Culture is a Major Piece of the Corporate Value Puzzle

(June 2018 by Shepherd G. Pryor IV and William J. Hass)

Why do even blue ribbon Boards and CEOs make big mistakes?

You may describe today's companies as clubs, tribes, authoritarian regimes, or micro-civilizations, but the social nature of people always results in the creation of a corporate culture. Culture develops over time and is partly defined by leadership, but also arises spontaneously from myriad interconnections among employees, management and their interface with customers, vendors, and others. It interweaves with leadership, strategies, performance measures, decisions, and actions, affecting every dimension of corporate activity to impact corporate value.

As stewards of value, the board of directors must be prepared to evaluate the health of the company's culture, and to take action when they detect a decline. The PDA's Body of Knowledge (BOK) foundation book, **Board Perspectives: Building Value through Strategy Risk Assessment and Renewal**, examines the oversight duties of Effective Directors. We presented 12 principles that support the building of corporate value. The following comments emphasize the importance of culture to the board's success:

1. **Understand Customer & SBU (Strategic Business Unit) Value**: A common corporate value framework is needed to guide the capital allocation process, but it is frequently missing. This can lead to inconsistent conflicting goals.

2. **Involve those Accountable**: Command and control environments are suited to quick decisions, yet buy-in at all levels of management is crucial to performance.

3. **Communicate Cash & Performance Measures**: Key performance measures should target sustainable long-term cash to build value. If the metrics –both hard and soft-- are understood by all involved and clearly contribute to the overall goal, they will guide productive activity.

4. **Adapt Processes to Capability**: Organizations are endowed with different levels of sophistication. The board can help ensure that a new leadership team develops the right approach to make best use of the skills of its work force and assets.

5. **Encourage Open Debate**: The broader the involvement in the planning process, the more likely management will receive enthusiastic cooperation toward performance goals. Effective CEOs respect the opinions and insights of others.

6. **Quantify Magnitudes and Likelihood**: Quantifying and communicating risks and opportunities in terms that can be debated helps provide a common ground for collaboration and better decisions.

7. **Monitor Execution**: When the board monitors execution, it helps promote a culture of valuable action

8. **Renew Continuously**: A changing environment requires agility. Boards that promote dynamic responses to problems can promote a culture of creativity and adaptability.

9. **Communicate Thoroughly**: Words and actions matter to establish culture. Employees who believe the clearest and best information comes from their reporting chain are less motivated to "mine the rumor mill" for answers.

10. **Recognize Owner & Customer Priorities**: The board and CEO play crucial roles in ensuring the culture of the company aligns with goals and values of owners and customers

11. **Focus on Strategic Initiatives**: When all attention is turned to the hot topic of the day, little energy remains for doing what matters. Maintaining focus on strategic initiatives is critical to an effective culture and value.

12. **Monitor Results**: Results include both hard financial outcomes and "soft" metrics such as customer and employee satisfaction.

Each of these principles either impacts or is affected by the corporate culture. Maintaining the right culture is of great importance. Prime lessons of the impact of culture arises from the experience of Home Depot in the early 2000s and GE in

2018. Strikingly, prospective and retrospective views of a CEO's and Board's impact culture change can be dramatically different.

In December 2000 Bob Nardelli, a senior executive at GE, lost out to Jeffrey Immelt in the race to succeed Jack Welch as CEO. Mr. Nardelli was quickly hired as CEO of Home Depot, with high expectations of success. However, after numerous CEO-directed changes, he departed Home Depot in January 2007 prompted by stockholder dissatisfaction. One author concluded: "In a brief period Nardelli managed to destroy the customer-oriented culture [and value] that Home Depot's founders…built over 20 years."