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What is the moral responsibility of commercial organisations? It was once thought that an executive team’s sole responsibility was to its shareholders, whether that be family owners or institutional investors. But times have changed as increased attention is focused on how business behaves, both in terms of ethics and sustainability.

Some companies, like Unilever, have seen this coming and are leading efforts to align their business activities with sustainability. But there are many more lagging behind and struggling to walk the tightrope of balancing profit with ethical and sustainable practices.

And yet it is in every organisation’s interest to model their purpose around the benefit they bring to the community they live and work in, the people that work for them, and the future prosperity of the company.

Investors are responding to the public pressure that business should be a force for the good of all of society. Chendi Zhang has discovered that firms investing in Corporate Social Responsibility reduce their systematic risk, ie the chances of going under when a downturn in the economy hits.

For example, companies investing in green practices are recognised and valued by consumers, and are able to charge higher prices, thus giving them a buffer when a recession arrives. Hence, ESG (Environmental, Social and Governance) investing has become an increasingly popular way of pushing corporations to adopt ethical business practices, and it now comes with the added bonus of diversifying risk.

Taking a moral stance, however, is not without risk and can damage short-term profits, as Nike found out when the sportswear multinational used Colin Kaepernick as the face of its latest ‘Just Do It’ campaign. Nike supported Kaepernick after he was ostracised and without a team due to his protests against racial injustice in the US by ‘taking the knee’ during the national anthem that starts every NFL game. To use him in their adverts was a bold move by Nike which drew widespread criticism, including from President Donald Trump.

In this issue, Hari Tsoukas argues that the stance was worth the short-term hit to Nike’s share price. It redefined the company with a moral purpose. Nike had taken a stance and used its considerable economic clout to drive change. Even if Nike had not backed Kaepernick, it would still have had to make a moral decision as it has many black athletes on its roster.

Nike’s actions highlight that business is much more than weighing up the data and taking logical decisions. Business requires people to take a stance when the outcomes are unknown and risky, which is where wider ethical values can guide business executives. Indeed, business leaders should directly confront their ethical dilemmas, and steer their organisation through them, thereby giving their employees a purpose they can be proud of.

Moreover, the welfare of their employees is arguably a company’s first moral duty, and yet Kim Hoque has found not all staff are included. Those with a disability are woefully ignored, with the UK shamefully having one of the worst disability employment gaps in Europe. In this issue, Hoque explores how the disability employment gap can be closed.

Finally, Frederik Dahlmann illustrates how businesses at the forefront of sustainable practice are bringing their supply chain along with them, where collaboration is key. He argues that sustainable practices are mutually beneficial for all organisations and are no longer an option, but a necessity.

Young people are driving businesses to confront their ethical dilemmas head on. To survive and prosper, organisations have to demonstrate to their employees, and potential employees, that ethics and sustainability are at the heart of their purpose, not excessive profits.
Six factors crucial in lifting design to a strategic level

Design thinking has become an established part of successful innovation, but many firms are missing out on the benefits of design being part of strategy.

by Pietro Micheli
This quote is not from the Head of Design of a leading architect, but from a large financial services company. Just a decade ago, the idea that a bank would have design embedded at a strategic level on its board would have been fanciful. Since the turn of the century design’s influence has grown, with design thinking well established as the best way to produce innovations and new products. But in recent times some leading companies have been attempting to push design further up the organisational chart and into the C-suite. Global management consultants Accenture have acquired design firm Fjord, bank Capital One snapped up user experience consultancy Adaptive Path, while pharma diarrhoea multinational Pfizer Co have appointed designers to their boards. Indeed, PepsiCo’s Chief Design Officer Mauro Porcini argues design is central to succeeding in today’s business environment and has been charged with making part of not just the firm’s strategy but its culture as well. Mr Porcini told Fortune: “People don’t buy, actually, products anymore, they buy experiences that are meaningful to them, buy solutions that are realistic, that transcend the product, that go beyond the product, and mostly they buy stories that need to be authentic.”

But even he admits it is a gargantuan task to become a truly design-led company. Despite its well-researched benefits, very few firms have managed to push design all the way to the boardroom for it to be part of a company’s strategy and even fewer have succeeded in it becoming part of their culture. Strategic design – which is defined as design affecting the long-term sustainability and competitiveness of an organisation – has been found to be of great benefit to branding, innovation and differentiation, while designers have methods that can bring unique insights to strategy formation and implementation. Design brings to strategy how people emotionally relate and engage with a product or service – it informs strategy. It’s a way to create and develop a strategy or a strategic way of thinking.

For example, a hotel might want to differentiate its rivals in a town, and design can help do this by observing people’s experience and getting in touch with what users want. It might find they don’t want a person at reception; they’re happy with a computer because it is quicker. The organisation then builds a strategy around such insight to be the first automated hotel.

So it’s not that it’s developed by a technologist that has created the so-called software or, and therefore, wants to make the hotel robotic; but that’s because that’s the isn’t design has enabled the hotel to understand what customers want – it is a bottom-up process to strategy.

They can or become the strategy, where design becomes a way to get closer to the customer. For example, Virgin Atlantic has retained all its staff around design thinking. Design is part of everybody’s remit and so user-centred innovation becomes a strategy that can deliver a competitive advantage.

There are many more examples and insights that follow suit, yet little is known about the how this is achieved. But we can learn from the early adopters as to exactly how an organisation elevates design to a strategic level and what the pitfalls and the enablers are to doing that.

After undertaking 53 interviews with key executives and designers at 12 companies attempting to elevate design to a strategic level, I found six important factors in implementing strategic design. But each of these factors can have a positive or negative effect, depending on how they are deployed.

1 Top management support

Any major change at a company needs to have top management buy-in – with somebody from the top driving it or at least endorsing it. It is the same with strategic design. But it depends how that kind of buy-in and leadership support manifests itself. From my research, where it worked out well, the head of design or CDO was not only given the necessary resources, but was left alone and given a large amount of autonomy.

Top management were not oppressive. They said: ‘Off you go. I’m going to manage a bit of the politics, but it’s your role now.’

In cases where it went wrong, top management became completely oppressive. They started to interfere with all sorts of decisions and forced their opinions on employees or, in one case, the company to create that kind of buffer for design. And if design is pushed into a company to create that kind of buffer for design, then it doesn’t go anywhere. Where companies did well was when they changed the process of creating or a product or service for design to have flexibility.

So strategic design relies on whether there is clarity around which rules it can play across the process, from ideation to prototyping, with flexibility and a bit more time given to these areas. This is particularly true at the beginning, where ideation sits. Altogether, organisations that wanted to make design more strategic hopped in their intentions because they kept, essentially, their own development processes the same. So design may need more time on one bit of the process for a particular project, but they’re not getting more time on the rest.

A good example of developing this flexibility in the process is Grapple, a manufacturing company in the UK that produces swapping devices for farming. It has a process that works, but it is not formalised – so much so that employees don’t have job descriptions. Instead they are encouraged to work on all projects, plus they have a lot of interaction with clients in their innovation and ideas office.

And yet they have targets, such as 25 per cent of sales have to come from products less than four years old, and they work towards them.

4 Inter-function collaboration

Design needs to be able to work with others from a variety of functions because they will have different points of view on the same project. But this needs to be done carefully or it can be overcomplicated and not at all good design.

As the start of the project, it is really important for a company to have a very multifunctional team, with input from marketing, design, operations and more working together iteratively.

This is what Barclays tried to develop, it changed the incentive of its headquarters to reflect this inter-functional teams-building approach, installing what it called ‘hopper’ tables, so that teams made up of operations, business analysts and designers could stay focused on a project without multiple meetings throughout the building. That worked well if you still have a clear finishing line with a clear decision maker. Otherwise you create design by committee; everybody wants to have a say, there is no clear leading voice and a product is eventually produced that nobody would say anything against, but nobody would actually buy, because it’s a compromise.

Third party voices can slow the project down.

The process needs to have input from many areas and lots of research, but it needs a designer to be decisive and to distil that information down to the crucial guiding elements for it to succeed.

5 Evaluation of design

The measurement of the performance of design was also crucial. Companies typically like to have a tightly defined performance measurement system, but this is not appropriate for innovation and design.
For example, a chair manufacturer will have a certain idea of volume, pricing, profit margin, who will buy it and an understanding of where it will make the money that justifies and covers the costs.

But, if it wants to be innovative, it can’t do this as much because it is impossible to know these measurements when creating something new, such as a stool, so it needs to be a bit more flexible.

What some companies did was they almost removed any form of measurement or targets, but that just created vagueness. Leaving design with a blank piece of paper and telling them to go off and express themselves – that doesn’t work.

Companies swung back and forth from measuring everything to measuring very little. But what really worked was collecting the data at the end of a project and producing a really solid review.

So once the product or service has been launched, let’s see how that works – what is the take-up? What are the levels of complaints, satisfaction and repeat purchase?

Companies were excellent at showcasing their design successes. They would hold an annual event internally where they would display products or case studies of services being used.

For example, a packaging company called Agile would display the bottles and boxes it had designed for Johnnie Walker or Baileys, so the finance department and the CFO could see how beautiful they were and appreciate the importance of design.

And big successes can become a symbol of design’s importance. They should be showcased and be the legendary tale for design, like General Electric’s MRI scanner for children.

Herman Miller, the US-based furniture manufacturer, did this well by creating a little bible of stories on all its projects. After each post-mortem review, it would be included in the manual, so employees could dip in and see what worked and what didn’t in each project.

6 Showcasing design
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This internal communication really helped elevate the status of design, especially through events where it could be seen and touched – they were very effective.

In cases where this showcasing didn’t take place other departments held a stereotypically cynical view of designers as simply good at drawing and had unrealistic expectations on how long it took to produce a concept.

If a company can get these six factors right it is on the way to pushing design to a strategic level, which, in these times where experiences are valued more than possessions, is a real competitive advantage.

In a culture of experience design is vital. We live in a world where organisations offer a product or a service and we, the users, have an experience. We have experiences every time we drive, when we are looking at our monitors and when we get into a classroom; and the whole point of design is to try to be empathetic.

That is design in the strategic sense – that focus on the user – which started with Bill Moggridge, who co-founded global design consultancy IDEO, and his concept of user-centred design that evolved into what he called interaction design.

But even more worthwhile is when design becomes the culture of an organisation, the dominant perspective of the company. That is the next level and something I saw at Herman Miller, where even the CFO thought and spoke like a designer.

In the fast-changing digital world of today, it is increasingly hard to stay relevant in the eyes of the customer. Design can bring the insight and innovation to do that.

Following these six factors can, over a long time, see an organisation embed design in their psyche, so they, too, become a design-led company.

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Do the right thing
An increasingly savvy public is demanding firms are ethical. It’s time corporate strategy reflected this.

by Hari Tsoukas
he numerous corporate scandals that regularly grace the pages of the national media remind us how difficult the challenge is to maintain organisations, the executives that run them, and the people who work in them, behave responsibly.

A common cause of these types of problem is the multiplicity of objectives in an organisation: the pursuit of excellence in organisations, as well as a better alignment between the organisation and the demands of external stakeholders.

Ethics may seem a remote and academic topic for managers to consider. However, ethics has very practical and meaningful relevance for managers, who, through specific actions to incorporate ethical considerations into the organisation’s strategic decision making, can achieve the alignment outlined.

In a broad sense, ethics is about asking certain types of questions – how we ought to act, morally speaking. These are questions we not only ask in our personal lives, but questions that senior executives necessarily ask when determining the strategy of their organisations.

What is the organisation’s purpose? What direction should the company go in? How is the firm going to compete with other firms? These are fundamental, practical questions about the strategic interests of the organisation – how they are to be conceived, broadly or narrowly, short term or long term – through which the leadership comes to understand and set the strategic tone for the organisation.

They are also questions that need revisiting regularly, as part of repurposing the business in a constantly shifting business landscape.

To understand how ethics plays into corporate strategy in a way that allows managers to better balance excellence and success, I favour an approach that references elements and ideas that date back as far as the work of classical Greek philosophy, Aristotle in particular. We work on virtues – the “good life”, character virtues and practical wisdom – remain of great importance for us today.

As old as these concepts are, they are equally relevant to our 21st-century corporate world.

Essentially, for Aristotle, a life is worth living when it aims at becoming a good life. A good or fulfilled life is one that fosters the cultivation of virtues, as without virtues we cannot get on well in life. To have a virtue is to strive to excel at something, and there is a moral dimension to this, as it involves, for example, humility and hard work.

The character (or moral) virtues that people develop, such as courage, generosity, and justice, for example, shape the way that individuals conduct their activities and meet collective ends.

In a way, the virtues ‘programme’ people to make good choices of action. However, individuals also have to deliberate and consider what to do in a given circumstance.

What kind of virtuous behaviour is required in this or that particular context? This demands practical wisdom – an intuitive sense of what is the “master virtue” in the sense that it takes into account the particular circumstances in which the moral virtues, which sometimes may clash (for example kindness versus sincerity), are activated.

Practical wisdom, when developed, provides knowledge of the moral virtues, the circumstances that are being encountered, and an intuitive sense of what to do, acquired and inculcated by previous experience and working with others.

As we are reminded all too frequently, in the corporate world, being highly skilled or having a thorough understanding of company policies and procedures is not enough to ensure ethical behaviour. After all, corporate wrongdoing is often perpetrated by highly skilled, exceptionally knowledgeable individuals.

What is lacking are the character virtues and practical wisdom that ensure the right course of action is chosen at the right time.

Elements of Aristotle’s work are potentially useful in helping organisations understand how to embed a more ethical approach into their corporate strategy work. But to reach these elements more practically useful for managers and organisations we must also add some of the ideas of Scottish philosopher Alistair MacIntyre, author of After Virtue.

MacIntyre wrote about “practices”, by which he meant coherent, complex forms of socially established co-operative human activity, through which particular “goods” associated with that form of activity are realised.

For the purposes of building an ethical component into organisational strategy work, we can think of practices as the productive core practices of an organisation, without which that organisation would not exist.

Take practitioners such as software writers developing open code, nurses attending patients, or maintenance technicians servicing a mobile telephone network.

All these people are working in their respective “practices” – software development project teams, A&E nurses staff, field engineer units. They are engaged in the ongoing pursuit of that practice, in which they produce and deliver satisfaction from the internal goods of the respective practice – software development, nursing care and telecoms engineering.

These practitioners, engaged in their practices, need virtues in order to do their jobs well – virtues such as honesty, diligence, tenacity, prudence and fortitude, for example. Virtues also shape the relationships practitioners have with each other as they go about to further their practices.

MacIntyre also introduced the idea of the “institution”, recognising that core practices do not produce organisational success on their own. Core practices need to be institutionalised – to be involved in the competitive allocation of resources and rewards – in order to be sustainable over the long term.

In other words, core practices need to be managed for attaining an overall organisational purpose. If core practice members carry out the primary task of the organisation, managers carry out institutional work.

The latter is a practice in itself. To put it simply, organisations consist of two practices: the core practices that produce products and services and the institutional practice that seeks to provide coherence, direction and sustainability to the core practices.

Although closer to creating a practical framework for executive action, there are still some challenges to overcome. MacIntyre’s view of practice is one of inherent co-operation. However, co-operative behaviour towards organisational goals requires specific types of structures and expectancies to be in place within the organisation.

Research shows that individuals will often identify strongly with their practice – as an A&E nurse or a telephone engineer, for example – and seek to protect and defend those interests at the expense of the organisation’s overall interests. They may, for example, engage in behaviour to protect their local autonomy at the expense of headquarters-led initiatives. Also, a close and narrow focus on excelling at their own activities may blind practitioners to what is needed for the organisation to succeed as a whole.

Practitioners may create a bubble removed from the realities of the world around them. As a result, they may lose sight of the fact that what they are achieving within their practice, no matter how accomplished, may no longer serve the interests of the organisation’s overall purpose or indeed meet the changing expectations of the organisation’s stakeholders.

Instead, the practitioners continue to preserve and improve existing standards of excellence, impervious to the fact that their efforts are ultimately unproductive when considered in the context of the organisation’s strategy.

These issues need addressing. The senior management must ensure that both the institution and its core practices work together in a coherent way, serving the interests and goals of the organisation overall and allowing core practices to be successfully sustained over time.

## Ethics versus Virtues

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These issues need addressing. The senior management must ensure that both the institution and its core practices work together in a coherent way, serving the interests and goals of the organisation overall and allowing core practices to be successfully sustained over time.
An ethically alert senior management can sense the changing shifts in public opinion, in customer requirements, in legislation, in what people want broadly, and rearticulate the organisation’s value and purpose and the behaviours required to deliver that purpose when necessary.

To do this, I suggest that managers engage in a few distinct types of decisions-making activity, which should be a central part of strategic management in any organisation. The first of these activities is endowing the organisation, and its doing so the core practices, with a unifying purpose and common values. I call this ‘values articulation’ work. Senior management needs to arrive at an organisational purpose that contributes to the good of the community at large. This relates to the idea of the ‘good life’.

The good life is about purpose. Indeed, corporations have recently been asking these types of fundamental question – what is the purpose of our business? For example, are social media firms just platforms or are they also publishers? Do they merely connect people or do they deliver content as well? Or do they publish content as well? Do they provide, for example, identifying appropriate rules, structures and routines. It means developing internal capabilities. It involves putting in place what is required to consistently perform the co-ordinated tasks required to achieve the organisation’s purpose.

This will include, for example, defining and rearticulating the organisation’s value and purpose, and the behaviours required to deliver that purpose when necessary.

A second aspect of strategic management should concern capability development. This kind of activity involves putting in place whatever is required to consistently perform the co-ordinated tasks required to achieve the organisation’s purpose. This will include, for example, identifying appropriate rules, structures and routines. It means developing internal capabilities. It involves putting in place what is required to consistently perform the co-ordinated tasks required to achieve the organisation’s purpose.

It goes without saying that for an organisation to continue to be successful it must keep differentiating itself from its competitors. Using conventional strategy tools, senior managers analyse how the organisation can maintain a sustainable competitive advantage by meeting changing stakeholder demands. However, in order to do this, especially as this is a constant struggle, there will be inevitable disruption of the organisation’s core practices. While these values may not be explicitly articulated, although they may be in a narrow way for legal, regulatory and trade purposes, for example, individuals at all levels of the organisation should be aware and understand what they are. Insofar as values are internalized and practised by the members of an organisation, they develop into dispositions for action, namely virtues.

When an organisation avows a purpose and makes a value commitment, creating value for a community, it forms a relationship with that community and the various stakeholders involved. But, over time, the needs of the community change, prompting further questions. For a provider of a social platform, for example, what personal information is it allowed to share with others? Should certain types of communication be filtered or censored? The organisation needs to be self-aware since the various ways in which it currently creates value for external stakeholders may be at odds with the shifting interests of those same stakeholders.

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Further Reading:
The luck of the prepared

Great performance doesn’t always indicate great talent, luck plays a part as well, but people ignore this. It’s something strategists can take advantage of.

by Chengwei Liu

A rational person would ever enter the lottery. The chance of picking the right six numbers and hitting the jackpot in the UK’s National Lottery is one in 45,057,474.

But even in something based purely on luck a strategy can be found. If it was mandatory to play the lottery, how do you enhance your prospect of winning a bigger pay-out? Answer: always pick numbers above 31.

This is because analysis has shown that the majority of people choose numbers associated with their birthday or a family member’s birthday as their ‘lucky’ numbers. So picking above 31 will ensure that if your numbers are chosen you will get a much larger slice of the winnings.

This kind of contrarian thinking can be applied to business as well, where strategy and behavioural science can be combined to exploit the many seemingly irrational biases we all have. It is something I have been researching for nearly a decade.

I show how recognising biases that we have, fixing your own and then exploiting others can lead to a successful strategy for business. How exactly you do it needs solid evidence and analysis to provide a strong foundation for strategising.
Hence, I call my approach 'Analytical Behavioural Strategy', in drawing on behavioural science knowledge to search for contrarian opportunities and then utilising data analytics to formulate a specific exploitation strategy to gain a competitive advantage.

For instance, most people don’t recognise regression to the mean, which can be used to quantify the impact of luck on performance. Regression to the mean happens whenever a performance is not entirely under the control of the person or organisation, such as sports performance or firm growth. A great performer suggests the manager is a lucky star but should be as good as their current performance, i.e., regressing downward to the mean. The good thing for a contrarian strategist is that many rivals will naively assume that the great current performance will persist. Let’s look at the music industry. If a new band or musician has a top 20 hit should a music label immediately try to sign them? My analysis of 8,297 acts in the US Billboard 100 from 1980 to 2008 would suggest not. Music label bosses should rely on attracting top talent, not more so than universities. Typically, if an academic can publish in one of the recognised world elite journals they can demand a premium wage from universities.

But when I evaluated 1,100 leading journals across natural and social sciences, I found that having a high number of citations does not persist. If a journal published an exceptionally highly cited paper – higher than 500 citations – its next volume’s expected citation regresses disproportionally down to the mean.

The implication is that the additional citations received beyond the cut-offs are ‘unilateral’; these extra citations should not be attributed to the journal’s superior quality, but should instead be due to the ‘Matthew Effect’, which is when eminent scientists will often gain more credit than a comparatively unknown researcher, even if their work is similar. Here is the problem: these leading journals tend to acquire their elite status by having a high impact factor, but the impact factor is sensitive to exceptionally highly cited papers. My results show that these ‘outliers’ do not indicate superior quality. Hiking policies solely based on counting the number of publications in these elite journals are as if universities are rewarding good luck. Universities could use my approach to pick up underachieved talents, such as those academics who publish in journals with a few exceptional impact factors in their field but do not do consistently. Otherwise, universities not only overpay some academics for their luck, but will inevitably be disappointed when the hired stars’ academic performance regresses to the mean.

Another question growing businesses face is which markets to export to. Naturally, companies tend to those Asian markets with a high GDP growth rate like China or India. The problem with such a strategy is that most of their competitors will be heading for those countries as well.

A careful analysis of GDP growth around the world reveals the problem to be. Some countries have a very poor growth rate (in the bottom 10) it will perform significantly better than a comparatively unknown researcher, even if their work is similar. Here is the problem: these leading journals tend to acquire their elite status by having a high impact factor, but the impact factor is sensitive to exceptionally highly cited papers. My results show that these ‘outliers’ do not indicate superior quality. Hiking policies solely based on counting the number of publications in these elite journals are as if universities are rewarding good luck. Universities could use my approach to pick up underachieved talents, such as those academics who publish in journals with a few exceptional impact factors in their field but do not do consistently. Otherwise, universities not only overpay some academics for their luck, but will inevitably be disappointed when the hired stars’ academic performance regresses to the mean.

A third example is when eminent scientists will often gain more credit than a comparatively unknown researcher, even if their work is similar. Here is the problem: these leading journals tend to acquire their elite status by having a high impact factor, but the impact factor is sensitive to exceptionally highly cited papers. My results show that these ‘outliers’ do not indicate superior quality. Hiking policies solely based on counting the number of publications in these elite journals are as if universities are rewarding good luck. Universities could use my approach to pick up underachieved talents, such as those academics who publish in journals with a few exceptional impact factors in their field but do not do consistently. Otherwise, universities not only overpay some academics for their luck, but will inevitably be disappointed when the hired stars’ academic performance regresses to the mean.

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From cloud to fog: Our connected future has arrived

Tech giants are coming together around the world to deliver a revolutionary new connected way of living and working.

by Sotirios Paroutis
The devices that surround us in and out of our homes, the devices that we carry with us, these devices collect a vast amount of data that can be stored and analysed, and hospitals will benefit from smart diagnostic tests and the automation of routine procedures, allowing extra resources to be channelled where they are needed in A&E departments and intensive care wards. Agriculture will benefit from smarter analysis of soil and growth conditions, enabling crops to be farmed more efficiently.

Fog computing will have an even bigger impact in the development of ‘smart cities’, where traffic management systems, public transport, healthcare provision and social services, for example, can be linked to provide greater efficiencies.

The changes to our work environment can be summed up by the acronym CHANGE. This stands for Cloud computing, Healthcare, Agriculture, Networking, Geolocation services and Ecosystems.

Cloud computing or data storage will be supplemented by fog computing, which enables the retrieval of data and decision-making, fog computing can provide greater efficiency because the more data travel in the cloud the more it can be intercepted. Fog computing devices can be encrypted using stored biometric data. The use of mobile phones to make payments and conduct banking transactions, for example, would not have been possible without the strongest possible security. Finally, fog computing supplements the storage capacity of the cloud. This is the technology that underpins the development of driverless cars. Smart vehicles currently being trialled generate 33 gigabytes of data per hour, roughly a quarter of the capacity of the average laptop. This data can only be processed locally via a secure fog computing network.

IoT continues to expand rapidly. Market research company Gartner has forecasted by 2020 there will be 26 million smart devices worldwide. This is focusing corporate minds on investment opportunities. In January 2019, the OpenFog Consortium merged with the Industrial Internet Consortium to form the largest consortium of its kind in the world. By bringing together the two consortiums, there are now more than 200 corporate members such as Cisco, Intel, Dell, Bosch, General Electric and Huawei.

Fog computing is the key to effectively co-ordinating services. This is where the big gains are to be made – for example, in the design and operation of citywide traffic management systems, centrally co-ordinated waste disposal, citizen healthcare initiatives, shared bicycle schemes, telecommunications hubs and citywide crime detection and prevention. All of these initiatives are based on the city’s ability to capture and share vast amounts of data.

A good example of this can be seen in Chicago where the Illinois Medical District (IMD) and the global consulting company, PwC, have collaborated to create a national hub for medicine, innovation and research. With more than 40 healthcare organisations, four world-class hospitals, two universities and research labs, IMD is set to become a health innovation destination. This in turn is leading to wider improvements and leveraging investment in the area’s transport infrastructure and public services.

Fog computing will connect people, devices and services, managing two train lines and seven bus routes that move 82,000 people throughout the area weekly, as well as protected bicycle lanes and bike-share stations.

The proposed development of public Wi-Fi, digital kiosks, transportation and intelligent lighting will enhance the quality of life for citizens as well as create new opportunities, sustainable urbanisation, smarter infrastructure, and scalable services.

The OpenFog and Industrial Internet Consortium is assessing 31 smart city projects around the world including Paris, Nice, Amsterdam, Barcelona, Chicago and Milton Keynes. In each case the threats and benefits are different. But information sharing could create a blueprint for the city of the future.

33 gigabytes of data per hour is really 1/3200th of the average laptop. This data can only be processed locally via a secure fog computing network.

In the future, firms may install smart technology to assist with decisions or carry out tasks that humans perform at present. An example I often cite is the impact of automation on the freight and logistics industry. The development of driverless trucks would reduce the demand for truck drivers, as freight could be transported at night, travelling non-stop on less crowded motorways. Driverless technology would mean freight companies not being bound by the legal number of working hours a driver can spend on the road to comply with safety practices.

Another example is hospital automation where diffusion pumps used to administer drugs intravenously can store and feed back information on the drugs being prescribed and alert doctors to possible dangerous combinations of drugs. The advantages are clear, but firms need to assess the challenges involved in introducing fog computing and allow time for new working practices to evolve.

Companies should design solutions based on the technology they get from the end-users, while in smart city pilots, like Chicago’s healthcare hub, success will come from the active participation of citizens in the change process.

Fog and edge computing can really come into its own as a viable ecosystem of the future when stakeholders are fully engaged in the process and where the participatory and end-users can feed back their ideas to create solutions with wider societal impact.
ALGORITHMIC MANAGEMENT LEARNING FROM UBER’S WOES

Mareike Möhlmann

Uber has fallen foul of relying on computers to manage its drivers. Platforms can learn from its mistakes.

by Mareike Möhlmann

Next time you relax into the back seat of an Uber after a night out, spare a thought for your driver.

They have spent the evening at the beck and call of an algorithm, which dictates who they pick up, what route they take and how much money they earn. If they fail to obey the instructions imposed upon them, they risk getting bounce-off the platform — and if they have a problem or want to dispute a decision, they are at the mercy of an automated phone line rather than a human being.

As organisations increasingly turn to digital platforms to deliver their services, the algorithmic management practices used by Uber are becoming more widespread. It’s not hard to see why organisations are keen to go down this route. It allows them to respond quickly and efficiently to customer demand and to manage huge amounts of people (three million worldwide in Uber’s case) with very little management manpower.

Our research suggests, however, that not all in the automated garden is rosy. The way the ride-hailing company is managing its drivers may well be leading to significant cost savings, but it is also resulting in bad feeling and subversive behaviour among drivers, which is counterproductive and has the potential to cause real harm to the business.

A tense situation

My joint research with Lise Zalmanoo, Ola Henfridsson and Robert Gregory revealed that algorithmic management practices are causing tension and leading to fault lines opening up in the employer–employee relationship.

Based on a snapshot of Uber drivers in London and New York, we find, on the one hand, that self-employed Uber drivers have a degree of autonomy. They can decide when and for how long they work, giving them the flexibility to meet family commitments, juggle work or study, or even kick-start a fledgling business.

On the flip side, however, as soon as they log onto the app, drivers are effectively under surveillance, with their every move controlled and scrutinised by the platform’s algorithms and no wriggle room to diverge from instructions, even if what they are being asked to do is not in their best interests.

Lack of transparency is one of the main causes of driver discontent. The algorithms behind Uber’s platform are complex. Drivers struggle to understand how rides are allocated, how ratings are distributed and how earnings are calculated. This leads to accusations of unfairness and manipulation (Uber has previously admitted using behavioural science to nudge drivers into working longer and harder).

These feelings of dissatisfaction are compounded by the fact that drivers feel lonely, isolated and dehumanised. They have no contact with a human manager and typically don’t know other Uber drivers in their area. There are no colleagues to compare notes with, nobody to call on in times of trouble and no community to be part of.

Gaming the system

Anyone who has come across a belligerent cabbie won’t be surprised to hear that drivers have responded to this by raging against the machine. Our research revealed that they were ‘gaming’ the system, finding clever ways to work around the algorithms that Uber uses to control them.

We found examples of drivers secretly colluding to organise mass ‘switch-offs’, leading to a shortage of rides in certain areas and a subsequent price surge. Drivers were also finding ways to break free from the unpopular UberPOOL, which forces them to take multiple passengers who are heading in the same direction, even if it’s not economically beneficial.

There are lessons here for organisations who are developing digital platforms and want to avoid the kind of backlash Uber has experienced. For a start, companies can’t expect to position themselves as ‘partners’ with their employees if they persist in keeping them in the dark about the way algorithms work. Finding ways to get employees actively involved in designing algorithm-driven systems will do much to counter negative feelings and build more supportive and engaged workforces.

Adding a human element to the way people are managed will also help workers feel less like they are being treated as a machine. Uber has recognised this with the recent launch of ‘Greenlight hubs’, which offer walk-in support services for drivers. Developing formal employee communities, which give staff the chance to network and socialise, will also help to create a sense of belonging.

It’s impossible to say whether having these kind of measures in place would have helped Uber avoid its high profile and ongoing run-in with regulators.

What is clear, however, is that current models of algorithmic management are tearing employers and employees apart, rather than bringing them together. More research is needed to understand how digital platforms and the algorithms that sit behind them can be redesigned to bring about a better balance and meet the needs and goals of both parties.

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Inside IBM’s $100m office revolution

The tech multinational has designed a purpose-built office to accompany its agile innovation strategy.

by João Baptista & Kamaran Sheikh
The digital revolution was meant to free us from the office. But visions of sitting on a balcony in the sun with a cool drink and a laptop connected to colleagues around the world has not become reality. Contrary to expectations, the rise of agile brings adaptability and the ability for companies to develop new ways to work. This research has now influenced the creation of a new studio workspace for the IBM team, which has been developed as part of a multi-million pound expansion in London. Interestingly, it is technology companies that have emphasised the crucial role of the physical office in creating an attractive and effective work environment in modern organisations. The office space is the hub at the centre of the most innovative and successful digital ventures, with companies such as Google and Facebook investing heavily in entirely new campuses.

Organisations that empower teams to craft their workspaces - for urgent responses

The flexible nature of the workspace reacted to new demands, stimulated innovative thinking, prompted collaboration and empowered individuals to be creative. This was not the standard static office environment. Organisations that empower teams to craft workspaces by combining physical and digital realms will be the ones that are most effective and attract the employees more able to work innovatively. This requires a culture of open communication where people feel connected and that they are the autonomy to to do things.

There is a growing trend to bring workers back to physical offices around the world has not become reality. Contrary to expectations, the rise of agile brings adaptability and the ability for companies to develop new ways to work. This research has now influenced the creation of a new studio workspace for the IBM team, which has been developed as part of a multi-million pound expansion in London. Interestingly, it is technology companies that have emphasised the crucial role of the physical office in creating an attractive and effective work environment in modern organisations. The office space is the hub at the centre of the most innovative and successful digital ventures, with companies such as Google and Facebook investing heavily in entirely new campuses.

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ut a decade ago, execs at the Financial Times talked about being in the newspaper industry and nervously looked at their rival UK broadsheets The Times and The Telegraph.

Now, with its business model smashed by the internet, the Financial Times’ rivals span the seemingly endlessly wide rainbow of online news sites across the internet.

Similarly, those in the music industry 10 years ago were wondering what Warner Brothers and EMI were doing in their boardrooms - now it is Spotify and Apple and a host of streaming sites across the world wide web who dictate the pace of change.

The digital revolution has disrupted and broken industry boundaries to such an extent that the very notion of working in an industry is dead.

Every MBA student is familiar with Michael Porter’s Five Forces in building a strategy for a company. The oft-quoted strategic tool starts with defining the industry and then building barriers to stop rivals entering.

But thinking about your industry is irrelevant in the digital sphere; barriers are just not possible, especially as the fourth industrial revolution evolves around us with almost everything, from cars to ovens, being connected to the internet.

As a strategy tool, Porter’s Five Forces is less relevant in the digital world. Instead, strategists in the digital age need to think about what we term ‘value paths’ and how their digital product or service can be recombined by users, whether that is a person, another company or even a bot.

Creating value through innumerable connections is how to prosper in the digital world and that involves actively leaving your product open, not building barriers.

To understand where your digital offering fits in the complex web of the digital world, we have formulated the ‘Value Spaces Framework’ as a tool to map the connections and visualise the value paths available.

Traditionally, a product or service can be described as a vertical, such as a car. It may be made up of many different parts from different suppliers, but it can only be assembled in one way to make that one product. Thus, it has a clear product boundary, and strategy frameworks like Porter’s Five Forces look at the product and its industry with that kind of mindset.

The whole industry is based around that product, and value is created within those parts that combine a car. So car manufacturers can compete on features like braking, cornering performance, chassis style and engine power against other cars in the same industry and position themselves around certain features.

But in the digital world value is not created within those vertical industries; instead it arises in horizontal spaces, cutting across industry verticals. Today, for a carmaker, what goes on in Google HQ is just as important as what is happening at Ford or General Motors.

This is because these digital resources are agnostic, in the sense that their meaning is largely defined by their relationships to other digital products or services.

A chair is purpose-built, the parts cannot be used for anything else other than being part of that chair, but a digital product or service can be used in many different ways; it can be recombined with other digital resources to make a totally new service.

Navigating a world without boundaries

Traditional strategy tools are less relevant for today’s connected world. The Value Spaces Framework remedies that problem.

by Ola Henfridsson & Joe Nandakumar
Joseph Schumpeter introduced the notion of recombination as innovation in the 1930s, but the digital world has taken it to a new level. Schumpeter was talking about companies recombining features to make new products, where the design team might take the different components of a car to create a new model.

In the digital world, there is also what we call ‘design recombination’, where the firm purposely recombines digital resources to deliver a new offering. But digital resources are also being recombined by users. They are being left open to be recombined with other digital resources in ways the designer has not even imagined.

Take Google Maps, a product, thanks to its open API that, as of February 2012, was embedded in 2,337 other services, all using it in different ways to mix and match with other digital resources to create new value for consumers. It is the same content, but it invites users to recombine it in thousands of different offerings. Google Maps can be a stand-alone service in a web browser, but it is also a digital resource that can be used as a building block in the creation and capture of value in services like Rightmove. The UK-based online real estate portal uses Google Maps to plot properties available on its site.

Although there are some terms and conditions involved, it is nothing like the car manufacturer signing a long-term contract for a new navigation system supplier. It is a very lean system. Rightmove can, in theory, move to another map supplier relatively quickly if it wanted.

In our Value Spaces Framework, we have four horizontal levels of digital architecture where value is created. In Context – this is data or information like music, news and video that is stored and shared.

Service – software like heart monitors, social media apps and media browsers, which directly serve users as they create, manipulate and consume content.

Network – the transmission software and the physical cables of the digital world.

Device – hardware like smartphones and software that enable storing and processing.

So a digital resource, like Google Maps, would sit on all these levels, most likely content. Thanks to its open-ended nature Google Maps has 2,337 value paths connecting it to other digital resources either across value spaces on the contents level, or up and down the various different levels of the framework. It is these value paths that are the key to success in the digital world.

The more value paths created, the more important the service becomes and the more users it has – this is the network effect, where the more users there are, the more valuable the service becomes for those users. Even if it does not lead to network effects, the value path can still be monetised, whether it is through advertising, subscription or selling the data on to third parties.

To compete in this world, firms need to create as many value paths as possible through their digital resources, what we call path channeling. Once a firm has realised its position on the Value Spaces Framework, it can plot ways to cut paths to other digital resources by creating better and more user-friendly value paths and so channelising the value from ecosystems dominated by others to themselves instead.

This is a competitive strategy that Google is adept at. For instance, in its attempt to tap into the value paths dominated by Microsoft in word processing, Google has offered users of Microsoft Word plug-ins to make Word work directly from Google Drive. Thus Google is seeking to channel value paths through its own digital resources and increase its ‘value intensity’ – this is a rough measure of a digital resource through the number of users or hits on a web page.

It is a very different mindset to the traditional industry-orientated starting where creating barriers is necessary. The digital world is the opposite; it is about lowering barriers and bringing as open and as easy to use as possible – you want other users to take it on and recreate it to generate more value paths.

Thinking of and defining an industry is an irrelevance. After all which industry is Google Maps in? Is it housing or cars or something else? With it being used in 2,337 other digital resources, it is impossible to define and it doesn’t actually matter. A company, instead, wants to dominate these horizontal layers that we refer to as value spaces.

We have seen industries disrupted by digital innovations time and again, and many more are facing this now, such as the car industry. The car is increasingly becoming digitalised, which means more and more of the value that is produced for the customer is related to digital.

As long as car manufacturers keep outsourcing the digital services inside in cars to somebody else, they will quickly lose control of what is creating value and hence the opportunity to monetise. The car will just be the box for the value paths owned by other companies.

Google may be testing its own autonomous car, but is it unlikely it is looking to enter the ‘car industry’ – it thinks much bigger than that. It is all about data and maybe it is looking at using all that data from Google Maps, which has traffic flow data, plus its search engine and mobile phones to redefine transportation around a connected smart city.

It is thinking in this horizontal way, at how it can combine many digital resources in its transportation – and data will be the key. Data can allow it to control all cars and the traffic flows, then the car makers become suppliers for Google.

Instead of thinking about an industry, the Value Spaces Framework prompts companies to look through industries and at the value paths they can create that break those artificial boundaries. In order to be relevant, firms want to have overlap between their offering and among the users in the space they are targeting.

Car companies want to engage with the customer and generate data about the customer that can be turned into value, but it is very difficult to turn that information into something useful unless they open up and become part of the digital ecosystem, allowing others to recombine the ‘digital resources’ in a car. But this is where it becomes very difficult and where a company needs to understand its position in the Value Spaces Framework. Opening up could increase a car company’s value with many more paths, but it also could be hijacked by users.

Apple spotted this dilemma very early on. It was not the inventor of the App Store. When it released its first iPhone it found users breaking into it and installing applications. It could have tried to stop this through legal means and security software, but instead it saw the potential in creating many value paths for its product and devised, with the help of the App Store, to make downloading applications available to everybody.

But Apple also realised the danger in Google Maps sucking value paths out of its phones and so uninstalled it, cutting the value paths by creating its own map service.

In the digital world this reassessing and hunting for value paths is constant as, without boundaries, a new value path can come from anywhere. If a company is not innovating then it will be overtaken; it has to be updating and looking for more value-creating paths all the time.

Digital innovation is at the heart of any strategy in the digital age and to be successful doesn’t stop at a one-off cleverly designed resource. Launching the product or service is just the beginning; it then needs to be attractive enough so it is recombined many times by other users, with new updates and value paths constantly being sought.

In the digital world, innovation is not a way to get ahead in an industry, it is a way of life to thrive in an ecosystem.
When Apple legend Steve Wozniak came off stage in Vienna and said it was the best crowd he had ever talked in front of, Ben Ruschin knew he had cracked it.

Ben had paid the co-founder of Apple a good sum to appear at his second WeAreDevelopers World Congress conference, but the reaction from the crowd and Wozniak had made him more than covered the costs.

‘It was unbelievable, grown men with beards were crying when they met him,’ says Ben. ‘People were lining up with their tablets and iPhones to get Wozniak to sign them. He was a god for them, a true rock star and they were so glad to meet him.’

A year later and Ben moved the annual World Congress to Berlin with 10,000 packed into the CityCube to listen to big names such as Garry Kasparov.

‘Having started out as a digital marketing agency Ben’s business has now morphed into a hiring platform with the biggest developers’ conference in Europe – and it is the secret to his company’s success.’

WeAreDevelopers is a two-sided hiring platform, but the key is the sense of community. Ben and his co-founders have created the legendary games Doom and Quake, speak as well and he was treated like a rock star – these guys and girls he is a genius and a big part of their lives. ‘This is the reaction we want. Our goal is to be a community providing amazing experiences that developers will associate with our brand. When they get any automated emails from us, they won’t ignore them, they will think about us as the cool guys and open them.’

The events and the sense of community create an emotional connection with their key audience. And creating a sense of brotherhood among developers does not stop with an annual conference. Ben and his team of 70 staff are using the WeAreDevelopers platform to help developers create their own local events, just as TLDs – the ideas conference – has done with TLDs.

‘Developers go to meet-ups in their city and listen to talks about tech and programming language. It can be 10 to 100 people,’ says Ben. ‘We will support them and pass on our knowledge to help them set it up. They are happening all across Europe and we will support them and provide expertise. We have partnered with 300 organisations to promote their events, it helps us stay in touch with the community.

‘The better we understand developers, the better we can match them to their perfect job. Money is not the priority for developers – they are travel-savvy want to move locations and work in cool cities for cool companies and be challenged by their work.

Our research shows that even where the offer is located in the cities in developers’ top five wishes, along with flexible working hours, the meaning of their work and the culture. We need to understand this and find companies that fulfil their ambitions.’

To remain a trusted source for developers, potential employers are carefully vetted and need to meet certain criteria, such as already having at least 10 developers, hiring 10 developers in the next 12 months, and having English as their main language.
Companies like Uber and Airbnb rely on the trust of strangers. Here is how they can repair it.

by Mareike Möhlmann
The sharing economy sounds like an attractive idea, with its promise of more convenient access to services and products, at low cost. Via digital technology, the sharing economy brings billions of people together to interact and transact. This relatively new and rapidly growing corner of the digital universe is worth many trillions – $229 billion in China alone, according to The Economist.

Yet, while the sharing economy might be expected to be an unalloyed success story, accompanied by runaway growth and stellar media coverage, the reality is less straightforward. Unfortunately for its proponents, the sharing economy is having something of a bumpy ride. Take Uber, for example. The ride-sharing firm has been mired in disputes across the globe, its CEO resigned in 2017 following investor pressure, and it posted a loss of a billion dollars in the quarter ending September 2018. Other sharing economy firms have run into difficulties too. With ride-sharing firms, there have been reports of sexual assaults on passengers and inadequate driver background checks, for example, while ride-sharing drivers have gone to court to claim that they are employees rather than contractors. Home-sharing firms have tangled with municipal authorities over local laws restricting the use of residential property for short-term rentals, as well as having to deal with stories of accommodation being used to host pop-up parties and brothels. The result is a trust deficit – a lack of confidence that needs to be overcome if the full potential of the sharing economy is to be realised.

The sharing economy has led to the creation of some extremely highly valued technology businesses and in a very short space of time (Airbnb was founded in 2008 and Uber in 2009).

While there is no universally agreed definition, one can think of the sharing economy as digitally enabled, peer-to-peer exchange platforms for goods and services, which connect spare capacity with demand, or offer access-over-ownership by enabling renting, lending, reselling or swapping.

While there may be some discussion about definitions, an essential, undeniable truth about the sharing economy is that its lifeblood is trust. Trust is the oil that lubricates the engine driving the sharing economy.

Without trust underpinning the confidence to engage in billions of sharing economy transactions every day, there is no sharing economy, no Airbnb, no Uber, no BlaBlaCar.

And by trust I mean, at its most simplistic, our willingness to be exposed to the actions of someone else, person or business, in the expectation that they will behave in a way that we would want them to, regardless of whether we are able to monitor or control their behaviour.

The concept of trust in a commercial context has evolved from family and community settings to an international rules-based globalised economy over centuries.

The world moved from person-to-person trading relationships based on interpersonal trust, backed by individual reputations, shared norms and behaviours, to institutional trust underwritten by governmental and political institutions, with enforceable rules and regulations, legally binding contracts and sophisticated dispute resolution systems.

However, the digital world has created a new dynamic. The ubiquitous nature of digital technologies allows billions of people from across the globe to interact and communicate in ways that were impossible just a few decades ago.

In the digital age, people are deluged with information, and can access a bewildering variety of products and services. All this opportunity, though, is accompanied by risk.

The digital world is often portrayed as a lawless frontier land, with hackers and fraudsters at every turn. Media headlines, such as the Marriott International’s data breach involving the personal details of some half a billion customers, stories of initial coin offering scams, tales of identity theft and catfishing, or details of the latest malware that internet users must guard against, do little to dispel this impression.

The growing digitisation of the modern world creates an increasingly complex, anonymous and impersonal society that many perceive as unpredictable, uncertain, even intimidating. We are confronted with a much-expanded world, but one that is full of strangers. In many countries and cultures people are taught to mistrust strangers.

Trust is the oil that lubricates the engine driving the sharing economy.
digital technologies is based on the fundamental mechanism of strangers interacting in the digital sphere – even over large distances, or when they have never met in person before.

Hence the importance of trust in online, digitally mediated settings. Trust is a basis for co-operation and community. It is a foundation for the relationships we form, including business relationships, and the decisions we make about obtaining products and services in the marketplace.

Trust helps alleviate the uncertainty experienced in complex environments and mitigate the risk of ‘stranger danger’. And if digital disruption has eroded trust mechanisms created by chance, trust must be reestablished and regained, both interpersonal and institutional, in order to unlock the potential of the sharing economy.

When platform providers get it right, evidence suggests that the trust levels in sharing business models can be extremely high. In an article published in IEEE Security, together with co-authors Frédéric Mazzella, founder and CEO of BlaBlaCar, and Stern School of Business Professor Arun Sundararajan, I looked at the effect of BlaBlaCar’s trust-building DREAMS framework.

BlaBlaCar is a platform that brokers empty car seats to passengers that want to travel long distances and as such is highly reliant on members trusting each other. Our research revealed that the users’ levels of trust in members with full profiles on BlaBlaCar were exceptionally high, and only marginally less than as high as they were with family and friends.

So how can platform providers begin to engender trust at these levels? One step they can take is to incorporate into their services features that are likely to foster trust.

My recently published work with Andrea Geisinger of Oerebro University, highlights the fact that platform providers can use various digital trust cues to build both interpersonal and institutional trust. These cues can help reduce the ‘stranger danger bias’ and boost confidence in the sharing economy, even if they are likely to have a cumulative effect, so the more cues a sharing platform provides, the greater the trust created.

The cues can help to reinforce trust-building dimensions such as reliability, benevolence and integrity. They also relate to aspects of trust that focus on social relationships, and include factors such as shared values and calculative trust, which is based on rational calculation and economic considerations of whether or not to trust.

There are, for example, a number of digital cues that are more focused on providing reassurance about the transactional elements of the sharing services. Payment is an area, for example, where consumers often have concerns.

When a consumer is an item in a store, regardless of how they pay, there are usually well-established protections governing that transaction. And the consumer will often be aware of their rights.

In the world of remote digital transaction there is less certainty. Service users may worry about paying a fee, then not getting what they expected or promised, and not having any recourse or means of obtaining a refund.

However, as the platform providers are often the facilitators of financial transactions across the platform, they can offer escrow services and other dispute resolution mechanisms to provide greater certainty and peace of mind.

Similarly, insurance cover is another area where platform providers can provide assurance. Understandably reports of substantial damage to accommodation rented via home-sharing services, or of serious accidents involving ride-sharing vehicles, prompts questions about liability.

Adequate communication of any relevant insurance covering-sharing services can help reduce uncertainty about what happens in the event of loss or damage.

Trust Information is another important area for sharing services. The ‘fake news’ phenomenon heightens the challenges around verification, verification and trust in a digital environment.

Veracity is also a problem for the sharing economy. But while the news media is still struggling to find a remedy, platform providers can take steps to assure users that information, whether it is user or service-provider information, is reliable.

They can, for example, use secure transaction processes that incorporate digitally deployed certification or validation, as well as other authentication measures. It is also possible to involve trusted third parties, such as government institutions, trusted consumer and trade associations, and companies specialising in certification, in the valuation process.

Furthermore, blockchain technology may be vulnerable to cyber-hacking for example, the loss and theft of digital coins that have been reported in cryptocurrencies. There have also been concerns about how blockchain technologies are rolled out – with some European data-protection laws, as well as other legal measures.

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However, it is also possible to involve trusted third parties, such as government institutions, trusted consumer and trade associations, and companies specialising in certification, in the valuation process.

Further Reading:
Möhlmann, M. and Geissinger, A., 2018. Trust in the sharing economy: platform mediated peer trust. In: N. Baadsgaard, J. Johansen and P. Knick, eds. 2018. Cambridge handbook on social norms, rules and social codes around their visions of the future. And so far the results have been mixed. Given the potential economic power and growth involved, it is questionable whether regulators should be the main arbiters for constructing the sharing economy universe and its rules. It is crucial that civic society, governments, NGOs, regulators and legislators rise to the challenge of allowing the sharing economy to innovate and flourish.

Working together and using a range of tools, whether that is through platforms such as those deployed by BlaBlaCar, digital cars, blockchain technology, or other trust-promoting mechanisms, these stakeholders should be able to go a long way towards overcoming any current trust deficit and insuring trust in the sharing economy overall.

In doing so, they can fulﬁll the promise of the sharing economy as a way to use resources more efﬁciently, deliver environmental and economic beneﬁts, and enable strangers across the globe to connect in conﬁdence.

“Service users may worry about paying a fee, then not getting the service promised or expected, and not having any recourse or means of obtaining a refund.”

Mareike Möhlmann is Assistant Professor of Information Systems & Management and teaches Business Analytics on the Warwick Executive Diploma in Digital Leadership.
WHAT THE NHS NEEDS IS MORE MANAGERS by Ian Kirkpatrick

So long the target of tabloid and political invective, research finds the ‘fat cats’ actually improve hospital outcomes.
Drew criticism from the 'left' for not backing up their doubts about the value of professionals who were not clinicians. Moreover, our research debunks that myth, finding instead a strong statistical link between the increase in the number of managers and the performance of management on a number of measures. In fact, according to the data, the NHS would be wise to put aside the notion of the annual £20 billion to hire more managers, especially as the Government will apply five tests to plans to hire the money, which are:

- Improving productivity and efficiency
- Eliminating provider deficits
- Reducing unnecessary variations in treatment in the system so people get consistently high standards of care wherever they live
- Getting much better at managing demand effectively
- Making better use of capital investment

Meeting these tests will require good management, and that will probably require more managers, something the NHS is severely short of as compared to other countries.

In a highly complex organisation like the NHS – the fifth biggest organisation in the world – managers are needed to coordinate tasks to meet the Government tests. Currently there are around 85,000 managers employed in the English NHS. About a third of those are ‘hybrids’ – doctors or nurses with a frontline position and a management role – while the rest are dedicated managers. But in an organisation of 1.36 million NHS employees, that amounts to less than 9.5 per cent of the workforce in an average hospital trust.

Although having only a modest impact on patient satisfaction, larger numbers of managers resulted in a five per cent improvement in hospital efficiency and a 15 per cent reduction in infection rates. As we noted in an earlier analysis of NHS scandals, the narrative in the media and the poor public reputation of managers is having an effect. Our research also uncovered that Foundation Trusts were significantly more likely to attract media scrutiny, which in turn was found to be a powerful factor in attracting relative lower proportion of managers to staff ratios. It has almost become perceived that managers in those hospitals could be a drain on the NHS. Yet managers can shield clinicians from media scrutiny, dealing with the politics so doctors can concentrate on caring for patients. But it is not just the popular press pointing this idea. Our analysis of four years of data found that in 2009/10, for example, business experts on the board of trusts had no negative impact on service quality and patient wellbeing, but did have a positive impact on efficiency and a range of financial management measures.

These findings run counter to the popular view that slashing managers won’t have any effect on trust performance. Instead, a conservative investment in managers and improving their numbers slightly is more likely to have a positive effect.

So why has slashing managers been so unpopular? There is one key factor that has added fuel to this most notably the case of Mid Staffordshire NHS Foundation Trust, which between 400 and 1,200 patients died as a result of poor care from January 2005 to March 2009. From 2001 to 2009, according to the Francis Report into the scandal cited cost-cutting by management as a significant factor, with managers cutting clinical staff and not spending money on equipment.
Making innovation travel the NHS

Jann Gardner is Chief Executive of the Golden Jubilee Foundation, which combines a hospital and centres for research, clinical skills and innovation to create a crucible for innovation in NHS Scotland.

Core: How does the Golden Jubilee Foundation diffuse its innovations across NHS Scotland?

Gardner: The Golden Jubilee Foundation is unique within the NHS in Scotland. A national NHS Board, the Golden Jubilee family includes the National Hospital, Research Institute, Innovation Centre and Conference Hotel. It is the only national board that is a provider of elective and acute hospital care while having a national provider/insurer role.

Our overarching focus is on delivering care, innovation and excellence through collaboration. We are a strong values-based employer, firmly believing that it is both what you do and how you do it that delivers innovation and excellence. As such, we are very proud of the feedback from our patients about their experience of care and our partners about working in collaboration with us.

We have direct critical partnerships with all Scottish NHS boards and innovation networks and have a formal R&I programme. The Golden Jubilee Foundation designs and develops innovations on a ‘Once for Scotland’ basis through these partnerships and networks. In addition, key opportunities are available through our provision of conference facilities to biotech and medical industries, where best practice and innovation are often shared.

The Golden Jubilee also leads the Innovation Fund for Scotland, allowing us to work with partners across Scotland to bring innovations from bench to bedside.

Working on behalf of the Scottish Government, we have established the Director of Global Development and Strategic Partnerships role as a position in our executive team. This is an exceptional strategic role that allows us to remove boundaries, more creatively develop key partnerships, and work across NHS, industry and academia interfaces.

C: What innovation process does the Golden Jubilee Foundation use in its Innovation Centre?

G: Innovation and values are at the heart of the Golden Jubilee’s vision (leading quality, research and innovation). We use a combination of design thinking, agile and quality improvement approaches, and our values system both encourages staff involvement and recognises their successes.

In addition, we are at an exciting stage of developing our innovation work to provide scale and pace to this programme by establishing an innovation accelerator unit as part of our portfolio.

C: What are the biggest issues in NHS Scotland that need innovation to tackle?

G: Scotland has an ageing population, high areas of deprivation and some of the highest instances of cancer and heart and lung disease in the UK. NHS Scotland needs to develop innovative new approaches to the provision of care that enables the sustainability and resilience to our services. We see the harnessing of technology and the development of new advance practice roles as critical components of this. The fourth industrial revolution of AI and digitisation will help Scotland respond to these legacy challenges from the third industrial revolution.

C: How do the Golden Jubilee Foundation’s Research Institute and Innovation Centre work together?

G: The different parts of our organisation work both independently and in collaboration with one another. Our Research Institute focuses more on conventional clinical trials and the Innovation Centre is working to develop future products and initiatives.

Going forward, we have ambitious plans to create an innovation accelerator unit to undertake strategic partnerships with industry, start-ups and academia to attract significant investment to this area.

C: A WBS study has argued that the NHS has a lack of managers and needs more to improve patient care and efficiency.

G: I believe that NHS Scotland needs to develop effective and values-based leaders who have the skill set to foster innovation. NHS Scotland is committed to developing clinical and other leaders with a range of skills, including entrepreneurship, innovation and digitisation, who are committed to creating or supporting a values-based culture, and the Golden Jubilee has a critical role in this work.

C: How does Golden Jubilee Foundation connect its work with social care in Scotland?

G: Going forward, we have ambitious plans to create an innovation accelerator unit to undertake strategic partnerships with industry, start-ups and academia to attract significant investment to this area.

What are your thoughts on that?

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C: What impact will the fourth industrial revolution have on healthcare?

G: The fourth industrial revolution will be transformational for healthcare in Scotland and indeed globally. This journey has already begun for NHS Scotland and is fully supported by the Scottish Government, industry and academia. There will be huge opportunities for the application of the Internet of Things, AI, robotics and beyond for diagnostics, monitoring, care at home and staff/patient education, but the scope is infinite.

The Golden Jubilee is thrilled to be at the heart of Scotland’s innovation at this really exciting time, and has the ambition and capability to be a critical player in this landscape.

Core: Using technology to remotely monitor heart failure patients, reducing the need for hospitalisation and potentially saving lives through early intervention.

C: What is your opinion on that?

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Four factors
to deal with long-term health conditions

An ageing population is putting huge demands on the UK’s healthcare system. This is how to relieve the pressure.

by Graeme Currie

The headlines in the mainstream media over the 2017–18 winter highlighted the scale of the challenge faced by the UK’s National Health Service (NHS).

During a difficult flu season, accident and emergency (A&E) services across the country were under severe and sustained pressure. Ambulances queued, patients waited on trolleys in corridors due to a lack of beds, and waiting times stretched to six hours and beyond. Terms like ‘crisis’, ‘disaster’, and ‘breaking point’ became synonymous with the state of the nation’s healthcare provision.

Like many other healthcare systems across the world, the NHS is facing a set of factors that makes the delivery of effective, affordable healthcare far more difficult than in the past.

A population that is both growing in numbers and living much longer, technological innovation that increases the healthcare options available, rising costs of treatment (in many cases coupled with constrained resources): all of these factors mean that significant change is required to ensure a healthy NHS.

There are frequent calls for wholesale structural change. Indeed major restructuring in order to make the NHS fit for the future seems to be permanently under discussion.

Rather than consider the transformation of the NHS in its entirety, though – a topic that could easily fill several books rather than a brief article – I want to focus on a specific area of care that presents one of the most difficult challenges for healthcare systems in developed nations: the way that we deal with long-term conditions.

Here, I am referring both to conditions that may be physical (such as diabetes, ulcerative colitis, or obesity), those that are more specifically mental health-related (such as dementia). These long-term conditions affect all age ranges, but many disproportionately affect older people.

The negative impact of poorly managed long-term conditions is huge. Care of some 15 million people with long-term conditions consumes 70 per cent of the NHS budget in England, that is £37 billion annually, and £10.3 billion of the £15.5 billion spent on social care in England.

Without taking appropriate action on long-term conditions, for example, you will continue to get unnecessary acute admissions. Patients end up at A&E, are discharged unsafely, and then end up returning to A&E. It is a revolving door and unsustainable.

Yet, attention to a few distinct measures would make a considerable difference to the effectiveness of dealing with long-term conditions and, in doing so, to the overall effectiveness of the NHS.

Of course, structural reform of the NHS is nothing new. Yet, despite the best efforts of policymakers, the provision of care for long-term conditions remains inadequate. Much of the structural reform thus far, notwithstanding some recent reforms, has focused predominantly on healthcare.

However, long-term conditions offer a different set of challenges from situations that take up a short, finite period of time that might involve, for example, diagnosis, surgery, a brief hospital stay and then being discharged home to recover fully. Instead, long-term conditions involve discontinuous intervention and the movement of patients in and out of different care settings.

Someone might have a more preventative problem that could be dealt with in the community by the GP through lifestyle and diet changes, for example. They may have an associated mental health problem. They may have issues relating to social care – a housing problem, perhaps. An education setting may be involved, given that many mental health issues increasingly affect young people – like eating disorders.

When an older person is discharged from hospital, there is often nowhere for them to go because it is not possible to put a social care package in place. You get admission problems due to ‘bed blocking’, but arguably these are social
There are four process issues, in particular, that are worth highlighting, where action is possible and would make a significant difference.

1. Mobilising knowledge

To begin with, the provision of first-class integrated care for long-term conditions is not possible without the mobilisation of knowledge across organisational and professional boundaries.

Unfortunately, many people seem to eschew the concept of knowledge mobilisation with the implementation of an IT system that facilitates data sharing. And that is part of the problem. Knowledge is different from data, you know that you can hit your target. However, nobody in primary care trust will have their job linked to time targets for the ambulance service that is being provided. If the process are stuck waiting outside at the hospital then there will not be enough ambulances to respond to calls.

Professionals will orientate themselves towards their respective professional indicators. A lack of performance indicators aligned to delivery of the overall service across domains, coupled with intense scrutiny and cost and quality pressures, creates incentives for organisations, or parts of an organisation, to act in dysfunctional ways that lead to inefficient and ineffective delivery of care. It is clear, then, that understanding the fragmentation of the system. Instead, we need broader, more sophisticated performance indicators that relate to overall service provision in the long term, rather than just narrow and very direct performance indicators, such as waiting times at A&E.

In turn, this will create the conditions to allow leadership to be distributed across organisations and professions, rather than having hospital medical leadership as the dominant force, for example. At the same time, this must be supported by collective responsibility.

At present, in the care provision chain feeling that their duty to the patient is discharged after their professional interaction with the patient. Accountability is important, but we need to encourage a sense of collective responsibility for care of the patient over the longer term, focusing on long-term outcomes, particularly where care is discontinuous.

2. Making distributed leadership and accountability work

Work needs to be done on aligning performance. Typically, under the existing performance management systems, different parts of the organisation point in different directions with respect to the performance indicators that they need to meet.

A classic example is targeted waiting times for A&E. If your job is likely to be at risk if you don’t meet a target, you might, as a hospital manager, keep ambulances waiting outside at A&E and not count them as coming into the hospital until they have been there long enough so that you can claim your goal was met.

3. Collaborative strategies

In the current fragmented system, individual service providers – whether in health, social care, education or another domain – develop their own strategies in isolation at an organisational level.

One reason that they do this is because marketisation and competition incentivises organisations to seek competitive advantages over other potential providers as they seek to sustain and develop the business.

However, although strategy needs to take place at an organisational level, it also needs to take place in the context of the care ecosystem.

So, as all these organisations have a local population to provide care for, if they need to engage in a strategy that is collaborative and that takes account of the other. There is some progress on this measure via STPs. Nevertheless, the local level is always a disproportionately powerful player.

Similarly, within and across organisations, managerial and professional conflict must be mediated in order to encourage those in managerial and professional roles to work collaboratively towards shared objectives.

For example, there is a need to bring policy and delivery together. Otherwise, policy is developed without any reference to preexisting process and practice.

Thus, we need to ensure that policymakers, and not just executives but also middle-level managers with clinical expertise, engage with those who are delivering the care.

4. Workforce development

Delivering integrated care requires a multidisciplinary delivery system. It needs a local-level multidisciplinary team that pulls in people from different organisations and professions to address patients with long-term needs.

In addition, there should be a focus on hybrid roles professionals who move into managerial roles. This ensures that there is both the knowledge about what is required in clinical and social care, for example, but also that there is local understanding about the resources needed for implementation in the particular local context.

The answer is not simply to doctor more nurses or doctors, either – something that is likely to take many years to filter through to improvements.

It is to find ways to enable doctors, nurses, social workers and other professionals to develop the skills that deal with long-term conditions to become embedded in practice.

Here, it is worth acknowledging that workforce development is not simply about one element of process reform that the Government has paid attention to.

This can be seen in initiatives such as the NHS Leadership Academy. It is clear, then, that while structural reform of the NHS is inevitable, it is unlikely to be effective unless it is accompanied by the necessary process reform.

Furthermore, while reform of the NHS is a huge endeavour, there is much to be said for looking on long-term conditions given their prevalence among the population and the associated costs. Here, substantial improvements could be made by concentrating on the four critical areas of process reform that support structural reform.

In addition, besides reducing the cost burden of mismanaging the treatment of long-term conditions, addressing these will undoubtedly encourage practices that are new to the NHS.

The introduction of market competition into national healthcare systems is a global trend. The question is not whether healthcare systems will be marketised, but rather the extent to which they will be marketised.

A major challenge, therefore, will be how to optimise both competitive and integrative practices across and within domains, as intuitively the two seem to counter each other.

But by focusing on long-term conditions, it will be possible to test a range of practices that promote both cooperation of all parts of the NHS family, regardless of whether they are private-sector firms, social enterprises, public-sector organisations or from the voluntary sector.

Further Reading:


Graeme Currie is Professor of Public Management and works with the National Institute for Health Research at Warwick Business School.
Taking a moral stand – risky business?

Nike risked a public backlash and upsetting its commercial partnership with the NFL when putting Colin Kaepernick at the centre of its latest campaign.

by Hari Tsoukas

On September 18, 2016, two American football players for the San Francisco 49ers, Colin Kaepernick and Eric Reid, knelt during the playing of The Star-Spangled Banner prior to their clash with the Carolina Panthers in Charlotte, North Carolina.

Predictably, the action sparked a fierce backlash from allegedly patriotic media and provoked the ire of President Donald Trump, who urged the National Football League (NFL) to suspend or fire players involved in the protest. Both players were duly dropped from league matches. Angry at the way they had been treated, they filed a collusion grievance against the NFL, accusing the organisation of blacklisting them.

The footballers’ high-profile protest encapsulates the concept of moral responsibility. In any organisation, employees must always ask themselves “how am I fulfilling my role?” But we would argue that these two men are much more than team players; they undertook a leadership responsibility. It is clear that they are role models for other athletes and black people in general. And this is where moral responsibility lies.

Mr Reid was quickly rehabilitated and signed for Carolina Panthers the following season. On the other hand, Mr Kaepernick, a star quarterback with a huge public following, refused all offers, including a lucrative opportunity to join the newly established Alliance of American Football. He decided to stay on and fight the power and influence of the Super Bowl’s governing body head-on.

The controversy was reignited when, in 2018, sports equipment manufacturer Nike appointed Mr Kaepernick as one of the stars of its ‘Just Do It’ campaign, which featured a series of uncompromising role models. Dramatic images of an unrepentant Mr Kaepernick were seen on billboards and in magazines across the US.

The Nike ad displayed a black-and-white close-up of Mr Kaepernick’s face and the words: “Believe in something. Even if it means sacrificing everything. Just do it.” This added a new twist to the moral leadership debate. In response to rising racial discrimination across the US, Mr Kaepernick faced clear choices. He could have played it safe and stuck to his profession in a narrow, technical sense. He was a footballer, not a politician; he could have turned his back on this issue. He could have conformed but did not.

CHARING OUT – Colin Kaepernick became the face of Nike’s advertising campaign after highlighting racial discrimination in the US.
What Mr Kaepernick’s dispute with the NFL tells us is that there are no clear distinctions between having strongly held personal beliefs and expressing them in public.

What he did, in fact, was to redefine his role by taking moral considerations into account. He showed moral imagination. Being a footballer was not simply a question of technical expertise but, more broadly, living a certain sort of life—a life in which football is played in a society where equality prevails.

Many people identified with Nike’s decision to use an image of Mr Kaepernick in its advertising campaign. Mr Kaepernick’s position was affirmed by one of the US’ biggest sports companies. The company had taken an uncompromising moral stand. Its advertising campaign, which featured black sporting celebrities, was supported by athletes like tennis player Serena Williams and golfer Tiger Woods.

Nike’s decision strengthened Mr Kaepernick’s hand in his ongoing collusion lawsuit against the NFL because the sports brand had been the governing body’s main corporate partner since 2012. Switching the focus of the debate to the corporate world polarised public opinion and reopened the debate over racial discrimination.

Nike’s public support for Mr Kaepernick resulted in an immediate fall in the value of the company’s shares of 3.9 per cent. It provoked a Twitter storm, including several tweets from President Trump such as: “Nike is getting absolutely killed with anger and boycotts. I wonder whether they had any idea it would be this way? So far as the NFL is concerned, I just find it hard to watch, and always will, until they stand for the FLAG!”

But here is the point: although sales initially dipped, they then bounced back. Since the ‘Just Do It’ campaign was launched in September 2018, Nike’s online sales have taken off and have, so far, risen 31 per cent, according to a leading e-commerce analyst.

When a company takes on a leadership role that combines moral imagination with moral responsibility, it can make a positive difference to public perceptions and brand image by stating the company’s values. It is often a risk worth taking.

The latest news is that, since Nike weighed in behind Mr Kaepernick, the NFL has had to reassess the reputational damage it has suffered because of the affair. In February 2019, the NFL and Mr Kaepernick settled their long-running legal dispute out of court. Taking into account lost salary and legal costs incurred, the athlete’s settlement could have been in the region of tens of millions of dollars.

The NFL’s president of communications and public affairs issued the following statement: “We embrace the role and responsibility of everyone involved with this game to promote meaningful, positive change in our communities. The social justice issues that Colin and other professional athletes have raised deserve our attention and action.”

So what lessons have been learned? There is no clear-cut distinction between a frame that prompts moral awareness and a business-driven agenda in which moral considerations are ignored or are brushed aside.

Nike’s position was that it wanted to unite people, not to divide them. And the company saw that the best way of achieving this was to take an uncompromising stand.

Nike’s position was that it wanted to unite people, not to divide them. And the company saw that the best way of achieving this was to take an uncompromising stand.
Leadership activities in the recruitment and retention of disabled people.

Government policy. Until recently, this has focused largely on and to facilitate reintegration after the onset of long-term health develop in adulthood once individuals are already in organisation’s existing workforce, given that most disabilities matter of concern for the large numbers of working-age disabled people themselves (around a fifth of the working-age population around 10 per cent, while in Luxembourg it is less than three per cent.

The extent of disability disadvantage is, however, not just a matter of concern for the large numbers of working-age disabled people themselves (around a fifth of the working-age population is living with a long-term health condition or disability), but also for employers. This is for a number of reasons. The first is a straightforward moral argument. Disability equality is a social justice issue; hence disability employment rates and disabled people’s opportunities. They also report lower work-related wellbeing and lower job satisfaction than their non-disabled counterparts. They also suffer a 1.5 per cent pay gap, which means that, on average, disabled people earn about £3,000 less per year, based on a 35-hour working week. The Trades Union Congress has recently sought to establish a ‘Disability Pay Gap Day’. In 2016, this fell on 10 November, the day of the year on which disabled people effectively stopped getting paid.

Equally worrying, if not more so, is the size of the disability employment gap. This has remained stubbornly high in the UK, and stands at around 29 percentage points, with only 55 per cent of working-age disabled people being in work in comparison with about 82 per cent of the non-disabled working-age population. This does not compare well with other EU countries. Across the EU as a whole, the disability employment gap is around 20 per cent. Finland, Ireland and Luxembourg have gaps of around 10 per cent, while in Luxembourg it is less than three per cent.

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“Every man gotta right to decide his own destiny,” sang Bob Marley in 1979.

But when it comes to long-term interest rates, trying to decide their destiny has become increasingly difficult for the US Federal Reserve and central banks around the world.

In 1979, when Marley sang about Zimbabwe’s revolution, the US base interest rate was at 16 per cent and the following year reached a record high of 20 per cent, while in the UK it reached 17 per cent.

But since the global financial crisis interest rates have been at an all-time low across the Western world. The base rate has been hovering around 0.5 per cent in the UK for the past decade, and it was the same in the US before climbing to above two per cent in 2018.

It had been thought these incredibly low levels were the result of the global financial crisis, as the developing world tried to limit the damage with the extreme measure of quantitative easing.

But policymakers are increasingly coming round to the idea that something more powerful is at play – something they are powerless to control, something that controls real interest rates despite their best efforts to control their own monetary destiny.

And that’s demographics.

Former US Treasury Secretary Larry Summers has popularised the secular stagnation theory to explain this era of low growth and low interest rates, while Andrew Sentance, Professor of Practice at WBS and former member of the Bank of England’s Monetary Policy Committee, similarly talked of a “new normal” after the Great Recession of 2007 to 2009, with low interest rates failing to budge spluttering GDP growth. Both suggest demographics is a potential factor, pointing to low population growth and increasing life expectancy.

But my research, along with other colleagues Carlo Favero, Andrea Tamoni, Haoxi Yang and Annaig Morin, indicates a population factor that has been largely ignored in the thinking of why real interest rates – that is the nominal or base interest rate minus the inflation rate – are so low in the US and much of the Western world, and that is the ratio of the number of middle-aged (40 to 49 year olds) to young (20 to 29 year olds), a variable first introduced in a model by John Geanakoplos, Michael Magill and Martine Quinzii.

Demographics has been used in other models before to explain long-term interest rates, but these have predominantly looked at the size of the population. We have found that the composition of the working population, specifically the middle-aged to young (MY) ratio, is a more important factor.

Mounting evidence is persuading policymakers that a country’s population structure has a significant influence on interest rates.

by Arie Gozluklu
So the middle-aged are the savers and if there are more of them than the young spenders, that means there is more demand for financial securities, pushing prices up and yields, or interest rates, down.

When the MY ratio is small, there will be excess demand for consumption by a large cohort of young people and therefore the price for bonds and stocks decreases, so the yield rises and saving is encouraged for the middle-aged.

When you look at interest rates over the very long term, over the last 100 years, you can see that the low rates the US is experiencing today is not just a cyclical story—they had been falling for nearly 20 years, long before the 2007–08 crisis, and this is just a continuation of that trend.

Just why has been vexing economists. And although demographics has been cited, our research suggests that the MY ratio seems to be the telling factor in helping us determine the future path of interest rates. The MY ratio goes up and down in waves over time, as different size bulges work their way through the population structure. Right now, we are feeling the tail end of one particularly large bulge in the US demographic.

After the Second World War, the US, along with many Western countries, enjoyed a baby boom, which created a giant MY ratio wave running through the country’s demography.

The 1960s thus saw a big rise in the MY ratio, pushing up bond prices and sending yields low, but by the 1980s, as Robert Marley’s battle cry echoed through the decade, this had swung the other way.

It saw yields high and prices low, so the MY ratio was low. The baby boomers had gradually fallen out of the expansion over the last 20 years, that has swung back again, slowly seeing more middle-aged people compared to the young with a rise in savings, boosting financial asset prices and bringing-down yields.

According to our data, and using the Census Bureau projections, the MY ratio is coming down, so a standard forecasting model that adds the MY ratio as a variable to projections, the MY ratio is coming down, so a standard forecasting model not only provides improved long-term yield forecasts, but can also aid long-term horizon investors in stocks and bond allocation.

The destiny of interest rates might still not be in the hands of policymakers if we knew the link between demographics and inflation. However, our results in a recent paper with Moris suggest that demographics does not affect inflation as much as it affects the real rate, and there is no robust empirical evidence, even though there are papers suggesting otherwise.

Central banks react to monetary events in the economy by moving the short-term interest rate, in an effort to stabilise the long-term yield or interest rate of bonds, which are critical for business investment and household’s mortgages as they care about the next 10 years or more.

Our research shows that using the MY ratio in a standard forecasting model not only provides improved long-term yield forecasts, but can also aid long-term horizon investors in stocks and bond allocation.

The destiny of interest rates might still not be in the hands of policymakers, but we can at least improve our inference of the future by taking into account slow-moving changes in demographics.

Farther Reading:

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The 2007–08 financial crisis ushered in a host of new regulations on banks, but is the latest, Basel III, counterproductive?

The 2007–08 financial crisis prompted policymakers and regulators to revisit the rule book and determine, given the apparent inadequacy of the existing Basel Accords regulatory framework, what action might be taken to better regulate banks and the banking system. The policymakers and regulators were assisted by the academic community and the publication of numerous papers focusing on the causes of the financial crisis and possible remedies. The result was an addition to the Basel Accords regulatory framework developed under the auspices of the Bank for International Settlements. Moving on from the inadequacies exposed in Basel II, Basel III is due to be fully implemented by 2022.

Among those academic interventions in the aftermath of the financial crisis was a paper I produced in 2012 and published in 2014, together with colleagues from the International Monetary Fund and the Ca’ Foscari University of Venice. That paper adopted a microprudential, firm-level, view of banking regulatory issues. In particular, we considered the impact of three regulatory provisions on two measures of capital efficiency and welfare.

The regulatory measures were: capital requirements—the amount of capital a bank has to hold, usually expressed as a capital adequacy ratio being mainly common stock and Basel III: Will it harm the broader economy? by Andrea Gamba

The 2007–08 financial crisis ushered in a host of new regulations on banks, but is the latest, Basel III, counterproductive?
Finance activities. The overall value to society of banking companies in the productive sector; to provide long-term loans offered in the form of customers’ short-term deposits, and providing credit to the productive sector and helping to drive economic growth (after all, it is one thing to give credit: they provide liquidity.

The role of banks in the economy

This is usually when the banking lobby protests, arguing that capital requirements should not be raised too high, because otherwise it would be impossible to run the banks. Their usual argument is that, when regulators impose higher capital requirements, it increases the cost of capital for banks, because they must rely more on equity capital, which requires a higher return than debt. That increased cost is then passed on to borrowers, who will have to pay more for their loans, and so it is bad for the economy. Interestingly, our research shows that there is some merit in the protest of the banking lobby but not for the reasons they suggest. In terms of how capital requirements are applied, they could be applied using a constant capital ratios rule: the same for all banks and for all states of the economy. Alternately, they could be state-contingent – that is, depending on the state of the economy.

Basel III introduces the notion of a ‘discretionary counter-cyclical buffer’ as part of the capital requirements. This provides for national regulators to demand the bank to hold additional capital during periods of high credit growth – rapid credit growth is often followed by banking crises.

However, our research suggests that this approach may not be optimal for the broader economy because of the role of banks in creating liquidity. Imposing conditions that make leverage counter-cyclical reduces deposits, thus increasing their price and therefore reducing their return. In this sense, bank capital becomes more expensive relative to debt. The overall result is a reduction of consumption and productive investment, reducing wealth and welfare in general. In detail, during an expansion, consumers want to consume more. Therefore, they tend to use deposits more in order to fund their short-term consumption. If capital requirements become more stringent in this phase, the banks are constrained regarding the extent to which they can use deposits in order to take on more debts. Thus, there is a high demand from consumers for deposits, but a restricted supply. Consequently, consumers are willing to accept very little return, if any, on their deposits.

The regulatory framework increases the cost of capital for the bank. This is the direct result of what, it might easily be argued, is over-regulation.

It seems only natural that there should be an expansion of leverage allowed in good times. We argue that it is beneficial for the economy to allow the leverage to be pro-cyclical. In our model, the best regulatory approach would be one that allows the bank to expand leverage during periods of economic prosperity, just ensuring that there is a sufficient degree of resistance to restrain the banks’ inclination to further increase leverage substantially. The capital requirement would be reduced steadily, allowing leverage to increase, although never to the extent that leverage might expand if it were a completely unfettered market, without regulation. And there is no need for the regulator to resist the expansion of leverage at all when the economy enters a downturn. That is because the economic slowdown imposes a natural brake on a bank’s desire to increase its leverage. Overall, optimal bank

response that depends on the state of the bank: You only intervene when the bank is in trouble, rather than in advance, in anticipation of the bank getting into difficulty, and certainly not when the bank is doing well. On the other hand, measures that are not contingent on the state of the bank, and that combine capital and liquidity requirements, may be detrimental to the bank.

Taking a banking sector perspective

Our findings were well received in the academic community at the time, including regulators. However, there were limitations to our approach and looking at each bank in isolation. So, with colleagues from New York University and the Ca’ Foscari University of Venice, we decided to expand our perspective and talk about the banking sector’s risk rather than an individual bank’s risk. In order to examine the regulatory challenge from the perspective of the banking sector we devised a general equilibrium dynamic model with aggregate shocks that represents the whole economy in its upturns and downturns.

One of the primary elements of Basel III (and the Basel Accords generally) has been the need to increase capital requirements reducing bank debt. In our new analysis, we considered capital requirements in a world in which banks have another important role besides making credit: they provide liquidity to consumers.

As mentioned previously, banks have a maturity transformation role: They intermediate between households and the productive sector of the economy, taking money from consumers in the form of short-term borrowing, and using that money to create long-term loans. Hence, banks create liquidity for households and consumers by selling deposits to them, and in doing so, they make sure that the money is available to consumers at any moment in the future to be withdrawn and spent on consumption. This is a liquidity service and banks create money in the economic system by allowing consumers to carry forward wealth into the future.

In an upturn, when times are good, banks have an incentive to make more loans and therefore take on more debt in the form of deposits. However, the risk is that banks over-extend and the economic situation changes, leaving them exposed to large liabilities to households and to increased delinquencies in their loan investment. Individual banks are, understandably, focused on delivering returns for their shareholders. They have the incentive to act further the interests of those shareholders by pursuing high returns at significant risk, knowing that any losses due to the failure of the bank and disruption of the banking system are likely to be distributed much more widely.

Because a banking crisis has large economic and social costs, rather than allowing a completely laissez-faire approach to banking, governments seek, through regulation, to prevent banks from running into trouble and harming themselves and the economy. One popular measure, as with the Basel Accords, is to apply capital requirements. The challenge is knowing what the optimum approach is for setting capital restrictions given the special role of bank deposits. And in particular, in times of stress there is pressure to increase the levels of capital restriction.

After all, it is one thing to give leverage to banks and thereby increase their debt, in the form of customers’ short-term deposits, to provide long-term loans offered to companies in the productive sector; and social welfare: the contribution to the overall value to society of banking activities. After all, it is one thing to give leverage to banks and thereby increase their debt, in the form of customers’ short-term deposits, to provide long-term loans offered to companies in the productive sector; and social welfare: the contribution to the overall value to society of banking activities.
leverage is pro-cyclical and regulation is counter-cyclical, in the sense of being more restrictive in economic upturns. In the alternative regulatory approach of a constant capital ratio, regardless of upturns and downturns, there would be less debt, fewer deposits, and less consumption in upturns. So eventually the economy will be adversely affected due to a reduction in investment. This situation will also create a bigger differential between the cost of debt and cost of equity for the banks. So, in a way, our research confirms the banking lobby’s argument that bank capital becomes expensive. Yet it is not, as the banks suggest, because of the level of capital requirement – but rather when the regulations imposed are non-cyclical.

The role of the regulator

One of the implications of our analysis concerns the role of the bank regulator and more specifically what can be reasonably expected from a regulator. This is an issue that has not been fully discussed in the debate on bank regulation, but which is central to it. Because only once we are clear about what can be expected of a regulator can we actually decide what the regulator should do.

Bank regulators are not like the central planner figure from economic theory. All they have are a relatively small set of regulatory levers that essentially affect one aspect of the economy—how banks operate. It seems unrealistic to expect to maximise the overall welfare to the economy by just regulating bank leverage or bank liquidity, for example. That is a very narrow perspective, after all. If we are thinking of the benefit to the broader economy, perhaps these should be full integration between monetary policy and bank regulation, as the two are integrated ways of creating liquidity in the economy, as our analysis shows.

If a government is to successfully re-launch the economy in the aftermath of a crisis, it makes sense for the arbiters of monetary policy—often the central banks—to work closely alongside bank regulators. It should not be the role of the bank regulators alone, as they possess insufficient levers to drive economic growth at a macro-economic level. It requires additional measures, such as the quantitative easing deployed after the recent crisis, which are beyond the scope and tools of what a bank regulator can do. In other words, bank regulation should be integrated into the broader monetary policy that central bankers control.

Although such an approach may be some way off, it merits serious discussion. In the meantime, our research shows that regulators can achieve something that goes a long way towards optimal—if the degree of leverage allowed is naturally pro-cyclical—exactly because this allows a monetary expansion, through bank leverage, in upturns. Capital restrictions may be counter-cyclical, in the sense of “leaning against the wind” and making the bank leverage less pro-cyclical than in the corresponding unregulated approach, as the economy expands. But an entirely counter-cyclical approach to leverage—as currently suggested in Basel III—would be a mistake.

Further Reading:


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and collaborative. And it is at the collaborative stage where we see the most comprehensive approach to managing supply chain partners and customers. The basic level sees companies typically send their suppliers a survey to fill in on their emissions. US software firm Syntropy produces an annual report on its suppliers’ GHG emissions, while Bank of America has done a CDP supply chain survey since 2009.

This is the first step for a comprehensive carbon reduction plan, measuring and collating data. Perhaps tellingly, responses from firms drawing on basic engagement were relatively shorter in length and qualitatively less detailed. More advanced firms, at the transactional and collaborative levels, are using that data for more productive means. At the transactional level, firms are calculating their carbon footprint and identifying opportunities for improvements. Those with more experience in this area are then using the data to provide their supply chain with targets and incentives.

Virgin Atlantic Airways, for example, aims for reductions in emissions from its supply chain each year, while nuclear power firm Exelon sets goals for its suppliers to reduce energy usage and GHG emissions. This data is also being used to develop key performance indicators that can be utilised to select a supplier or worked into contracts to assess a supplier’s performance. They can then send warnings to companies who are not hitting the required performance levels and demand improvements, so the emissions data is becoming part of their selection criteria for suppliers. For instance, pharma giant Pfizer reported that the aim of its data collection is “to provide benchmarking to suppliers regarding their GHG emission reduction and water conservation programmes, in order to identify sustainability improvement opportunities.”

At the collaborative level, though, firms are working with their suppliers to develop shared goals and values around sustainability. This means more meetings, seminars on best practice, phone calls, emails and even the establishment of online discussion groups as firms and suppliers build mutually beneficial relationships designed to develop innovations to reduce their carbon footprint as well as encourage greener products and services. And the discussions and information are built into supportive supplier training and development courses, brieﬁngs, summits and even award ceremonies to identify joint development and innovation projects.

Food multinational Kellogg’s has built a Sustainability Consortium with its supply chain to “drive scientiﬁc research and the development of standards and information technology tools to enhance the ability to understand and address the environmental, social and economic implications of products”. While InterContinental Hotels Group is working with the International Tourism Partnership to reduce the environmental impact of the cotton used in its bed linen.

Firms at the collaborative level also seek to engage customers and consumers, persuading them through marketing and PR of the beneﬁts of new greener products and how to use them in a way that is less harmful to the environment. In the B2B sphere, two-way engagement with customers is used, with a more proactive and strategic approach on show. Chemicals giant Ecolab partners with its customers to reduce their energy demands and GHG emissions through innovations.

There are also partnerships with industry associations and university research teams, with French hospitality ﬁrm Sodexo funding a Professor of Sustainable Sourcing professor at the EuroMouel School of Management in Marseilles. We found some firms are able to employ transactional and collaborative modes of engagement simultaneously with different suppliers and customers. If ﬁrms are having to report all their emissions, from the supply chain to the customer, then what each one does affects the other, which makes the collaborative approach increasingly important. Companies need to understand that they are all part of a system that has to work together and help each other, rather than use it as another supply chain management tool.

When you analyse the life cycle of a product, such as a plastic travel mug, there are the raw materials – which needed energy in order to be extracted and more energy is used in the production. Then, at the end of the mug’s life, what happens to it? Does it end up in a landfill site? Should that be included in the measurement of each company’s carbon footprint and how is that measured? Working with the whole supply chain, both customers and suppliers, will help solve these problems and ultimately bring down emissions for all ﬁrms along the value chain. To do it across the whole value chain can be incredibly complex for a company like Walmart, and the amount of data involved is probably why we are seeing tech companies leading the way in reducing their carbon footprint. Their data analytics skills mean it is natural for them to not only collate data but to put it to good use and work up and down the supply chain.

Their experience of handling and managing data also means they see this trend and increasing requirement to record and measure emissions for companies as an opportunity. If they ﬁgure out and produce a comprehensive software package that does all this effectively, they can then sell that platform to other ﬁrms looking to manage their whole carbon footprint.

Verizon, for example, now sees its Internet of Things products, designed to reduce carbon emissions, as “providing signiﬁcant revenue opportunities.”

It is clear, with the youth of today engaged as never before in the climate change political battle, that sustainability will be the issue of this generation. If businesses are to prosper in this climate, they need to include their whole supply chain to claim they are truly on the planet’s side and not be accused of creative carbon accounting.

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So long seen as greenwash, corporate social responsibility is now sought by institutional investors as a way of futureproofing their bets.

by Chendi Zhang

By the end of the financial crisis in December 2009, the Conservative party estimated almost 27,000 businesses in the UK had gone into liquidation or been declared insolvent.

Meanwhile, the US had seen three of its biggest banks go to the wall in Lehman Brothers, Washington Mutual and Bear Stearns, while the Treasury Department injected $412 billion into banks, carmakers and other struggling companies, and investors saw $8 trillion dollars wiped from the stockmarket between late 2007 and 2009.

The Great Recession was the severest example of a systematic risk to businesses since the Great Depression of the 1930s – that is, the risk from macroeconomic factors beyond the influence of an individual organisation.

It means planning for the next systematic shock should be a priority for investors, especially those surveying the UK’s imminent exit from the European Union, the world’s biggest free trade zone. Plus, investors know systematic risk is the main driver of their portfolio, as idiosyncratic risk – that at the firm level – can be diversified away.

My research with Rui Albuquerque, of Boston College, and Yrjö Koskinen, of the University of Calgary, has discovered one avenue for investors to futureproof their portfolio against recessions and economic shocks, and that is Corporate Social Responsibility (CSR).

By developing an industry equilibrium model within an asset-pricing framework, and analysing the performance of 4,670 US listed companies from 2003 to 2015 – and so covering the Great Recession – we have found that investing in CSR reduces a firm’s systematic risk.

This is because firms investing in CSR face relatively less price-elastic demand – that is, demand for their goods does not fall that much with a price hike – so they can have higher product prices and retain higher profit margins.

It was thought that, because of this, more firms would adopt CSR policies and so with every firm increasing their costs it would wipe away any reduction in systematic risk.

But our model found that there is a limited amount of consumer spending on CSR products, and so limiting the number of companies that can effectively adopt it. Thus, we found that CSR firms had lower systematic risk compared to companies who had not invested in CSR, with this backed up by us also finding that those invested in CSR saw their profits not as affected by the boom and bust business cycle.

Customers are more loyal because they appreciate the firm’s green credentials and environmentally and socially responsible products, which are in line with their values.
and concerns about sustainability, so they are not so swayed by price.

In fact, environmentally conscious consumers are willing to pay a premium for products like organic food or electric vehicles, with CSR becoming a form of differentiation for firms. For those companies in tune with the changing demands of society and growing concerns around climate change, they can build a loyal customer base, making profits more stable and less correlated with economic cycles, which reduces their systematic risk and in turn increases firm value. And the impact on firm value is substantial, with an average increase of five per cent across the firms we studied. Investing in CSR is akin to an insurance policy to make a company less sensitive to economic cycles.

In the model we created, we assume investors are not interested in CSR and are instead standard investors only interested in their risk and returns, so what is generating our results are consumers. And, as they are the driving force, our model predicts the reduction in systematic risk is 40 per cent stronger for consumer-facing companies, especially as these firms spend more on marketing, which will amplify the effect of CSR. And the effect on firm value for these firms is 20 per cent stronger.

To come to this startling conclusion, we used investment analyst company Morgan Stanley Capital Investments’ ESG (Environmental, Social and Governance) research database, which has assessed around 6,800 companies, to construct an overall CSR score for each of the 1,670 firms in our study each year. The score combines information on the firm’s performance across community, diversity, employee relations, the environment, products and human rights attributes.

Combining this with the firm’s Capital Asset Pricing Model, which measures a stock’s expected rate of return compared to its risk, and a company’s beta, a measure of its systematic risk, we created a model to measure CSR firms and non-CSR firms. We then controlled for many factors and tested the causality, but found the link between CSR and systematic risk still strong.

Of course, not all CSR is geared towards customers, but employees as well. Further research I have done has discovered that higher job satisfaction among staff leads to higher share prices, and so investing in CSR could also lead to other spin-off benefits.

The case is growing for companies to invest in CSR. In fact, in this increasingly fast-changing and volatile world, with trade wars escalating and the rise of populism across the developed nations, is not investing in CSR a risk worth taking?

Further Reading:

A study involving chimpanzees unearths an evolutionary theory for our desire for scarce goods.

by Alicia Melis & Daniel Read

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Luxury fashion brands have long realised that people have a strong desire for scarce goods.
Is your credit card nudging you into more debt?

Experiments have discovered that minimum repayments are having a perverse effect on people.

by Neil Stewart

One morning when opening my credit card bill and after digesting the bad news, I suddenly thought, ‘is the minimum repayment really as helpful as it looks?’

An incredibly robust finding from behavioural science, which has been repeated many times in experiments, is “anchoring”. Anchoring happens when the presence of irrelevant information biases people’s decisions or judgements. One experiment by Dan Ariely, Drazen Prelec and George Loewenstein is typical. It asked students to bid on items in an arbitrary auction using social security numbers as their anchor. The researchers held up items to be auctioned, like a bottle of wine or book, and then asked each student to write down the last two digits of their social security number. Then they asked for bids on the item.

They found students with high social security numbers bid up to 346 per cent more than those with low numbers, which is due to the anchoring effect. It has even been tried with a roulette wheel, where just landing on random numbers influenced people’s subsequent estimate of the percentage number of African countries in the United Nations.

Although social security numbers are arbitrary and have nothing to do with the price of wine, and random roulette wheel outcomes have nothing to do with United Nations membership, the numbers get into people’s heads and affect their judgements.

Thus, was it beyond the realms of possibility that the minimum repayment amount on my credit card bill was also producing the same psychological bias? If it was anchoring repayment amounts, it had big implications not just for me but for everyone with a credit card.

In 2014, in the UK alone, credit card debt stood at £70 billion across 30 million card holders, while according to the UK Financial Conduct Authority’s (FCA) latest credit card market study, two million people are either in arrears or have had their debt written off, plus another two million have persistently high levels of debt and are at risk of not paying off their debt.

The FCA also estimates that 1.6 million people are making just the minimum repayment and so are taking longer to repay, adding to the overall cost of the debt due to compounding interest rates and having implications for their wider financial situation. Indeed, it found 360,000 people actually paid more in interest than they had borrowed, while another five million credit card holders will take more than 10 years to pay off their balance.

Perhaps some of the slowness in paying down credit card debt is because people simply misunderstand the minimum repayment. The minimum repayment is required by regulation in the UK and US to stop people feeling the full effect of compounding interest rates. It makes sure they pay off at least the interest charged each month, plus a little more. In the UK, minimum repayments must be at least 1.6 per cent of the outstanding balance.

In a survey of UK credit card holders by consumer campaigner Which?, of those who reported they made the minimum repayment, 48 per cent said that they thought it was an amount recommended by their credit card provider and 50 per cent believed it was the amount most people chose to pay.

And the effects of debt can be devastating. A survey by StepChange, a debt charity, suggests that rising debt can have a negative impact on people’s physical and mental health and badly impacts their relationship with family and friends.

DROWNING IN DEBT? – Credit card users are being hindered in paying off their loan by a bad nudge.
Additionally, the Consumer Protection Partnership found debt worries have an impact on people’s ability to work, affecting their attendance or concentration. Plus they might also lose access to cars, telephones or the internet, and so make it doubly difficult to work or seek employment.

Nudges gone bad

It might seem that people taking longer to pay off their debts is good news for credit card companies, but only up to a certain point. After all, they also want the debt paid off. Writing off debts means they are making a big loss and so they want customers who can pay off their debts.

Firms can also earn revenue from the ‘interchange fee’, which is when the credit card is used to purchase goods and the provider takes a small percentage cut of the transaction. The FCA believes firms benefit from people continually paying the minimum repayment. Thus, if people continually pay the minimum, they are profitable to the credit card firms and so might like to consider paying down more.

Thus, we conducted an experiment to test the theory by sending 413 volunteers a mocked-up credit card statement with a balance of £435.76. They were asked to pretend it had arrived that morning, with participants either seeing a minimum repayment of £5.42 or a statement without a minimum repayment.

Removing the minimum repayment information had a dramatic effect. The average repayment increased by 70 per cent from £99 to £175, thus providing evidence that the minimum repayment amount was having a strong anchoring effect – that is a bad nudge.

However, warnings about sticking to just the minimum repayment have been found to be ineffective in research I did with Daniel Navarro-Martínez. And more research providing alternative options to pay off more had no effect on total payments, while telling people about anchoring in other domains has also failed to alter behaviour.

In collaboration with Benedict Gutman-Kenney and Jesse Leary at the FCA, we put together a survey and a much larger randomised controlled trial to de-anchor repayment choices from the minimum. Again, we used a hypothetical online credit card bill, directing the control group to a standard online bill, where they had to enter how much they were paying back. Meanwhile, another group received the same online bill but with the minimum repayment amount and the button to pay it removed.

In both cases, if somebody entered an amount less than the contractual minimum, a prompt appeared on screen that showed the minimum repayment and asked the consumer to reenter the quantity.

The experiment was split between groups having a low balance of £532.60 with a minimum repayment of £11.98 and a high debt of £3,217.36 with a minimum repayment of £72.38. This time, the reduction in minimum repayments was even more dramatic. Removing minimum repayment information nearly eliminated people paying at or below the minimum level. Removing the minimum repayment also saw a surprising rise in the number of people paying in full, with between 4.4 per cent and 9.9 per cent more being paid in full, as it seemingly became a target for them to aim for.

Taking out the minimum repayment successfully de-anchored repayments, with a 44 per cent rise in the average amount compared to the control group. This was broadly consistent with a low balance and a high amount to pay.
back. In monetary terms, there was an average increase in repayments of £60 in the low balance scenario and £355 in the high balance scenario.

Of course, this was all a hypothetical situation. Would people react like this with real bills? Working with the FCA, they were able to compare the hypothetical repayments from our experiment to 1,200 real repayment decisions matching our low balance scenario and 3,218 actual repayment decisions that matched our high balance scenario.

Just like in our experiment, we found more repayments closer to the minimum in the high than the low balance scenario. Although for those with a real high balance, we saw a higher proportion of minimum repayments and fewer paying in full than the experimental version. Whereas in the real low balance world, the proportion of consumers choosing full repayments and minimum repayments was very similar to our hypothetical scenario.

Some doing the experiment also gave us consent to check their decisions against their real credit card repayment behaviour. There were 779 matched with the low balance scenario and 774 with the high and we found a reasonably strong correlation with their decisions made in the experiment. Another statistical analysis comparing people’s repayment decisions in real life with their hypothetical ones again found they closely matched.

It shows people were taking the hypothetical bill seriously and acting as they would in real life, which means we can be more confident that de-anchoring bills by not showing the bad nudge – the minimum repayment option – when deciding how much to repay in real life could have a huge impact on consumer debt.

People would be prepared to pay their bills off quicker, thus reducing the amount of interest they pay and lowering their debt. It would also help firms as people would be less likely to fall behind on their payments and into financial distress, with their debt eventually being written off, which is expensive for credit card providers.

However, an increasing amount of consumers are using automatic payments or direct debits to handle their credit card bills. This seems the ideal system to avoid late payment charges.

But in research with Hiroaki Sakaguchi and John Gathergood, we found that people will often set the default at the minimum repayment level and then ignore their bills. And yet it is the exceptional one-off payments when they are feeling flush that finally pays off the credit card bill.

We have found that people typically pay more in extra interest for taking longer to pay off the bill than they would have done in late payment charges. In fact, we calculated that those setting automatic payments at the minimum level could save one third of the cost of their debt if they paid it off manually.

Once again, the minimum repayment has acted as an anchor for people to set their automatic payments too low. The FCA is now considering consulting on a ‘de-anchoring’ rule that would prevent customers making repayments online or by telephone from being automatically told their minimum repayment. Our research indicates that this would increase debt repayments, reducing the total cost and duration of the debt.

Further Reading:


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