Stewardship:

Fostering Responsible Long-term Wealth Creation

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Contents

Introduction: Stewardship in a nutshell *5*

1. Why: Stewardship matters *7*

2. Concept: Defining stewardship *8*

Thoughts and theories 8

Main players: Owner, board and management 11

Owner 12

Board 12

Management 12

Principal 12

Defining stewardship 13

3. Context: What conditions foster stewardship? *15*

The cultural dimension 15

Common characteristics 17

4. Leadership: What distinguishes a steward leader from others? *18*

Leading with impact 19

Safeguarding the future of the institution 20

Delivering meaningful benefits to society 20

5. Implications: Owners and stewardship *22*

Private owners 22

Public firm shareholders 22

Foundations 23

Institutional investors 23

Sovereign wealth funds 24

State as owner of companies 24

Corporate governance and ownership mentality 25

6. Can good stewardship be encoded? *26*

The United Kingdom stewardship code 26

Comply or explain versus legislation 26

Stewardship codes: Risks and benefits 27

7. The role of government: Should stewardship be regulated? *28*

How does government impact stewardship? 28

What are the incentives/disincentives to stewardship? 29

8. Performance: How does stewardship relate to performance? *30*

"Stewardship returns" 30

"Stewardship risks" 31

Non-financial stewardship returns 31

9. Future: Scenario of stewardship 32
References 33
Appendix I: Questions for reflection 39

Introduction: Stewardship in a nutshell

How can a business thrive and sustain growth while enhancing the wealth of its stakeholders and the well-being of the societies in which it operates? This, in essence, is the question stewardship aims to answer.

The landscape for business is ever evolving. Business structures and relationships among stakeholders are becoming more complex and interdependent. Businesses face unrelenting short-term pressures when making decisions.

Corporate governance practices are reevaluated after every financial crisis, but often move in the direction of increasing guidelines and regulations. Such corporate governance measures are helpful and often necessary. However, sound stewardship has a longer term and wider view, with a motivation that extends beyond a "comply or explain" mentality.

In short, the stewardship question needs to be considered from a perspective that includes, but goes beyond, merely complying with corporate governance requirements or seeking short-term benefits solely for a specific group of people, namely the shareholders.

This concept paper seeks to define and to engender a discussion on stewardship and its landscape. This landscape comprises various key players, whose actions and interactions have impact and implications for sustainable wealth creation across organizations and communities. With this paper, we hope to contribute towards enhancing the understanding and fostering of stewardship for corporations and business leaders across the world.

Building on existing theories and factoring in practical considerations of business, we define stewardship as an inclusive and holistic approach. Stewardship has the following dimensions: a clear sense of purpose, an intertemporal horizon and the engagement of different stakeholders. Stewardship leaders take action that is characterized by the combination of three seminal attributes: leading with impact, safeguarding the future, and driving social good.

The concept paper examines a number of vital questions:

- Who are the key players? How are they linked in a stewardship ecosystem?
- What are the processes by which companies can best achieve stewardship solutions through the relationship between and amongst key internal and external agents? Do the different agents each play unique roles within the stewardship landscape? (These players not only include shareholders, the board of directors, the chief executive, management and employees but also extend to society and beyond.)
- Does stewardship depend on context or is there a universal approach to stewardship? While contexts may vary, are there characteristics that are common to well-stewarded companies that thrive over a long period? Do differences in cultural traits and situational contexts influence the occurrence of stewardship? What factors in particular support steward leaders in staying true to their purpose? Do organizational contexts help to bring about stewardship?
- What part does governance play in fostering effective stewardship? For sound governance to result, what are the roles that the key players in the system need to fulfill?
- With the emergence of large institutional investors adding complexity to the landscape, how do they influence stewardship situations and outcomes? What roles could they play? How could investors and

companies efficiently engage in conversations so as to better align their long-term goals? Is the establishment of stewardship codes useful and effective in engaging shareholders and facilitating responsible interaction?

- How can governments play a key role in providing a stable and predictable operating framework for stewardship to thrive? How could the regulatory framework be calibrated to have the desired effect without jeopardizing the business agility and motivation necessary to deliver sustainable wealth creation?

Through an awareness of the stewardship ecosystem and the factors at play, firms can better understand how to steer wealth creation in the context in which they operate. Steward leaders need the courage to chart their firm's path based on their own values and culture, so as to exert a positive influence towards the longer term and a more impactful outcome – sacrificing the shorter term where required. With a clear sense of purpose, stewardship enables companies to ensure that their success is sustainable and contributes to their future prosperity as well as the well-being of society at large.

1. Why: Stewardship matters

How can a business contribute to the wealth and well-being of the societies where it operates over the long term? The role and responsibility of business in society has long been a topic of discussion and study. A renewed focus on this after each financial crisis reflects an underlying question: What are the boundaries of business responsibility beyond wealth creation? Viewpoints abound. Much past discussion can be positioned on a continuum with shareholder primacy at one extreme and stakeholder theory at the other. In nations where the state plays a more active part in the business sphere, the situation can differ. With the growing affluence and influence of sovereign wealth funds (SWFs) in many countries, there is the potential for the various players in the economic sphere to work together for long-term wealth creation and the benefits of the wider community (see **Section 5**). The best way for businesses to contribute constructively is to maximize their sustained wealth creation capability and to have a sense of responsibility towards the community at large – to do well so as to be able to do good in a broader societal sense.

While many have suggested the need for a long-term perspective, business leaders continue to face short-term pressures. Such pressures place them squarely and continually at the center of dilemmas -- making daily decisions about trade-offs. What can be done to engender the right set of circumstances to allow leaders to take a longer term, more holistic perspective? Stewardship is the much-needed process that will help business to take its rightful role within the societal ecosystem, and have meaningful impact. It safeguards and enhances the capability of the organization to create economic and societal value over time. It broadens how we view the role of business, extending the contextual lens of company decision-making to include the societal and economic environment. In practice, this means actively considering the interplay between different stakeholder concerns with the organization's wealth-generating activities. It also means building the firm's capability to process and balance these to maximize its creation of economic and societal value over the longer term.

What are the benefits of stewardship? Do well-stewarded companies generate above-average financial and social returns for their stakeholders over time? At a broader level, stewardship enhances the quantity and quality of connections between business and the communities in which it operates. In better understanding what stewardship means for the different players involved and their roles - including the firm, the board and its shareholders, as well as the government - we hope to set out the implications for embracing stewardship as a concept.

KEY POINTS

- Stewardship provides an approach to help business take a more holistic approach to wealth and well-being.
- Stewardship is the act of protecting and enhancing the capability of the organization to create economic and societal value over time.
- Stewardship can provide the traction that business needs to connect with its stakeholders – across societal and temporal boundaries – to redefine the scope of its activity and the role it takes in society.

2. Concept: Defining stewardship

Our tradition of stewardship builds upon a rich body of thought – much of which implicitly addresses the underlying question of why firms exist. We feel it is useful to make these explicit and to list the different actors and how we define their roles. In this way, we seek to clarify the terms of the discussion, the legacy of existing concepts upon which we draw, as well as where our understanding of stewardship makes a unique contribution.

Thoughts and theories

Stewardship has its theoretical origins in several very diverse areas of thought. One area of thought is rooted in the belief that humans have a duty and a responsibility to the world and their fellow human beings. Several branches of ethics stress that humans have a moral obligation to take care of their environment by maintaining and wisely using natural resources, and adhering to a code that balances one's responsibilities with the rights of others. According to the German philosopher Immanuel Kant and his principle of the categorical imperative, one has a moral duty to treat people as an end in themselves – not for the expected consequences. Many philosophical schools of thought and religious traditions stress the importance of human responsibility to the environment as well as to the community. The Bible makes references to stewardship through the astute management and deployment of resources, with integrity and high moral standing, with a view to serving the wider community. The Hindu Vedas also encourage responsible use of resources and acting to the benefit of humanity. The Qur'an preaches the importance of justice and truth. Buddhist texts highlight the importance of selfless charity and ethics, as well as integrity.

Stewardship draws on notions of accountability and a long-term orientation and responsibility for protecting assets over time. However, used in the corporate and business sense, stewardship means something conceptually quite different. The theory of the firm provides a useful conceptual basis upon which to build on. Agency theory assumes that managers will act in their own self-interest at the expense of shareholders. Stewardship theory – on the other hand - suggests that managers will act as responsible stewards of the assets they control on behalf of the owners.

The principal-agent problem is the following: how can owners ensure that managers promote the organizational interest above their own self-interest? Agency theory says that the principals (shareholders) need to limit the losses that result from managers acting in self-interested ways by putting incentives and control structures in place.[1] Stewardship theory, on the other hand, depicts management executives as having motives aligned with the objectives of their principals.[2] Stewards are not purely self-interested. They identify themselves with the business, and are motivated to maximize organizational performance. As such, their behaviors are aligned with the interests of the business owners. They act in this pro-organizational manner since this provides them with more utility than they would gain through their own individualistic behavior.

The probability of stewardship versus agency behavior evolving in a given context depends on a number of variables.[3] These include cultural/societal contexts, organizational frameworks, and culture and individual psychological characteristics. There are a number of individual psychological factors that influence stewardship behavior in organizations, such as motivation, identification, power, risk and culture. For instance, collectivist cultures tend to encourage steward relationships more than individualistic cultures, since individuals are socialized to put the well-being of the community above their own individual interests. Power distance is another cultural factor relevant to stewardship. The Dutch social psychologist Geert Hofstede (1991) defined power distance as "the extent to which less powerful members of institutions and organizations within a

[1] Jensen & Meckling (1976) proposed that the solution to the principal-agent problem was to maximize shareholder return, since the shareholders, it argued, were the principals of the firm.
[2] Davis et al (1997).
[3] Davis et al (1997).
[4] Hofstede (1991).

country expect and accept that power is distributed unequally".[4] Within low power distance cultures individuals are more likely to take on a stewardship orientation in management.[5] Hofstede notes that while average power distance seems to be greater or lower overall in certain national contexts, there can be considerable variance across organizations and individuals within countries. There are increasing numbers of cultural scholars in Asian and other countries who argue that other dimensions are relevant to view and assess differences. What is clear is that there are strong cultural influences.

At the individual level, some studies suggest that people who are motivated by higher order needs (defined by the famous psychologist Abraham Maslow as self-actualization needs) are more likely to act as organizational stewards.[6] This means that intrinsically motivated individuals – those who are driven by an interest or enjoyment in doing the work itself and are motivated from within rather than by external pressures or a desire for reward – are more likely to have a stewardship orientation. Executives who identify strongly with the organization – who assimilate internally the success or failure of the organization as their own success or failure – are also more likely to be stewards. Stewardship seems to occur more when executives internalize organizational goals – also called high value commitment. The use of personal power as a basis for influencing others – rather than reliance on institutional power – also seems to indicate greater propensity for stewardship behavior.[7]

A number of social, organizational and individual factors make it more or less likely for stewardship to emerge in a specific organizational context (see **Table 1**). Agency and stewardship orientation may even co-exist in an organization, with some parts of the organization operating more along agency lines, while others function predominantly along stewardship principles.[8] The resultant combination for any given organization depends on the individual, organizational and cultural context of the firm. These variables are not discrete but rather dynamic and affect one another. For example, the degree to which an individual is intrinsically motivated may be affected by how much the organizational culture emphasizes institutional power versus personal power. Or the degree to which an individual identifies with an organization may be strongly impacted by the authenticity of the corporate purpose. Also, these variables are not constant, i.e. some individuals may start out as highly intrinsically motivated but then become disillusioned and shift to a more extrinsically motivated psychological mindset. Or, on the flipside, an individual may start out solely motivated by financial incentives early in their career, but then start working on a project that is particularly meaningful for them, and develop an intrinsically motivated mindset over time.

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[5] Davis et al (1997).
[6] Ibid.
[7] Hernandez (2008; 2012).
[8] Davis (1997).

Table 1: Characteristics of agency versus stewardship orientation at the individual, organizational and social level[9]

Dimension	Agency orientation	Stewardship orientation
Social		
Scope of group identification	Restricted to immediate social groups (in-group)	Extended to societal collective as a whole
Degree of power distance	High power distance	Low power distance
Organizational		
Source of power (emphasis)	Institutional power (legitimate, coercive, reward)	Personal power (expert, referent)
Basis for relationship	Contractual	Trust
Corporate purpose	Defined in financial terms	Beyond profit
Leadership	Transactional, performance-based, Low level of trust in subordinates Short-term view	Transformational/emotional engagement with employees at High level of trust in subordinates Long-term view
Rationale for leadership action	Incentives	Values
On whose behalf is the leader acting?	Shareholder	Beyond shareholders
Governance structure	CEO versus Board (check and balance)	CEO and board (alignment)
Individual		
Psychological (motivation)	Extrinsic Lower order needs	Intrinsic Higher order needs
Identification with the organization	Low	High
Commitment to organizational goals	Low-value	High-value

Business executives constantly feel the pressure to demonstrate quick results. The impact of such a short-term outlook is clear;[10] it affects their investment decisions and, in turn, the ability of their companies to grow over the longer term. Fundamental to this discussion is an underlying central question: What is the purpose of the firm? In the absence of a well-grounded understanding of the answer, it is unsurprising that the operating assumption for firms today is the need to demonstrate growth – usually both bottom and top line – quarter after quarter, in order to be rewarded by the markets. There is an extensive body of management theory exploring the purpose of the firm. In the 1970s and '80s, the prevalent theory of the firm was that its sole purpose was to maximize shareholder return.[11] In this view, the owners' or shareholders' interests are of primary importance. The company has a fiduciary obligation to place their needs above all else. In effect, the company's mandate is to increase value for the shareholders. Whether this profit maximization should be

[9] IMD Research, multiple sources (2014).
[10] According to a McKinsey Quarterly survey conducted in 2013 (quoted in Barton and Wiseman, 2014), 63% of respondents said pressure to produce short-term results had increased over the previous five years and 79% felt particularly pressured to generate strong financial performance over a period of two years or less.
[11] Milton Friedman is credited with being the originator of this line of thought; as such, it is often referred to as the Friedman Doctrine.

short term or long term has been the subject of further discussion. However, the idea that the firm's primary goal is to maximize its market value gained wide acceptance.

In direct response to this view, stakeholder theory arose in the 1980s, arguing that a firm's impact on its other stakeholders is also important. Stakeholders include employees, customers, suppliers, financiers, governmental bodies, communities, trade unions and industry bodies. According to the stakeholder view, capitalism is a cooperative system allowing for exchanges of value (innovation, ideas, services, etc.) between stakeholders. With stakeholder theory, the firm's purpose is to facilitate exchanges between stakeholders; and companies that work to serve the interests of a broad group of stakeholders will create more value over time.[12]

While the definition of stakeholders itself is the subject of some disagreement, the idea of stakeholder theory is that the firm's responsibility extends far beyond maximizing shareholder return. Many voices have added their dissenting opinions on the shareholder theory view of the firm, including academics such as Lynne Stout, author of *The Shareholder Value Myth* (2012), and business leaders like Warren Buffett. They point out the destructive consequences of such an overemphasized and often single-metric view of company.

A firm may have multiple goals, which need to be compatible and prioritized. [13] These are different from the firm's purpose. It is important to define these, since organizations are not merely institutions that seek economic efficiency but rather are composed of human beings with individual aspirations. It is important to consider the many different processes that a firm undergoes in achieving its goals and ensure that this is aligned with its core purpose.

In his article "Bad Management Theories are Destroying Good Management Practices", the late Sumantra Ghoshal argued: "by propagating ideologically inspired amoral theories, business schools have actively freed their students from any sense of moral responsibility."[14] In its attempt to become a science, management theory has over-simplified the purpose of the firm and the behavior of the various actors, resulting in the "explicit denial of any role of moral or ethical considerations in the practice of management," as well as the wholesale adoption of a number of faulty assumptions (e.g. that labor markets operate with perfect efficiency).

Even where companies have a specified purpose, there is frequently a gap between the articulated purpose and managerial attitudes. An authentic corporate purpose is defined as the "alignment between a firm's perceived corporate purpose and the actual strategic decisions and actions that a firm takes."[15] There are many benefits of having an authentic corporate purpose – including integrity of vision and behavior, and clarity of connection between actions taken by employees and the overall impact of the organization.

Firms need to embrace a wider view of their purpose, their authenticity in implementing it, the impact of their activities, and develop better insight into the complexity of the human behaviors. In addition to shareholders, employees and customers, a firm needs to consider its impact on society, not just in achieving its stated purpose, but also in the totality of its operations and how these evolve over time. This should inform how a firm frames its purpose and codifies its values in order to deliver the impact that it has set out to deliver.

Main players: Owner, board and management

When considering the purpose and process which firms undertake in pursuing their activities, it is useful to consider each of the main actors and their roles. These may differ depending on the legal structure. Understanding the main actor types can help us form a view of the dynamics at play in either promoting or inhibiting stewardship in firms.

[12] Campbell (1997); Freeman (1984); Freeman, Harrison & Wicks (2007).
[13] Jordi (2010).
[14] Ghoshal (2005).
[15] Mazutis & Ionescu-Somers with Sorell and Coughlan (2015) p. 4.

Owner

Ownership structures vary by business types. In the case of a corporation, the business is a separate legal entity from its owners; these can be either private or government. The shareholders own publicly traded for-profit corporations. A privately owned corporation usually means the founders, management, or private investors own the company. There are also partnerships, where two or more people own the firm; the partners have unlimited liability for the business debts. In a sole proprietorship, the business is owned by one person who has unlimited liability for all obligations. A cooperative is a limited liability business that has members as its owners who share decision-making authority. Different ownership forms naturally lead to diverse approaches to objectives and risks that the organization can take, and exert influence on the ways in which stewardship is approached.

Shareholders are the owners of a limited company; they can be individuals or companies. They provide the capital to finance firm growth. Hence they are also termed investors, and increasingly they are institutional investors, such a pension funds. Shareholder rights are dependent on the class of stock held, but generally include access to information, participation in annual general meetings and voting rights. Shareholders do not intervene in the company's operation, but they generally have one important right, which is the right to appoint and remove directors.

Owners are shareholders, investors and principals, and often these terms are used interchangeably. However, a key element of stewardship is the concept of ownership mentality, defined as a strong sense of attachment to the business and a desire to work towards its sustained success for the longer term. Such ownership mentality is obviously more prevalent with founder-owners and family-owned business owners as compared with investors who are merely seeking short-term returns. Ownership also comes with responsibilities. While we frequently talk about shareholder rights, their responsibilities are rarely mentioned. A number of stewardship codes are now arising to address this area and to define the scope of these responsibilities of ownership. This is discussed in detail in **Section 6**.

Board

The board is the firm's governing body, which oversees its activities. The board sets the objectives of the firm and the tone at the top. The board appoints the leader, possibly supports him or her, monitors performance and ensures objectives are met. The board also ensures that the firm has adequate levels of financing, approves annual budgets and determines the compensation of the management. The board is responsible to and reports to shareholders for the organization's performance. The legal responsibilities of the board and its members depend on the nature of the organization and the jurisdiction within which it operates. In publicly held companies, shareholders elect the board members, whereas in other settings board members can be appointed. The board usually chooses one of its members to serve as its chair. The board is the key link between the shareholders and the firm. It ensures that the firm has the leadership capabilities to fulfill its mandate. It typically makes decisions on behalf of the principal(s).

Management

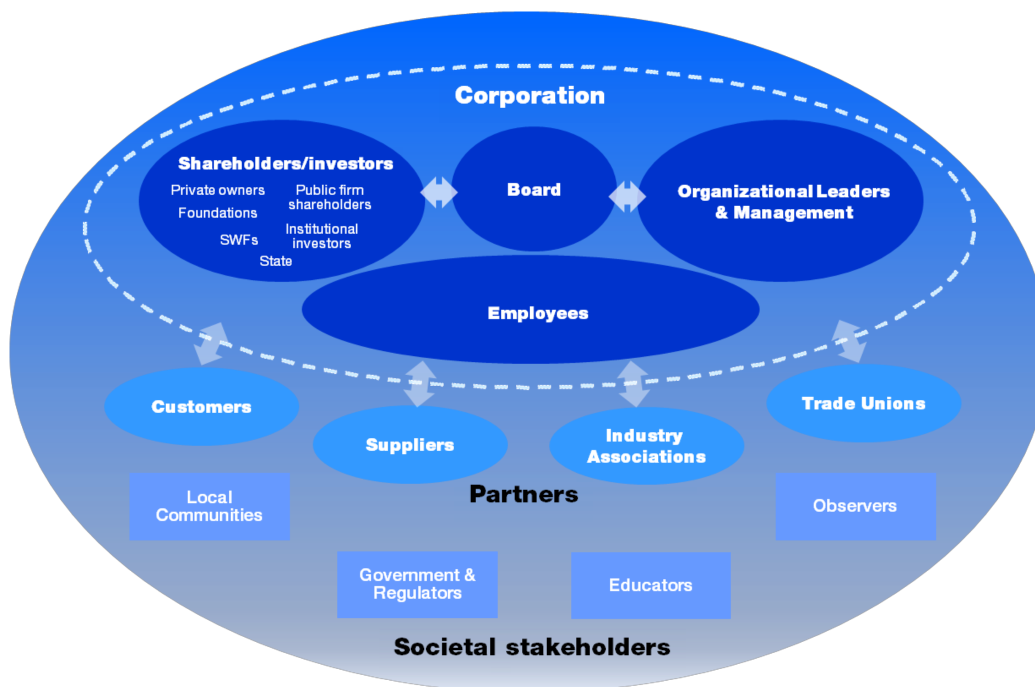
The chief executive and the management are the agents responsible for managing the firm's resources and operationalizing the firm's strategy. The CEO is ultimately responsible for all day-to-day management decisions and for implementing the firm's long- and short-term plans. The CEO serves as a liaison between the board and the management of the company, and communicates to the board on management's behalf.

Principal

The principal is the person or entity who takes responsibility for the actions of the firm and has the most at stake in its performance. This may be the owner in private companies or the majority owner in public companies – but needn't be. An external stakeholder, such as the state, can become the principal in some situations. There is no hard and fast rule as to who the principal is in a given firm; however, it is worth noting that this role may differ among firms – and even shift over time within an individual firm.

The important relationship among the shareholder, the board and the management is depicted in **Figure 1**. "How can a business thrive and sustain growth while enhancing the wealth of its stakeholders and the well-being of the societies in which it operates?" The answer to this critical question lies in understanding the roles of the key players and how they relate to each other in the context of stewardship. Together, all three players "steward" the firm – safeguarding and growing values, benefitting the firm's stakeholders and the larger community, over the longer term. As trusted and responsible stewards, they seek to be able to hand over a thriving business and organization in better shape to the next generation or to their successors.

Figure 1: The relationship of the key actors in the stewardship ecosystem



Defining stewardship

Stewardship is the process by which a firm can best create value over time, through its relationships with both internal and external key agents. To successfully do this over the long term, a firm needs to consider how these relationships may affect its performance in the future. Success can be measured as having a net positive impact on future generations – in a holistic sense, i.e. economic, social and environmental. We believe a number of conditions engender a healthy ecosystem for a firm to create value over time. Internally, by fostering the conditions which intrinsically motivate employees; externally, by understanding relationships with its partners and the communities in which it operates, the firm contributes to building a landscape of greater transparency and trust. Within this landscape, well-stewarded companies ensure that they build the capabilities and resilience to steer through financial crises allowing value to be built over time. Building on a clear statement of corporate purpose, a strong commitment to create wealth in both the mid- and long term, enabled by key interactions between engaged and committed players who have clearly defined roles, stewardship at the corporate level is characterized by three facets, which we explore below.

- **Corporate purpose:** Companies that declare a specific and concrete objective and align their values, structures and processes accordingly provide their leaders and employees with clarity of purpose. In addition to providing clear guidance about howto behave in any given situation, a corporate purpose

provides employees with a sense of belonging and identity, fulfilling a higher order need. One study shows that just 13% of employees are actively engaged in their jobs, finding satisfaction in their work and focused on creating value for their employer.[16] Active engagement leading to motivated employees yields clear benefits including efficiency gains, innovation, as well as enhanced branding and operating margins. Companies who invest in and attain higher employee engagement achieve a higher operating margin compared with those with low employee engagement, and stronger results.[17] There are also clear branding benefits, as employees communicate in an increasingly real-time and visible manner, using social media and other channels.

- **Intertemporal dimension:** In addition to undertaking activities that benefit the company itself and the people who surround it, well-stewarded companies provide the potential for benefitting and sustaining future generations.[18] Such companies consider the impact of their actions both today as well as over time.

- **Engagement of different stakeholders:** A company needs to interact with a number of different stakeholders, both internally and externally. Internally, employees and the boards of directors need to clearly understand their critical roles and responsibilities in fulfilling the purpose of the corporation. They also require the discipline to fulfill them diligently and the capability to execute them. This means, for example, having HR systems that are clearly aligned with the corporate purpose. Externally, suppliers, customers, trade unions, as well as the state and investors require careful management if they are to become enablers of helping the company to fulfill its mission. Engaging with these stakeholders is a key determinant in the success of the corporation in engendering stewardship.

Leadership is critical to promote stewardship. We have identified three key dimensions which foster stewardship in firms: leaders who are able to deliver real impact, an organizational capability to safeguard the future of the institution and a commitment to delivering meaningful benefits to society. We explore each of these in greater detail in **Section 4**.

KEY POINTS

- Stewardship is the process by which a firm can best create value over time, through its relationships with the full range of actors with which it engages – both internally and externally.
- Specific and concrete objective stating its role in society, well-aligned values, structures and processes, provide a firm’s leaders and employees with the clarity of purpose required to create value in a broader sense.
- Firms need to actively consider their own key stewardship agents, which may vary depending on their ownership structure; they need to empower them with the stewardship mandate.
- Well-stewarded companies balance their actions to benefit and sustain future generations as well as the present one.
- Meaningful interaction with an inclusive range of internal and external stakeholders is critical to informing the holistic perspective required by stewardship.

[16] Gallup (2013).
[17] Gallup (2013).
[18] Pirie & McCuddy (2007).

3. Context: What conditions foster stewardship?

Does cultural context influence the likelihood of stewardship? Is stewardship more likely to arise in specific cultural contexts?

The cultural dimension

While there appear to be similarities in the characteristics shared by companies in different cultural contexts, there are also specificities of different cultural contexts, notably between the Western liberal tradition and the cultures in many emerging markets. Culture is the shared set of values and assumptions of a specific group of people. Different theorists have highlighted dimensions along which cultures can be organized. There are many different lenses through which to look at cultural diversity. One way to categorize variations in cultural value orientation relevant to business is as follows. [19]

- **Environment:** Is our basic relationship with the world around us based on harmony, mastery or subjugation?
- **Relationships:** To whom and for whom do we naturally have responsibility? This applies whether a culture is hierarchical, collectivist or individually focused.
- **Activity:** What is our basic or natural approach to activity? This can be broadly categorized as being, doing, or thinking-oriented.

According to this framework, the relationships dimension appears most relevant to stewardship. Societies with cultures which rank higher on individualism have a preference for a loosely-knit social framework in which the expectation is that individuals take care of themselves and their immediate families only. On the other end of the spectrum, more collectivist cultures prefer tightly-knit groups, whereby the norm is that members of a particular in-group (family or other) look after one another and expect unquestioning loyalty in return.

At first glance, it would seem that societies that are more collectivist in culture would be more apt to promote stewardship. However, this may not necessarily be the case. It depends on what *kind* of collectivism. In fact, the degree to which collectivism may influence stewardship depends on which group the individual identifies. Collectivism is multi-dimensional in nature[20] -- which means that individuals feel affinity to different groups. **Institutional** collectivism refers to how much importance the culture places on the collective distribution of resources and collective action, and how much it emphasizes group performance and reward[21]. **In-group** collectivism, means that people value their connection to their family unit or employer organization. The value here is on pride, loyalty and cohesiveness of families or other groups.

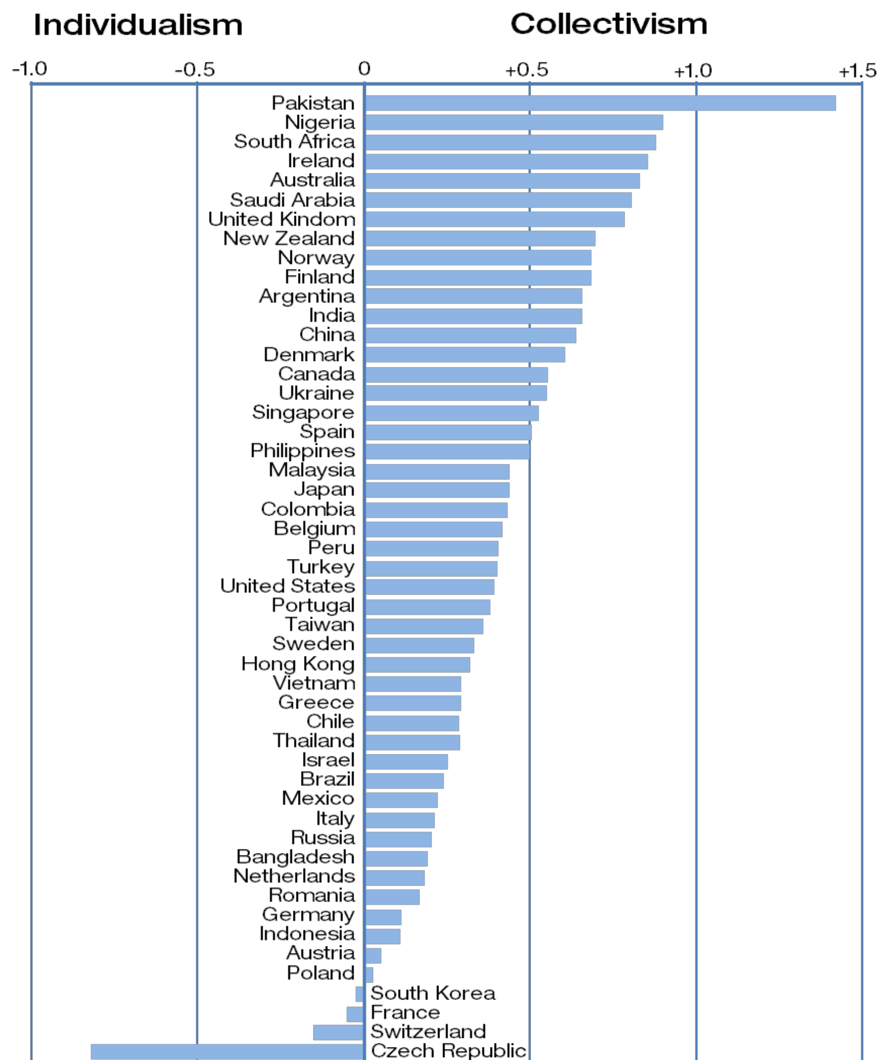
In a study of 10,000 businesspeople around the world, Lane & Maznevski examine the relative preference of a culture for individualism vs. collectivism. They point out that even for countries that have relatively similar levels of collectivism vs. individualism, the group itself may change. In Figure 2, Australia and the UK are actually very collective, with the reference group being your "mates". China's collectivism is more around family (in-group), while Sweden's is around society as a whole (institutional).

Hierarchy is another dimension that may influence stewardship behaviors. In more hierarchical countries (more common in many Asian countries), social order is an important organizing principle, with subordinates reluctant to question their superiors. Studies suggest that less hierarchical contexts, in which subordinates feel more empowered to question their superiors' decisions, encourage a greater degree of stewardship. One explanation for this dimension in many Asian countries where Confucian influence is strong is the value placed on harmony, which may discourage conflict and disagreement.

[19] Lane & Maznevski (2014).
[20] House et al (2002).
[21] Javidan et al (2006).

Many of the culture studies have been conducted in the West, and therefore may be biased in their analysis. One study of Chinese values developed a dimension, based on Confucian thinking, called long-term orientation (LTO) characterized by (a) a dynamic, future-oriented mentality; (b) an emphasis on persistence (perseverance); (c) an emphasis on ordering of relationships based upon status and observing this order; (d) an emphasis on thrift; (e) an emphasis on having a sense of shame; (f) support for interrelatedness through sensitivity to social contacts; and (g) a positive association with economic growth.[22] Another study comparing managers with a view to understanding Eastern values found that on average China's managers placed greater importance on social awareness (the need to be kind and courteous to others) than those from the United States, as well as on social hierarchy, protecting the status quo and personal virtue.[23]

Figure 2: Extent to which business people prefer collectivism to individualism[24]



Such studies seem to suggest that countries in which the business culture is influenced by values based on Confucianism, Taoism or non-dualism – more prevalent in Asian countries – are more culturally inclined to a long-term orientation. They also tend to place greater emphasis on harmony, sensitivity to social contacts and collectivism. As such, businesses in these countries may be predisposed towards stewardship. However, we must be careful to avoid generalizations, and to consider that there may be other factors that serve to counteract this, such as an emphasis on hierarchy and social order. Also, social forces are in flux and

[22] Hofstede & Bond (1988).
[23] Ralston et al (1992).
[24] Lane & Maznevski (2014).

management practices may be diverging from traditional values in many Asian countries. There is an increasingly significant body of scholarship emerging from Asian countries highlighting the importance of differences between cultures and values, and their impact upon business practices over the long term. This presents important learning opportunities warranting future study. In this way, we can help foster cross-fertilization of best practices from East and West.

Common characteristics

Are there certain characteristics across cultures that make a company more likely to survive and thrive? A 2008 report published by the Bank of Korea found that 5,586 companies (in 41 countries) were more than 200 years old. Of these, 3,146 were in Japan, 837 in Germany, 222 in the Netherlands and 196 in France. A Shell study in the 1980s that analyzed the characteristics of relatively large companies that had been in existence for 100 years or more (including DuPont, Kodak, Mitsui, Sumitomo, Daimaru, Mitsubishi and Suzuki) found that these long-established companies had an ability to adapt to social, economic and political conditions and consumer needs.

The analysis revealed the following common characteristics to these long-lived companies:

Conservatism in financing – including making sure they had enough liquidity to remain flexible.

Sensitivity to the operating context – their leaders were aware of the external world around them, noticing changes in their environment and helping the organization to build capabilities to adapt.

Cohesion and company identity – sensed among employees, i.e. a sense of purpose among employees and identification with company values.

Tolerance – regarding experimentation and outliers, which allowed them to stretch their conception of what was possible, frequently enabled by a decentralized structure and authority.

The fact that there appear to be characteristics that are common to long-lived companies across cultures would suggest that there is universality in stewardship orientation among companies in different contexts.

KEY POINTS

- Cultural differences may influence the likelihood of stewardship to emerge in different contexts.
- The Asian cultural context may be more likely to favor the emergence of stewardship behaviors, but there are conflicting forces making generalizations difficult.
- Asian cultures tend to value collectivism relatively more than individualism; also, they have a more long-term orientation, suggesting that such contexts may be more conducive to the emergence of stewardship behaviors.
- However, Asian cultures tend to place greater emphasis on hierarchy: some evidence suggests that less hierarchical cultural contexts, in which subordinates feel more empowered to question their superior’s decisions, may encourage a greater degree of stewardship.
- Facilitating cross-fertilization and sharing of best practice across cultures would provide a significant contribution to the understanding and uptake of stewardship.

4. Leadership: What distinguishes a steward leader from others?

In pursuing long-term organizational wealth, leadership rises to the level of stewardship when leaders not only succeed in their mission, but also seek to optimize the best interests of society, for all stakeholders not just shareholders.[25] Steward leaders recognize that stakeholder interests may not always be aligned. Their role is to balance these in a manner that creates value not just for the organization but for societal stakeholders too. This requires an inspired insight and vision, reinforced by an unwavering commitment to excellence and the ability to find a "middle way" that keeps competing interests in mind when making decisions.[26] At the organizational level, leaders do this by building trust in employees, which elicits a sense of personal ownership. Trust is a key building block for any free enterprise system[27] as it reduces transaction costs and facilitates collective action among societal stakeholders, which is beneficial for all. Trust is an emotional attribute that steward leaders need to earn and continue to build via consistent and reliable performance and integrity.

While trust is the prerequisite, steward leadership is demonstrated through behavior rooted in five fundamental values:[28]

1. **Compassion:** A willingness (empathy) to put the interests of others ahead of their own.
2. **Equity:** A desire to ensure that rewards are distributed in a way that corresponds to contribution rather than power or position.
3. **Prudence:** A commitment to safeguard the future while making the best use of opportunities for the present.
4. **Accountability:** A sense of responsibility for the systemic consequences of one's actions.
5. **Care:** A disposition to act in the interest of all stakeholders.

The above traits appear somewhat contrary to what is expounded by economic models of human behavior and theories of organizational economics, which assume that an individual's behavior is opportunistic, self-serving and motivated by satisfying personal goals.[29] The nature of some of these qualities also makes them difficult to assess in real time and they are best studied retroactively. In addition, stewardship goes beyond the values of individuals to encompass their experiences, exposure and reputation.

With this in mind, we could discern the dimensions for stewardship along the lines of three seminal attributes:

- Leading with impact.
- Safeguarding the future.
- Driving social good.

These attributes (see **Figure 3**) are broadly representative of the dimensions that model stewardship behaviors in individuals.

[25] Caldwell & Karri (2005); Hosmer (2010).
[26] Pava (2003).
[27] Solomon & Flores (2003) p. 11.
[28] Inspired by Hamel (2012).
[29] Podrug (2011).

Figure 3: Dimensions of steward leader behaviors[30]

Attributes	Dimensions	Faculty
Leading with impact	Influence	Mobilizes stakeholders around a compelling vision
		Drives social and economic impact (e.g. thought leadership, business success)
		Inspiring in character
	Contextual intelligence	Aware and proactive concerning their own strengths and weaknesses
		Sensitizes oneself to needs of others (and cultural nuances)
		Successfully seeks consensus among disparate stakeholders
		Acts as the kernel of transformative efforts
	Commitment	Possesses drive (tenacity, energy, initiative)[31]
		Acts conscientiously
		Executes quality communication with the stakeholders
	Reputation	Achieves ubiquitous trust
		Realizes consistency in actions
		Strives for authenticity
		Acts courageously in face of adversity
	Equity	Ensures that rewards are distributed in a way that corresponds to contribution rather than power
Safeguarding the future	Prudence	Employs a measured approach to risk
		Effectively combines short-term planning with long-term thinking
		Pursues caution in practical affairs
	Care	Protects the interests of the stakeholders
		Encourages strong forward-looking policies and standards
		Implements careful management of resources
Driving social good	Accountability	Adheres to moral and ethical principles
		Delivers responsible decision making
		Encourages openness and transparency
	Compassion	Displays and exercises empathy

Steward leaders lead with impact and ensure that their organizations foster positive relationships with stakeholders both internally and externally. They safeguard the future and ensure that it and its stakeholders thrive over the long term. And, they drive social good, behaving in a way that is accountable and responsible.

How can organizations build stewardship capabilities into their DNA? How can they best translate stewardship at the leadership level?

Leading with impact

At the leadership level, certain specific behaviors may promote stewardship in organizations. Leaders can foster stewardship in their followers through various relational, motivational and contextually supportive behaviors. The aim is to create a sense of personal responsibility in followers for the long-term well-being of the organization and society.[32] Such leaders tend to have a transformational style of leadership with employees, creating engagement at the emotional level. They place a high level of trust in subordinates and imparting a long-term view across the organization (refer to **Figure 4** for the key characteristics of transformational leaders). Transformational leadership occurs when "leaders broaden and elevate the interests of their employees, when they generate awareness and acceptance of the purposes and mission of the group, and when they stir employees to look beyond their own self-interest for the good of the group."[33]

[30] Stewardship Asia Center & IMD Global Board Center (2014).
[31] Kirkpatrick & Locke (1996).
[32] Hernandez (2008).
[33] Bass (1990) p. 21.

They lead by example, serving as a clear role model through their actions and attitude. The steward leader uses values (rather than incentives) as a rationale for taking and communicating action. They tend to frame the organization's aim as benefitting not just shareholders but all of society. In this way, the leader communicates the organization's clear purpose internally, reinforcing employees' identification with the company and helping to foster greater commitment to the principles it espouses.

Figure 4: Characteristics of transformational and transactional leaders[34]

TRANSFORMATIONAL LEADER
Charisma: Provides vision and sense of mission, instills pride, gains respect and trust. **Inspiration:** Communicates high expectations, uses symbols to focus efforts, expresses important purposes in simple ways. **Intellectual stimulation:** Promotes intelligence, rationality and careful problem solving. **Individualized consideration:** Gives personal attention, treats each employee individually, coaches and advises.
TRANSACTIONAL LEADER
Contingent reward: Contracts exchange of rewards for effort, promises rewards for good performance, recognizes accomplishments. **Management by exception (active):** Watches and searches for deviations from rules and standards, takes corrective action. **Management by exception (passive):** Intervenes only if standards are not met. **Laissez-faire:** Abdicates responsibility, avoids making decisions.

Safeguarding the future of the institution

Guided by a meaningful and authentic corporate purpose and led by steward leaders, well-stewarded organizations share a number of characteristics which enable a longer term and more integrated view of their role in society. Such organizations tend to have a corporate culture where relationships are based on trust, structures are decentralized (since this tends to ensure a more equitable distribution of power) and employees are actively engaged in meaningful corporate purpose over the long term. These employees have a long-term view of their career path within the company, concrete ideas about the possibilities afforded by the company, and an understanding of how they will best be able to contribute their talents and energies to creating company value. Steward leaders also, by their action and example, ensure "regeneration," inspiring the next generation, to ensure the succession of steward leadership.

Delivering meaningful benefits to society

Steward leaders understand the nature and scope of the organization's role in improving society. Accordingly, they articulate clearly, consistently and authentically what the purpose of the firm is – both internally and externally – and make sure both the strategy and the operational processes are aligned with this purpose. The steward leader understands that profit is the result of delivering benefit to society, rather than the objective. Staying in touch with external and internal stakeholders' expectations of the company and managing the gap between their expectations and the leader's expectations is required to minimize discrepancies. By understanding and actively engaging with stakeholders, steward leaders ensure that the corporation's impact on society is both positive and meaningful to all stakeholders.

[34] Bass (1990) p. 22.

KEY POINTS

- Steward leaders are a key catalyst in instigating and sustaining stewardship, ensuring that their organizations foster positive relationships with stakeholders both internally and externally.
- Steward leaders use values and a transformational leadership style to mobilize their employees' passion and sense of purpose, and lead with impact. They are transformational leaders who motivate their employees to excel through their charisma, inspiration, intellectual stimulation and individualized consideration.
- Steward leaders safeguard the future and ensure that the organization and its stakeholders thrive over the long term, to make sure that the capability for regeneration is preserved.
- Steward leaders drive social good, behaving in a way that is accountable and responsible, to effect positive change more broadly.

5. Implications: Owners and stewardship

Stewardship and corporate governance go hand-in-hand. Corporate governance codes focus on the relationship between the board and management, and place a great deal of attention on shareholder rights, etc. Stewardship is more inclusive; by focusing on the rights and responsibilities of the firm, it seeks to strengthen accountability. Owners are a key part of the stewardship value chain – specifically due to their role in relation to governance practices. By clearly stating their goals, exercising their rights in selecting board members and evaluating the board's performance, they can help ensure organizational oversight. The goals of different owners often diverge. In addition, ownership is increasingly complex. It is useful to explore how governance structures differ based on ownership type, and the potential impact this has on stewardship.

Private owners

In privately owned companies, owners often have direct input, with, for example, a seat on the board. Privately owned family companies do not face the same requirements as public companies, i.e. of disclosing information to the government authority that regulates transactions on the stock exchange, which are then made available to the public and shareholders. This means that management does not have to answer to shareholders based on this financial information. However, a private company must rely on private funding, which may increase its cost of capital and may limit expansion. Since wealth creation is the ultimate goal, this may be an important limiting factor.

What does this mean in terms of stewardship? Does the fact that a privately owned family business lacks this short-term reporting pressure make it more likely to practice stewardship? There is conflicting evidence and conclusions. Some studies have found that managers of family businesses are willing to make sacrifices for the long-term health of the company and to benefit the full range of stakeholders.[35] Other studies show family owners using their power and greater access to information in order to maximize benefit for the family rather than for all stakeholders, and this can manifest as little future investment.[36,37]

Of course family businesses are all different; one possible explanation for this variance is the degree to which the business is embedded within its owning family (i.e. the number of family directors, officers and generations). In this regard, one study suggests that the greater the degree of "embeddedness," the more stewardship behavior declines.[38] In contrast, when family executives are directly exposed to the business and its many stakeholders (and less susceptible to family pressure) they may be more likely to act in a steward-like manner. This raises interesting questions about the influence of social relations on economic behavior; such social relations could include inter-organizational affiliations within broad social networks, as well as macro-institutional influences. There are numerous studies examining privately owned family businesses' superior financial returns; however, it would be interesting to study to what degree stewardship behavior explains this rather than family ownership *per se*.

Public firm shareholders

In publicly listed firms, ownership is **diffuse** because of the large number of small shareholders. There is less incentive and ability for any one shareholder to monitor the behavior of the firm.[39] Consequently, shareholders' associations and shareholder activism surface to provide minority shareholders a bigger voice and better access to information. However, shareholder activism has come to have negative connotations. Nevertheless, shareholders do have an important role to play in staying informed and communicating regularly

[35] Arregle et al (2007); Bubolz (2001); James (1999,); Miller et al (2006) ; Miller et al (2008); Ward (2004).
[36] Wiseman & Gómez-Mejía (1998); Morck, Wolfenzon & Yeung (2005).
[37] Bertrand & Schoar (2003); Claessens et al (2002); Gómez-Mejía et al (2007); Morck et al (2000); Morck & Yeung (2003); Wiseman & Gómez-Mejía (1998).
[38] Miller et al (2008).
[39] Bertrand & Mullainathan (2001).

with the companies in which they invest. Though they are minority shareholders, they need to be active investors (removing intermediaries in the investment chain) and develop an ownership mentality.

Foundations

An individual, family, or corporation usually funds private foundations. Private foundations are separate legal entities, which do not have the legal requirements and reporting responsibilities of a registered, non-profit or charitable foundation. A corporate foundation obtains its funds primarily from the contributions of a profit-making business, and often maintains close ties with the donor company; however, it is a separate, legal organization, sometimes with its own endowment. There are a number of very large foundations, which are also increasing in influence as investors. Many foundations increasingly see for-profit investments as a way to have positive social impact, rather than making donations. The Investment Fund For Foundations (TIFF) was founded in 1991 by a network of foundations, as a vehicle to serve the investment needs of the non-profit community. As of September 30, 2014, TIFF served nearly 800 non-profit members and had managed over $11.0 billion in assets.

Institutional investors

Institutional investors typically include banks, insurance companies, retirement or pension funds, hedge funds, investment advisors and mutual funds. With large sums of money for investment, an institutional investor can exert influence on the management of a corporation because of its entitlement to exercise voting rights in the company. Also, with their ability to buy and sell shares, by their investment decisions, institutional investors have direct influence on the companies. Some large investors negotiate for a board seat via a shareholders' agreement. Institutional investors have a clear fiduciary duty to make sure that they are engaged in the companies in which they invest. They need to understand the business of the companies in which they invest and how their strategies and operations are creating or destroying value, and to monitor this on an ongoing basis. They can encourage stewardship by interacting directly with the companies in which they invest rather than outsourcing this to proxy advisors (currently a common practice). By having timely engagements with the companies, the investors can develop productive relationships with the companies in which they invest and influence stewardship.

With the increasing presence of large institutional investors, there are also trends in the opposite direction that may affect stewardship. One such "threat" to stewardship is the increasing reliance by institutional investors on asset managers. Asset managers are typically evaluated using short-term performance metrics and this often dilutes the long-term ownership perspective. In relation to stewardship, it is important that institutional investors strengthen internal capabilities. When institutional investors do make use of external asset managers, they need to hold them accountable – for example by insisting on high-quality information about the way different asset managers approach stewardship, including how they manage potential conflicts of interest.

Conflicts of interest at the institutional level can pose risks to effective stewardship.[40] While the institutional investors rely on fund managers to manage their investments, the fund managers themselves might be unwilling to hold boards and management accountable (for example by voting against the remuneration report). Another potential conflict is the practice of underweighting (by which a stock is held at a lower than market index weight), which makes improving company performance contrary to shareholder interest. A further potential for conflict arises from the compensation mechanisms of fund managers. Finally, some investors fear that if they are perceived as troublemakers, they may lose access to management, and sometimes thwart the expression of concerns that may be relevant to stewardship considerations (i.e. impact on the broader community level). Such potential conflicts of interest can impair the stewardship behavior of institutional investors in multiple ways. Failing to voice concerns on corporate governance is one such way. Potential impediments to stewardship, like potential conflicts of interests, have given rise to increasing discussion about what constitutes responsible investment on the part of shareholders, especially institutional

[40] Wong (2011).

investors and asset managers. The response has seen an increase in the number of countries establishing some form of stewardship code. Such codes attempt to codify what constitutes good investor governance by shareholders, particularly institutional investors (see **Appendix 1** for more detail).

As institutional investors as a group gain significance, their influence on stewardship orientation will correspondingly increase. If institutional investors have a short-term shareholder return mindset (i.e. short holding of shares, divest and exit anytime), they would weaken stewardship. Institutional investors need to have an ownership mentality and a longer-term view. They need to have a stewardship orientation, and to view themselves as trusted stewards.

Sovereign wealth funds

An increasingly important category institutional investor is the growing group of sovereign wealth funds – with an estimated almost $6 trillion worth of assets under management globally. While there are various definitions and types of SWFs, generally a SWF is a state-owned investment fund, with investment in a wide-ranging spectrum of financial assets such as stocks, bonds, real estate or other financial instruments. They could be structured as a fund or as a reserve investment corporation. They are usually funded with revenues from commodity exports or from foreign-exchange reserves. Of the more than 50 SWFs in operation, more than 38% are from Asia, and the rest from Western, Middle Eastern and African countries. In recent years more SWFs have been formed, and existing SWFs are growing. There is also a shift in the investment pattern of the SWFS from largely financial instruments such as bonds to also include acquisition of stocks in businesses. There is no doubt that SWFs will have an increasing degree of influence on the corporate governance landscape. There has been some concern that SWFs may be used for strategic purposes by governments, to invest in geographies for geopolitical considerations rather than for economic returns. As such, many SWFs have themselves refrained from taking an active corporate governance role in invested companies, since they wish to avoid the possibility of a backlash.[41] However, that may in fact be depriving portfolio companies of the useful contribution that an enlightened, active long-term investor could bring to their corporate governance. Moreover, while termed collectively as SWFs, there are differences amongst them in terms of the maturity of governance practices and degree of transparency. Their stewardship orientation and good corporate governance practices may over time be a differentiating factor amongst the SWFs.

State as owner of companies

In many emerging economies, the state is the owner of large companies. Some are in public services-related or strategic industries. One reason for state ownership may be the need for a longer term investment in such industries. Here, state ownership would add to stewardship with its longer-term perspective. However, in terms of governance, since the governments are also the regulators of businesses and the industries, there needs to be sound and effective structuring of the separation between ownership and management. When it comes to selecting members for the board – a key component of the governance system – state-owned enterprises need to pay attention to ensuring that members are selected based on their merits rather than connections. The presence of effective boards, comprising competent and independent directors, leads to strengthened corporate governance, a necessary requisite for stewardship.

[41] Bortolotti et al (2010).

Corporate governance and ownership mentality

As is clear in the above discussion, while good governance practices provide an essential foundation upon which to build, they are not enough – in themselves - to ensure that relevant actors have a stewardship orientation. Corporate governance views management and the board as trustees for the firm's shareholders and employees; stewardship goes further. By also including the notion that all types of shareholders and investors adopt a responsible ownership mentality, stewardship represents a fundamental shift in the lens through which investors view the firms in which they take a stake – and their responsibilities to these firms.

KEY POINTS

- Different types of investors have varying levels of commitment to the firm; this can also be described as "ownership mentality."
- Corporate governance – through clearly stated goals, active participation in board member selection and board performance evaluation - helps to shore up organizational oversight.
- Stewardship goes further to include an ownership mentality for all shareholders- including asset owners, asset managers, institutional investors and SOEs.
- In publicly listed firms, shareholders do have an important role to play in staying informed and communicating regularly with the companies in which they invest.
- Institutional investors can wield considerable influence, through their entitlement to exercising voting rights in a company, as well as through transmitting information to financial markets.
- There is a greater need for transparency by sovereign wealth funds in how they invest in companies, as well as by regulators in reviewing acquisitions made by foreign funds.

6. Can good stewardship be encoded?

Institutional investors have been much criticized for being part of the problem in the 2008 financial crisis and for their lack of engagement and oversight in the companies in which they invest. In an attempt to encode the responsibility that institutional investors have toward their beneficiaries, stewardship codes have been developed based on the belief that shareholders can serve a key stewardship function.

The United Kingdom stewardship code

The 2009 Walker Report in the United Kingdom recommended that the Financial Reporting Council (FRC) – the UK's independent regulator for corporate reporting and governance – take over the development and encouragement of adherence to best practices in stewardship by institutional investors of UK-listed companies. The UK Government requested that the FRC develop a stewardship code for institutional investors, which it did in 2010. The code sets out a number of areas of good practice and describes how asset owners can protect and enhance the value for the ultimate beneficiary. Since December 2010, all UK-authorized asset managers are required, under the Financial Conduct Authority's Conduct of Business Rules, to produce a statement of commitment to the Stewardship Code or explain why it is not appropriate to their business model ("comply or explain"). The Financial Conduct Authority (FCA) regulates the financial services industry in the UK, including setting standards of conduct in retail and wholesale markets, and supervising trading infrastructures. The code was revised in 2012 to include new disclosure provisions on board diversity, fair reporting, the work of the audit committee and a board statement that the annual report is fair, balanced and understandable and provides the information necessary for shareholders to assess the company's performance, business model and strategy.

Table 2: A comparison of stewardship codes (as of 9 September 2014)[42]

Principles	UK	South Africa	Canada	EFAMA*	Japan	Malaysia	Australia	Swiss
Public **disclosure** on how they will discharge stewardship responsibilities/whether they exercise ownership responsibilities	x			x	x	x	x	
Robust policy on managing **conflicts**	x	x		x	x	x		
Monitor their investee companies	x		x	x	x	x		
Establish clear guidelines on when and how they will **escalate** their stewardship activities	x							
Be willing to **act collectively** with other investors where appropriate	x	x		x			x	
Have a clear policy on **voting** and disclosure of voting activity	x		x	x	x	x	x	x
Report periodically on their stewardship and voting activities	x				x			
Incorporate **sustainability/ESG** considerations into its investment analysis		x				x	x	
Demonstrate acceptance of ownership responsibilites in its investment arrangements and investment activities		x						
Transparent about the content of their policies and how these are implemented		x						
Exercise **voting rights** in a considered way - seek to vote all shares held, explain where 3rd parties used			x	x			x	x
Engage with Investee companies			x	x	x	x	x	
Monitoring and engagement with **regulators and policy makers**								
In-depth knowledge of investee companies and business environment					x			
Incorporate **corporate governace** considerations into investment decision-making						x		
Take advantage of **technology** to faciliate disclosure and engagement								
Take due account of i**nterests of their clients** when exercising their participation rights								x
Assume reponsibility for **exercising the participation rights** to which they are entitled								x
Communicate principles and processes involved in exercising their participation rights to their clients								x

*European Fund and Asset Management Association

Comply or explain versus legislation

Since 2010, stewardship codes have been produced in a number of countries. The European Fund and Asset Management Association (the representative association for the European investment management industry)

[42] IMD research (based on multiple sources) (2014).

published its *Code for External Governance – Principles for the exercise of ownership rights in investee companies* in 2011. Similar codes have also been published in Australia, Canada, Japan, Malaysia and Switzerland. Denmark requires institutional investors to report against the United Nations Principles for Responsible Investment.

There are also international standards covering investor responsibilities. As mentioned in relation to Denmark, these include the United Nations Principles for Responsible Investment, which aim to encourage fund managers, asset owners and advisory firms around the world to incorporate environmental, social and governance (ESG) factors into their investment analysis and develop engagement capacities. The Organization for Economic Co-operation and Development (OECD) code for corporate governance includes provisions for shareholders rights. The OECD principles prescribe that institutional investors take stewardship responsibility towards investee companies only to the extent that this fits the primary fiduciary responsibility of institutional investors, which is to enhance value for their beneficiaries.

Stewardship codes: Risks and benefits

While stewardship codes differ in terms of the specific elements listed, they address many of the same broad principles, including disclosure, engagement and conflict management. The level of specificity and comprehensiveness varies (see **Table 2**). Overall, they promote greater disclosure and transparency as well as engagement on the part of institutional investors towards compliance. Compliance with stewardship codes is less onerous for investors than regulation would be.

However, it must be noted that for the most part, stewardship codes and standards provide guidance regarding the responsibility of institutional investors towards their clients and beneficiaries on maintaining and enhancing the creation of value for their beneficiaries as well as applying international best practices. They do little to enhance the dialogue between investors and the companies in which they invest. It would be helpful to foster such dialogues to facilitate direct exchange. There also needs to be greater guidance for asset owners, such as pension funds, in terms of how to monitor their asset managers. For example, how often should they have meetings with them and who should be there? What issues should be raised?

The biggest danger of stewardship codes is that they become a compliance document, where investors tick the boxes, rather than an exercise in real engagement between investors and the companies in which they invest. Also, in order to fulfill their stewardship mandate, stewardship codes should require reporting guidelines on disclosure of manager incentives and pay structures. Some critics have pointed out that requirements for investor engagement create a real danger for contravening rules of insider trading. Finally, how realistic is it to expect fund managers who choose not to comply to explain their business model?

KEY POINTS

- Institutional investors have faced staunch criticism for their lack of engagement in overseeing the companies in which they invest.
- Stewardship codes have been an attempt by a number of countries, including the Australia, Canada, Japan, Malaysia, South Africa, Switzerland and the UK, as well as many European countries, to encode the responsibilities investors have towards their beneficiaries, by promoting greater transparency, disclosure and engagement of institutional investors towards their clients and beneficiaries.
- Stewardship codes, however, do little to enhance dialogue between investors and companies in which they invest.
- There is a danger that stewardship codes become a compliance document, rather than an enabler for engagement. Critics have also pointed out that there are integrity benefits to maintaining a healthy distance between investors and the companies they invest in.

7. The role of government: Should stewardship be regulated?

How does government impact stewardship?

Finding the right balance on the cooperation–conflict continuum between government and businesses is essential to put in place the framework conditions for stewardship. The government's role is to set fair rules of the game to create a consistent and predictable set of operating conditions for all players, without stifling firms' abilities to raise capital, grow and create value. This differs depending on the nature of the business-government relationship in different national contexts. These can be characterized according to the degree of involvement of government in the economy on the one hand, and the degree of business involvement in the policy-making process. Schonfield (1965) famously categorized capitalism in three categories – neo-liberal, statist and corporatist.[43]

Neo-liberal: In the neo-liberal, Anglo-Saxon model (characteristic of the United States and the United Kingdom), market forces determine the allocation of investment and the coordination of different factors of production. The role of the state is to secure a business environment conducive to business success by maintaining the institutional infrastructure needed for commercial activity (such as a system of law) and by steering the economy at the macro level in order to avoid recessions or inflation. The character of business-government relations tends to be more adversarial than cooperative. In this model, business lobbies government to reduce regulations that cost them money. In terms of stewardship, this means that government views its role as keeping business accountable to standards of disclosure, accounting practices, treatment of employees and environmental compliance.

Statist: Under the statist model (as practiced in some Asian countries and France), the state fulfills extended functions and takes a close interest in the strategies and activities of corporations. The greater government involvement in the economy is based on its leadership role – that is, identifying markets and products that are likely to grow in the future. The advocates of such a major, direct role for governments in making investment decisions argue that governments are capable of taking a longer term, more-informed view of the prospects for growth and investment than the individual corporation.[44] The state also has a mediating role between powerful interests such as business and labor in order to promote consensus on the measures needed to achieve growth. In this model, governments can play a key-enabling role in the stewardship process, facilitating dialogue between the key stewardship players.

Corporatist: The corporatist model creates close integration between the state and business, as well as organizations of civil society. Shonfield described Japan as an example of a corporatist state. In this way, the state takes an interventionist approach, seeking partnerships with many economic actors, such as labor. This serves to stimulate the growth of interest groups that, in turn, have a say in government policy and assist government by helping to implement government policies among their members. Through such partnerships, the most promising prospects for future economic growth are identified and resources are steered to those sectors. In such contexts, government and business interests converge, allowing for alignment on stewardship goals. On the one hand, this may allow for greater efficiency in fostering well-stewarded organizations. On the other hand, the danger of conflicting interests may be greater.

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[43] Shonfield (1965); Katzenstein (1984, 1985).
[44] Wilson (1990).

Other political economy scholars have classified capitalism differently. For example Peter Hall and David Soskice[45] described varieties of capitalism according to liberal market economies, which are more reliant on market-based institutions (e.g., US, UK, Canada, Australia, New Zealand, Ireland) and coordinated market economies, which rely to a greater extent on non-market mechanisms for their strategic coordination (e.g. Germany, Japan, Sweden, Austria). Schmidt identified a third category: state-influenced market economies (France, Italy and Spain), where the state intervenes to a greater extent in business activity, rather than acting only as a facilitating agent.[46]

What are the incentives/disincentives to stewardship?

By providing the operating framework in which stewardship can either thrive or wither, governments can be an important enabler of stewardship. By fostering a favorable investment climate, macro-economic stability and a stable regulatory environment, governments can build the foundations for long-term investment by companies. Regulatory frameworks need to avoid incentives for pro-cyclical investment strategies and facilitate investment. Governments can also enforce the reporting mechanisms to avoid conflicts of interest from skewing fair access to information by all. By promoting information sharing and disclosure, as well as placing greater emphasis on financial education, governments can contribute to a healthy exchange between informed players. However, excessive reporting requirements are a burden to companies, diverting resources from creating value.

The way government involvement manifests concretely in specific national contexts may differ widely. For example, in countries where institutional frameworks are weak, governments may help to build incentives for stewardship by making it easier to do business through predictable, transparent and fair institutions. The World Bank "Ease of Doing Business" index highlights some of the key regulatory practices that facilitate business investment, including dealing with construction permits, enforcing contracts, registering property, getting credit, protecting investors, paying taxes, trading across borders, enforcing contracts and resolving insolvency. By contributing to the macro-economic conditions favorable for long-term investment, governments have an important role to play.

KEY POINTS

- The government has a key role to play in fostering the conditions for stewardship, creating an enabling environment without stifling value-creating activities by firms.
- The role of government differs depending on the political context. In the neo-liberal model, the role of government is too keep business accountable for key minimum standards; in the statist model, the government is involved in investment decisions and mediating relationships between key actors; in the corporatist model, the state partners with economic and political actors to steer resource allocation.
- Governments are critical to ensuring the right macro-economic conditions are in place to favor long-term investment.

[45] Hall and Soskice (2001).
[46] Schmidt (2003).

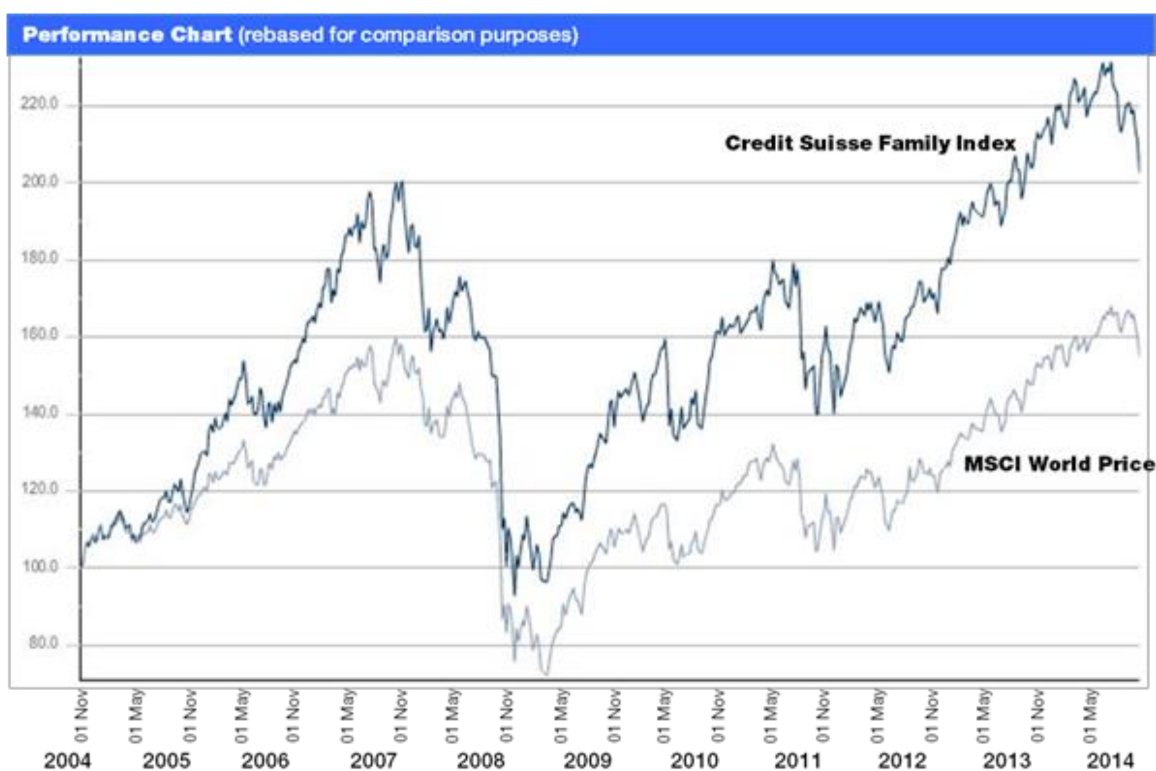
8. Performance: How does stewardship relate to performance?

Do companies that are well-stewarded yield better returns relative to others, if we compare their performance over the long term? In other words, does good stewardship affect long-term financial performance?

"Stewardship returns"

Does stewardship yield specific returns? This depends on how we measure stewardship. Family firms are sometimes used as a proxy for good stewardship, since they tend to be more long term and value oriented than non-family businesses. A number of studies indicate that family firms are more innovative, and they perform better than non-family firms.[47] **Figure 5** highlights the performance of family firms versus non-family firms over 10 years – demonstrating that family firms did indeed outperform non-family firms. However, can this difference be attributed to the better stewardship practices of these firms? This area requires further study to better understand the causality and dynamics at play between stewardship and privately owned family businesses. In public firms, there is evidence to suggest that shareholder returns, in terms of returns on equity, are superior when there is CEO duality (i.e. the board chair is separate from the CEO).[48]

Figure 6: Performance of family businesses versus non-family businesses (2004–2014)[49]



[47] Craig et al (2007).
[48] Donaldson & Davis (1997).
[49] Credit Suisse Family Index (USD) (2014).

There are studies that suggest that well-stewarded firms do correlate with competitive advantage, notably through enhanced strategic flexibility to develop core competencies and exploit firm specific advantages.[50] On average, they have better human resource practices, greater investment in R&D leading to more patents, fewer unrelated acquisitions, and less risky strategic investments than firms without a stewardship culture.[51] They also tend to have more loyal customers, greater investment in non-financial projects and work with trusted suppliers over time – thereby, generating greater ties with external stakeholders.[52]

"Stewardship risks"

When companies are dependent on steward leaders, the degree to which stewardship happens is highly dependent on the presence of the leader. This naturally creates a corresponding risk. In order to ensure consistent performance and continuity of stewardship orientation, there needs to be a clear succession plan or strategy, as well as attention to grooming the next generation of steward leaders. Additionally, a longer-term time horizon and succession considerations could potentially impact capital structure choices and make these corporations more risk averse and conservative from an investment and financial standpoint. Sub-optimal capital structure is therefore another stewardship risk. There are a host of other risks to stewardship, including risks related to reputation, personal biases of leaders, leadership feuding and geopolitical developments.

Non-financial stewardship returns

Besides the long-term financial performance, are there other indicators which help to evaluate how well companies are stewarded? One possible factor could be peer admiration, as defined by the Fortune "Most Admired" global companies." Highly successful companies rank highly on the nine reputational attributes: innovation, people management, use of corporate assets, social responsibility, quality of management, financial soundness, long-term investment value, quality of products and services, and global competitiveness. One conclusion could be that company success depends on emphasizing both financial and stewardship considerations within the context of a clearly articulated mission.[53]

Consideration of sound stewardship includes the components of performance over time as well as beneficial impact to society and accountability. If we analyze the leading companies in terms of reputation (which include the notions of accountability and impact) and longevity, is performance and stewardship positively correlated and can we establish causality? Can stewardship be an effective way to mitigate risk? Perhaps this enhanced capability is what explains the superior financial returns of well-stewarded organizations. This is explored in greater depth in IMD and Stewardship Asia Centre's fbook *Inspiring Stewardship*.

Our conclusion for now is that stewardship is an effective way to mitigate risks, and that it builds organizational resilience and superior financial returns.

KEY POINTS

- With greater attention to the long term and corresponding investments in future growth opportunities, well-stewarded companies may indeed contribute to better and more sustainable performance over time – in financial terms as well as other respects.
- If risks are well managed (e.g. leadership succession), stewardship can be an effective way to build the organizational resilience, which helps to build value over the long term.
- If we look at measures like return on equity per share and return on invested capital, do we find that well-stewarded companies outperform poorly stewarded companies? What proxies can we use to measure stewardship of companies externally?
- The link between stewardship and long-term sustainable financial performance deserves more academic analysis.

[50] Zahra et al (2008).
[51] Miller & Le Breton-Miller (2006).
[52] Miller & Le Breton-Miller (2006).
[53] Pirie & McKuddy (2007).

9. Future: Scenario of stewardship

What would a world look like that embraced stewardship and acted on its principles and values? In this stewardship utopia, our scenario would be the following:

1. All players in the stewardship ecosystem are committed to inclusive, long-term value creation. They work together to support and enhance stewardship, by recognizing the responsibility for the part they play and understanding the dynamics of the interdependent relationships.
2. Shareholders are committed to the long-term value creation of the company; they engage in a transparent and efficient exchange with the boards of directors of the companies in which they invest, to share information on investment goals and the companies' strategies and progress towards delivering long-term, sustainable performance that also contributes to the well-being of society.
3. At the societal level, interaction is based on trust between all stakeholders within the stewardship ecosystem. Where interests are aligned, community and corporations can form effective coalitions to progressively shape the stewardship agenda.
4. Steward leaders engage and empower their people, creating a vision of the future toward which they are collectively working, to inspire them with the passion they need to help them to achieve their own potential while ensuring the company fulfills its purpose.
5. Organizations have a clear purpose and mechanisms in place to safeguard both short- and long-term viability, acting in a way that warrants the trust that the community in which it operates places in them.
6. Steward leaders are able to rise above tough and challenging economic realities, confronting difficulties head-on. Driven by their strong moral force, sense of responsibility and balanced judgment, steward leaders provide the even keel organizations need to weather times of crisis. Guided by their values, steward leaders have a wide-angle lens when assessing the lasting impact of their actions; they create positive, lasting legacies for society at large.
7. Inspired by great stewards, other areas of society are inspired to emulate them, creating greater trust among societal actors. Better relationships and communication would lead to greater information symmetry, opening up possibilities for new kinds of collaboration and long-term wealth creation that benefits a wider number of societal actors.

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Appendix I: Questions for reflection

Organizationally

- How do stewardship values influence corporate culture?
- What stewardship values does your organization espouse?
- Is your corporate purpose aligned with your key stewardship values?
- How assured are you that your organization makes decisions based on your values?
- How do your leaders inspire stewardship at all levels of the organization?
- What societal legacy will your company leave in the long-term?

Culturally

- Are some societies more favorable to great stewardship?
- Are there cultural elements that favor stewardship in your culture?
- What are the universal elements of stewardship?

Investors

- How do your owners engage with your stewardship commitments?
- What are key elements of responsible ownership for stewardship success?
- How active should institutional investors be on stewardship?
- Will institutional investors' stewardship increase? What are the risks?
- Do stewardship codes play a real role in fostering stewardship behavior?
- What is the oversight role of boards on the one hand and institutional investors on the other in ensuring stewardship?

Government

- In your national context, how does regulation help or hinder stewardship?
- How can policy makers best regulate what businesses can do while maintaining flexibility for stewardship creativity for the social good?
- Is the state the greatest of all stewards?

Educators

- How can business schools and other educators proactively steer different forces to contribute to greater stewardship?