakeholder capitalism movement and the role it will play in shaping business, the economy, geopolitics, and greater society in the years ahead.

You are a champion of inclusive capitalism/ESG. What does that mean, and how important is it? How should companies be thinking about ESG when it comes to their overall business strategy? And given the current gray area when it comes to ESG standards, how should companies look to handle this?

ESG is a loosely defined term that is aimed at measuring non-financial activities that de-risk a business and lend to long-term sustainable profitability. In its broadest sense, it refers to the environmental, social and governance policies of a business. It is also often used to assess how businesses address "stakeholder capitalism."

I believe there are two reasons ESG is extremely important to society, and to businesses themselves.

"CEOs' license to lead corporations is at risk; we see this in attacks by governments, activists, customers, and even employees. With ample access to information and social media platforms, these stakeholders are finding their voices and exercising their opinions more readily."

First, CEOs' license to lead corporations is at risk; we see this in attacks by governments, activists, customers, and even employees. With ample access to information and social media platforms these stakeholders are finding their voices, and exercising their opinions more readily. Business leaders need to listen and understand the message these stakeholders are sending.

This is not surprising. Businesses have a critical role in society. Businesses create the products and services that sustain and improve our lives. In the U.S., many of the most important means to increase wealth and reduce income inequality are administered through business; practically all upskilling of workers post university, most savings plans, and much of the distribution of healthcare is managed through business. Businesses also create economic wealth for their investors, provide livelihoods for employees, and improve communities where they operate. Recognizing these contributions, business is given certain legal protections and licence to operate.

"Businesses have a critical role in society. Businesses create the products and services that sustain and improve our lives."

As a result, business has a significant responsibility to discharge its obligations in an appropriate way. Across the world, people are questioning whether business leaders are effectively executing all these important responsibilities. Workers, customers, governments, and communities are rightfully concerned about the increase in wealth disparity, social injustice issues, and anecdotes of CEO pay unrelated to results. Governments and social activists are challenging the status quo and asserting businesses needs to do more in order to enjoy the benefits they receive. In Europe, we have seen the most progressive changes to the system. In the U.S., we will likely see increased attention and efforts to address the issue. If business doesn't lead, then government may force change.

"The reality is these are not just social issues, they are business issues."

Second, and what I believe is a more important reason for business to focus on ESG issues, is that if you get these issues right, you will de-risk the business and create sustainable long-term profitability. The reality is these are not just social issues, they are business issues. Many studies back this up, and frankly, most business leaders – certainly the good ones I know – totally understand this. Yet, they don't always do a good job discussing the importance of ESG issues, why it's critical to their business, and the benefits they provide to stakeholders. Moreover, there is currently no good way for stakeholders to assess how a business is doing in these areas, and for businesses to be held accountable.

Inclusive capitalism is the only way to approach economic growth in the future

But companies need the right incentives, the right long-term strategies, and the right metrics to make this come together.

We know the value that companies create can't be measured by the balance sheet alone. In the 1970s, the vast majority of a business' assets were measured on their balance sheets in the form of tangible assets. Today, the majority of many companies' assets are intangibles – brand, workforce, culture, intangible property, etc. – which are not measured by traditional accounting approaches. This is absolutely critical – how can leadership, or an investor, know what an organization is worth if they don't understand the value of its brand, or of its innovation pipeline, its culture or of its talent?

Although these are difficult things to measure, we've come a long way in terms of understanding that stakeholder impact and ESG considerations absolutely contribute to the overall long-term value of an organization. CEOs are already leading this way, and now the frameworks and metrics are catching up. FCLT Global, a non-profit that develops research and tools to encourage long-term investing and business decision making, estimates that there are currently about 600 different frameworks out there. Investors, however, are beginning to demand more consistency, standard setters are beginning to work together, and the work the World Economic Forum has just completed – in conjunction with the Big Four professional services organizations – is a major step forward.

"FCLT Global, a non-profit that develops research and tools to encourage long-term investing and business decision making, estimates that there are currently about 600 different frameworks out there."

Inclusive capitalism is the only way to approach economic growth in the future – but companies need the right incentives, the right long-term strategies, and the right metrics to make this come together. It's a journey, but we are getting there.

Are CEOs sufficiently committed to the transparency of their corporate practices and the connectedness of their businesses to large societal challenges?

Yes, and I think that commitment is growing. Over the past decade I've spent a lot of time with CEOs from all over the world and across all sectors and while transparency and a focus on stakeholders was always part of the conversation, over the past few years it's come to dominate the conversation. Corporate leaders everywhere increasingly understand that their organizations don't operate in isolation, but as part of society and within complex ecosystems made up of diverse stakeholders. They realize that to succeed in that ecosystem, transparency is really important.

A great example of this emphasis on transparency is the heightened interest in ESG reporting standards we've seen recently. There's been great progress made over the past several years through initiatives such as the Embankment Project for Inclusive Capitalism and the World Economic Forum International Business Council's stakeholder capitalism metrics framework, which was launched in September. It contains reporting standards that include metrics covering a wide range of ESG criteria from carbon emissions to employee gender ratios to governance targets. As we see more and more organizations using these frameworks for their corporate reporting, it will really demonstrate just how committed CEOs are.

The Business Roundtable put a big stake in the ground by having over 180 large businesses publicly declare that they are committed to stakeholder capitalism and not just shareholder primacy. I was on the board of the BRT when they developed this position. Some have criticized it – often from the opposite sides of the political spectrum. I believe the statement was powerful and necessary. It acknowledged how CEOs were already leading their businesses. Now, businesses need to be held accountable for following through on their commitments.

Is the move towards stakeholder capitalism a temporary phenomenon caused by current events, or is this a permanent change in the way companies do business?

We're seeing a more permanent change, and our experience with the COVID-19 pandemic has helped to demonstrate that. We might have expected that with the sharp economic downturn we would see companies revert to a short-term focus. But we've actually seen the opposite – companies everywhere are embracing the broader role they play in society and looking to how they can work with all their stakeholders to help address pressing and often connected issues such as racial and economic inequality and environmental sustainability. There's recognition that when the pandemic ends, organizations will not be judged by their financial recovery, but on how they treated their stakeholders and reacted to events more broadly.

Is an "activist CEO" a benefit for a company, a risk for a company, or potentially both?

The question that every CEO needs to ask him or herself is not "What are the risks of being an activist?" but "What are the risks of NOT being an activist?" I'm not suggesting that a CEO should focus entirely on societal issues and neglect to run their business, nor do I believe a CEO should espouse personal political views. But CEOs have a great opportunity to add to the public debate about how policies affect their business and industries. They should speak up when external policies or events challenge their values, or the ability for their business to continue to provide value to its stakeholders. Stakeholders increasingly expect this from CEOs – as evidenced in the recent Edelman Trust barometer findings.

It's impossible today to just focus on a business without looking at the wider societal context and working with a broad range of stakeholders. CEOs who take an insular approach expose their companies to greater risks – in terms of reputation and growth – than those who run their companies while looking to address relevant societal issues.

"CEOs who take an insular approach expose their companies to greater risks – in terms of reputation and growth – than those who run their companies while looking to address relevant societal issues."

In what ways are customers and employees becoming greater drivers of company policy?

These days there's a much greater sense among customers that not only do they want the best goods and services; they want to do business with companies that share their values. It's similar in terms of employees: a good wage and benefits are still important, but people want to have a sense they're doing good in the world on top of doing well professionally and personally. Importantly, it's much easier for customers and employees to make these sentiments felt – and translated into policy.

First, in a globalized world, customers and employees have more choices than ever in terms of where they buy or for whom they work. If your policies or practices don't match their values, they can vote with their feet and find what they feel is a better match. Second, communication channels are much more open and direct. We've all seen things quickly get traction on social media, and while that's really raised the game in terms of speed of response, it gives a level of insight into stakeholder sentiment that we've never had before. Within organizations, the culture around communication has changed – connected to the immediacy and increasing informality of channels. Employees are far more willing to go directly to CEOs and board members on issues that are important to them. When I was starting my career, I'd never have dreamed of writing to the CEO about anything. Yet when I was Chairman and CEO of EY, I would receive lots of passionate, well-argued emails from people across the organization, many of them very junior, on important issues such as climate change or EY's work with the U.S. Administration.

All these changes are really positive – for stakeholder capitalism to work, all stakeholders must be engaged in an ongoing discussion about what's most important to them.

How do the values of a company affect its ability to attract and retain talent?

Employees – especially millennials and Generation Z – are looking to work for organizations that share their personal values and sense of purpose. If a company isn't clear about what those values are, if it doesn't talk about them and, most importantly, live by them – then it will struggle to attract and keep the best talent.

That's why EY places so much emphasis on its values and purpose – ***Building a Better Working World*** – and on helping its people understand them, feel part of them, and live by them. When that happens, current employees and potential recruits can definitely feel it. You can see the results for EY in its continual recognition for its great workplace culture from organizations such as Universum, Great Places to Work and *Working Mother* magazine. And it's why EY receives about 2 million applicants every year and hires around 70,000 – which works out to something incredible like one person about every eight minutes. Since we externally expressed our purpose of *Building a Better Working World* in 2013, our brand, employee engagement scores, recruiting and retention, and therefore our success in the market, grew to record levels. I am absolutely convinced that there was a strong correlation.

What are the risks for CEOs attempting to engage in stakeholder capitalism?

There are always risks, even when you're doing the right thing. For public company CEOs, for instance, there's the risk of clashing with activist investors who may have different views about value creation. There's also the chance that a company falls short of a CEO's rhetoric, which can expose the company and the CEO to charges of hypocrisy. Finally, there's always the chance of making an honest mistake as you raise your head above the parapet – offending people when you don't mean to, for example.

But, as I said earlier, CEOs who don't attempt to engage in stakeholder capitalism face greater risks than those who do.

What kinds of steps should companies be taking to better engage with their stakeholders?

A big part of it comes down to open, honest, two-way communication – being willing to engage with any group of stakeholders is the first step. Then it's about being true to yourself and true to your organization – otherwise there is the very real risk of being seen to be "greenwashing." You want to get involved in issues where your organization has a legitimate role to play. If you're a big FMCG manufacturer, then sustainable manufacturing processes and distribution are right in your wheelhouse. If you're an energy company, moving toward renewables is an important focus. If you're a Big Four professional services organization, tackling questions around ESG reporting is a good way to make the world a better place. Engaging with investors, employees, communities, supply chain partners, etc. on a regular basis is really important. Reaching out and engaging your stakeholders regularly helps you build trust – it helps you build capital when times are good. This will go a long way when you need their attention, trust, and patience, when times are challenging. You have to make the investment with your stakeholders consistently.

"If you're a big FMCG manufacturer, then sustainable manufacturing processes and distribution are right in your wheelhouse. If you're an energy company, moving toward renewables is an important focus. If you're a Big Four professional services organization, tackling questions around ESG reporting is a good way to make the world a better place."

What do companies look like 50 years from now if the trend towards stakeholder capitalism continues?

I'm not a futurist, and 50 years is a long time, especially with the world changing as fast as it is. That said, I am an optimist, and if the trend toward stakeholder capitalism continues, a lot of really positive things will continue to happen. As business plays a greater role in tackling society's greatest challenges, we'll see trust in business increase and – most importantly – some real social and environmental change. I think that business will play a hugely important role in tackling climate change, for example – not only because it's the right thing to do, but also because there will be sizable profits to be made.

"I think that business will play a hugely important role in tackling climate change, for example – not only because it's the right thing to do, but also because there will be sizable profits to be made."

What is your outlook for the economy, five years out?

Assuming that we will have a widely available vaccine against COVID-19, which it looks like we will, then I think the economy will rebound strongly. It may not be a straight line back to strong growth – it may be more of a sawtooth shape, but on the other side of the pandemic the conditions for growth are still strong.

There will be some different characteristics to the global economy in 2025. The pandemic has shown the fragility of certain industries and especially of global supply chains, so many companies will be thinking about how they can build resilience. That may mean less complex supply chains or allowing for more redundancy in different business processes.

The pandemic has accelerated a lot of companies' digital transformations, and that's a trend that will continue, and I hope will bring about a corresponding increase in productivity, which the global economy sorely needs.

Of course, during the pandemic, governments around the world have taken on a great deal of debt that they'll need to service and pay down. If government spending is focused on that, then it may force business to focus even more on its societal role.

Identify the key factors in what you are calling the Fourth Industrial Revolution?

I can't claim credit for coining the Fourth Industrial Revolution – that was Klaus Schwab of the World Economic Forum. For me, the most important aspect of Klaus' idea is what I'd describe as the "interconnectedness of all things." The combination of sensors that are so cheap you can put them in even the simplest machines, plus the computing power to crunch all the data that they provide, allows for some incredibly powerful technological use cases. Take commercial airliner jet engines, for example. Sensors on these are generating millions of data points as the planes fly around the world; data points that can help flag issues before they become problems, save fuel, or help engineers design new, better engines. These kinds of industrial applications are much more interesting and will have a bigger impact than some of the consumer "internet of things" applications that we hear more about. Your fridge ordering more milk for you is useful, but virtualizing machines such as jet engines, or industrial robots, is going to have a bigger impact on the global economy.

Which technological innovations will be the most transformative?

Well, as I say, the Industrial Internet of Things will have a huge impact. The other technology that has huge potential to improve productivity in a field like EY's, for example, is artificial intelligence. It's not about replacing people with machines – it's about people using machines to get more done, more accurately, than they could otherwise accomplish. I'll give you an example. One of the tools EY's AI team has created is something called Document Intelligence. Right now, EY's lawyers are using it – it can read hundreds of pages of contracts in minutes and then answer any question about those contracts the lawyers want to put to it. It takes a lot of the drudgery out of a task and gets to the answers needed faster and with fewer errors than a person could. It has lots of other applications, and the more it's used, the better the tool becomes.

We have obviously seen digital transformation and ecommerce accelerate in the past six months. That will continue. But we really need to see how much the changes in consumer trends and customer preferences are permanent versus reactionary. And government policy, during the pandemic and in response to actions taken during the pandemic, will have a major effect on business decisions going forward.

Is the upcoming generation receiving the educational preparation for managing the new economy?

I've spent a lot of time on college campuses over the past few years – both for work and because I have four kids who are university students or recent grads. So, this is a question I've thought about a lot – and my view is that it's a real mixed bag. Some universities are preparing some students really well for their careers, but I'm not sure that's true for all students. When I think about the people who work for EY today, for example, they may have trained as accountants, or consultants or lawyers – and those skills are still very important – but today all of those accountants, consultants and lawyers also need to have a really good understanding of technology and how it can help their clients. Do they need to be able to code in C++? No, not all of them, certainly. But EY's lawyers, for example, need to be able to use AI tools to scan through reams of documents, which involves a level of tech savvy they never used to need. There needs to be much more focus on technology when teaching these professional disciplines – as much from a mindset perspective as a skillset one.

Related to that, we need to think about education differently in the 21st century. The 20th century model is that you go to high school, then university, then into the workforce. First, I think in the future, hiring decisions will increasingly be based more on “skills” as opposed to “degrees/certificates.” Everyone won’t necessarily need to go to the top universities and get multiple degrees and certifications to earn a livelihood. I think this will be good for business, for the individuals, and frankly for improving opportunities for children who today can’t afford the time or cost of those credentials. There is a huge opportunity to transform our education systems and workforce training programs here.

“I think in the future, hiring decisions will increasingly be based more on ‘skills’ as opposed to ‘degrees/certificates.’ Everyone won’t necessarily need to go to the top universities and get multiple degrees and certifications to earn a livelihood.”

Second, things are changing so fast now that we really need to think in terms of life-long learning. People are going to have to be prepared to change careers as new opportunities open, or old ones close down. While I was at EY I was really proud that we started a learning program called “EY badges,” which are based on completing accredited courses that result in recognizable, portable credentials in topics ranging from machine learning to analytics to design thinking. It can’t be that our education finishes at age 21 or 22 and then we work until we retire.

You have been a member of Russia’s Foreign Investment Advisory Council. What is the outlook for Russia and is the relationship with the U.S. likely to remain adversarial?

This is a very complicated relationship – and a complex situation for business to be in. When the FIAC was founded, there was a lot of optimism about the transformative, cooperative, and collaborative impact of foreign investment. This has, of course, come under significant strain as the U.S.-Russia relationship has deteriorated. Sanctions have also had a significant impact on the Russian economy. The reality is, however, that even in the most trying times business relationships can be a way to keep a dialogue going – to spark a positive turn in an otherwise adversarial relationship. During the height of the Cold War, several key U.S. companies were part of Russian lives. The current U.S. Ambassador is also an advocate for increased business relationships in areas that are not impacted by sanctions. It's hard to make a call about the future of the U.S.-Russia relationship, but we do know that foreign investment and business collaboration can provide an incentive for policy makers to find common ground…and, we could use that in the volatile world we live in today.