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June 2022

“Geopolitics and Global Business Impact”

ESCP Impact Papers

Third Edition

Edited by

Pramuan BUNKANWANICHA
Régis COEURDEROY
Jaime PÉREZ LUQUE
Stefan SCHMID
Sonia BEN SLIMANE

ESCP RESEARCH INSTITUTE OF MANAGEMENT (ERIM)

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ABOUT
ESCP BUSINESS SCHOOL

ESCP Business School was founded in 1819. The school has chosen to teach responsible leadership, open to the world and based on European multiculturalism. Six campuses in Berlin, London, Madrid, Paris, Turin and Warsaw are the stepping stonesthat allow students to experience this European approach
to management.
Several generations of entrepreneurs and managers were thus trained in the firm belief that the business world may feed society in a positive way.
This conviction and ESCP's values: excellence, singularity, creativity, and plurality, daily guideour mission and build its pedagogical vision.
Every year, ESCP welcomes 8500 students and 5000 managers from 122 different nationalities. Its strength lies in its many business training programmes, both general and specialized (Bachelor, Master, MBA, Executive MBA, PhD and executive education), all of which include a multi-campus experience.

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Professor Frank Bournois
Dean and Executive President, ESCP

Discerning and making choices

I remember when Ukraine was invaded back in February 2022. Once the initial shock passed, the Executive committee and myself quickly started to think about what it would mean for our school and the business world. Throughout the months, we quickly saw its impact: shortages, price increases, political changes, social unrest even. All these events have a strong social impact as well, showing us again how companies, governments and societies function, thrive and sometimes suffer together.

This is but an example of what is explored in the third series of our Impact Papers that gather 33 articles from Faculty across our six campuses. It shows again how our professors and researchers contribute to society and business, and how connected our various fields of studies are, reinforcing the ESCP commitment to dual skills for all students. Ten years ago, geopolitics were mostly an afterthought in business schools. Today, they are one of the key components of the curriculum.

Geopolitical skills are used by our current or former students, now business leaders, to make sense of a complex world. Warren Buffet said “he has usually made his best purchases when apprehensions about some macro event were at a peak. Fear is the foe of the faddist, but the friend of the fundamentalist.” Being able to grasp and tame that fear, but also see opportunity, and most importantly, make a positive impact on the world, is the objective. We are past the age of the golden calf, where profit was all businesses looked for. As our Chairman Philippe Houzé regularly reminds our Board, more than ever, our mission is to *train responsible leaders and entrepreneurs who will have a positive impact on businesses and the world*. The well-being of our companies is the well-being of our societies: delivering powdered milk, building housing, preserving the environment, making transportation affordable. All these challenges, from the very practical to the boldest, are impacted by geopolitics, whether positively or negatively. Geopolitical skills are becoming part of the list of criteria for the development and detection of high flyers.

These impact papers help us make sense of a difficult world. On behalf of our Executive Committee, I would like to acknowledge and thank all the Professors who have contributed to this second edition of Impact Papers. I would particularly like to thank Professor Pramuan Bunkanwanicha, Associate Dean for Research, the main Co-editors, Professors Régis Coeurderoy, Jaime Pérez Luque and Stefan Schmid, and of course Valérie Moatti, Dean of the Faculty, Dimitri Champollion, Director of Brand and Communications and Sonia Ben Slimane, Research Fellow, Executive director of ERIM (ESCP Research Institute of Management) and Editorial Coordinator and Emmanuel Surun, head Popularizer Chairs & Research, in Communication division.

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Many observers consider that the process of globalization that has characterized these past decades has stalled, or may even be in retreat. This is, for instance, reflected in the resurgence of debates on the increasing role of national political and regulatory institutions within the development of economic activities. Recent events also show us that geopolitical issues are once again central to business activity and its future development.

The objective of this series is to explore from various angles how geopolitical issues can influence the strategies of companies and their managerial practices at the international and national levels– not only as potential risks (the "dark side") but also as opportunities for innovation and societal change ("the bright side").

Business and the socio-political arena are intimately entwined and influence each other mutually, contradicting Fukuyama's famous claim that we are not at the end of history. In particular, the most recent militarized conflicts in Eastern Europe dramatically remind us that business and management challenges are embedded in economic, political and societal issues. Business is not a world apart, but contributes to the question of making sense of human activity.

In calling for contributions, the aim was to encourage the ESCP academic community to reflect and generate insights on the complexity and the uncertainties of a multi polar word and how management can help tell a story in a world "full of sound and fury".

Life's but a walking shadow, a poor player,
That struts and frets his hour upon the stage,
And then is heard no more. It is a tale
Told by an idiot, full of sound and fury,
Signifying nothing.
(Macbeth, Shakespeare)

ESCP's academic community has played a significant role in advancing academic knowledge on how businesses engage with economic, social and political issues. This call for papers focus on geopolitical topics from a variety of perspectives. More generally, the objective has been to explore the interconnections between the business and socio-political worlds. Varieties of topics have been proposed, including:

- The future of globalization
- Sovereignty in business
- International relations in a changing environment
- Imperialism and neo-imperialism
- Trade and foreign direct investment
- War, peace and business
- Firms as political actors
- Managing geopolitical risks
- The future of corporate globalization
- Disinvestment and de-internationalization
- MNEs and government relations
- Geopolitics and the European context
- Business and democracy
- Geopolitics and financial markets
- Geopolitics and sustainability challenges
- Geopolitics and artificial intelligence
- Geopolitics and management control
- Geopolitics and HR management
- Geopolitics and real estate
- Geopolitics in curricula of universities and business school

We follow the same principles of the first two editions of ESCP Impact Papers, the contributions having been gathered within the B.E.S.T. Impact framework (Business, European, Societal, and Teaching):

The breakdown of the number of contributions for this third edition following the B.E.S.T strategy is as follows:

B.E.S.T strategy	*Numbers*
Business	*16*
Europe	*13*
Societal	*3*
Teaching	*1*
Total	*33*

Finally, we would like to thank our editorial supporting team: Anna Marie, Chantal Gueudar Delahaye, Emmanuel Surun, Sandrine Kiefer, Vincent Blanc and Maud Autrechy.

Editorial
Executive Summary

ESCP Impact Papers, 3rd edition
Geopolitics and Global Business Impact

Pramuan Bunkanwanicha
Régis Coeurderoy
Jaime Pérez Luque
Stefan Schmid
Sonia Ben Slimane

The first edition of ESCP's Impact Paper Series was marked by urgency; the Covid19 health emergency and crisis of 2020, leading to the publication *"Managing a Post-Covid19 era*". A year later, ESCP decided to focus on the topic of sustainability, which has gained in relevance over these last decades, but which has acquired significant attention more recently. The focus and title of this 2021 Impact Paper was *"Better Business: Creating Sustainable Value"*.

This third edition, in 2022, that we are presently publishing is aimed at addressing the geopolitical emergency following the large-scale armed conflict in Europe which started at the beginning of this year. The Russian-Ukrainian war, like any war, is first and foremost a humanitarian crisis. Beyond this dramatic event, it is also very likely to mark a turning point in the history of Europe and the world.

At the end of the 20th century, after the fall of the Berlin wall, many politicians, managers and academics were convinced that we had entered a new era. The famous statement by Francis Fukuyama underlines this:

> *"What we may be witnessing is not just the end of the Cold War, or the passing of a particular period of post-war history, but the end of history as such: that is, the end point of mankind's ideological evolution and the universalization of Western liberal democracy as the final form of human government."*— Francis Fukuyama, "The End of History?", The National Interest, No.16 (Summer 1989)

This "end of history" went alongside with an unprecedented wave of globalization across the world, with some authors even claiming that "the world is flat" (Friedman, 2005).
However, contradicting the famous claim by Fukuyama, it seems that European history keeps changing and that the geopolitical nature of relations in Europe and its neighbours may change once again. This recent militarized conflict in Eastern Europe reminds us that business and management are impacted by economic, political and societal shocks.

Many observers consider that the process of globalization that has marked the past decades has stalled, or may even be in retreat. This is, for instance, reflected in the resurgence of debates on the increasing role of national political and regulatory institutions within the development of economic activities. The events in and around the Russian-Ukrainian war also show us that geopolitical issues are once again central to business activity and its future development. Business and the socio-political arena are intimately entwined and influence each other in both ways.

The faculty of ESCP Business School – a leading international business school – turns its attention to geopolitics in this special issue. The goal of this third series is to explore from various angles how geopolitical problems can influence the economy and the strategies of companies as well as their managerial practices both at the international and national levels. We not only focus on the potential risks (the "dark side") but also on the opportunities for innovation and societal change ("the bright side") following a potential change in the world order. More generally, we aim to explore the interconnections between business and the socio-political world.

We have grouped the contributions under four thematic headings that fall within the framework of our B.E.S.T. research impact framework: Business, European, Societal and Teaching.

Each contribution is first and foremost the contribution of its respective authors, who have complete freedom in choosing the subject and the manner in which the problem is dealt with. ESCP Business School is committed to respecting the academic freedom of its faculty. The call for papers has been extended to our School's doctoral students and external collaborators.

We are delighted to witness such a strong commitment from the ESCP academic community in this special issue.

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Part I: Contributions in English (EN)

B. Business Impact

Europe and Economic & Business Policies [E. European Impact]

ESCP Impact Paper No.2022-01-EN

The great exodus?
How economies fall behind in the global race for talented employees

Sebastian Baldermann*
Stefan Schmid

ESCP Business School

Abstract

The “race for talent” forces firms in a globalized world to become attractive employers. But what does being “closed”, i.e. being coined by protectionism or conflict, imply for the competitive position of an economy in the global race for talent? In this paper, we elaborate on this question and indicate what economies should do – and avoid – if they do not want to fall behind in the global race for the best talent in a turbulent world.

Keywords: employees, globalization, race for talent, open economy, closed economy

* Research Assistant and PhD Candidate, ESCP Business School

The great exodus? How economies fall behind in the global race for talented employees

The race for talent and globalization: a short overview

The global "race" (or "war") for talent has become a distinct characteristic of our globalized world (Abeuova and Muratbekova-Touron 2019; Frank, Finnegan and Taylor 2004; Wanniarachchi, Kumara Jayakody and Jayawardana 2022). With economies globalizing, employees in general, and skilled employees in particular, have become more mobile and willing to seek professional success beyond the borders of their home country (Lewin, Massini and Peeters 2009). Economies, and herein firms (as employers) alongside governments setting the framework (as legislators), depend on skilled employees. However, as skilled labour is a scarce resource (Fasani, Llull and Tealdi 2020), employers (as well as legislators) are forced to figure out ways to attract the best talent in an interdependent world.

Therefore, what can firms and governments do to make a specific economy an "attractive" place to work in a globalized world? For firms, despite obvious factors like compensation or career opportunities, many additional factors have gained importance. In this regard, studies such as Dauth, Schmid, Baldermann and Orban (2022) point out the relevance of employer attractiveness: nationality diversity in the top management team or efforts of firms to promote diversity (and the communication thereof) signal to skilled job seekers that the organization is a worthwhile employer, no matter from where an employee originates. In terms of the general conditions in an economy that governments could try to affect, skilled individuals from different parts of the world might favour working in those economies that promise them (professional) developmental space irrespective of their origin, ethnicity, religion, etc. and advocate candidness towards (skilled) labour migration.

Apparently, in recent years, the globalized, interdependent world has revealed some cracks (Ciravegna and Michailova 2022; Witt 2019). An increasing number of economies is, more or less, closed.[1] Some economies that used to be passionate proponents of free trade have engaged in protectionism, i.e. limiting the free flow of goods and services into and from their market[2], and still do so ("America first").[3]

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[1] In this impact paper, being described as « closed » shall not imply that an economy is completely secluded from the rest of world ; « closed » is here used as an expression that describes economies that do not have a free, but limited flow of goods and services into and from the economy (where the degree of « closedness » may vary between economies).

[2] Of course, protectionism as a contributor to the closedness of an economy comes in many forms (tariffs, quotas, barriers to foreign direct investment (FDI), and many more). Accordingly, the « configuration » of protectionist measures may differ from country to country. This paper follows the (simplified, yet valid) notion that all forms of protectionism directly or indirectly contribute to an economy's closedness by limiting the free flow of goods and services, which in turn can cause similar outcomes for an economy irrespective of the configuration of protectionist measures (for an overview on protectionism, see Bhagwati 1988; see also the remainder of this impact paper).

[3] In this connection, however, it also has to be noted that no economy has ever advocated an entirely free flow of goods and services. Interests of individual countries or groups of countries have always played a decisive role in trade agreements etc. (Kohl 2014). Nevertheless, the degree of protectionism and the tendency to communicate protectionist measures openly has increased over the past few years.

Moreover, armed military conflict has returned to the European continent. In the midst of this turmoil and the pressing issues associated with it, one may ask: what does being closed, as opposed to openness, imply in the global race for talent?

Open and closed economies: implications for the race for talent

A fundamental notion of foreign trade theory is that the openness of an economy favours its productivity growth and therefore, eventually, its output and GDP (Alcalá and Ciccone 2004; Edwards 1998). Openness thus stimulates economic development, especially in the long term (Kim, Lin and Suen 2010; Sarkar 2008). So, what does openness imply in the race for talent in a world in which an increasing number of economies is "closing"? If qualified individuals from closed economies decide to leave, they might turn to economies that are considered open. Open economies could thus, in general, benefit from the "brain drain" of protectionist or conflicted countries – in particular if they convincingly convey that they are attractive places to work for people from abroad. The latter means that openness is no end in itself. An economy could be open and yet fail to provide favourable conditions for skilled job seekers from abroad. Only to mention a few examples, there could be resentment towards foreigners entering the domestic job market, i.e. a diverse workforce may not be cherished, or firms in the open economy may have no jobs available at all. Such factors could contribute to a situation in which an open economy may not necessarily have a disadvantage in the race for talent, but in which it could also not "benefit" in terms of attracting foreign talent from economies in other parts of the world that are closing off. A good example of an open economy which, nonetheless, must find incentives to attract skilled employees from abroad is "modern" Germany in its endeavour to counter its "Fachkräftemangel" (shortage of skilled specialists) with international talent.

Turning to closed economies, protectionism is a means to deliberately seclude the market from parts of or the entire rest of the world. Protectionism limits the free flow of goods and services as well as the general access to an economy from abroad (Fajgelbaum, Goldberg, Kennedy and Khandelwal 2020; Gunnella and Quaglietti 2019). To evaluate protectionism's implications in the race for talent, one may differentiate between its short-term and long-term consequences. In the short term, an economy with a protectionist agenda might be able to prevent a brain drain. For instance, stimulus packages could be issued by the government that enable firms to retain or attract talent (with financial or other benefits). Immediately after the introduction of protectionist measures hindering the free flow of goods and services, domestic firms might also find themselves in a better position because, for instance, international competitors are forced out of the market – which naturally improves their position in the race for domestic talent. However, in the long term, a protectionist economy will likely experience problems in retaining talent domestically, let alone attracting talent from abroad, especially in case of a high degree of protectionism. Accordingly, firms from protectionist countries will also not have the same opportunities to offer their goods and services that firms from open economies have. In this connection, their competitive position will deteriorate, and firms will not have leeway to attract or retain talent, e.g. with financial incentives such as compensation. The economy will also increasingly struggle to support its firms, as the general economic decline limits its options to provide stimulus packages etc. Consequently, aside from applying force, the protectionist economy will have no tools to avoid a brain drain of skilled employees to other (open) economies. A textbook example of the “brute avoidance” of a brain drain is the “Mauerbau” (i.e. building a wall at the border to Western Germany) executed in the former GDR starting in 1961.[4] It is very likely that a protectionist country will fall behind in the race for talent, at the latest in the long run.

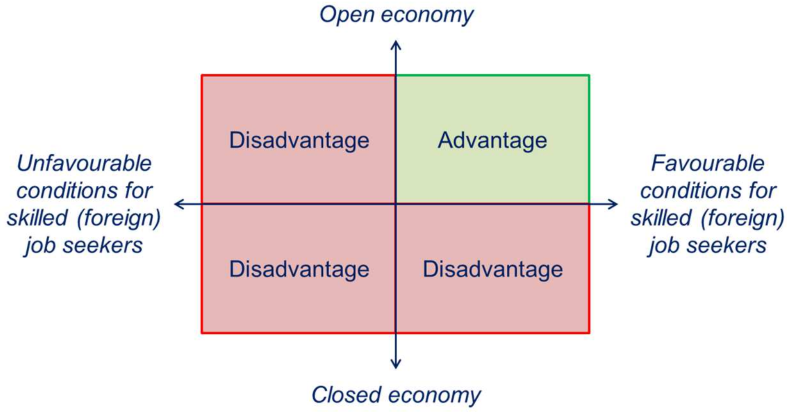
An economy may, however, also close involuntarily, as a result of military conflict. Military conflict has significant growth implications and involves an even worse outlook for retaining and attracting talent – in the short run and also, potentially, in the long run (Jalili et al. 2019; Koubi 2005). As military conflict ensues, a significant proportion of the population – including skilled talent – will leave the economy, if possible, to seek refuge in safer places. A short-term brain drain is the consequence. The long-term consequences are uncertain, but they could become likewise problematic. In a best-case scenario, after a conflict stops or cools off, skilled individuals might return to their home country and aim to “rebuild” the economy. However, depending on the length of the conflict and the extent of destruction the military conflict has left behind, a significant proportion of (unintentionally) migrated talent might also be reluctant to return. This is especially the case if they have managed to build a successful existence in the economy to which they fled, and if prospects at home are not promising. In the worst case, the conflicted economy therefore faces a long-term brain drain of skilled talent. This unfavourable condition sets the economy on the losing track in race for talent, harming its development for years and decades to come.

Conclusion

Figure 1 provides a simplified visual summary of the consequences of economies being open as opposed to closed in the global race for talent. It is apparent that, depending on whether an economy is either open or closed, there are different opportunities for firms and governments to improve their position or fall behind in the global race for talent. In a nutshell, an open economy is the best starting position to make the most of the race; being closed, in turn, can be considered a severe handicap in the global race for talent.

[4] Of course, secluding the domestic labour market, i.e. applying force to prevent a brain drain, could also be considered a (harsh) kind of protectionism. However, this paper considers such “harsh protectionism” as an ultimate consequence of prior protectionist measures that limit the free flow of goods and services from and into an economy.

Fig. 1: Advantages and disadvantages in the global race for talent.



Source: authors' own representation.

Arguably, current tendencies of economies deliberately or involuntarily closing, via protectionism or conflict, will most likely not stop globalization – albeit they might slow it down or set it back to some degree for a certain time (Contractor 2022; MacIsaac and Duclos 2020). Findings in studies about a globalized labour market, as in Dauth, Schmid, Baldermann and Orban (2022), will thus remain relevant. Accordingly, economies are well-advised to be "open" to qualified talent from abroad and to support (potential) employees (from abroad) in their endeavour to enter the respective domestic job markets. However, openness is no guarantee of winning in the global race for talent. Without sustained efforts to actually ensure the material and immaterial wellbeing of international talent, even economies that label themselves as "open" will fail in the race for talent. International talent will feel welcome not only through monetary incentives, but also especially, for instance, by being provided mentoring and guidance in a new environment. Understanding this will put economies on the "fast track" in the race for talent, which is arguably the most valuable resource in the global knowledge economy (Lewis and Heckman 2006; Valenti and Horner 2019).

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ESCP Impact Paper No.2022-02-EN

Riding the waves: How cruise lines use lobbying to navigate Geo-political complexities while balancing sustainable goals and economic interests

Ken Chan*
Corey A. Hancock*

ESCP Business School

Abstract

Cruise lines operate in a complex geopolitical arena by nature of their global presence and multi-country operations. Given the nature of their business, they are subject to scrutiny due to their multipronged impact on local communities, which include concerns of overtourism and environmental degradation. Prior research has shown that companies which engage in corporate political activity such as lobbying perform better. This paper explores how lobbying has been used by the industry to navigate complex political issues. We posit that when used to good purpose, lobbying can help companies to achieve their environmental, social, and governance (ESG) goals, while working with governments to protect the stakeholders' economic interests.

Keywords: Cruise Industry, Lobbying, Sustainability, Tourism, Trade Associations

*Global Executive PhD Candidates, ESCP Business School

Riding The Waves: How Cruise Lines Use Lobbying to Navigate Geopolitical Complexities while Balancing Sustainable Goals and Economic Interests

Cruise lines are large multinational businesses that operate across various jurisdictions and, by their very nature, are highly susceptible to the impact of geopolitics and government policies. As their ships sail to a variety of destinations, they operate in countries where they have no permanent, on-the-ground presence. As such, they often lack local legitimacy compared to other types of multinational companies which have ongoing operations throughout the year. Further, they face justifiable opposition from local community groups in certain destinations due to environmental sustainability issues as well as concerns regarding overtourism. This paper explores how the cruise industry uses lobbying to help navigate political obstacles, especially where there is tension between the economic benefits and sustainability goals.

A Primer on Lobbying and the Cruise Industry

According to the Cruise Lines International Association's (CLIA) *2021 State of the Cruise Industry Outlook*, the number of passengers taking a cruise vacation has increased substantially - from 17.8 million in 2009 to 29.7 million in 2019. Cruise lines intentionally design their revenue operations to maximize the portion of a traveler's budget that stays with their company. However, industry studies claim that, on average, passengers spend an additional $100 a day while on shore. Prior to the pandemic, there were 1.2 million jobs in the cruise industry with salaries and wages totaling $50 billion. The total economic output worldwide was $154 billion (Cruise Lines International Association, *n.d.*). These figures are used by the industry to show stakeholders, including governments, the substantial economic impact of cruise lines.

As multinational companies that operate within a varied geopolitical environment, cruise lines are regulated by countries with differing labour law standards, environmental protections, and tax regimes. Even though the largest cruise lines (Carnival, Royal Caribbean, and Norwegian) have corporate offices in the United States and other developed countries, they are respectively registered in Panama, Liberia, and Bermuda. These overlapping authorities entail challenging legal analyses to determine which entity holds authority over a particular issue, making cruise lines subject to regulations by a wide variety of governmental actors, each with varying levels of government transparency and ethical standards. Additionally, they are bound by the laws of the countries they sail to - adding to the already complex geopolitical environment. As such, we posit that cruise lines engage in lobbying to help navigate their relationships with governments, especially in key markets.

Lobbying occurs when individuals and organizations communicate with government officials to influence policy-making and government decision-making (Zibold, 2013). Companies undertake lobbying using various resources such as in-house lobbyists or outside entities (Jia, 2018). The latter include trade associations like the CLIA. The industry uses economic data together with their investments in sustainable technologies to paint a positive picture when engaging with authorities. A recent example where lobbying was deployed was the resumption of sailings from ports in the United States following the COVID 19-related order to halt sailings in the interest of public health. At the start of the pandemic, governments mandated that cruise lines suspend operations to slow the spread of COVID-19. It is estimated that between mid-March and September 2020, the suspension of cruise operations resulted in a loss of over $77 billion in global economic activity, in addition to 518,000 jobs and $23 billion in wages (Cruise Lines International Association, *n.d.*). Unlike airlines and hotels in the United States, cruise lines did not benefit from generous government subsidies as they are not registered in the United States and are not entirely bound by American laws. In this context, there was an increase in lobbying by cruise lines, largely aimed at getting their ships back to sea, with the goal of restoring passenger numbers to pre-pandemic levels. From 2009 to 2019, cruise lines spent an average of $3.5 million annually on lobbying, and once the global pandemic took hold, spending increased to $4.4 million in 2020 and $5.3 million in 2021 (OpenSecrets, 2022). Government filings show companies such as Norwegian and Carnival lobbied federal authorities in the United States on safety guidelines and a gradual return to sailing. Carnival and Norwegian spent 100 times more on lobbying in 2021 than it did in 2020 (O'Connell & Narayanswamy, 2022). Starting in June 2021, the Centers for Disease Control and Prevention (CDC) allowed cruises to sail from the United States as long as the sailings complied with strict public health regulations. Since then, the CDC has gradually relaxed its measures and protocols for cruise ships, ultimately allowing its order to expire in January 2022. An analysis of CLIA's press releases over this period show a sustained advocacy campaign by the trade association on behalf of cruise lines, aimed at relaxing restrictions for cruise travel while ensuring that measures to slow the spread of the virus were adopted, suggesting that lobbying by the cruise industry contributed to the return of sailing operations.

Striking a Balance Between Environmental and Economic Imperatives

While the cruise industry provides a certain level of economic benefits for destination ports, it also presents governments with political challenges, including excessive congestion, and adverse environmental effects due to emissions and other discharges from the ships (Vayá, Garcia, Murillo, Romaní & Suriñach, 2018). Historic European destinations such as Dubrovnik and Venice have drawn the attention of international media keen to report on the impact of cruise ships on local communities (Street, 2019). The daily flow of tourists, when uncontrolled and unmanaged, leads to undesirable consequences in their ports of destination and a sub-par visitor experience, with overcrowding of local infrastructure, environmental damage, and excessive wear and tear on iconic cultural, historic, and religious sites (Hancock, 2022). Consequently, governments cannot ignore the negative impacts of cruise activities, despite their perceived economic benefits. This creates tension between environmental and economic priorities for industry and government alike. We explore two examples where the industry engaged with authorities through lobbying to identify practical solutions that could help achieve a balance between financial and sustainable goals.

#1. Sailing in Canadian Waters

In Canada, environmental groups have been advocating for tighter rules around the dumping of toxins. The World Wildlife Fund - Canada published a report arguing that cruise ships are the top producers of four streams of waste (sewage, toxic scrubber wash water, greywater, and bilge water) and called on the federal government to develop new regulations that would prohibit dumping into Canadian waters (Kloster, 2022). At the same time, small businesses in coastal cities argue that cruise ships are important for the local economy. The Tourism Industry Association of British Columbia states that the industry contributes around $2 billion a year to the provincial economy (CBC News, 2022).

The Registry of Lobbyists shows that CLIA has engaged with the federal government on pollution-related matters. In their advocacy materials, CLIA outlined efforts made by cruise lines to implement green maritime technologies and sustainable tourism practices. In April 2022, to coincide with the resumption of cruise sailings on Canadian waters, the federal transportation ministry announced new environmental measures developed as an outcome of dialogue between government and industry. According to the announcement, these measures pertaining to cruise ships in Canadian waters exceed international standards and will "support the work that is underway to conserve 25 percent of Canada's oceans by 2025 and 30 percent by 2030". Pending the finalization of the regulations that would make these standards permanent, the cruise industry agreed to comply with the measures as they resume sailing following the suspension of operations due to the global pandemic (Transport Canada, 2022).

#2. Accessing a Popular Italian City

Cruise activity in Venice has long been a controversial issue for government agencies, the travel industry, special interest groups, tourists, and the Venetian public. Environmental groups argue that large ships have caused significant damage to the lagoon and erosion to buildings within Venice's treasured UNESCO World Heritage sites. At the same time, longtime residents have complained that their hometown has essentially been turned into a large museum in which the very character, charm, and neighborhood feel of the historic destination has been significantly damaged by the daily throngs of tourists who far exceed the city's carrying capacity. In 2021, the Italian government announced a ban on cruise ships entering the port (Giuffrida, 2021). Press releases by CLIA suggest that the cruise industry has been working with government authorities to identify a sustainable solution to the issue. Cruise lines have engaged in lobbying efforts to protect their access to this popular destination, be it through the cruise port in Venice, in neighbouring Marghera, or in Ravenna (140 kms south). As part of their advocacy efforts, CLIA outlined the cruise industry's contribution to the local economy, reporting that it supports over 120,000 jobs and a turnover of over $14 billion.

Conclusion

Cruise lines are exposed to a multitude of geopolitical risks that have the potential to greatly impact their operations. This is further compounded by the complexities of political issues at global, national, and local levels. As such, the industry strategically deploys experts in politics and government to help navigate the obstacles and challenges. They put forward economic and other arguments to back up their case for industry-friendly policies, knowing that governments need to balance economic interests with those of competing stakeholders, such as environmental advocates, sustainability champions, and local communities. This is not a zero-sum game, meaning that well-crafted, duly-researched, and fully-informed policies can be amenable to all of these somewhat disparate stakeholders. While no one entity will get everything they want from the complex policymaking process, a harmonious solution can be reached when the authorities arrive at a happy medium.

While the interaction between business and politics is complex, lobbying is a tool that can help companies and governments to arrive at an optimal public policy solution as seen in the examples provided in this paper. The significant increase in lobbying activities since 2020 points to the value cruise lines place on the work of lobbyists to help them engage with policymakers. When used to good purpose, lobbying can help companies achieve their environmental, social, and governance (ESG) goals while working with governments to protect everyone's economic interests

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Employee experiences of telework in times of crisis

Almudena Cañibano
Argyro Avgoustaki

ESCP Business School

Abstract

Teleworking has been often introduced as a means of responding to turbulent events such as epidemics, wars, natural disasters, financial crisis. However, only few studies explore how individuals make sense of the practice when faced with the uncertainty caused by macro level factors, especially before Covid-19. The existing limited literature reveals that the context of crisis can alter employee experiences of telework. We have recently contributed to this literature with a study exploring how employees experienced telework during the financial crisis of 2008. Our key finding is that in the context of financial crisis, employees interpret telework as a potential threat to their jobs and careers prospects. In this impact paper, we highlight how telework may be used as a means of dealing with crises, we present a few studies that explore telework in context and, based on our review of the literature and our own study, we draw some general implications that could be relevant for employees, managers and governments alike.

Keywords: Telework, turbulent context, employee experiences, financial crisis.

Employee experiences of telework in times of crisis

Telework as a means to deal with global and regional crisis

Global and regional events such as epidemics, wars, climate change, natural disasters, terrorist attacks, financial crisis, have changed the parameters regarding the way work is performed and the way the workforce is managed. Because such events create uncertainty, disrupt the regular flow of work, and threaten the general well-being of individuals, employers and governments must take urgent action. Flexible working, and in particular telework, has been introduced as a means to respond to such events in an effort to minimize uncertainty and the discontinuity of work while ensuring employee protection. The practice is defined as "*work that is conducted away from the usual place of business but mostly at home and that is often supported by telecommunications, internet access or computer*" (Kossek, Lautsch and Eaton, 2005: 348). In particular, Covid-19, "*pushed the incidence of telework to an unprecedented tipping point*" with many regions including the United States, Europe and Asia reporting record rates of teleworking (Chong, Huang and Chang, 2020: 1408). Never before has a human resource practice been adopted on such a scale and pace, sparking interest within the research community, with scholars trying to answer how employees have responded to teleworking during the Covid-19 crisis.

The literature on telework

While there is already a plethora of research examining the consequences of telework for employees and organisations (e.g. Bloom et al., 2015), few explore how individuals make sense of the practice under the uncertainty caused by macro level factors, particularly pre Covid-19. Only a few studies have been conducted at a time when telework was introduced as a temporary or permanent measure to deal with turbulent contexts and events, such as natural disasters (e.g. Donnelly and Proctor-Thomson, 2015). Therefore, some of the "accumulated knowledge on remote working might lack contextual relevance" (Wang et al., 2021:17) and the existing evidence might not be applicable in different social, economic and political circumstances. In addition, one criticism in the literature is that although telework may be seen as an employee-centered practice, because it often serves employees' interests, the positive side of telework may have been inflated (Wang et al., 2021). Another criticism is that research needs to consider the dynamic nature of employee experiences. Employees may initially experience a practice positively but, as they are more frequently exposed to it, their views may change. Over time, some may reconsider their suitability for the practice or think differently about whether or not the practice benefits them (Bloom et al., 2015; Wang et al., 2021).

Indeed, evidence shows that a turbulent macro-economic context can alter employee experiences at work and that for specific categories of employees such change can be for the worse. Indicatively, in the context of Covid-19, Çoban (2021) examines the telework experiences of professional, middle-class, married women with childcare responsibilities, in Turkey. Her findings show that telework puts employees' careers in jeopardy and threatens their employment while it "consolidates their roles as traditional housewives" risking alienating them from the labour market. The experience of those women is overall a negative one and telework therefore within the Covid-19 context may not be an ideal option for them. Another study (Wang et al., 2021) conducted within the Covid-19 context on different employees, i.e. Chinese employees of different genders and family responsibilities, among other factors, identified four main challenges related to telework. During the pandemic, teleworkers experienced challenges related to interference (more interruptions from family), ineffective communication (online communication is more challenging that offline communication), procrastination and loneliness. According to their study, social support and job autonomy attenuated some of these negative effects while workload and monitoring aggravated them. The most significant moderator was found to be self-discipline. It appears that less disciplined employees experienced more challenges related to telework than more disciplined employees, suggesting that they are perhaps less suitable for the practice. Donnelly and Proctor-Thomson (2015) examined individuals' experience of telework in a different crisis context, that of Christchurch's earthquakes in New Zealand. Their research focused on managers, team leaders and staff and revealed that during a natural disaster crisis, team leaders had less positive experiences compared to other types of employees, mainly due to greater work demands forced upon them related to maintaining employee monitoring and coordinating operations.

Overall, the aforementioned examples reveal that employee experience is somehow negative during crisis, and that the repercussions for certain categories of employees such as women with children, employees who lack discipline and employees with higher levels of responsibility, may be even more severe.

Telework during financial crises

Although there are similarities between crisis situations, in that they often cause economic recession and that employees experience more difficult working conditions, there are also major differences. In crisis contexts such as during a pandemic, a natural disaster, or a terrorist attack, telework can be mandated by the government and be practiced full-time. In addition, the introduction of teleworking is more abrupt and, as such, organizations are less prepared to deal with, for example, issues related to cyber security or the necessary remote systems so employees can directly switch over to telework. Under the aforementioned types of crises, the line between personal and professional life becomes even more blurred as schools may be closed and people may be advised to stay at home, forcing employees to work while caring for their children or others. By contrast, in a financial crisis, telework is not necessarily abruptly introduced so organizations may be better prepared for the switch. For employees, telework can be practiced occasionally and on a more voluntary basis, when the home environment allows it.

Given these differences, it is important to explore how employees experience telework under different types of crisis contexts.

The financial crisis of 2008 had a significant impact on workers' lives, affecting work arrangements, pay and working conditions. Despite its impact and significance, little is known about the extent to which the crisis and the economic uncertainty that came hand in hand with it, played a role in shaping workers' understandings of telework. In our forthcoming paper for the Human Resource Management Journal, we tried to address this gap in the literature by examining how workers make sense of and respond to telework in the context of macro level uncertainty and crisis.

We drew on the premises of signaling theory (Spence, 1973) to consider telework as a signal sent by the organization to employees and argue that employees' interpretation of that signal will largely depend on the environment in which it is sent out. We analyzed interview data collected from the Spanish branch of a major international consultancy firm. We focused on professional knowledge workers in areas such as strategy, finance, and operations.

Our key finding is that in the context of financial crisis, employees interpret telework as a potential threat to their jobs and careers prospects. In the literature, telework is often presented as an employee-centered practice that benefits individuals (Avgoustaki and Bessa, 2019) and may pose a threat to organizations if teleworkers behave opportunistically (Peters and Van der Lippe, 2007). In contrast, our study indicates employees may feel threatened because, in accepting telework, they may be putting their careers and even their jobs at risk. Therefore, it appears that employees have not interpreted the signal as intended by the organization because it was interpreted within a financial crisis context. The meaning that employees ascribed to telework exceeds formal human resource policies and practices (Cañibano, 2019). This suggests that "the meaning of telework is not predetermined, but continually shaped socially, in light of events that go beyond the firm's boundaries" (Cañibano and Avgoustaki, 2022).

General implications

Based on our study and our review of the literature, we draw some general implications that could be relevant for employees, managers and governments alike.

1. Companies operating under uncertain environments caused by macro level crises often need to reassess the spatial nature of work.
2. Telework can be implemented by companies or can be government driven in an effort to deal with uncertainty, securing the continuity of work, and protecting employee health and general well-being.
3. During crises, it is the human resource function that becomes the primary source of change as it must address the needs of employees by promoting, if not new, then different ways of working.

4. Employees and employers may need to consider the fit between teleworking and the individual. As we observe in certain studies, which took into consideration the crisis context within which telework was implemented, certain categories of employees, e.g. women with children, team leaders, and employees who lack discipline, may have a negative experience of telework.
5. Employers may need to consider the fit between teleworking and the environment. In the context of the financial crisis in Spain, employees seemed to experience telework in a negative light and interpret it as a threat. Employers could try to reduce any negative interpretations by providing job security and career opportunities.

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Davids and Goliaths: Hidden champions in an age of state capitalism

Bernardo Melo Pimentel

Nova Forward College
SBE and ISEG Lisbon

Guillermo Ramírez
ESCP Business School

Abstract

We review the state of the current industrial champions debate and make the case for small, nimble Davids, rather than resource-hungry Goliaths. These export-based SMEs have shown robust performance in recent years and may help economies increase their resilience in times of significant uncertainty. They are more autonomous than traditional champions and they are already in our midst. The challenge for policymakers is how to foster an environment that supports Davids while keeping an eye on national strategic interests.

Keywords: Industrial policy; National champions; hidden champions

Davids and Goliaths: Hidden champions in an age of state capitalism

This last January, in his address to the European Parliament, President Macron reiterated the urgency to create and stimulate 'European champions'. With the prospect of the Russian invasion of Ukraine looming on the horizon, Mr. Macron emphasized the need to invest more in the defence sector champions, as a means to "remain open without being dependent". While recent, the content of the speech was neither surprising nor novel. Just two years prior – in the aftermath of the European Commission's block of the rail merger between Siemens and Alstom – a similar push had been made. In a joint communication with the German Chancellor, the two leaders urged the European Commission to prioritize strategic interest over antitrust policy. In chancellor Merkel's words, Europe should follow the lead of countries such as the United States, South Korea, Japan, or China. In short, the EU "must not be afraid to have global champions, but we must work towards them".

Typified in the two examples above is the growing political will to foster the development of large national or regional, state-sanctioned conglomerates. These 'Goliaths', are colloquially known as champions and come in different guises. Broadly speaking, they can be defined as individual companies – or a set of oligopolistic firms – that add the strategic national interest to their more common value-maximizing mandate. Champions are either directly established by governments – as a form of state capitalism – or are private organizations that directly or indirectly benefit from preferential treatment by public authorities. Traditionally, champions operate within strategically sensitive, or critical industries, such as defence, commodities, or non-tradeable essential goods. They also tend to have a strong prevalence in natural monopolies – sectors where the significant weight of fixed costs requires few, large scale operators to attain competitiveness. These include utilities such as water, gas, or electricity, and infrastructure, ranging from the road and rail network to wireless telecommunications.

The case for champions

In principle, there are many arguments to be made for the strategic and economic advantages of industrial champions. In critical sectors, they act as gatekeepers for national or block interests. The previously mentioned EU defence argument used in President Macron's speech is an example of this line of reasoning. There are, however, other instances in which this argument has been employed. During the rollout of the 5G wireless network throughout Europe in 2019, strong political pressure from national governments and multilateral organizations (notably NATO) alike was put in favour of a European, rather than a Chinese backend operator (Friis & Lysne, 2021). The prospect that countries like the Czech Republic would have Huawei – a Chinese telecommunications company – rather than Ericsson – a Swedish telecom – as a provider in their networks generated a strong political backlash. While not explicitly a matter of territorial defence, the issue was categorized as one of national security, in which non-intervention could lead to "possible loss or interruption of availability, integrity or confidentiality in such systems" (Kaska, Beckvard, & Minárik, 2019).

A second, and increasingly popular, argument for the support of champions is that of supply chain resilience. The ongoing pandemic and its lockdowns as well as the invasion of Ukraine have led to growing calls for 'onshoring' or 'reshoring' production. The aim of such policies would be to mitigate the effects of price surges, shortages, and delivery fulfilments in a wide range of raw materials, intermediate components, and final goods (Kammer, Azour, Selassie, Goldfajn, & Rhee, 2022; Nikolopoulos, Punia, Schäfers, Tsinopoulos, & Vasilakis, 2021). This is, however, a multi-layered problem. Despite talk of 'slowbalization' and even deglobalization, the ever-increasing sophistication of consumer and business goods has made us heavily dependent on close-knit networks of highly skilled, specialist suppliers. Required resources and competencies in a complex production process make it virtually impossible for any given country to be able to be fully self-reliant. Additionally, the matter of raw material scarcity still plays a vital role. Responses such as former USA's president Trump's bilateralism or its more recent incarnation in the form of 'friend-shoring' or 'ally-shoring' demonstrate the implicit acknowledgement that even with active industrial policy, economic autonomy may remain a mirage for the foreseeable future.

The third set of viewpoints defending champions can be summarized as them bringing in a number of positive externalities. Large domestic groups frequently develop their own resources and knowledge base in-house. Theoretical support for this view can be grounded on Michael Porter's notion of clusters and industrial districts – geographic concentrations of companies and institutions of a particular field (Porter, 1998). Clusters use their local knowledge, relationships, and motivation to achieve a competitive advantage. In addition, clusters generate spill over effects and positive externalities in terms of employment, taxation, and support industries (Delgado, Porter, & Stern, 2014). Finally, the climate agenda and the control over emissions have also been pointed out as a reason for taking up industrial action at home (Rodrik, 2014).

But do we need champions?

Listing the pros of champions is naturally only one side of the story, with a long and rich tradition in economic literature. Perhaps the single greatest concern with the promotion of industrial champions is the increase in the market concentration it generates – and the subsequent reduction of competition and rise in prices it produces. Firms are only too aware of the effect that reduced competition has on their market power and often lobby for such policy outcomes. Unsurprisingly, the link between active industrial policy and political corruption has been verified in multiple instances and across contexts, syphoning public resources and eroding trust in institutions (Ades & Tella, 1997; Bahoo, Alon, & Floreani, 2021).

On the other hand, evidence in support of the level of innovations brought up by state-sponsored industrial champions is, at best, lacklustre. The issue seems to be not so much the difficulty in spawning innovations, but their adoption and distribution (Geroski, 1992). Here too, the monopolistic framework of analysis may be of use. Larger firms with a dominant position in the market will have little incentive to perform the necessary investments required to implement new innovations. At the core we have a type of agency problem: public officials are interested and will promote research and development at national champions while decision-makers at the firm level may be reluctant in facing the costs associated with operationalizing their own innovations (Musacchio, Lazzarini, & Aguilera, 2015).

Competition and anti-trust authorities also have it tough: being specifically mandated with targeting excessive market concentration, how should they act when politicians ask for the opposite? Greater market share does contribute to market power and potential for abuse of dominant position by monopolistic players. That this may be a known – or even acceptable - risk has been acknowledged explicitly by politicians. In the speech from the opening example, President Macron expressed that competition law has perhaps been too focused solely on the consumer and not enough on defending European champions. But can this be a false trade-off?

The future is already here

Unlike many economic models, not everything else was held *caeteris paribus* as the debate on the merits and risks of promoting industrial champions unfolded. A strand of literature –mostly studying the export performance of German companies – has identified a set of relatively low-profile, high-performance firms, the aptly named 'hidden champions'. Initially coined by Hermann Simon, hidden champions can be defined as midsize, highly specialized export leaders, taking up a top three global market share position – or number one in the company's home continent (Simon, 1990). They "spearhead" their respective markets via differentiation – rather than cost leadership. They are also highly specialized, which enables hidden champions with economies of scale in single product markets. Thirdly, they operate in highly complex, path-dependent, manufacturing industries, prone to the creation of lock-in effects by their customers (Simon, 2009).

At first glance, our 'Davids' differ significantly from their older and larger siblings; they are not household names, ostensibly lacking the 'national interest' mandate, and are not started by governmental decree. Their origins lie not in strategically 'sensitive' industries, but rather in knowledge-intensive, niche sectors, that enable these champions to establish long-term relationships with their customers (Audretsch, Lehmann, & Schenkenhofer, 2018). And while they compete in global markets, they do so not by virtue of their size, but rather by virtue of their superior export performance.

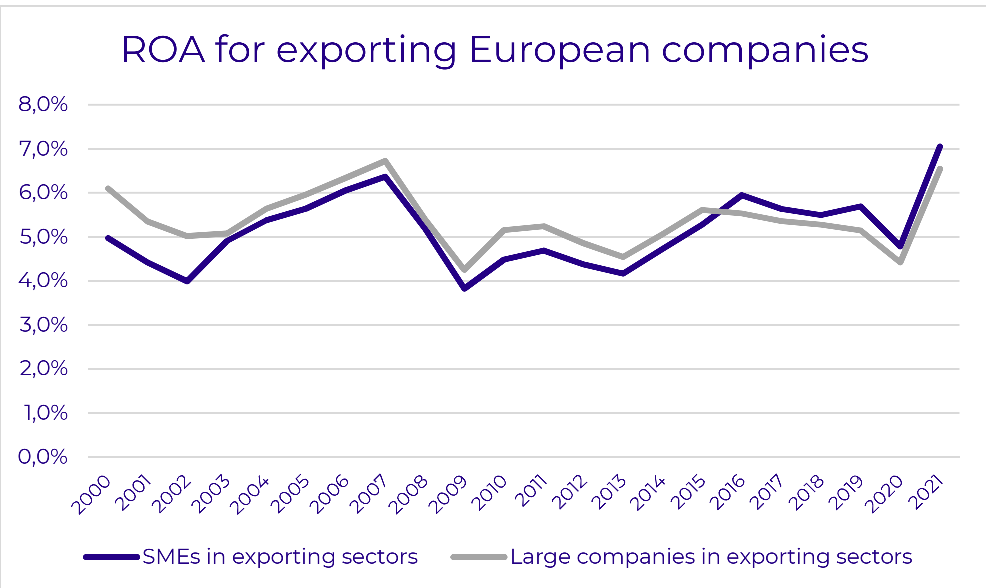

Figure 1: ROA of exporting SME and large companies.
Source: BACH European sample.

Figure 1 depicts the 2000-2021 series on the return on assets (ROA) for the BACH sample of 11 EU countries. The information pictured directly compares the performance of small and medium-sized exporting enterprises (SMEs) with large companies (of an annual turnover greater than EUR. 50 million). While the comparison is merely exploratory and differences between sampled firms are modest, an observable switch in trend over the period of the analysis is present. Up until 2015, larger companies outperform SMEs. Afterwards, it is the SMEs that lead.

It may be premature to attribute the performance improvement of SMEs to the rise of hidden champions alone. However, it would be interesting to dive into some of the underlying factors that contribute to the explanation of their success. A recent review identified the quality of human capital (particularly at the managerial level), innovation in form of patented proprietary technologies, and nimbleness (a combination of flat organization structure with relatively small size) as the most distinct resources controlled by hidden champions (Schenkenhofer, 2022). Technological developments also play a role; recent experimental research has shown additive manufacturing techniques, such as 3D printing, to significantly reduce the levels of output required to access the full extent of economies of scale (Baumers & Holweg, 2019). This de facto mitigates the size advantage of larger operators and may in the future dilute the power of some industrial champions operating in natural monopolies.

The role policymakers

Policymakers can play a constructive role as well, as many of the arguments often touted to support 'Goliaths', can also be used for 'Davids' – with fewer negative externalities. If the goal is to increase autonomy and shorten supply chains, the hidden champions can chip in. If export competitiveness is the main concern, hidden champions have proved they can lead. In short, hidden champions have demonstrated that SMEs can be leaders in international competitiveness and innovation. The question then is how to create these conditions and foster the success of these new champions.

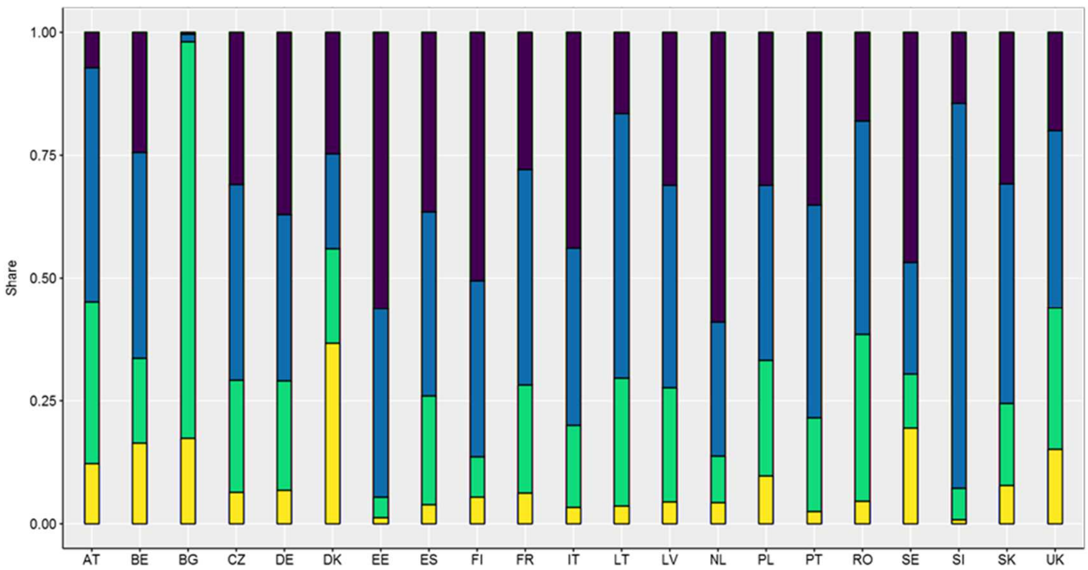

Figure 2: Distribution of total values by country and firm size (2007 - 2013).
Sources: OECD and ORBIS.

In a way, the aforementioned question has already been acknowledged and is being actively tackled with both domestic- and European-wide policies (Bachtrögler & Hammer, 2018). Figure 2 depicts the distribution of EU funds – encompassing structural funds, financial instruments (e.g. the SME instrument), thematic funds, and internationalization support – per member state and firm size[5] during the 2007 - 2013 period. A quick glance at the distribution of funds confirms that – with the exceptions of Bulgaria and Denmark – SMEs are already the biggest group of beneficiaries. Medium-size companies, the most likely 'Davids', make up a respectable share of funding in most member states, corresponding to roughly half the sharing of support in Austria, Lithuania, and Slovakia. In profile, support recipients exhibit many value creating, desirable traits; they are more likely to be in high-tech sectors, already have a track record of previous venture capital funding and demonstrate high-growth potential (Mina, Di Minin, Martelli, Testa, & Santoleri, 2021).

It is also relevant to look at the pool of applicants, not only recipients. Here, we observe that a very significant portion corresponds to younger firms still facing financing constraints. This should be regarded as an opportunity and call for action. Rather than seeking existing 'Goliaths', legislators should be concerned in identifying future 'Davids'.

The new 'NextGenerationEU' stimulus package provides a rare opportunity for shaping the future for European wide manufacturing. The 'InvestEU' fund in particular – itself encompassing thirteen centrally managed EU financial instruments - has an explicit mandate for the support of SMEs. With an endowment of EUR. 10.28 billion controlled by the European Investment Bank, the fund is tasked with investing in the innovation, digitalization, sustainability, and green transition of small and medium-sized enterprises and mid-caps. However, its policy goals also mentioned the support of public 'strategic investments' that support the 'common European interest'. Excessive reliance on these projects will inevitably crowd-out private investment and reduce resources available for SMEs. For policymakers, the hard challenge is then to understand what 'common interest' genuinely means.

Conclusion

In the present piece, we reviewed the current state of the industrial champions debate, recentering the discussion on the rising phenomenon of hidden champions. The present climate of high uncertainty has sparked renewed calls for state intervention in sectors of the economy deemed sensitive for geopolitical and strategic reasons. The promotion of large industrial champions that can safeguard national interests and withstand future shocks has been a frequently voiced argument by policy makers. However, this option has in the past come at the expense of direct public funding, indirect preferential treatment, and increased industrial concentration – with all its implication in terms of higher prices and reduced innovation.

We instead made the case for the new 'Davids', the hidden champions. These export-based SMEs have shown robust performance in recent years and may help economies increase their resilience in times of significant instability. They are more

[5] ORBIS firm size categories: Very large companies: 1,000 or more employees; large companies: 150 or more employees; medium-sized company: 15 or more employees; small company: all others.

autonomous than traditional champions and evidence shows they may be outperforming them. Rather than lobbying for state interventionism or for the scrapping of anti-trust mandates, hidden champions welcome global competition. They rely on high-quality human capital, patent portfolios, organizational nimbleness, and incisive usage of novel technologies like 3D printing to compete in global markets.

The benefits of supporting hidden champions appear to be evident, but the cost of perceived inaction for policymakers is often too high; the devil will find work for idle hands to do. This is only amplified by the unique opportunities that the 'NextGenerationEU' will bring. The pathway then must start by accepting that it is the 'Davids' and not the 'Goliaths' who are in fact the best paladins of national interests. It may be time for the hidden champions to come out and take their place in the limelight.

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How does global business instability put resilience back on a firm's strategic agenda? Resilience impact on performance

Anna Souakri*

ESCP Business School & Square Research Center

Abstract

Unexpected geopolitical conflict disruptions such as the Ukraine war could act as "external enablers" of performance. By strengthening the company's autonomous resources and capabilities as well as developing new ones, companies are able to increase their resilience and generate profitability gains. These strategic levers should be favored when situations of disruption occur. Despite the importance of resilience within a context of high volatility, few empirical testing of its impact on performance exist. We fill this gap and propose a predictive analysis of resilience on performance to show that resilience is a core strategic capacity that should be developed to sustain strategic competitive advantage and performance.

Keywords: Resilience; performance; strategic advantage; disruption; innovation

*Affiliate professor, ESCP Business School

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Introduction

In a context of accrued geopolitical instability, the macroeconomic environment in which companies evolve is ever more uncertain and prone to radical disruptions that significantly impact the companies' activity. Value chains are intertwined in a globalized business configuration in which different firms interact directly and indirectly with each other. From this viewpoint, resilience is a strategic asset to prioritize to be able to control the impacts of disruptions on performance and to make the most of them. Disruptions as unexpected geopolitical conflicts , like the present Ukraine war, or sanitary crisis such as Covid-19, could act as "external enablers" on performance. Most resilient companies manage to leverage disruptions, pivoting and turning them into favorable opportunity and increased performance. In a VUCA world (Volatility, Uncertainty, Complexity and Ambiguity), resilience is a core strategic capacity to build sustained strategic competitive advantage and performance.

While much research shows that resilience is a fundamental determinant of performance, most of it is still conceptual. Even though some empirical studies have been undertaken, quantitative measures are rare, mainly indirect and very general. The objective of this paper is to propose and empirically test a predictive model of performance underpinned by resilience. How can resilience be made tangible and sustain performance in a context of uncertainty ?

1. The facts

End of February 2022. The spiral of the continuous price rise of raw materials and the collapse of stock markets and profits opens our eyes to the vulnerability of French companies, most of which have activities and holdings in Russia. How did we get here? Could this situation have been anticipated and can we minimize the losses?

Nearly 200 years ago, on November 22, 1812, Napoleon's Grand Army had been trapped by the Berezina River and surrounded by the Russians. Cornered, Napoleon decided to cross the river at any cost. He succeeded and won this distressing battle, but at the expense of considerable losses and the weakening of the Grand Army, which had consequences for the final fall of the First Empire.

Today, companies find themselves in a somewhat similar situation, forced by the escalating prices of their inputs on the one hand, and their dependence on Russia for their energy supply on the other, with a clear lack of being able to compensate with other alternatives. Commodity prices have risen steadily since the outbreak of hostilities and on 7 March, Brent crude oil reached almost $140, and a 17% rise in gas prices had repercussions on wheat and metal prices (nickel, copper, aluminum, zinc).

The result: a collapse in the stock market price and a spiral of falling profits and rising costs. On February 24, the CAC 40 lost more than 4% at its opening. An example, Société Générale, heavily exposed via its majority stake in its Russian subsidiary Rosbank, collapsed by more than 11% on March 7. The impasse in which these companies find themselves leads us to question their dependence: how did they reach such a degree of vulnerability? Have they not learned the lessons from the COVID crisis?

It would seem, not. Once again, it took economic disruption for companies to realize the importance of resilience in order to preserve their strategic autonomy and maintain their performance.

As we have seen with previous shocks (the 2008 financial crisis, COVID), companies that had put resilience at the heart of their strategic management were able to anticipate and cushion the shock on their performance, and even increase it for those that were able to take advantage of the crisis. Such companies were able to pivot by reconfiguring their strategy and their associated business model, to rely on performance levers other than those affected by the shock, as well as developing new ones.

By strengthening the company's own and autonomous resources and capabilities as well as developing new ones, companies can increase their resilience and generate profitability gains. They will then be able to identify which of their resources and competencies are a sources of value to be optimally exploited to strengthen resilience, and which have the greatest impact on performance. These strategic levers should be favored in situations of disruption. For example, investing in energy transition, digital twins, applied R&D, and diversifying sourcing into higher value-added activities, are resilience vectors.

Overall, most reactions to the Russian-Ukrainian conflict have invoked the concept of resilience as the number one priority. The observation seems simple: it would be enough to develop resilience to create value and maximize performance in the long term. But in reality, the proposals remain vague and do not really demonstrate how resilience can contribute to performance. Let's clarify what resilience is and what it means for the company.

2. Resilience concept in management

In a disruptive environment where upheavals are increasingly frequent and intense, the ability to be resilient becomes fundamental when aiming for sustainability. It is a continuous process that takes place over time and refers to "external enablers" that mark a breaking point in the company's current activities, such as a major crisis (e.g. stock market crash, Covid) or a brutal and disruptive change in the macro-environment (new regulations). Resilience is assimilated to a dynamic capacity of the company, i.e. a capacity to "(1) identify and create an opportunity, (2) seize the opportunity and (3) maintain competitiveness through the improvement and reconfiguration of the company's tangible and intangible assets. (Teece, 2007, p.1319).

From the multiple conceptualizations and definitions of resilience, a general typology emerges according to two perspectives, which we can describe as passive and active: passive resilience can be defined as the ability of an organization to absorb a shock without implementing major changes in organizational functions or structure and to return to its initial state after overcoming the shock. In addition, active resilience goes beyond the restoration of the pre-breakdown state and involves the development of new capabilities and an increased capacity to create new opportunities. It is a process of continuous renewal of the organization, which must be able to identify environmental factors, analyze them, interpret them and formulate new responses adapted to environmental requirements. It is therefore essential to define indicators that allow these factors to be integrated and to establish a permanent monitoring system in the performance measurement system.

3. Complex interactions between resilience and business performance

With an active approach to resilience, the company is in a state of continuous renewal, so that changes in resources occur more quickly than in competitors, and so that it performs relatively better than them. This implies a planned dimension of resilience that has the potential to further increase performance in an unstable environment thanks to a steering system that allows for the monitoring of weak signals, and thus to anticipate the actions to be implemented.
Viewed as a dynamic capability, the permanent modification of resources and competencies should enable organizations to maintain their competitive advantage and generate benefits that are superior to those of competitors.

Overall, resilient organizations perform better than their competitors in times of disruption and are distinguished by five common characteristics: (1) preparedness, (2) adaptability, (3) collaboration, (4) trust and accountability, which enable them to gain a competitive advantage in terms of anticipation, buffering, adaptation and shaping (the ability to influence the dynamics of their environment).

Existing studies, however, remain relatively superficial on how they measure resilience and are generally limited to very qualitative and macro approaches. Let's look at how these measurements can be refined.

4. How to quantify resilience? Measures that are still superficial

The resilience of a company is a latent variable that is not directly observable and research has therefore chosen to infer it indirectly through its impact on other post-crisis consequences of the company.

Thus, most studies have considered the speed of stock price recovery, sales growth after multiple shocks or ROE. Others have been based on the reaction of the firm to a particular shock, such as the recovery of the airlines from the September 11, 2001 attacks.

The majority of empirical studies have therefore considered a posteriori, very general and macroeconomic variables, without making it possible to measure precisely the contribution of resilience to financial performance. There is a need for alternative measures based on empirical and standardized metrics of corporate resilience as a process a priori so that we can measure its predictive impact power on performance. We provide preliminary suggestions to address this need.

5. Empirical testing of resilience on performance

We analyze[6] the predictive impact of resilience on performance (profitability). We proxy performance with profitability and we take the ROE. Much research shows that innovation plays a critical role in rapid recovery from economic shock The higher the innovative capacity of a company, the higher the resilience. A growing body of work has also highlighted the importance of innovation as critical to the long-term renewal and restructuring processes that enable companies to adapt their industrial and technological structures over time to changes in the economic landscape. From this standpoint, R&D spending stands well out among different innovation proxies because it allows for the renewal and enrichment of the core functioning structures and processes in a dynamic way such that companies can quickly adapt them to their ecosystem changes. Thus, R&D spending- operating revenues ratio measures the ability to bounce back and thrive and we take it as our proxy of resilience.

We take a sample of a hundred companies from different industries, mainly GAFA and energy firms, and then corrected the corresponding variations, over 10 years of observation. Our dependent variable is ROE from net income (%), our independent variable is R&D spending-operating revenue ratio (%). We perform a panel regression.

[6] This a preliminary testing process and a wider model is currently under progress.

We obtain a positive and significant coefficient of 0.640 (95% confidence interval, p value <0.05), meaning that resilience proxied with R&D spending-operating revenues ratio is a strong predictor of performance. The coefficient indicates that as the value of the R&D spending ratio increases, the mean of the ROE also tends to increase, such that a one-unit shift in R&D spending ratio (while holding other variables in the model constant) increases the average ROE from net income by 0.6%.

In our sample, we also compare the regression results of GAFA companies to energy companies. Unsurprisingly, GAFA companies (Amazon, Apple, Alphabet & Samsung) outperform and their sustained and progressive R&D investments over the last years have a strong predictive impact on their future performance. In contrast, energy companies are lagging behind. Does the amount of spending explain the gap? Not fully.

It would be simple to bridge the gap by increasing R&D spending. If needed, to strengthen resilience, the key is to make innovation a core strategic advantage sustained by a structural and unique innovative culture that continuously improves itself. When innovation substantially modifies one or several assets and processes with, for example, smart use of data, software or virtual sales and logistics interfaces that can be a core strategic capability and generate significant performance improvements. Tik Tok is overtaking competition thanks to a unique value proposition leveraged by powerful innovation such as the hybridization of video-sharing and social media. Tik Tok's ability to use AI in a smart and novel way very quickly, enables them to continuously refine their value proposition at the pace of users' preferences. Innovate and update is a virtuous loop to strengthen resilience and turn any disruption into a good opportunity.

This is the main difference between GAFA and energy industries. GAFA are in a close-to-oligopoly position thanks to their wide access to data that they exploit beyond monetization: their ability to transform and exploit data for high-level research (e.g Alphabet' Google X and Deep Mind) sustains their value proposition. GAFA products and services now appear as essential in the era of connectivity. Beyond active users and individuals, most businesses and utilities depend on them to function. Remember the panic caused by the Amazon Cloud (AWS) outage in December 2021, and who does not suffer from nomophobia?

Conclusion

Very often, disruptions act as external enablers for new innovations building new strategic capabilities and increased performance. One example is the strict regulation on video gaming in China on startups and entrepreneurial activities. A further example is how the firm Lego has reacted by announcing a future new range of products based on 3D modelling and new features to substitute video games. Other actors are pivoting their business model as witnessed during the COVID-19 pandemic (e.g. fabric companies developing smart masks) and the recent

Ukraine war with NFTs and crypto-trading companies featuring charity-based transactions. The Shanghai lockdown and increased components shortage have spurred a wave of partial vertical integration with, for instance, Apple developing micro-chips and new products free of components made of rare materials. Will energy companies leverage the Ukraine war to radically develop innovation and increase their resilience? Accrued concern for conservation of the planet coupled with high oil extraction price could be a favorable external enabler not only for energy companies but for the Earth as well.

The tragedy of the current crisis will hopefully serve as a trigger for companies to finally put resilience back at the heart of their strategy as well as at the top of their agenda.

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Brand Activism and geopolitical Crises

Laetitia Mimoun

ESCP Business School

Abstract

As consumers increasingly expect brands to take a stance on societal issues, managers need to decide how to react to geopolitical crises. Given the financial and political risks on the one hand and the reputational and branding risks on the other, brands face a dilemma regarding how to act. Based on an archival analysis of brands' reactions to the Russian-Ukrainian war and the recent academic literature on brand activism, this paper sets out different potential strategies to respond to such a dilemma.

Keywords: Branding, Brand activism, Geopolitical crisis, War, European Union

Why are brands increasingly taking a stance in geopolitical crises?

Historically, brands have often been considered as geopolitical actors, carriers of ideologies which they help disseminate to consumers (Holt & Cameron, 2010), thereby advancing the interests of their country of origin. For instance, scholars have analyzed the role of global U.S. brands such as Coca-Cola and McDonald's in supporting the "Americanization" of the world, the spread of U.S. culture and the neoliberal model, and, more generally, Western imperialism. Traditionally less at the forefront of media attention, brands as the reputational facets of corporations, also participate in geopolitical conflicts to support their financial interests, such as access to markets and resources. In the last couple of decades, the role of brands as geopolitical actors has become ever more explicit with the rise of brand activism.

Brand activism can be defined as a strategy that requires brands to position themselves as "moral actors promoting social, legal, business, economic, political, and environmental reform through their communication and practice" (Sibai, Mimoun, & Boukis, 2021, p. 1651). Brand activism has been associated with a variety of positive outcomes, such as favorable brand attitudes (Mukherjee & Althuizen, 2020) and price premiums (Sarkar & Kotler, 2018). In recent years, consumers have increasingly pressurized brands to take a stance on societal issues (e.g., sustainability, LGBTQ+ rights, fight against racism). As a result, some degree of activism and activist policies are no longer reserved for edgy, niche brands, but have spread to mainstream brands. Academic research has tried to elucidate how to practice brand activism, to delineate its outcomes, and to identify best practices (Mukherjee & Althuizen, 2020; Sarkar & Kotler, 2018; Sibai et al., 2021). While adopting an activist positioning can help differentiate the brand and generate brand loyalty and advocacy, it also carries the risk of a backlash that can damage brand equity and sales if the stance adopted is seen as opportunistic (e.g., in reaction to a brand crisis or weakness), inauthentic (e.g., accusations of greenwashing, pinkwashing, or wokewashing), or deviant (e.g., overly controversial and transgressive).

From a managerial perspective, it has thus become necessary for brands to carefully design strategies to decide on the type and scope of issues on which to take a stance, and the extent of their involvement in societal issues. When a geopolitical crisis arises, however, such as the recent and destructive war between Russia and Ukraine, brands suddenly come under heightened scrutiny from the media and public opinion. Thus, all the carefully thought-out strategies are disrupted as brands must decide quickly on whether and how to respond. We address this issue by analyzing news media data and brands' reactions to delineate different potential responses and their key trade-offs. The goal is to provide a managerial guide to the right questions to ask before deciding on a strategic response to such geopolitical crises.

How have brands reacted to the Russian-Ukrainian war?

While the conflict between Russia and Ukraine has been building up for several years, it escalated on February 24, 2022, when Russia moved forward with an extensive military invasion of Ukraine. Three months later, the crisis has yet to subside, with a death toll of around 13,300, the exodus of almost 4.7 million refugees, and extensive material damage (UNHCR, 2022). The geopolitical conflict involves the interests of many stakeholders, including the neighboring European Union, the U.S. through Ukraine's efforts to join NATO (one of the factors at the origin of the conflict), and China by way of its usual alignment with Russia among others.

With the escalation of the conflict, Western consumers began putting pressure on brands to take a stance, and in particular, to demonstrate their condemnation of Russia. By mid-March, European and U.S. news media not only reflected, but also strongly encouraged, this type of consumer reaction, building a public opinion consensus around the need for brands to cut all ties with Russia (Adams, 2022). By mid-April (i.e., at the time of our analysis), over 600 companies had reduced or ceased operations in Russia (Yales, 2022). Some brands reacted immediately and strongly (e.g., the Irish professional services group Accenture, withdrew very early on), while others tried to find an intermediate solution (e.g., U.S. FMCG company, P&G, reduced its product portfolio to necessities and suspended advertising and capital investments), bowed under pressure (e.g., U.S. fast-food chain McDonald's ended up temporarily closing its stores following the #BoycottMcDonalds campaign), found themselves unable to act (e.g., French hotel chain, Accor, is tied to its Russian activities due to long-duration franchising agreements), or chose not to react (e.g., French retail chain, Auchan, is conducting its business as usual in Russia).

One way to map out these reactions is to explore Yale Business School's "nice-and-naughty" list that classifies the top 1000 brands based on their reaction to the war. The list, which is regularly updated since February 28, has been deemed crucial in motivating companies to react given the extensive media coverage it gathered (Stewart, 2022). The list initially classified companies as ceasing their Russian activities or not, but soon had to move beyond this binary categorization. To add nuance to its analysis, it ended up classifying brands into six categories, from total inaction (a category labeled as "Defying Demands for Exit or Reduction of Activities") to the highest level of commitment (labeled "Clean Break - Surgical Removal, Resection"). What is highlighted by Yale's list is the variety of brands' responses, not only in nature but also over time (as an increasing number of brands decided to act under media and consumer pressure).

This refined categorization also reveals the complex stakes at play in brands' response to geopolitical conflicts. These include legal pressure (e.g., government sanctions on Russia for E.U. and U.S. brands), the cost of the response (e.g., the uncertain cost of the reputational impact vs. the certain loss of revenue if activities are terminated), the potential long-term implications (e.g., Russia promised future sanctions on brands that sanctioned the country), and the sector of activity (e.g., is it acceptable to punish laypeople by depriving them of necessities such as food or hygiene products?). Since morality can be understood and justified from multiple worldviews, it can be complex to delineate which brand actions truly have the higher moral ground (Sibai et al., 2021). For instance, from a "market" worldview, the cost analysis should predominate. In contrast, from a "fame" worldview, the reputational analysis should be decisive, while a "civic" worldview requires an evaluation of how the brand's actions will contribute to collective interests and well-being. What this means is that seemingly consensual media reporting hides a far more complex decision-making process, but also the possibility to justify different paths of actions when framed in the right way.

Conclusion

In conclusion, opting for a brand response to a geopolitical crisis involves a complex decision-making process. This process should be understood as a strategic decision that relies on a good grasp of the brand positioning in relation to societal issues. It requires an analysis of:

- *The brands' identity, values, and mission*: To what extent is societal commitment central to the brand positioning and practices? What is the scope of the brand's activist activities? How has this evolved over time (e.g., stable/increasing, broadening/narrowing)?
- *The target consumers' values and motivations*: To what extent is societal commitment important to target consumers? To what degree does consumers' societal commitment translate into their purchases?
- *The competitive environment*: What are the industry standards in terms of societal commitment? How is the brand situated in relation to its closest competitors?

In other words, the brand needs to decide how it wants to be positioned in relation to its resources and capacities, in answer to consumers' motivations, and in comparison to its competitors. The following table presents some possible reaction pathways determined by the positioning adopted by the brand.

Positioning	**Definition**	**Tradeoff**	**Timing of reaction**	**Scope of reaction**
Activist brand	Proactively takes action on a wide range of societal issues, with consistent communication and policies throughout its value chain	Finds a balance between activism and deviance: the brand can court controversy but should not fall into transgression	Proactive – first actions announced within 24h	Extreme (e.g. cut all ties with invading country)
Enlightened brand	Takes action when issues are closely related to its main sector of activities	Identifies the scope of the crisis to determine the brand's reaction and timing	Between proactive and bandwagon timing depending on the sector of activity, the type of crisis, etc.	Between extreme and light measures depending on the sector of activity, the type of crisis, etc.
Mainstream brand	Limits its actions to corporate social responsibility	Finds the right time to act after enough momentum has built up, but before media/consumer condemnation for inaction	Bandwagon approach – acts once a consensus has been built	Light (e.g., condemning communication, charity work, risk mitigation)
Non-socially engaged brand	Limits its societal actions to the legal requirements	Protects short-term economic interests, but risks long-term damage to brand equity	Wait-and-see	Business-as-usual

In our contemporary world in which brands are faced with strong pressure to react swiftly to societal issues, it is crucial to plan the scope and timing of such reactions in advance as delayed responses to crises carry significant risks to brand equity.

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War, Peace & Business

Maxime Lefebvre*

ESCP Business School

Abstract

In contrast to the globalization trend which followed the Cold War, the World today is rediscovering wars and conflicts between nations. Companies and private actors have to cope with this new reality linked to the growing rivalry between the West on the one side, Russia and China on the other. The relationship between public affairs and the private sector, between geopolitics and business, becomes more and more relevant. The necessity to study and understand more accurately and in a more integrated way such interactions will be central to the new ESCP Master of Science called 'International Business & Diplomacy'.

Keywords: Business Geopolitics Globalization International Relations

* Affiliate Professor, ESCP Business School

Trade and Business are a matter of Peace. “Sweet Trade” (“doux commerce”) has even been conceptualized as a factor of peace in Montesquieu’s view in the 18th Century. Today, as the World rediscovers wars and conflicts, Business has to cope with a new reality.

Why Geopolitics matters more and more to Business

After the end of the Cold War, Francis Fukuyama developed the famous thesis of ‘the End of History’, according to which the World would be ruled by the principles of democracy and market economy. This paved the way for the process of globalization, encompassing trade liberalization, new international organizations such as the World Trade Organization (WTO), the dazzling development of exchanges of information, goods, services, capital and people, and the multiplication of global companies treating the World as a single market. The World became flat, as the journalist Thomas Friedman wrote in a bestseller (2005).

However the post-Cold War World never lived up to the expectations of peaceful globalization. States’ security strategies emphasized new threats such as the proliferation of weapons of mass destruction or terrorism. Western interventions in the Yugoslavian wars, the long lasting US interventions in Iraq and Afghanistan, and in a more limited way the French interventions in Africa, exemplified the new security situation where the competition between great powers was replaced by asymmetric conflicts in ‘uncivilized’ zones. But in 1998, 3 years before China joined the WTO and accelerated its economic development, India and Pakistan let several nuclear devices explode and officially became nuclear powers. In the same year, the curb on world military expenditure stopped its post-Cold War decline with a steady expansion starting, growing from 1000 to 2000 bn $ in less than 25 years, today reaching almost 3 % of the World’s GDP.

In retrospect, post-Cold War globalization appeared to be a product of the ‘hegemonic stability’ (Kindleberger, 1973) provided by US strategic dominance. The French Foreign Minister Hubert Védrine even characterized the US as a ‘hyperpower’ in the 1990s. The US was approaching 50 % of the World’s military expenditure under G. W. Bush’s Administration, and still today represents 35 % of it (against a little more than 10 % for China). Thanks to its economic, technological, military and diplomatic superiority the US still dominates the seas, airspace, outer space and cyberspace.

Things are changing at present due to several factors:

- The economic and geopolitical competition between the US and China, characterized by Graham Allison as the Thucydides’s trap (2015), is shaping new international relations. China under the rule of Xi Jinping aims at becoming the World’s leading power by 2049 at the latest, for the 100th anniversary of the proclamation of the People’s Republic of China. The US doesn’t wish to be overtaken by a China ruled by the Chinese Communist Party, which would threaten the international liberal order it has been building since 1945. This is a bipartisan consensus in Washington and there is no difference between the Trump and the Biden Administration in that regard.

- Russia is not such a challenger for the US dominance, but is a longstanding geopolitical and ideological rival from Washington's point of view. The current conflict in Ukraine crowns growing competition which started with Vladimir Putin's accession to power in the year 2000. The European strategic theater seems to have become secondary compared to the Asian-Pacific one but both are interrrelated: by reinvigorating NATO against Russia's aggressive policy, the US (the Biden Administration) has also bound together in a much stronger way the democratic Western coalition's stand against authoritarian (non democratic) regimes which favor nationalist and conservative values in trying to revise the existing international order, that is to say, Western dominance.

For Business this has several and considerable consequences. The process of 'hyperglobalization' had already stalled after the World economic crisis of 2008. Contrary to some economists' predictions, such as Pascal Lamy, claiming that the value chains would become more and more internationalized, world trade has not grown any faster than economic growth. The Covid-19 pandemic as well as geopolitical tensions and environmental pressure (e. g. the need to replace fossil fuels by nuclear and renewable energy), have led to a relocation of production. Look at how the European Union, traditionally sticking to the principle of free trade, has launched the concept of 'open strategic autonomy' in the context of the pandemic (2020). The US for its part has started a strategy of 'deglobalizing' China and Russia, even though Western countries can no longer claim a monopoly of globalization for themselves. We can assume that this shift is preparing us for a new kind of Cold War.

How do Geopolitics and Business interact?

Companies primarily see their international activities in terms of business opportunities. They also need to address the competition with other firms in a global context. For example, German car companies became global leaders because they played out the development of their business in the fast-growing markets of China. Volkswagen, the global leader in car production before the pandemic, has almost 40 % of its cars sold in China. The shift in the geopolitical context is particularly challenging for a country like Germany, which invested a lot in the development of economic relations with China and Russia.

During globalization in calmer weather, as it developed during the 1990s and 2000s, governments had to encourage and support their companies willing to conquer world markets. They promoted exports and tried to achieve major contracts through economic diplomacy. They wanted to attract foreign investment. They developed 'economic intelligence'. They cooperated with other governments in order to improve the regulation of globalization. Geoeconomics was a concept coined by Edward Luttwak (1990) to characterize the new forms of economic competition between States and nations at the time of peaceful globalization.

But the role of the State has been transformed in the aftermath of several international crises. States were the main actors responding to sanitary and economic crises triggered by the COVID pandemic. The growing importance of environment and climate change forces Business to adapt to such ecological and energy transitions, to comply with new regulations, to look after their ecological reputation ('environmental and social responsibility'). Companies have also to adapt to the new geopolitical context. This was always the case in sectors such as the defence industry, which is very much dependent on public purchasing at home and arms sales abroad, and the expansion of military expenditure has boosted the production and export of weapons overall. A country like France, which was the 3rd largest arms-supplier in the World from 2016 to 2020, has always been a strong actor in this market. But also in other sectors such as space, health, energy, digital economy, electronics, raw materials, food products - which are all sectors covered by the EU's concept of 'open strategic autonomy' - there is a growing combination between the public and the private actors. Look at how Europe and the US are presently boosting the production of chips or batteries to reduce such a dangerous dependency in those fields.

There are other public policy tools which create constraints for companies in this context. Export control is one of them. Most notably it always existed for arms exports. For example France restricted its arms sales to Turkey after the political crisis with this country in 2019. Foreign investment is another area. The EU has adopted legislation to establish common control on foreign investments (2019), although many member states already had such control at the national level. Sanctions are a third example. They were already being used against countries such as Iraq, Iran, North Korea, or countries and movements supporting terrorism. China is subject to an arms embargo by the US and the EU since its repression of Tiananmen in 1989. Russia has also been sanctioned by the West since its aggression on Ukraine in 2014 and these sanctions have been strengthened after her direct attack in 2022. Companies have to comply with these sanctions and some of them have even decided to totally leave the Russian market.

With the war in Ukraine we are experiencing a kind of 'War economy'. Russia has been hit hard by Western sanctions which are close to a total embargo (except for the supply of Russian gas which still accounts for 20 % of the European gas consumption). It will have to rely on its domestic forces and to diversify its economic relationship towards China and the rest of the World (which generally doesn't apply Western sanctions). For their part, the West and the rest of the World are also suffering the consequences of the war in Ukraine through inflation, shortages, and possibly an economic recession.

But Business does not only undergo the law of politics, it can also be an influencer if it is able to organize itself and to formulate its own requests, in particular by practicing an adequate corporate diplomacy. I will give two concrete examples, one from the past and a more recent one. During the 1970s, as the East-West 'Détente' was becoming crucial, economic relations in agriculture, industry or energy expanded rapidly between Western and communist countries and multinational enterprises became major stakeholders of them. Economic cooperation was indeed one of the three 'baskets' of the Conference on the Security and Cooperation in Europe (CSCE). More recently, the designation of China as a 'systemic rival' was proposed by the German BDI (*Bund der Deutschen Industrie*) before being taken up by the European Commission in its communication about China in March 2019, and by NATO in 2021 which designated her as a ‘systemic challenge’.

Conclusion

The relationship between Geopolitics and Business is likely to take on more and more significance in the future. That is why ESCP has decided to reinforce its courses on Public Affairs and International Relations. In particular, it has decided to launch a new Master of Science dedicated to International Business & Diplomacy starting in the Academic Year 2022-2023. This is quite unique within the higher education market. While many Schools and Universities offer either Master Degrees in Diplomacy or International Relations or International Business, they do not offer a combination of all these fields. The MSc ‘International Business & Diplomacy’ will offer courses on international Business (international finance, international strategy, international consulting, corporate globalization, corporate diplomacy, intercultural management, negotiation, lobbying, the importance of law) while also offering Geopolitics, Diplomacy and economic Diplomacy, economic intelligence, international organizations, Globalization, ecological transition, international taxation, public and development policies, the role of civil society and NGOs. Indeed, the necessity to study and understand these fields in an integrated way is more relevant than ever.

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AI as a new geopolitical battleground: What are we competing for?

Hao Zhong

ESCP Business School

Abstract

This impact paper seeks to highlight and discuss the intrinsic relationship between the development of the artificial intelligence (AI) industry and geopolitics. We point to the disparities in AI technology advancement across nations and focus on four aspects of their competition: talent, data, chips, and energy consumption. The United States continues to lead in AI technology and talent acquisition. China comes second with its vast market advantage and massive quantity of available data. Europe unfortunately lags behind but is at the forefront of data and individual privacy protection. Many other nations are indispensable contributors to the global supply chain of AI chip manufacturing. Nonetheless, all governments should think about the overconsumption of energy caused by AI development and the need to devote collective effort to address this urgent issue.

Keywords: Artificial intelligence, geopolitics, AI talent, specialized AI chips, energy consumption

AI as a new geopolitical battleground: What are we competing for?

Stuart Russell, a professor at the University of California, Berkeley and co-author of the textbook *Artificial Intelligence: A Modern Approach,* defined artificial Intelligence (AI) as "the study of methods for making computers behave intelligently". AI technologies include machine learning, computer vision, intelligent robotics, biometrics, swarm intelligence, virtual agents, and natural language processing (Miailhe, 2018). Recent big data technologies and high-performance computing breakthroughs have significantly boosted the development of AI, which is becoming a key national strategy and security topic. As Elon Musk, the founder of SpaceX and Tesla, recently tweeted, "Competition for AI superiority at national level is the most likely cause of WW3."

With regards to the development of artificial intelligence, the US and China are unquestionably in leading positions with significant competitive advantages. The US has cutting-edge hardware, research and talent, while China pertains a vast market and massive AI-ready data that are driving its technological development (Engagemedia, 2022). Being in a "catch and surpass" position, China has ambitiously integrated the digital and AI technologies into its geopolitical strategy (Engagemedia, 2022). The Digital Silk Road (DSR), a key aspect of the Belt and Road Initiative (BRI), had garnered approximately US$79 billion in investments as of 2019 (Engagemedia, 2022).

Europe, another major player, is lagging behind the US and China in terms of technological advancement. European AI companies are valued at less than $1 billion, while GAFA (the US tech giants: Google, Apple, Facebook, and Amazon) will soon be worth $1 trillion each (Miailhe, 2018). Nonetheless, Europe has discovered its own AI model: an imperative quest for AI power with primary concern over personal privacy and data protection (e.g., the release of the General Data Protection Regulation (GDPR)). A heated debate is now underway about whether such regulations could hamper its own rise to power.

Africa is currently a "Blue Ocean" for AI. Several leading countries in AI technology (notably China) are making significant investment in Africa to develop a competitive edge, with multiple examples of Chinese industrial presence: Transsion Holdings became the first smartphone company in Africa in 2017; ZTE provides infrastructure for the Ethiopian government; CloudWalk Technology will work on facial recognition under an agreement with the Zimbabwean government (Miailhe, 2018).

AI talent war

Any country that strives to become a global AI leader must invest in talent. In fact, talent is the first and foremost resource that competing nations use to hold the AI front line. The US is by far the clear winner in this talent war. Its AI talent pool contains over 78,000 AI researchers, while China has approximately half that number at 39,000 (Miailhe, 2018). Assuming the US has 100% AI talent penetration, China ranks second with about 92%, followed by India, Israel, and Germany with 84%, 54%, and 45%[7].

The Global AI Talent Report by Jean-François Gagné (Gagné, 2020) categorizes nations into four classes based on their inflow and outflow of AI talent: i.e., producer countries, anchored countries, platform countries, and inviting countries. Examples of *producer countries* are India, Singapore, and Israel, where we see less inflow and more outflow. Japan, Belgium, and Russia are what we call *anchored countries*. They have less talent inflow and less talent outflow, which signals the relative stability of their talent pools, but perhaps also a risky insularity. *Platform countries* are those with high inflow and outflow, which are best exemplified by the U.K., China, and Canada. Lastly, the US, France, and Portugal are called *inviting countries* with more inflow than outflow, indicating that they are relatively more successful at both retaining their existing talent and drawing in talent from other ecosystems (Gagné, 2020).

One major strategy to attract AI talent from other ecosystems is through attractive and motivating immigration policies. The United States' internationally recognized education institutions, innovative industries, top-tier research laboratories, and relatively liberal immigration policies, have attracted large numbers of AI talent from across the globe, and it now leads the world in AI technological innovation (Huang, 2020). Over the past five years, the UK, Canada, France, and Australia have adopted significant immigration reforms to attract talent in AI and other technical fields. Canada has devised new immigration policies to bring in skilled migrants and integrate graduates into its workforce. The UK proposed similar reforms to expedite the immigration process for technically-skilled migrants (Huang, 2020). There is no doubt that the talent war between countries seeking a competitive advantage in AI will continue.

Data as the fuel powering AI

In the era of AI, data are as crucial as (if not more important than) talent. As the new fuel powering AI, unlike the common functionality of fuel, data is not ready for direct use until they have been properly organized, processed, cleaned, and analyzed. And data are more valuable when they are linked to more relevant and heterogeneous sources. Like wind or solar energy, data can be used in multiple forms to serve more than one purpose. Data may find their atypical use and value when new analytical technologies become available. As an example, people barely knew how to make use of ubiquitous online pictures and photos until computer vision and deep-learning techniques reached the mainstream.

Historically, geopolitics were mainly governed by oil and natural gas, and most private sector organizations had little impact on the global economy. In modern society, tech giants are geopolitical players and have become de facto global stakeholders (Paganini, 2021). The biggest tech giants in the US, for example, include GAFAMI (Google, Apple, Facebook, Amazon, Microsoft, and IBM), while in China, the main tech companies are BHATX (Baidu, Huawei, Alibaba, Tencent, and Xiaomi). Owing to less stringent data regulations in the US and China, these companies can collect and analyze massive amounts of data to profile and better

[7] https://albertchristopherr.medium.com/ai-talent-pool-in-2019-past-present-future-30bcd8162744

understand their users, and subsequently provide personalized products, services, and experiences at the right time (Miailhe, 2018). European officials, on the other hand, place high hopes on data regulation, including the GDPR regime and data localization. However, putting its faith in data regulation may leave the EU lagging even further behind the US and China in the global geopolitical AI battle (Tabansky, 2021).

Specialized AI chips

Apart from talent and data, chips also play an indispensable role in developing AI competitiveness. Depending on the chip type, the market can be categorized into GPU, ASIC, FPGA, CPU, and others. Modern specialized "AI chips" are essential for deploying AI at scale. Developing AI applications using general-purpose or older AI chips may be tens to thousands times more expensive in both processing time and financial cost (Khan, 2020).

In several semiconductor industry sectors, the United States and its allies have a competitive edge in the production of specialized AI chips as they dominate the design of such chips, which includes electronic design automation (EDA) software. Chinese AI chip design firms are still behind and reliant on US EDA software (Khan, 2020). However, it is believed that China will soon move forward with the help of significant government-backed investments, a large engineering pool, and dozens of semiconductor fabs under construction or on the books (Ernst, 2020).

The European Union is unfortunately falling behind in the competition for AI chips. During the 1990s, Europe held more than 40% of the chip market. By the early 2000s, however, this figure had fallen to 24% and is barely 10% today[8]. It is still questionable whether the EU will be able to fund a multi-billion Chips Act, given that European member states' budgets are already overstretched. Meanwhile, private investors might not see Europe as an appealing place for investment.

In fact, it is exceedingly challenging for the two superpowers (the US and China) to maintain a full supply chain on their own. The United States is dominant in sectors like intellectual property, chip design, manufacturing, and non-wafer materials, while China is the largest supplier of raw materials like the silicon needed for manufacturing. But they are both strongly reliant on South Korea, Japan, and Taiwan in contract manufacturing and other fields[9]. Thus, geopolitics and AI chip manufacturing are likely to remain in an enduring relationship in the foreseeable future.

Energy consumption and decarbonization

Demand for computing power is rapidly increasing with the rise of artificial intelligence and machine learning. A feedback loop is observable between AI and computing power: additional computing power nurtures new AI and facilitates AI advances, while AI optimization necessitates more computing power[10]. To illustrate AI's shocking energy consumption, we take an example of AI model training.

[8] https://www.euronews.com/2022/02/11/for-the-eu-microchips-and-geopolitics-are-two-sides-of-the-same-coin-view

[9] https://www.csis.org/blogs/strategic-technologies-blog/chip-shortages-light-geopolitics-and-climate-change

[10] https://redanalysis.org/2018/06/25/artificial-intelligence-computing-power-geopolitics-2/

OpenAI (an advanced AI company) trains its GPT-3 model on 45 terabytes of data. To train the final version of MegatronLM (a language model similar to, but smaller than, GPT-3), Nvidia ran 512 V100 GPUs over nine days. Given that a single V100 GPU can consume at least 250 watts, 512 such GPUs consume a total of 128,000 watts, or 128 kilowatts (kW). Running for nine days means that training the MegatronLM costs 27,648 kilowatt hours (kWh). Given that the average household in the US uses 10,649 kWh a year, MegatronLM's training consumes almost three times the amount of a single household's annual energy use (Labbe, 2021).

Energy consumption results in CO2 emissions, which aggravate the global issue of climate change. The Paris Agreement urges governments to drastically cut carbon and other greenhouse gas (GHG) emissions over the next few decades. However, the decarbonization process has an inevitable impact on a nation's economic growth, domestic, and foreign policy, and hence has significant geopolitical implications. It is imperative for nations and regions to work together to support decarbonization processes beyond their own borders (Dennis, 2020).

Conclusion

The artificial intelligence industry exhibits disparate development worldwide. This impact paper discusses the intrinsic relationship between AI and geopolitics from four main perspectives: talent, data, chips, and energy consumption. The United States continues to dominate in AI technology and has a clear advantage in AI talent. With its vast market and massive consumer data to power AI, China is catching up and is emerging as a strong rival. Europe has put more emphasis on data and individual privacy protection and, in the meantime, strives to advance its AI technology. Other nations and regions also play an indispensable role in the supply chain of AI chip manufacturing. Nonetheless, no government can overlook the potential energy overconsumption and greenhouse gas emission issues, and all need to work together to develop a healthy and sustainable AI ecosystem.

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Why are leaders not taking political risks seriously enough despite a turbulent international business environment and geopolitical instability?

Frédéric Jallat

Lorenzo Coronati*

ESCP Business School

Abstract

World leaders (CEOs, policy makers and more broadly anyone who oversees a process of social influence to maximize the efforts of other stakeholders for a given purpose) make important decisions, whether to address a new international development process, to enter new markets or to define new investment projects abroad which can have a considerable impact on the company.

In our current highly volatile environment, every decision involves some degree of political risk, a still widely debated concept which, together with new insights from behavioural economics, has recently underpinned new developments in the fields of political decision-making and of uncertainty.

Despite their importance and potential negative consequences, empirical studies and research in political or business disciplines show that leaders tend to *ignore political risk*, often assimilating it with the context of simple uncertainty, and the vast majority of decision-makers *do not integrate in-depth and meticulous political analyses* into their overall risk management and international assessment process (World Bank Group, 2014).

The centrality of the issue related to profitable commercial and socio-political decisions is not sufficiently reflected in the management literature to date or in current reflections on organisational behaviour.

There is an obvious gap between international business, behavioural theories, and current practice that we attempt to analyse and explain here.

Research and practice have yet to articulate what political risk is, its probability dimensions, and its implications for decision-making in international business development. Nevertheless, developing the capacity and the mental habit of evaluating and responding to multiple (political) risks in a prospective international approach is a key skill for managers and essential to the long-term profitability of the activities for which they are responsible.

Our article attempts to understand why high-level personalities find it difficult to anticipate political risks in their professional capacity when taking short-term decisions that are often vital for their organisations or that can have a significant human or financial impact.

Keywords: Political risk, Decision-making, Organisational behaviour, Risk management

* Global Executive PhD, ESCP Business School

Why are leaders not taking political risks seriously enough despite a turbulent international business environment and geopolitical instability?

Introduction

McKinsey - annually collecting responses from almost 2,000 executives representing the full range of countries, industries, company sizes, and functional specialties - identified geopolitical instability as a major threat to economic growth and international prosperity.

Despite the fact that both the pandemic and inflation are now considered top risks to economic growth in the next 12 months, geopolitical instability and political conflict still remain major concerns among experts, executives, and political decision-makers.

In every region and despite major issues like the COVID-19 pandemic, inflation, supply-chain disruptions, and labour shortages, a possible international conflict - perceived as a major source of severely damaging disruption to global prosperity - is still considered a top risk by between 15% and almost 30% of respondents and experts from around the world (McKinsey, 2021).

In the same vein, experts interviewed at the Davos Forum 2022 considered geopolitical risk as one of the main factors threatening the global economy (World Economic Forum, 2022).

Even climate actions taken to combat global warming, currently perceived as the most critical threat to the world, may have deleterious and significant consequences on international (in)stability and social unrest: “As carbon-intense industries employ millions of workers, their rapid termination could trigger economic volatility and increase societal and geopolitical tensions. Up to 8.5 million jobs in the energy sector (almost 30%) could be lost in fossil fuels and nuclear energy by 2050” (IRENA, 2020).

In the same way but on a more micro-level, major international companies like Renault or McDonald’s who have *rediscovered war* since the start of the Russian offensive in Ukraine, said they will sell their business operations in Russia.
In May 2022, Renault decided to close its plant near the Russian capital, despite Russia being Renault's second largest market after Western Europe, with nearly 500,000 vehicles sold in 2021. The company's presence in the country has been called into question, however, since the start of the Russian offensive in Ukraine. Before the final closure of its Russian operations, the automotive group was also facing logistical problems due to a shortage of imported components caused by Western sanctions, halting most of its production in April (Capital, 2022).

McDonald’s, which has a 32-year history in Russia, with over 800 restaurants and 62,000 employees, said its “continued ownership of the business in Russia is no longer tenable, nor is it consistent with the company’s values” (CNBC, 2022).

These preliminary considerations clearly show that anticipating and understanding political risk may be key to many successful international projects, be they in the private or the public sector.
As is clearly illustrated in the current context, and despite its importance, many corporations actively spend a great deal of time managing credit, markets, talent, and operational risks, but spend just a limited amount of their time and resources in dealing with political risks in areas where it is nevertheless critical to anticipate, identify, and manage them. Many decision-makers tend to ignore political risk until it leads to a crisis for their organisation, subsequently reducing operational efficiency and turnover (Rice & Zegart, 2018).
Our paper attempts to understand why high-level personalities find it difficult to anticipate political risks in their professional activities when taking short-term decisions that are often vital for their organisations or that can have a significant human or financial impact.

Concept clarification

The first endogenous problem is that the specific feature of a multifaceted element as a political risk (in contrast to the general topic of risk or uncertainty) is not widely communicated or addressed. Therefore, what is a political risk in our globalised world today and how can we improve the process that inhibits its proper evaluation?

In a nutshell, political risk determines an uncertainty that matters because it positively or negatively affects something. From this general definition, it is clear that formulation of a standard classification of political risk is still ongoing, and a homogeneous consensus on the precise meaning of the term in management (but also in other disciplines such as socio-political science or economics) has not as yet been reached.

In this sense, the definitions of political risk fluctuate widely between general descriptions, which suggest that political risks are all "non-business" risks (Truitt, 1974), and the more specific ones that embody political risks as a function of some external elements that negatively impact operations (Robock, 1971; Kobrin, 1979) or the specific area or segment of the company related to the business environment (Fitzpatrick, 1983; Beazer & Blake, 2018).

We believe that political risk is a multifaceted and constantly evolving concept that leaders in organisations try to explore before implementing international business development. There is no doubt that political risk and its critical management across companies is a modular process, also subject to leaders' behavioural approaches, in particular when corporations that intend to launch a business either internationally or locally need to assess developments to determine whether there is a substantial political risk which could jeopardise their investment and reduce their profit (Pahud de Mortanges & Allers, 1996).

Rice and Zegart made the most recent theoretical delineation and practical classification of political risks in their 2018 study, defining such risks as pervasive. The former US Secretary of State and her co-author describe it from the angle of its direct impact on firms, stressing the temporal actualisation of the phenomenon that can be unleashed by a wide range of actors and organisations. The more economic or social impact the occurrence inflicts, the more relevant it is for the authors. This modern definition is interesting as it goes beyond the old characterisation of political risk that was widespread in the last century. They argue that the phenomenon is not dependent on the government's actions alone, but is triggered by several (even minimal) factors.

Recent studies that focus more on the behavioural aspects and shift the level of theory from the firm to the actors highlight the clear distinction between the concepts of (political) risk and uncertainty. These analyses contend that a theoretical delimitation of the two concepts can be made by specifically stressing the importance of the underlying sources and mechanisms that trigger the effect of imponderable adverse consequences (Benischke, Guldiken, doh, Martin, Zhang, 2021).

It is evident that modern definitions must consider the (quantizable or not) probability that any indistinctly political act or action generated by any (even single and remote) actor can affect assets and business. This new broader clarification highlights the growing role of new technologies and young users (internet and social media have produced several textbook cases of inefficient risk management) as powerful triggers. Today, we can argue that political risk derives its full definition as a function of a practical disciplinary perspective rather than an objective and uncontroversial statement (Rice & Zegart, 2018; Jarvis, 2008) on managerial efficiency.

Political risk and the decision-making process

The target of this paper is to focus not so much on how the definition of political risk or political uncertainty can be correlated to its social or business function, but rather to identify the relationships that emerge from the process of understanding political risk as a variable that can influence decision-making in the approach to international development.

Two assumptions must be clarified from the outset, however. The first is that the decisions considered are only those crucial and rare selective choices that leaders make when running an organisation, decisions that have an organisational, financial, and operational impact on the entity's activity when exploiting the international market. The second is about the decision-making process, which is always expected to be dynamic, is frequently subjective and mobile, and involves perpetual learning. Decisions unfold and produce consequences over time, with information (because of the often imperfect context that leads to political uncertainty – Knight, 1921) becoming known at different rates and times as decisions are made in uncertain and frequently changing environments, like the geopolitical landscape and business environments. A better prediction of any potential changes in the social or political environment can lead to improved decision-making, enhancing corporate savings and decreasing the costs associated with each issue that could involve harmful risk.

We analysed several case studies associated with academic articles as a comparative method to extrapolate some useful insights. This approach was valuable as the business case literature provides a rich source of material that is suitable for collecting data and its analyses.

Following this approach, we found some intuitions about the delusion of some decision processes made by leaders that tried to anticipate, identify, analyse, and react to political risk occurrences.

In particular, we identified two main kinds of reason why leaders fail to respond to political risks in reasonable time. One is more emotional and irrational, involving systematic deviation from cognitive rationality in people's judgment and decision-making – these latter designated by psychologists and academics as heuristics and biases – or when a specific leader's interests affect the decision process (Benischke, Guldiken, Doh, Martin, Zhang, 2021), playing a crucial role in risk recognition during the strategic approach to the international business environment. The other is triggered more by the ambiguity of the political risk construct as an exogenous and extraneous element during the life of a company, making the phenomenon almost elusive and intangible.

Heuristics and biases

The definition of heuristics is widely acknowledged in science. Heuristics are clear mental shortcuts that can facilitate decision-making and probability judgments but can lead to severe errors caused by irrational and inaccurate conclusions.

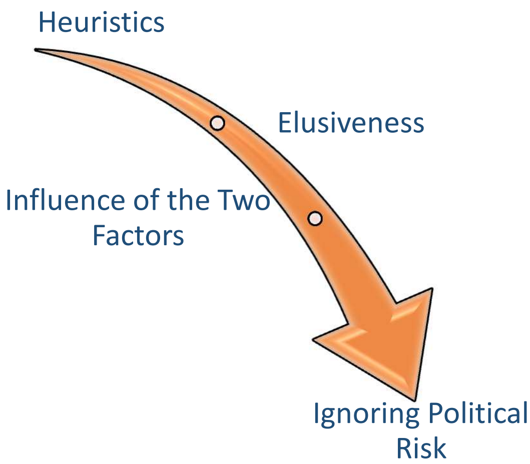
Daniel Kahneman (a Nobel prize behavioural economist) and his colleague Amos Tversky identified three different types of heuristics (Tversky & Kahneman, 1974): 1) availability (memory-based judgements of frequency or probability), 2) representativeness (judgements of likelihood of instances belonging to a category), and 3) anchoring and adjustment (quantitative estimates on a unidimensional scale).

Leaders use each type of heuristic to reduce the mental effort needed to process thoughts and to decide under pressure. However, their use can lead to various cognitive biases and impair decisions when judging and predicting. Following these pivotal studies, Kahneman and Tversky developed prospect theory as a behavioural alternative to the expected utility theory. This theory found that individuals are cautious in their decision-making (which is usually risk-averse) when dealing with a profitable business (prospecting profits). However, they tend to accept the risk (risk acceptance) when threats challenge their comfort status (prospecting losses). They are far more likely to take risks to recoup previous losses or recover from a failure to revert to an earlier position. This finding can explain why development leaders have difficulty making some evaluations when contexts are intricate and unexploited. In addition, as behavioural research has shown (Benischke, Martin, Glaser, 2019; Wiseman & Gomez-Mejia, 1998), leaders can be influenced by self-interest when the concept of loss aversion is linked to equity wealth (at risk of loss) during the development of a strategic decision-making process for a specific investment abroad. The "perceived threat to the agent wealth", an insight postulated by the behavioural agent model (BAM), can shift a leader's choices from interest at organisation level to a more personal conservative level. The underlying purpose is to preserve and accumulate more equity wealth that can be at risk of loss in an international context when performance and salary are related to restricted stock. As such, leaders tend to use these techniques in the cognitive process to reduce the decision-making effort, and also because heuristics *per se* are not always wrong. They are mental simplifications that can generate positive results in some specific environments. However, even if by coincidence the conclusion is favourable, it is not achieved through logical mental resources or patterns. Heuristics may induce a leader's reasoning to avoid or ignore some information, while overestimating other information that might be extraneous. The ensuing decisions are drawn from a mental shortcut with no rationale and no logical pattern that can ensure they will work out.

It is the same story for biases, which can create challenges to successful decision-making in today's international contexts. Identifying biases such as confirmation bias, halo effect, status quo, optimism or desirability, and doing one's best to limit their perverse effects is key to dealing with (political) risks. Attenuating their influence, leaders have the ability to assess the world through new lenses that are unbiased by preconceptions. Leaders need to familiarise themselves with the structure of assumptions and psychological mechanisms that can increase errors in judgment, train their teams to identify them, and develop a decision-making process that will not impede the identification, evaluation, and mitigation of political risks in developing countries, unstable or even blurry environments.

We believe that leaders cannot select the option to exclude biases which can arise in several forms, ranging from a programmed formula of personal utility (i.e., putting their equity at risk of loss) to the unprogrammed methodology of cognitive distortions. These biases are always present in every mindset of human beings. The good thing is that leaders can try to control them. They have to identify and learn from such preconceptions by limiting and correcting their impact on decision-making. In international markets today, a quick self-interest analysis may prompt leaders to make a baseless decision about a company's strategy management in developing areas, generating long-lasting and unexpected events and costs.

Understanding these pitfalls may contribute more awareness in decision-making (McCrystal, 2021).



Elusiveness of political risk

A second barrier to effective political risk management by leaders searching for international development is the difficulty in understanding the perils of an emerging political risk due to its subtle and unpredictable appearance in a globalised business world.

We have evidence that today's leaders are focused on short-term results (primarily when they oversee listed companies). From this perspective, their approach is as pragmatic and realistic as possible, aligning (quarterly) corporate targets with market expectations. This asymmetry between timing/targets and long-term planning creates a *vulnus* in the leader’s capacity for threat identification because political risk is, instead, something random, both temporally and logistically distant, and not readily programmable. It has an elusive form and an imponderable frequency timing. As Nassim Taleb clearly explains in his book *The Black Swan* (2008), it is almost impossible for leaders to process decisions with events that happen infrequently and without recognisable prodromic signals.

Episodes with a local distribution are unknown and are often unimaginable because the trigger might be unleashed in another part of the world. Take the famous case of Jack Welch during the acquisition of Honeywell International. The acquisition did not take place because Mario Monti decided to demonstrate the EU’s political independence from the United States. Monti, the Chief of European Antitrust, saw the problem from a different perspective: he wanted to protect EU competitors by avoiding the new corporation’s market dominance. Welch was so focused on the business and its revenues for the group that he failed to consider the geopolitical element as a factor affecting the business produced in other countries (after which Welch made the famous declaration: “you’re never too old to be surprised…”).

By definition, political risk concentrates on the simple (very often remote) probability of something concrete happening instead of the multiple reasoning methods by which it can be anticipated and managed. This modern fallacy is the tendency to judge political risk as a typical (single and unrelated) event or a clear, recognisable threat with an associated cost. It is not depicted by the objective reality that our globalised world represents, in which business is interconnected by multiple variables linked with a cause-effect feature on all five continents.

Thus, the main challenge for leaders is to formulate political risk assumptions as they are not always straightforward, rational, or well-founded. The mental process of managing these occurrences entails anticipating events and taking action to avoid additional cost. The problem lies in the fact that the detection of political risk is liable to be isolated in our minds, assuming that it may occur without any interaction or connection. Today this approach is a myth that can disrupt a business.

The decision process of spotting risks needs to be a gradual and collective mental process, which does not function automatically. It is essential to orchestrate the interactions and synergy of the elements informing the process. Leaders have to consider how risks are detected and perceived among units that are usually the closest elements to the dangers. Leaders should facilitate fast communication as a fundamental action able to incorporate all the information needed to lead to a good decision-making process. Since the risk is not unitary and consistent, leaders must recognise that they should not be prisoners of their personal perspectives. Even when they have the potential to gather specific information, the elusiveness of political risk remains because information can rarely eliminate the unexpected. Leaders cannot completely eliminate risk, but they can nurture and maintain a culture of resilience in their organisations.

Conclusion

In a globalised world, it is essential for successful leaders to effectively manage private companies or public institutions in order to incorporate a decision-making process that can identify and analyse political risks so as to mitigate the myriad potential risks, stepping up resource allocation in international environments. This process requires rethinking the decision-making approach to political risk and political uncertainty in an atypical way.

The use of data offers better tools to anticipate problems and analyse inefficiencies between entities, and leaders need to ensure that data analysis and decisions are merged for effective action.

We identified two related factors in our article that can help leaders to detect, assess, and respond to risks:

The first, stakeholders, boards, and C-suites, too often fail to understand the multifaceted design of political risk. They approach risk investigation as a traumatic stand-alone activity that should only be considered when the situation gets problematic and unexpected outcomes emerge. They perceive political risks as elusive, miscalculating the likelihood of their occurrence and failing to allow decision-makers to formulate mitigation strategies that can generate significant human resilience and business savings.

The second focal aspect that reduces the ability to spot risks is when decision-makers, motivated by personal or objective input, do not work hard and rationally enough to ensure that all elements of cognitive and heuristic biases will not lead to inefficiency. This means designing better communication strategies between overseas units while developing ways to encourage and reward potential long-term decision-makers who prepare for the unexpected, in particular establishing checks and controls to avoid self-serving behaviours.

Being aware of the mental constraints and biases that make it harder to recognise political risks enables leaders to mitigate and counter disruptive consequences, helping to prevent crises or at least to reduce their associated consequences and costs.

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Explaining the persistence of informal institutions: the role of informal networks

Dana Minbaeva
King's Business School, King's College London

Alena Ledeneva
University College London

Maral Muratbekova-Touron
ESCP Business School

Sven Horak
The Peter J. Tobin College of Business, St. John's University, New York

Abstract

The paper unpacks the "black box" of informal institutions and theorizes about the role of informal networks in channeling continuity and change in informal institutions. Specifically, we argue that when informal institutions are enacted by informal networks that are "relatively affective" and "relatively closed," their persistence is higher than the persistence of informal institutions that are enacted by "relatively open" and "relatively instrumental" networks.

Keywords: Informal institution, informal network, informality, network typology, institutional dynamic.

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Explaining the persistence of informal institutions: the role of informal networks

Introduction

It's been more than three decades since the Berlin Wall came down, and most transition economies have advanced in the development of their formal institutions and transparent, market economies. Yet in Kazakhstan, despite the trappings of a liberal economy, political appointments in the public sphere as well as recruitment and promotion in private companies still often comply with clan logic, or *rushyldyq* (Minbaeva & Muratbekova-Touron, 2013). The Chinese system of *guanxi*, a system of exchange of favors that emerged during the Maoist period to obtain scarce products, is still used to obtain business permits, jobs or purchase real estate (Yang, 2018).

Furthermore, even in established democracies with strong and effective formal institutions, some unwritten rules are still strong; for instance, in France informal practices such as *piston* (preferential treatment obtained through personal acquaintances) still coexist along formal recruitment and selection channels; traditional Confucian values still permeate South Korean society and lay the foundations for informal networks such as *yongo* and *inmaek* to flourish (Horak, Taube, Yang, & Restel, 2018), despite the country being one of the most advanced in the world, etc.

This begs the question: Why do informal institutions persist?

It is a part of the story that needs to be explored, because these informal codes of conduct have a pervasive influence. Indeed, informal institutions are defined as "a set of rules, compliance procedures and moral and ethical behavioral norms designed to constrain the behavior of individuals in the interests of maximizing the wealth or utility of the principals (North, 1990). As such, they are an integral part of the institutional framework that must be explicitly considered, for example, in international business strategy.

Unpacking the "black box" of informal institutions

In order to explain the persistence of informal institutions, we must unpack their relationship with formal institutions and understand the mechanisms at work in their interplay.

Overall, institutions, formal and informal, have been characterized as durable social structures that are relatively resistant to change. Across the disciplines, from sociology to international management, both types of institutions are viewed as dynamic in nature. We also find a common understanding that informal and formal institutions cannot be analyzed in isolation, but in relation to each other.

In fact, their relationship could be best described by borrowing a term from evolutionary biology: symbiosis ("living together" in Greek), a word usually employed to describe long-term interactions between two species, like ivy living on a tree or birds eating parasites off hippopotamuses' backs.
So how do formal and informal institutions live together?

The two dominant views of informal-formal symbiosis

Two approaches to defining informal institutions relative to formal institutions are widely established.

Advocates of the first approach take the general view that, in short, what is not formal is informal. For instance, political scientists often contrast unwritten, socially shared rules with those enforced through official channels such as state institutions (Azari & Smith, 2012). In that stream of literature, formal and informal institutions are seen as two ends of a continuum. In this case, institutional change starts with formal structures, and informal institutions follow because they act as "compensatory structures" to the former (Matten & Moon, 2003; Peng, 2003; Peng et al., 2009; World Bank, 2002). For example, they are expected to fill a void, with firms relying more on informal institutions if and when formal ones are lacking. Borrowing the evolutionary biology metaphor, this type of symbiotic relationship could be labeled "parasitic symbiosis" in the sense than one species benefits from the relationship while the other is harmed by it.

Advocates of the second approach follow a logic of formalization, i.e. "put informal first and formal will follow" (Baudrillard, 1987; de Soto, 1989; Gidden, 2013). The general idea is that informality is slowly absorbed into the institution-building process (Spiegel, 2005). One paradigmatic example of such "informality first" is offered by urban development studies. For instance, informal dwellings such as favelas in Brazil or slums in India start off as camps without sewage systems, running water or electricity; as these infrastructures are gradually brought in, the (originally) informal homes remain, because it is simply impossible to remove so many at once. Evolutionary biologists would call this type of relationship commensalistic: one of the species benefits (formal institutions) whereas the other is unaffected.

Beyond established approaches: introducing the role of informal networks

Despite the quality of these two approaches, we argue that there could be a third alternative in which formal and informal institutions benefit from each other. This third type of symbiotic relationship is called "mutualistic symbiosis". We suggest that coexistence does not indicate competing logics, nor can we determine whether formal or informal institutions came first.

Instead, we view the interplay between both through the prism of informal networks upon which informal institutions rest. We define this interplay as dynamic changes in social structures and social practices in response to changes in their formal and informal use, channeled through the informal networks upon which informal institutions rest.

We prefer the term “informal network” over “social network”, as it better conveys the tension with formal settings and the ambivalence in the use of personal networks to get things done. An informal network can be defined as culturally embedded channels formed by informal dyadic ties between individual actors; it draws its cohesion from peer pressure.

The social practices and structures produced by the interactions among actors act as touchpoints with formal and informal institutions. Specifically, through social interactions, individuals develop a shared meaning of the “rules of the game” (Geertz's “local knowledge”, Polanyi's “tacit knowledge”); as a result, when faced with a problem, individual actors rely on commonly accepted practices like *jeitinho brasileiro*. This technique of problem solving, which utilizes emotional ties between Brazilians, is just one example of a social practice that may work so efficiently as to potentially undermine the workings of formal institutions. In other words, informal networks have effects at the behavioral and structural level.

The ambivalence of informal networks as society's “plumbing”

Let's return to our key question: Why do informal institutions persist in the face of formal institutions?
In line with our definition of the interplay between both types of institutions, we argue that informal institutions persist because of their ability to change and adapt in the face of mature formal institutions, while enduring internal consistency, continuation and legitimacy (Deephouse & Suchman, 2008). This unique ability of informal institutions to remain stable and be flexible at the same time is enabled by the dual functionality of the informal networks upon which they rest.

It is all the more important to understand the complexity and the role of informal networks in channeling continuity and change in informal institutions as firms operating in foreign environments deal with informal institutions on a daily basis, whether they are aware of this or not.

Networks perform a dual function that originates from their “plumbing” role (Podolny, 2001). They are the channels through which “market stuff” – information, goods, services, payments – flow in market economies; when informal, networks channel mutual help, favors, and other emotional currencies, so to speak, that create competitive advantage, itself inalienable from the relationships that keep the informal networks together (Ledeneva, 1998; 2018).

Informal networks thus play a dual role: transmission and transformational. They both channel and adapt to changes brought about by informal institutions and guard the continuity of informal institutions. At the nexus between the behavioral and structural levels, informal networks create positive feedback loops, in autocatalysis mode (Padgett & Powell, 2012: 8). Indeed, as Owen-Smith and Powell (2008: 618) suggest, networks are “essential to institutional fields because they are both the pipes" through which the institutional flows circulate, while the networks "are the prisms" that individual network actors use to make sense of their actions.

An example illustrates this dual role of informal networks: in South Korea, *yongo* are networks based on blood ties, region of origin or university (Horak, 2014); they adhere to Confucian ideals of seniority and hierarchy, whereby women have historically been treated as secondary to men. Although formal legislation has been introduced in support of gender equality, it is not effective because local informal institutions (Confucian values) are strong, as are the male-dominated networks that guard and enact those institutions (Patterson & Walcutt, 2017; Pattterson, Bae & Lim, 2013).

In sum, informal institutions persist because informal networks enact, enable and advance them by serving two purposes. Informal networks mitigate the pressures brought about by changes in formal structures. At the same time, they enable the informal constraints, thus maintaining the continuity of informal structures.

Network features are factors of continuity or change

Some informal networks are vectors of increased change whereas others are factors of continuity, depending on their features. We differentiated among four types of informal networks, depending on their nature, open/closed and instrumental/affective.
> "Relatively closed" informal networks are relatively tight. Examples include kinship-based networks – kin being more or less loosely defined, through blood or marriage – and elite alumni networks (old-boy networks in the UK etc.). The strong sense of belonging can express itself as solidarity, with clans or extended families helping each other out during hard times, or as social domination, where alumni of France's *grandes écoles* create insider ties between government cabinets and the private sector.
> "Relatively open" networks can include members from different circles, through school, family or hobby connections developed over an individual's lifetime. Examples are *wasta* in the Middle East and *guanxi* in China.
In the same way as large-diameter pipes have higher flow rates, relatively open networks channel more change to their informal institutions than relatively closed networks do.

The second key feature of informal networks relates to the nature of ties between members and the affective commitment they are willing to make to the relationship itself. Relations can range from "purely instrumental" (based on calculation) to involving "a degree of affection", where personal sentiment is a primary component (Li, 2007).
But this is not a case of "either-or": both instrumentality and affection are present in all kinds of networks, though to different degrees.
We argue that informal institutions based on informal networks with affective ties exhibit a higher degree of persistence than those associated with instrumental ties. Instrumental relationships may disappear if no longer perceived as useful, possibly when economic change happens and formal institutions become more effective.

Conversely, affective ties are a constituent part of personal identity and as such are "more sticky" – a bit like a viscous liquid flowing more slowly through a pipe.
For example, market-exchange networks, like *blat* ("useful" friendships) in the former Soviet Union to obtain scarce resource by bypassing the official system, may disappear over time – though whether modern-day *svyazi*, or administrative resources, is entirely new or merely a different name for *blat*, is open to debate.

To summarize, we propose that the persistence of informal institutions enacted by informal networks that are "relatively affective" and "relatively closed" is higher than the persistence of informal institutions enacted by "relatively open" and "relatively instrumental" networks. However, it is possible to move between these network types. Permeability may be as follow: an individual who benefits from elite school ties may also belong to a powerful clan and gain an advantage from kinship ties.

Conclusion

In today's highly network and interconnected societies, strong formal institutions may coexist with equally strong informal institutions using solidarity (clans in Kazakhstan) or domination networks (Oxbridge networks in the UK). Of course, it is hard to distinguish the borderline between survival strategies ("weapon of the weak", Scott, 1985) and the gaming of the system. Yet viewing the interplay between formal and informal institutions as symbiosis provides contextualization and will help professionals better understand informal networks for business or policy purposes. In particular, our typology of informal networks will be useful for multinational corporations operating in foreign markets, to respond to the complexity created by the interplay between home-based formal institutions and host-based informal institutions. For instance, companies need to "buy" or "borrow" human capital to achieve local embeddedness in markets with "relatively closed" networks, but "build" human capital in markets dominated by "relatively open" networks. In markets dominated by "relatively affective" networks, it is up to management to decide how ethical or risky it is to compose with local kinship rules.

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Impact of geopolitical risks on the innovation activity of multinational corporations

Xuejing Yang*

Regis Coeurderoy
ESCP Business School

Valérie Duplat
VU Amsterdam

Abstract

As the core driver of competitiveness for multinational corporations (MNCs), technology innovation has become a key battlefield for determining future geopolitical games between regions. On the other hand, given that MNCs' innovation activities are increasingly dependent on international cooperation, geopolitical risks will also affect their innovation activities. However, the impact of geopolitical risks on MNCs' innovation activities is still unclear. This article cross-references data from MNCs around the world from 2013 to 2019 to study the magnitude of firm-level geopolitical risk exposure of MNCs from each triad region, using some recent geopolitical events to discuss the geopolitical risks that MNCs R&D activities around the world are liable to encounter in the near future. Finally, based on the above discussion, we will make some recommendations for MNCs on IP protection.

Keywords: geopolitical risk, innovation, MNC

* Ph.D. Student, ESCP Business School

Impact of geopolitical risks on the innovation activity of multinational corporations

Introduction

Since the Russian-Ukrainian War began, Western countries have imposed various financial sanctions on Russia. As a countermeasure, Russia has challenged the current intellectual property protection system. On March 7, the Russian government promulgated Decree 299, according to which, if the patent-holding company is from an "unfriendly" country and its patents registered in Russia are used without authorization, the user is not required to give any compensation for the unauthorized use of the patent. Recently, the Russian government suddenly lifted the blockade of RUTRACKER, the once largest pirated resource website, which includes audio-visual work, games, software, and other products. Multinational companies (MNCs), especially technology-driven MNCs, protected by the current intellectual property protection system, have become the main victims.

The more MNCs gain from the host market in peacetime, the more vulnerable they are to geopolitical risks in wartime. At present, Russia has put 59 companies from Western countries, including Volkswagen, Apple, IBM, Microsoft, etc., on the "nationalization list". In addition, many medical companies have registered a large number of patents in Russia and are vulnerable to uncompensated technology transfers from the Russian government, although the latter has not yet taken any action in this regard. The impact of geopolitical risks on the innovation activities of MNCs in particular come from two dimensions. First, foreign MNCs face a higher likelihood of intellectual property infringement. Second, foreign MNCs register a cliff-like decline in their revenues in the host region in times of trouble, reducing their capacity to invest in R&D. The aims of this paper are twofold: first, by exploring the industrial structure of each triad region and the level of dependence of the most innovative MNCs in each regional market, we analyse the potential geopolitical risks faced by MNCs globally, as well as the extent of risk exposure. Second, based on the results of data analysis and the complex international situation, we also put forward some ideas that can help prevent and protect MNCEs against geopolitical risks by way of some practical cases.

The dataset used in this article is based on the R&D investment ranking, annually released in the EU Industrial R&D Investment Scoreboard by Bureau Van Dijk since 2004 (Hernandez et al., 2017). The EU Industrial R&D Investment Scoreboard (hereafter the Scoreboard) compiles company-level data from the 2500 MNCs that make the largest investments in R&D in the world (European commission, 2022). These MNCs invested in approximately 90% of the world's business-funded R&D. To select and rank the top R&D spenders, the Scoreboard counts the R&D financed by a given MNC from its own funds, regardless of where the R&D activity takes place. It consolidates data at corporate group level, i.e., including all subsidiaries, while excluding R&D financed by third parties such as governments or other companies. It also excludes a given company's share of any associated company or joint venture R&D investment, which is listed separately. Economic activities are classified according to the ICB classification (Industry Classification Benchmark), based on the ICB 4-digit level (119 industries) or the ICB 3-digit level (82 industries). The

Scoreboard data have previously been used in a series of academic publications on corporate R&D and innovation (e.g., Cincera & Ravet, 2010; Cincera & Veugelers, 2014; Coad, 2019; García-Manjóna & Romero-Merino, 2012; Montresor & Vezzani, 2015).

Panorama of R&D Investment across the Triad Regions

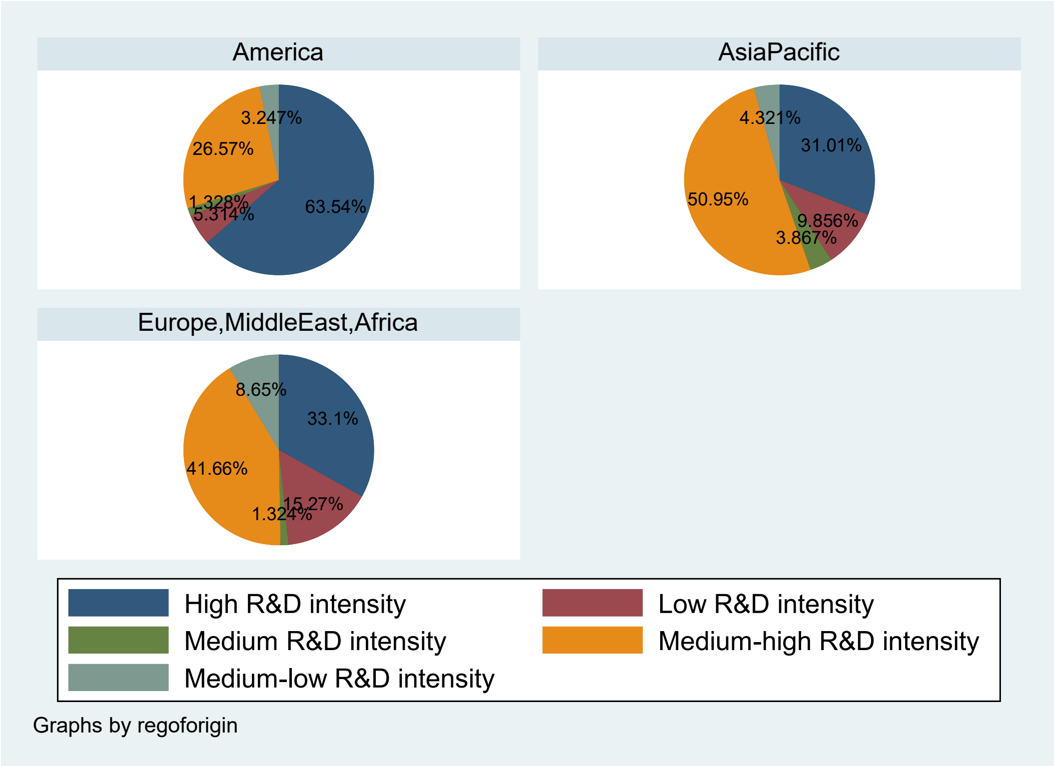
OECD has introduced a taxonomy that includes five industrial groups differentiated according to their level of R&D intensity- high, medium-high, medium, medium-low, and low R&D intensive categories (OECD, 2017). The OECD created a classification to summarize the presentation of a number of innovation-related industrial level statistics, including skilled labour force, patents, innovation expenditures, and knowledge-based capital.

As can be seen from Figure 1, most of the MNCs included in our sample are classified as active in high or medium-high R&D intensive industries. In comparison with MNCs in the Americas and Asia-Pacific regions, MNCs from Europe, the Middle East and Africa (EMEA) are proportionally more active in low R&D industries, and intensive and medium low R&D intensive sectors, including food & beverage, banks, general retailers, financial services, construction materials, oil producers, mining, chemicals, alternative energy, etc. The R&D intensity gap between companies in Europe and the US and Asia Pacific is mainly due to the dependence of their economic structure on traditional industries, differences in their company demographics (European companies are generally older, but smaller), and EU economy policy. Europe's economic structure and corporate demographics prevent the liberation of resources from old industries into new high-tech ones (van Ark et al., 2008; Cardona et al., 2013; Kumbhakar et al., 2012; Cette et al., 2015). Moreover, the government's economic policies provide insufficient support for emerging industries (Voigt and Moncada Paternò-Castello, 2012).

In order to investigate the respective R&D investment levels of companies in the three regions, we calculated the average R&D intensity level of companies in each region. From Figure 2, we can see that companies in all three regions have increasingly invested in R&D since 2014. Before 2019, US companies' investment in R&D was much higher than that of Asia Pacific and EMEA companies. By 2020, however, the level of R&D investment of EMEA companies was as high as that of America, and much higher than that of Asia-Pacific companies. However, combined with Figure 1, since EMEA MNCs are more concentrated in low and medium-low R&D intensive industries, the transformation from R&D investment to innovation performance is weaker than that of American MNCs.

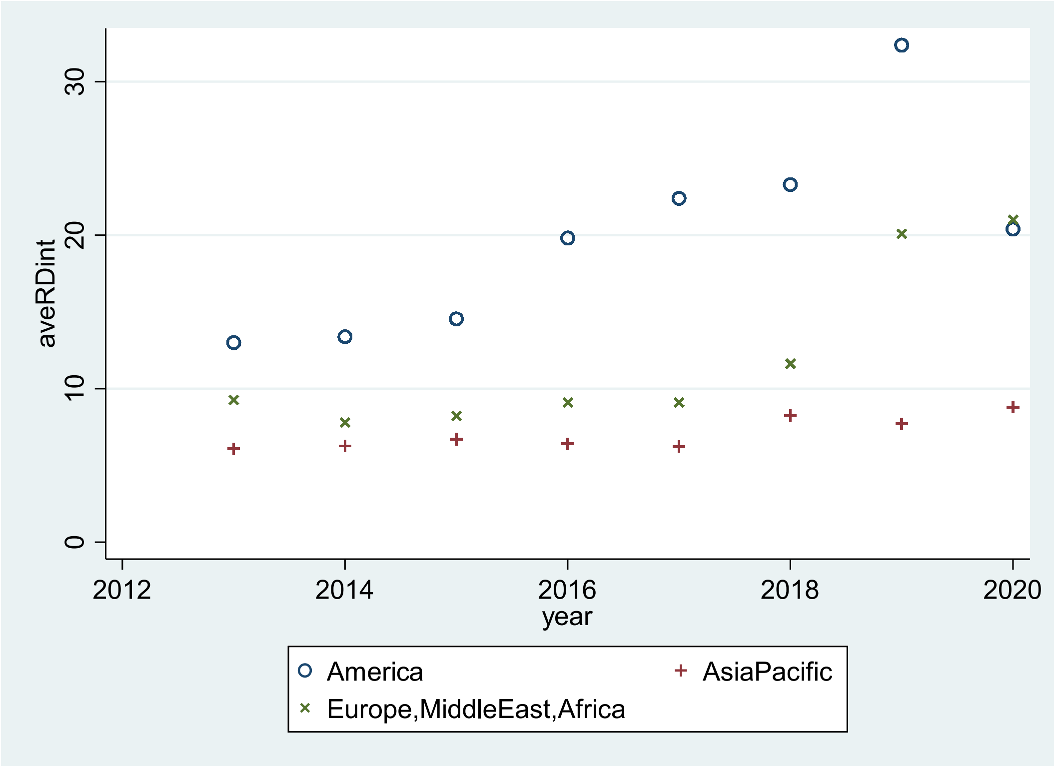
Since 2015, the R&D investment growth of American and EMEA companies has been substantial, especially for EMEA companies, while the growth of R&D investment of Asia-Pacific companies has been relatively flat. This also shows that innovation, as the core competitiveness factor in EMEA and American companies, plays an increasingly important role in industry competition. The focus of the current competitive strategy of Asian companies is still the integration of the global value chain, which is, however, mainly concentrated in the supply chain of the following industries, General industrials, Industrial engineering, Support services, Electronic & Electrical Equipment, Automobiles & Parts, Chemicals, Travel & Leisure, Health Care Equipment & Services, Household Goods & Home Construction, and Personal goods.

Figure 1. R&D intensity-based industry classification of MNCs in the triad regions



Note: The percentage in the figure is the ratio of the number of high R&D intensive, medium-high R&D intensive, medium R&D intensive, medium-low R&D intensive, and low R&D intensive MNCs in each triad region to the total number of MNCs in the region. This way of classifying industries was developed by the OECD.

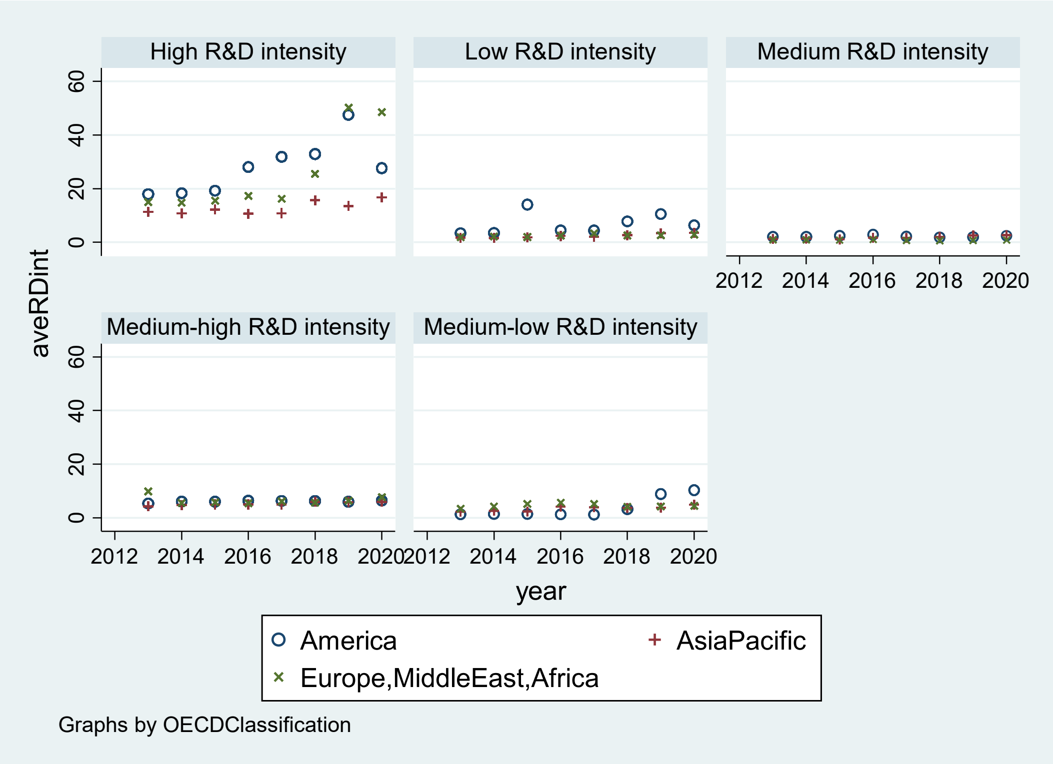
Figure 2. Average R&D intensity of MNCs in the triad regions



Technological Breakthrough & Blowout of R&D Investment

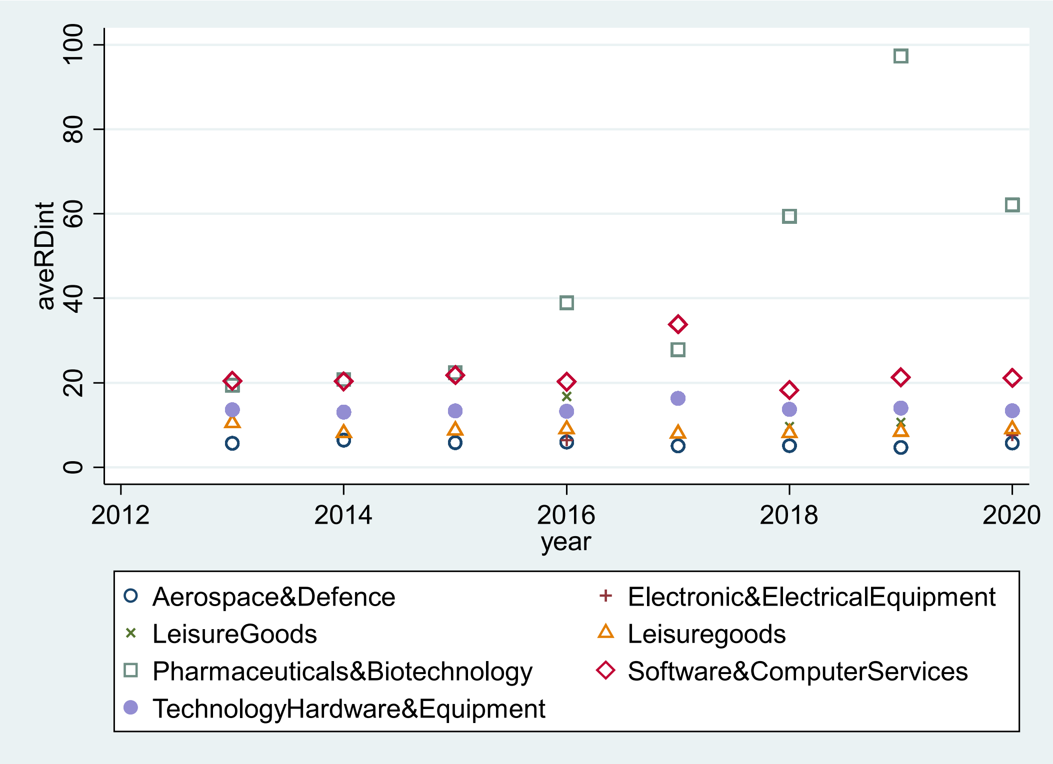
From Figure 3, we can see that, except for the high R&D intensity industries, the R&D investment levels of MNCs from the Asia-Pacific region, EMEA, and the Americas are already similar to other industries. In high R&D intensity sectors, the R&D investment gap between EMEA companies and Asia-Pacific companies has widened since 2018. Before 2018, the difference in R&D investment between Europe and the Asia-Pacific region was not large, but since 2019, the gap has become wider, while the R&D level of EMEA companies has been similar to that of American companies.

Figure 3. R&D intensities of different categories in the triad regions



As high R&D intensive sectors with the most intense competition in innovative activities, R&D investment in the pharmaceutical industry has grown far more in recent years than that of other high R&D intensive companies (Figure 4). 2019 was especially notable as pharmaceutical companies even invested all their revenue in R&D activities. This sector is followed by the software & computer services industry, whose R&D expenditure has always accounted for 20% to 40% of total revenues. This is related to recent technological breakthroughs, such as big data, block chain around 2017, and the CRISPR technology in 2020, which won the Nobel Prize, requiring firms in related industries to invest considerable sums to convert technological achievements into commercial products.

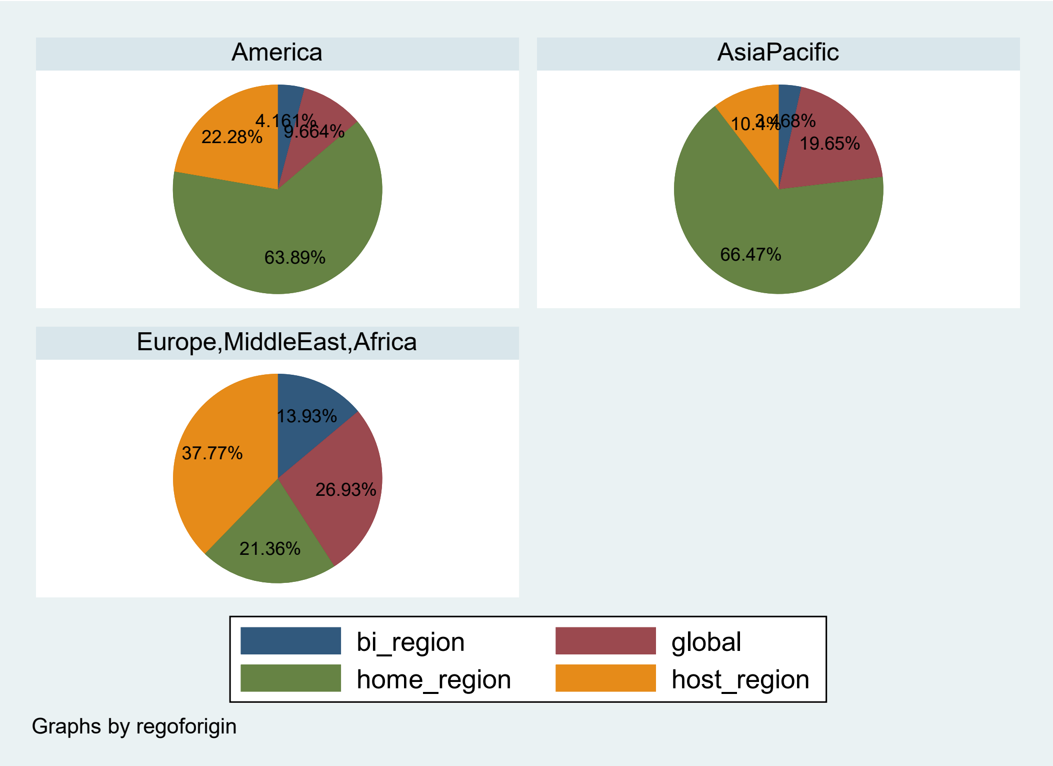
Figure 4. R&D investment in high R&D intensity industries over time



In general, except for a few high technology reliant industries, EMEA companies account for a smaller proportion of high R&D intensive industries compared to American and APAC MNCs. However, EMEA companies still have a large share of high R&D intensive industries and R&D investment. The R&D spending of companies in EMEA is much higher than that of companies from Asia Pacific. These companies have large numbers of patents and other intellectual properties around the world. When MNCs encounter geopolitical events, these IPs are at risk of being frozen or transferred. During the Russian-Ukrainian war, many pharmaceutical and software companies from the United States, Europe, and Japan face the risk of their Russia-registered patents being frozen.

Geopolitical Risks & IP in host regions

Figure 5. Globalization status of MNCs in high intensive industries



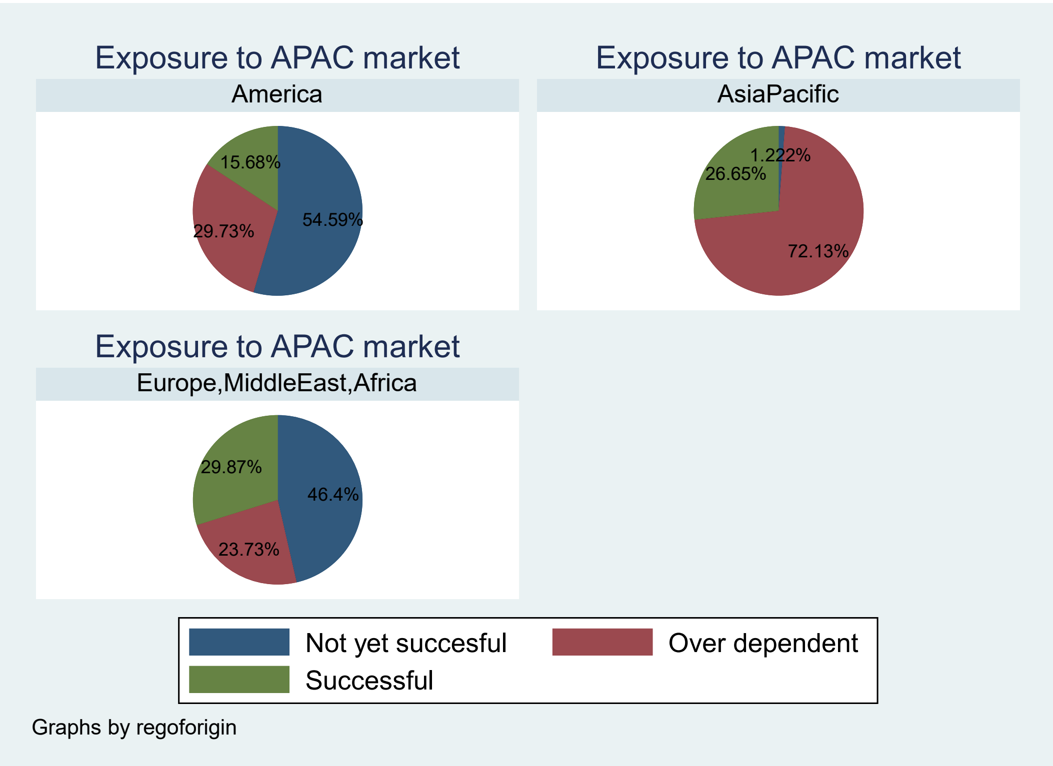
Previous empirical studies have shown that the higher the exposure of MNCs to host regional markets, the higher the geopolitical risks the company faces (Astvansh, Deng & Habib, 2022). To explore geopolitical risks, we can measure the proportion of MNC revenue in the host regional market to total revenue as a firm-level proximation of the geopolitical risk faced by MNCs. We began with the triad classification methodology proposed by Rugman and Verbeke (2004) and Arregle et al. (2009). The Triad perspective has been widely used when exploring globalization issues, as each triad represents a different cultural and institutional context. In Rugman and Verbeke (2004), the triad is defined around trade agreements: NAFTA, the EU, and ASEAN, as the vast majority of trade is done in these areas. In line with Rugman and Verbeke (2004), we divide corporate globalization strategies into four categories based on their geographic revenue distribution: home-regional, host-regional, bi-regional, and global.

As shown in Figure 5, in the high R&D intensity industry, only 21.36% of the EMEA company MNCs are home regional firms. In particular, the proportion of host regional and global firms is very high compared to that of MNCs from Asia-Pacific and the Americas. Generally speaking, MNCs are least exposed to geopolitical shocks in their home region. Host-regional and bi-regional MNCs are highly affected by other forms of institutional uncertainty due to their dependence on the host regional market. Consequently, EMEA companies face higher host region or cross-regional political risks than US and Asia-Pacific companies.

If we look at the way MNCs in each region are connected to the Asia-Pacific region, and also consider the institutional voids concerning intellectual property protection in this region and the urgent need of Asia-Pacific companies for advanced technologies, the risk of R&D misappropriation in Asia-Pacific is considered by many scholars as the highest among the three regions.

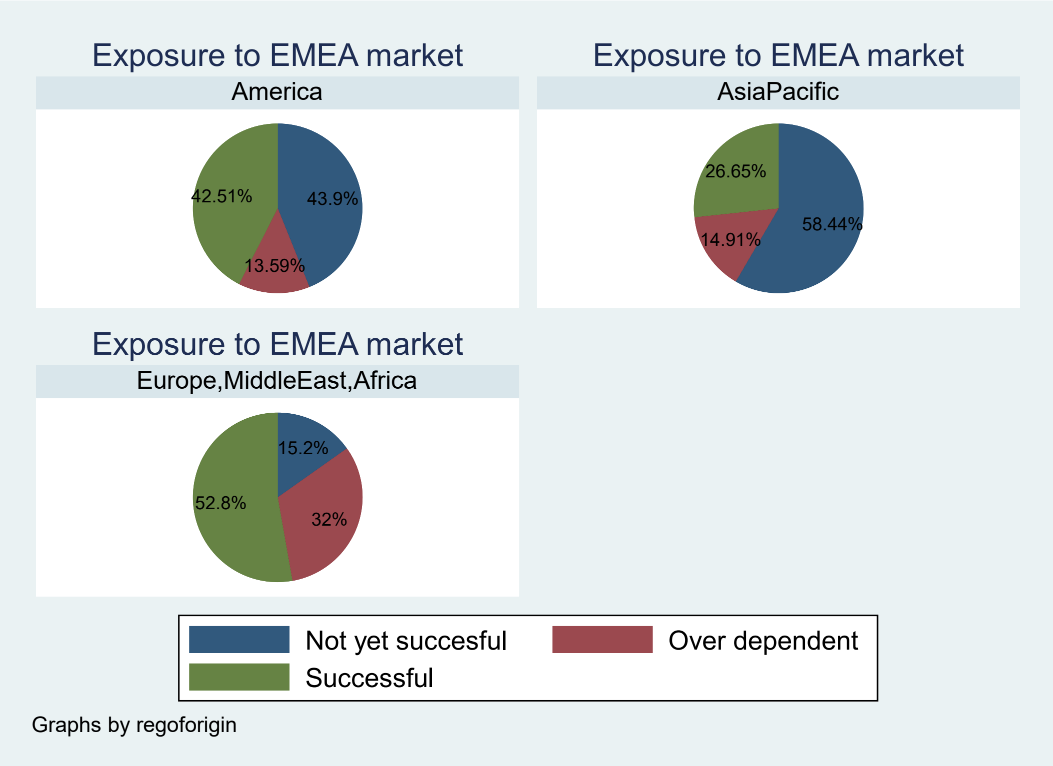
As shown in Figure 6, we see that 29.73% and 23.73% of MNCs in the Americas and Europe are over-dependent on the Asia-Pacific market (over 50% of their revenues are generated in APAC). In contrast, 29.87% of EMEA companies have achieved commercial success in the Asia-Pacific region (at least 20% of their sales are generated in this region). Geopolitical risks could put companies at risk of losing their industry status or even going bankrupt after being kicked out of the region. When a company succeeds in the region, it faces the risk of technology transfer in exchange for staying in the regional market. Generally speaking, EMEA companies face the highest risk of R&D misappropriation, while also facing high degree of geopolitical risk. On the other hand, from past experience, when EMEA and American high-tech companies enter the emerging market in the APAC region, the local government often takes a series of administrative measures to promote the transfer of technology from multinational companies to local companies, thereby promoting the competitiveness of domestic technology development (Cannice, Roger & Daniels, 2004).

Figure 6. Exposure of high R&D intensive MNCs to the APAC region



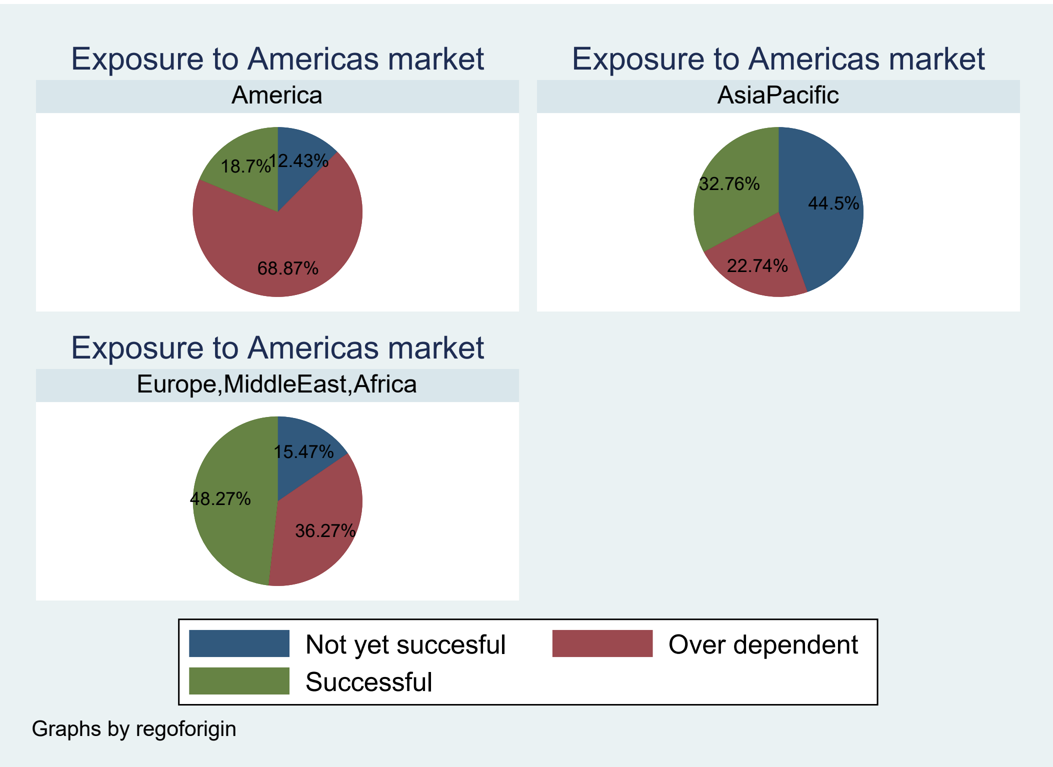
As can be seen from Figure 7, only 32% of EMEA companies mainly rely on the home regional market. At the same time, the dependence of US and Asian companies on the EMEA market is relatively low compared to the other two regional markets.

Figure 7. Exposure of high R&D intensive MNCs to the EMEA region



In Figure 8, we can see that both Europe and Asia are highly dependent on the US market. 22.74% of Asian companies and 36.27% of EMEA companies are overly dependent on the US market (50% of the total revenue comes from the US). 68.87% of American domestic companies are overly dependent on the home regional market. The attractiveness of the US market for MNCs is multifaceted, including scale of consumption and accessibility to advanced technologies.

Figure 8. Exposure of high R&D intensive MNCs to the Americas region



In addition to the aforementioned technology transfer issues in emerging markets, MNCs also face the threat of geopolitical risks in developed markets such as Europe and the United States. Since the outbreak of the US-China trade war, global trade has been severely impacted, and the global supply chain has also faced significant restructuring pressure. Self-reliance is now likely to be a mainstream trend for both China and the United States in the foreseeable future. In this political current, the US government is increasingly moving toward local protectionism. Another outcome of the trade war is the shift in the world's personal value orientation brought about by the change in political winds. EMEA and American consumers are increasingly inclined to take personal values into consideration when choosing brands and products. For example, in the Xinjiang cotton incident in 2020, the Swedish fashion company H&M was accused by the NGO BCI of including cotton produced in Xinjiang, China, in its supply chain, despite the forced labour issue there. Subsequently, the United States passed the *Uyghur Forced Labor Prevention Act*, which prohibited the export of Xinjiang cotton products to the United States. Then, after H&M announced that it would quit using Xinjiang cotton, the brand faced a massive boycott in China. In recent years, with Western consumers' growing awareness of consumer values and corporate responsibility, more and more consumers choose brands and products according to the values represented by the company. And increasingly prominent values and political conflicts between regions are making MNCs walk an increasingly fine line.

H&M, which was boycotted by Chinese consumers amid the labour right controversy in Xinjiang, suffered a huge decline in sales. Since the Russian-Ukrainian war, more than 400 MNCs, including McDonald, have abandoned the Russian market. And Russia is apparently not willing to dispose of the assets left behind by these companies in accordance with international law. Putin has already ordered the seizure of assets of companies that left Russia in March and has allowed Russian companies to claim their intellectual property with zero compensation for companies from “unfriendly countries”. The impact of geopolitical risks on the innovation capabilities of multinational companies mainly stem from their repercussions on an organization’s financial constraints. When a multinational company's business activities in a country or region are suddenly interrupted, or its assets are seized, the company will face considerable financial constraints, thereby reducing its potential to invest in R&D.

Reflections on geopolitics and technological transfer risk for MNCs

Regarding ways to deal with the technology transfer risks that MNCs are exposed to in host regional institutions, we can learn some lessons from the experience of industries we mentioned earlier that are most likely to experience globalization (Coeurderoy, Duplat & Yang, 2021). For example, a wave of technological innovations centred on data processing and wireless communications has disrupted the automotive industry in recent years. In a bid to solve the environmental issues linked to carbon fuels, the development of electric vehicles has also become a major trend. Automobile companies including Volkswagen, Mercedes-Benz and BMW are investing heavily in research and development for electric vehicles, driving systems, and digital connectivity. However, the core technology research and development of these companies is concentrated in the home country. The R&D centres located in host countries or host regions are only responsible for research and development in certain peripheral areas or tacit know-how. For example, the BMW R&D centre in

China is responsible for studying local traffic laws and digital connections to mobile apps in China. Application of these peripheral technologies is dependent on headquarter-controlled technologies, so the value of technology transfers to potential usurpers, and the incentive to misappropriate is considerably reduced. In 2021, for example, most of Volkswagen's patents were registered in Germany. BMW has a global footprint of R&D centres in all three regions, but the R&D centres in China and the United States mainly study traffic-related laws. Research and development for core technologies remains in Germany. Mercedes-Benz has production facilities in Europe, North and South America, Asia, and Africa, but the company's core R&D strategy, the development and production of electric vehicles, remains in Germany.

The COVID-19 outbreak exposed some long-standing issues in the medical industry, including unequal distribution of medical resources and insufficient R&D investment. The ensuing digital transformation that swept the entire industry not only addresses existing problems, but has also led to new globalization trends. On the one hand, MNCs continue to seek resource integration and consolidation of their market position on a global scale. On the other hand, the COVID-19 crisis ignited nationalist and protective tendencies due to supply chain issues in China that have continued since the beginning of the pandemic. Thus, MNCs are more inclined to keep their main competitive assets in the safer domestic market, while looking for a loose coupling between core competitive advantages and overseas assets (Nambisan & Luo, 2022).

Philips Healthcare provides an example of how this novel model can work (Nambisan & Luo, 2022). The company has set up partnerships with many organizations in international markets, but it adopted different forms of partnership in the developed markets and the emerging markets. After creating a digital platform called HealthSuite, the company used the platform to enter long-term innovation partnerships with healthcare providers and technology companies that need to share platform-specific assets. For example, it entered a partnership with Validic to provide consumer-generated data from wearables and health apps, which is integrated and analysed with electronic medical records and other clinical data sources in HealthSuite. In South Korea, Philips partnered with Samsung to integrate the latter's Artik Smart IoT Platform with HealthSuite and to create interoperable, connected health solutions, such as advanced health analytics.

In contrast, Philips adopted a narrower scope of innovation collaboration with local players in China due to the high technology transfer risks. The company opened an R&D centre in Shanghai as a digital innovation hub, but its collaboration with local Chinese companies mainly involves sharing digital infrastructure rather than developing new products (Nambisan & Luo, 2022). Philips Healthcare has entered a partnership with Huawei, for instance, to deploy products that use the Huawei Cloud AI platform. It has also partnered with Baidu, Alibaba, Tuya, and Tencent to use their digital infrastructure to expand Philips' product offerings in China. The products Philips sells in China rely on its R&D centres in other countries, but the R&D centres in China have no access to the company's patents or other IP assets.

Conclusion

In a peaceful world, all countries have an interest in multinationals being vectors of innovation diffusion, which can potentially even out the economic development of different regions. In this sense, technology transfers are powerful levers of harmony across the globe. However, the rise of geopolitical risks reminds us that technology can also be used as a significant lever of power between different states and regions. The presence of multinationals from another country in a given region can thus potentially induce a more or less conflictual battle for power between States. With the electroshock of the Russo-Ukrainian war, we find ourselves today and in the future at a crossroads. Should we move towards regional quotas on technological development and limit transfers in order to reduce exposure and the risks involved? But this would also mean accepting potential technological deficits (i.e., renouncing the benefits that other regions could bring). Should we instead let transfers seek out mutual benefits, even though this also means potentially being excessively exposed to abuses of power by certain countries outside the region. In this case, we are not far from a Catch22 situation.

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Legal and practical suggestions for boards as they navigate the crossroads of corporate governance and geopolitics

Drew Shagrin
David Chekroun

ESCP Business School

Abstract

Recently, hundreds of multinational companies needed to make the same decision: to what extent should the company change the way it operates in Russia in response to the invasion of Ukraine? At first glance, the decision appears to concern geopolitical risk. This impact paper will explore what geopolitical risk is and is not, with suggestions on how company boards can better evaluate and manage such risk.

Keywords: corporate governance, board of directors, geopolitics, geopolitical risk

Legal and practical suggestions for boards as they navigate the crossroads of corporate governance and geopolitics

Introduction and background

Recently, multinational enterprises based outside Russia, but with operations inside Russia, have needed to address the following question: to what extent should a company change the way it operates in Russia following the Russian invasion of Ukraine? With the whole world watching,[11] some companies have chosen to leave Russia entirely.[12] Other companies have suspended all activities temporarily, but without any permanent departure.[13] Still others have scaled back some activities while continuing to operate other activities as planned.[14] A similar option that some companies have chosen is to continue with all ongoing business commitments, scaling back none, while postponing future planned initiatives.[15] Finally, some companies are simply continuing to operate as usual.[16]

In most of these cases, the company decision on how to proceed in Russia was made by a board of directors. This kind of decision is made by the board of directors, and not by senior management, as strategy and risk management are among a board's principal missions.[17] Strategy and risk management are of course linked: companies generally adopt and then implement a strategy that takes into account various risks.

Board responsibilities regarding strategy and risk management cannot be fulfilled by one-shot decisions. Instead, boards need to continually monitor the risks that

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[11] See, for instance, Jeffrey Sonnenfeld and Steven Tian, *Some of the Biggest Brands Are Leaving Russia. Others Just Can't Quit Putin. Here's a List.* The New York Times, April 27, 2022 (https://www.nytimes.com/interactive/2022/04/07/opinion/companies-ukraine-boycott.html).

[12] "Companies totally halting Russian engagements or completely exiting Russia" run the alphabetical gamut from Belgium-based AB InBev and Ireland-based Accenture to Poland-based Zabka and Switzerland-based Zurich Insurance Company, according to the "Withdrawal" category in a database maintained by Jeffrey Sonnenfeld and a supporting team at Yale Management School (https://som.yale.edu/story/2022/almost-1000-companies-have-curtailed-operations-russia-some-remain, last consulted on June 3, 2022) (the "Yale Database").

[13] "Companies temporarily curtailing most or nearly all operations while keeping return options open" run the alphabetical gamut from US-based 3M and Sweden-based AAK to UK-based ZHA and US-based Zynga, according to the "Suspension" category in the Yale Database.

[14] "Companies that are scaling back some significant business operations but continuing others" run the alphabetical gamut from Switzerland-based ABB and US-based Activision Blizzard to Germany-based ZF Friedrichshafen and US-based Zoetis, according to the "Scaling Back" category in the Yale Database.

[15] "Companies postponing future planned investment/development/marketing while continuing substantive business" run the alphabetical gamut from Netherlands-based Aalberts and US-based Abbott Laboratories to US-based Young Living and France-based Yves Rocher, according to the "Buying Time" category in the Yale Database.

[16] "Companies that are just continuing business-as-usual in Russia" run the alphabetical gamut from Spain-based Acerinox and Austria-based Agrana to China-based ZTE and Hungary-based Zwack, according to the "Digging In" category in the Yale Database.

[17] The other main board missions relate to finance, ESG, leadership supervision, and regulatory compliance.

affect the company. They then need to consider updating the adopted strategy from time to time to take any shifting risks into account.[18]

When Russia invaded Ukraine, risks shifted in numerous ways for companies based outside Russia but with operations in the country. To better understand how the risks changed, we need to acknowledge the wide-ranging types of risk that a company board is supposed to monitor. These include economic risk, financial risk, compliance risk, security and fraud risk, reputational risk, operational risk, competition risk, and political risk. This last risk, *political* risk, becomes *geopolitical* risk when the political circumstances and events are outside the company's home country. For a multinational enterprise, geopolitical risks principally involve expropriation of foreign-owned assets, extraordinary regulatory burdens applied to foreign-owned businesses, and violence and civil unrest in areas where the company operates. Geopolitical risks may also include situations and events arising out of competition between states over such things as markets, natural resources, and strategic trade routes. Such competition can generate sanctions, embargoes, and other trade constraints, and in some cases is pursued through military means, in the form of armed conflict.

Purely domestic companies are not directly concerned by geopolitical risk as they have no foreign operations. They face political risk in their home country, of course, but the absence of operations abroad precludes them from having to confront geopolitical risk. Nonetheless, purely domestic companies can still be affected by geopolitical *developments*. If the supply chain or customer base extends beyond the company's home country, geopolitical developments clearly have the potential (the risk) to disrupt the company's trajectory. Even when the supply chain and customer base are solely domestic, the company can still be affected by geopolitical developments. For example, purely national companies in many countries have suddenly been faced with a steep rise in the cost of domestically supplied energy following the Russian invasion of Ukraine as even domestic energy is part of a worldwide energy market whose prices have gone up since the invasion.

A multinational enterprise might of course be similarly affected by geopolitical developments when there is no meaningful impact on geopolitical risk such as expropriation. Moreover, multinationals with operations in a location where a given geopolitical development has arisen may also experience a change in reputational risk.

Indeed, such a change in reputational risk is precisely what motivated many non-Russian multinationals to alter their strategy with respect to Russia. The companies changed their plans not because of a perception of increased geopolitical risk such as expropriation of company assets in Russia, or extraordinary regulatory burdens applied to foreign-owned businesses, or violence and civil unrest in the country. Nor did they fear a Ukrainian counter-invasion of Russia.[19] Instead, they were concerned

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18 A board can of course update an adopted strategy for other reasons too.

19 Armed conflict inside a foreign country where a company has operations can of course destroy company assets and disrupt its operations, but it can also expose employees in that country to mortal danger. Boards protect the interests of such employees more or less depending on how seriously they subscribe to stakeholder theory as opposed to shareholder primacy. In addition, in countries such as Germany, where the Codetermination Law of 1976 and related legislation provide for an employee's voice in selecting board members, the greater employee voice on the board might reasonably be expected to increase the board's protection of at-risk employees.

about reputational risk, and the way their ongoing operations in Russia might prompt current and prospective customers, employees, suppliers, lenders, and shareholders, as well as government regulators, journalists, and analysts, to think less highly of the company. Put more simply, they feared damage to their reputation.[20]

Legal and practical influences on boards where geopolitical risk is concerned

As noted above, company boards must monitor risk, including economic risk, financial risk, compliance risk, security and fraud risk, reputational risk, operational risk, competition risk, and political risk. Political risk includes its subset, geopolitical risk.

Evaluating geopolitical risk is difficult.[21] Most corporate board members are ill-equipped to measure and evaluate geopolitical risk independently, even though some may have relevant experience and expertise. For that reason, board members rely—as typically permitted by the law[22]—on the advice of third-party experts, whether colleagues on the board, in-house staff, or outside consultants.[23]

Publicly traded companies in particular are obligated by law in some countries to go beyond merely monitoring risk. They also need to discuss risk, including applicable geopolitical risk, in their periodic reports filed with securities regulators.[24] Such public companies are specifically required to disclose material risk factors for the benefit of real and prospective investors, who can then work from such disclosures to make informed investment decisions. Misrepresentation of material

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[20] In some cases there could be an additional non-risk reason, namely, distaste for doing business in a country whose leadership makes reprehensible choices.

[21] For a review of the legal and practical challenges that boards face in evaluating geopolitical risk in a context of armed conflict, see Nathalie Belhoste and Bastien Nivet, *Les entreprises et la guerre : vers la responsabilité géopolitique des entreprises?*, in Revue internationale et stratégique 2018/3 (N° 111), pages 16 to 25.

[22] Company laws vary, of course, but typically permit a board member to rely on information and advice provided by third parties, including company employees and third-party consultants to the company (including most visibly accounting firms that review financial statements, lawyers dealing with a broad range of corporate activities, compensation consultants advising on leadership team remuneration, and investment bankers handling transactions). An example of a company law provision authorizing such reliance can be found at Section 141(e) of the Delaware General Corporation Law (an influential state-specific company law in the United States)

[23] Third-party advice may be delivered to the board in several different forms, but are most commonly found in the executive summary of an expert's extensive written report; an expert's extensive written report; or an expert's in-person presentation at which the board can ask questions, followed by an extensive written report that includes the board's questions along with corresponding answers. The authors thank Willis Sparks of Eurasia Group and Mike Nowlis of the University of Cambridge for their help in understanding the deliverables of political risk consultancy firms.

[24] See, for instance, Item 105 of the American regulation implementing the Securities Act of 1933, the Securities Exchange Act of 1932, and the Energy Policy and Conservation Act of 1975, known as Regulation S-K, codified at 17 CFR § 229.105. Item 105 requires issuers of covered securities to discuss "material factors that make an investment in the registrant or offering speculative or risky. This discussion must be organized logically with relevant headings and each risk factor should be set forth under a subcaption that adequately describes the risk." Issuers must also "(c)oncisely explain how each risk affects the registrant or the securities being offered."

risk factors is a leading source of securities-related litigation.[25] To protect themselves against securities fraud claims, companies tend to detail risks so extensively that the disclosures lose their usefulness,[26] but the duty to communicate the risk can nonetheless focus more attention on evaluating it than might otherwise have been the case, and this attention can be important even if the communication itself is not always valuable.

We would like to add a psychological consideration: board members are susceptible to the same irrational tendencies exhibited by all human beings. One such irrational tendency, known as the Ellsberg paradox, involves decisions made in the face of risk: when given the choice, people generally prefer an option where the risk of success or failure is probabilistically known, and they generally avoid options where the risk of success or failure is unknowable, *even when doing so makes no rational sense when viewed strictly through the lens of probabilities*.[27] Concretely, when a board member examining risks in a company's entry or ongoing involvement in a country abroad perceives the risks of one option in probabilistically known terms, and the risks of a competing option in probabilistically unknown terms, he or she—like the vast majority of people—will tend to opt for the option where the risk is perceived in probabilistically known terms.

The last practical consideration we would like to raise is the common understanding of risk as the probability of a given negative outcome multiplied by the gravity of that negative outcome. In this understanding, a low-probability high-gravity risk and a high-probability low-gravity risk could be considered mathematically equal. A quasi-mathematical analysis would be ideal, but in the real world human bias tends to overvalue certain risk factors and undervalue others, undermining the reliability of estimations of probability and gravity.[28] And of course there are certain risks whose probability is unknown and even unknowable.

Tactics

Given the challenges identified above, company boards could benefit from specific tactics when they consider the general decision to enter a new country or exit an existing one, and the specific decision of how to enter or exit. We put forward four such tactics.

Periodic due diligence review of geopolitical risk

[25] When taken to its extreme, the need to disclose material risks transforms virtually every harm into securities fraud, a point made frequently by Bloomberg commentator Matt Levine. See, for instance, his 2019 article *Everything Everywhere Is Securities Fraud* at https://www.bloomberg.com/opinion/articles/2019-06-26/everything-everywhere-is-securities-fraud.

[26] See for instance the nearly 7700-word disclosure of risk by US-based Walmart Inc. in its 10-K annual report filed with the Securities and Exchange Commission for the fiscal year ended January 31, 2019 (https://www.sec.gov/Archives/edgar/data/104169/000010416919000016/wmtform10-kx1312019.htm#sBBC09961132151239331ED7A6E22065E).

[27] See Daniel Ellsberg, *Risk, Ambiguity, and Decision* (Garland, 2001), reviewed by Nicholas Leman, The Decision Theorist Who Leaked the Pentagon Papers, The New Yorker (November 4, 2002) (https://www.newyorker.com/magazine/2002/11/04/paper-tiger).

[28] See, for instance, the numerous heuristics and biases described by, and in many cases discovered by, Daniel Kahneman in his book *Thinking Fast And Slow* (Farrar, Strauss and Giroux, 2011). For our purposes, the salience bias is probably the most relevant: people tend to focus on remarkable (salient) information while disregarding information lacking in prominence.

First, we propose a periodic "due diligence review" to examine geopolitical risk outside the usual transaction-oriented context. Due diligence is typically viewed as a pre-closing phase of a transaction during which the transacting parties perform a factual and legal investigation to ensure that the reality conforms with their assumptions, and any non-conformity can lead to a renegotiation or even termination of the transaction. We propose extending the concept of due diligence to the monitoring of geopolitical risk, periodically investigating the factual and legal underpinnings of geopolitical risk independently of any specific transaction. In particular, a company board should periodically perform such an investigation to ensure that the geopolitical reality in each region of relevance to the company is factually and legally as expected, consistent with the board members' assumptions. As with transaction-related due diligence, whether the information gathered confirms or invalidates the board's assumptions, it will ensure a better-informed consideration of the company's strategy with respect to the region under review (notably, whether and possibly how to enter or exit a country).[29]

In transaction-oriented due diligence, a board typically relies on third-party expertise. In non-transactional geopolitical risk-monitoring due diligence, a board should similarly rely on third-party expertise. Whether performed by in-house staff or consultants, or even fellow board members,[30] geopolitical risk analysis is a specialty that calls for expertise and experience. Moreover, if the board committee structure has no risk committee, then an existing committee should be tasked with risk monitoring.

Upstream consideration of geopolitical risk before making decisions

Second, we propose an internal board procedure to ensure that geopolitical risk has received the attention it deserves before the board makes any decisions. The internal procedure we envision would create no new legal duty to third parties, and therefore should not lead to any of the litigation that so often accompanies legally imposed obligations. The procedure would be no more formal than an internal "best practice" process.

Our internal board procedure would consist of three parts. First, the board would periodically define a level of geopolitical risk that it found to be generally acceptable. For instance, it might adopt a perceived probability of less than 10% for significant negative geopolitical developments as its acceptable geopolitical risk standard. Second, for its own internal benefit, when the board occasionally makes a decision with possible vulnerability to geopolitical risk (such as entering or exiting a country), it should include an explicit finding that its decision is consistent with its previously

[29] A similar due diligence idea for human rights concerns as opposed to geopolitical risk is identified in Part 15(B) of the United Nations Guiding Principles on Business and Human Rights. In fact, human rights concerns and geopolitical risk concerns overlap one another, as with respect to armed conflict, for instance. See also the European Union's draft Mandatory Human Rights and Environmental Due Diligence Directive (summarized at https://ec.europa.eu/commission/presscorner/detail/en/ip_22_1145); the OECD Due Diligence Guidance for Responsible Business Conduct adopted in 2018 (found at http://mneguidelines.oecd.org/OECD-Due-Diligence-Guidance-for-Responsible-Business-Conduct.pdf); and the French Loi n° 2017-399 du 27 mars 2017, a law that imposes a duty of vigilance on multinational companies (found at www.legifrance.gouv.fr/eli/loi/2017/3/27/ECFX1509096L/jo/texte).

[30] See our suggestion below to increase an internal board's capacity to evaluate geopolitical risk.

approved geopolitical risk threshold. This finding should be based on the due diligence described above. Finally, if the board discovers that a desired decision would expose the company to a greater amount of geopolitical risk than the previously approved threshold, then it could either (1) explicitly decide to increase its threshold for acceptable geopolitical risk, or (2) explicitly find that the circumstances justify excessive geopolitical risk, with an internal explanation of the justifying factors, in either event still proceeding with the desired decision that would expose the company to more geopolitical risk than would formerly have been considered acceptable.

This upstream process would not legally prevent the board from reaching a decision. Similarly, it would not provide any prospective litigant with a possible legal claim. Nonetheless, such an internal non-law-based process would allow the board to better appreciate and manage geopolitical risk.[31] Furthermore, with this consideration of geopolitical risk just before a decision ('upstream" or "ex ante"), the board's geopolitical risk evaluation would necessarily be timely.

Recruiting board members with geopolitical risk expertise

Third, we suggest that multinational companies try to recruit individuals to the board with experience and expertise in evaluating geopolitical risk. Former diplomats,[32] other former high government officials,[33] international relations professionals, and geopolitical risk analysts (including former military analysts) can be exceptionally well qualified not only to evaluate geopolitical risk, but also to independently and critically evaluate the advice given to the board by third-party geopolitical risk experts.[34] We understand of course that board seats are limited in number and reserving a seat for a geopolitical risk expert would produce a zero-sum game, excluding other individuals with experience and expertise in other domains that could be valuable to the board. Hence, we are not saying that a board seat should be reserved for geopolitical risk experts. We simply suggest that the acumen of a geopolitical risk expert should be highly valued as boards go about attempting to fill seats with capable people.

Moreover, any board member with geopolitical risk expertise should be a part of the board's geopolitical risk review process, serving on the risk committee (if one exists) or on whatever other committee may be tasked with reviewing geopolitical risk.

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[31] This process takes its inspiration from the California Environmental Quality Act, codified at California Public Resources Code Sections 21000 *et seq*. This law, known as CEQA, compels a rejection of any discretionary public permit that could reasonably be expected to result in a significant negative environmental impact, unless the permitting body both makes an explicit finding of overriding considerations to justify permitting the project despite the risk, and imposes mitigation measures to limit the negative environmental impacts. Unlike CEQA, which is binding, our proposed process would be an optional internal process, a "best practice" that would not involve rights or duties, and would therefore not give rise to litigation.

[32] See for instance former French Foreign Minister Hubert Védrine, a member of the board of French multinational LVMH.

[33] See for instance former France President Nicolas Sarkozy, a member of the board of French multinational Accor.

[34] To be clear, we support reliance on third-party experts where appropriate.

Adding geopolitical risk to non-financial reporting

Finally, in addition to the non-financial reporting that many multinational firms are already required to provide, we propose adding a reporting category specifically for geopolitical risk. This would simply be a marginal extension of existing non-financial reporting requirements, as several of the matters that companies are already required to report on overlap in practice with geopolitical risk. The European Union, for instance, requires some firms to report on environmental matters, social and employee-related matters, respect for human rights, and anti-corruption and bribery matters, issues that can help an observer to better appreciate geopolitical risk. Notably, the EU directive requires reporting firms to specifically describe the risks related to such reported-on matters.[35]

Conclusion

We put forward four solutions to help boards to better navigate geopolitical risk: a periodic due diligence review of geopolitical risk; a pre-decision-making upstream consideration of geopolitical risk; recruiting board members with geopolitical risk expertise; and adding geopolitical risk to non-financial reporting. Deciding whether and how to enter or exit a country may still be difficult, even if a board follows our proposals, but adopting such proposals would ensure effective and timely consideration of geopolitical risk as boards navigate the crossroads of corporate governance and geopolitics.

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[35] See Directive 2014/95/EU of the European Parliament and the European Council of 22 October 2014 amending Directive 2013/34/EU as regards disclosure of non-financial and diversity information by certain large undertakings and groups (found at https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32014L0095).

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Geopolitics in the Era of AI : Upending assumptions

Kenneth Krushel *

ESCP Business School

Abstract

It is trendy but not altogether misleading to characterize our current socio-economic era as a fourth industrial revolution, also termed the Age of AI. In an effort to understand the essential discoveries, applications and influences of this era, we use labels – for example, digitalization, Machine Learning, autonomous systems, predictive algorithms, 5G, Web3, metaverse, blockchain and DAO. The list seems to expand by the day. The language is often intimidating and obscure, even contributing to deeply antagonistic geopolitical and socio-economic boundaries. To make sense of how to situate ourselves within these cross currents we often defer to a linear assessment of geopolitics, based on the "industrial revolution" precedent. If we put aside jargon and crowdsourced analyses, if we allow for wholesale reinterpretation, what do we discover when we move from abstractive layers and learn from AI as the defining authority? Is there something intrinsically ahistorical about this Age of AI and the influence of digital technology in challenging our geopolitical constructs?

Keywords: Artificial intelligence, Industrial Revolution, Digitalization, Interdisciplinary study

*Adjunct professor, ESCP Business School

Geopolitics in the Era of AI: upending assumptions

"…the essence of technology is by no means anything technological." – Martin Heidegger (The Question Concerning Technology and Other Essays)

To define geopolitics is not only an opportunity to question our dependence upon analytical frameworks, but in this era of AI to question ourselves as much as our cherished opinions and inherited doctrines. Certainly geopolitics is understood according to the activity and environment in which it exists, and we borrow upon historical insights to explain the geopolitical tangle of state rivalry, multinational monopoly growth and public anxiety. Yet historical predicates may not be illustrative. How then to introduce and embed our assessment of AI – given its scale, scope and speed - as central to the discourse of geopolitical competition?

In examining geopolitics in the era of AI we turn initially to a particular audience, perhaps the most germane one, allowing ourselves, as teachers, to be more teachable than the apprentice, more of a learner than the learner.

The Students

In a recent MBA class in Paris most students were from throughout the EU. Others were from countries now enduring a collision of hyper-nationalism, kleptocratic autocracy and a rabid rebuke of geopolitical cohesion. Regardless of background, students struggled to explain their individual and collective apprehension regarding political and socio-economic tensions. The study of artificial Intelligence added to this unsettled view of professional and vocational aspirations. Given the intensity they carried into the classroom another concern was self-evident, the nature of thinking, what Heidegger suggests is a response to a call, a necessity, a question: where do we belong?

These students live in an inherited geopolitical environment - something they define as chaotic, ominous, and unraveling. From the students' perspective, AI introduces a layer of complexity and displacement as they earnestly work to understand the concept of machine learning, the ability of a digital technology not just to automate a function, but to learn from interactions with its environment in order to construct optimized functions. The study becomes increasingly challenging when examining data surveillance and profiling, the persuasive and predictive AI that pervades digital social networks and autonomous systems.

We also examine the controlling elements of the entire AI supply chain, from the human source fueling datasets that AI technologies need to learn from, to research and development and technology transfers, as well as AI's ultimate effect on society. As one student commented: "Something within us wishes to flee from this. We have our bags packed, but we don't know where to go".

What the students revealed is a sincere questioning of purpose and future. There are few compelling answers to questions orbiting around AI's influence: there is no closure other than what is unimaginable, some form of digital dystopia. Despite this paradox of asking cogent questions without the expectation of definitive answers, perhaps because of this paradox, the vibrant, vulnerable and intensely focused students are determined to learn - as evidenced by palpable classroom attention, a defense against the savage irredentist, a drum beat coming from the not too distant horizon.

A student, whose homeland drives a deepening spiral of obscene and terrifying destruction, sat quietly following a class on data privacy and what students had termed "perversions caused by social media disinformation". She approached the instructor, her expression suggesting a diminishing sheltering ring of possibility. She says with scarcely conscious bravery and sorrow, "I don't understand. I don't know what to believe."

She has distilled the questions that had dominated the previous class meeting: the abuses of social media and platform dynamics, digital technology addiction, surveillance capitalism, and data privacy exploitation. The list of issues students identify is considerably longer, more carefully conceived. They are impatient with abstraction, aggregated statistics, and casual juxtapositions. They ask for evidence, wary of facile descriptions, and especially wary of conclusive verdicts that suggest there is an all-encompassing resolution.

We work to avoid becoming abstracted and dazed, sometimes privileged with unanticipated insights, even if only for the duration of one inexplicable moment, becoming aware of our own struggle to understand geopolitics and AI's piercing dominion.

There is something unsettling here. The students work for these brief flashes of insight, whereas algorithms, data sets, and deep learning computations linger forever. These students delve into the applications of AI, asking to understand its influence and repercussions, though AI doesn't in turn help with our education, remaining elusive and opaque, a digital technology form of *Deus absconditus*.

In "Pilgrim at Tinker Creek", Annie Dillard recalls a story about an Eskimo hunter who asked the local missionary, "If I don't know about God and sin, would I go to hell?" "No," said the priest, "not if you did not know."

"Then why," the Eskimo asks, "did you tell me?"

We are told because, regardless of unsettling headlines, there is a shared necessity to understand.

Reinterpreting Geopolitics

As we shift into the third decade of this century, making sense of geopolitics seems increasingly challenging, as if we have entered a "geopolitical winter" - to borrow a term which underscores disappointment with artificial intelligence applications from the 1970s -1990s, as well as cryptocurrency's current valuation crash. Political analysis generally interprets this condition as the legacy of colliding fractious politics, corrosive ideologies, greed, and overwrought enthusiasm, obstructing our grasp for what Epictetus considered an integral part of what it means to be human: "rational faculty", one of reasoned proportion.

We recognize, belatedly, that practically every liberal democracy is contending with populist political movements, nativism, xenophobia, contempt for civil society. There is widespread abhorrence for the very managerial class, entrepreneurial and "cosmopolitan elites" that use such language as "geopolitics" and "globalization". Accompanying the increasingly distinct geopolitical and societal divisions, are accelerating and astounding AI innovations, altering business models, value creation, wealth and income distribution, as well as the imposition of a rigid hierarchy – the gatekeeper for social mobility. Does the expansion of AI's influence fuel burgeoning shabby civil unrest, perhaps more accurately described as incipient volcanic nihilism?

Are conventional inquiry and conventional conclusion sufficient?

To understand the term "geopolitical", we cite flows of trade, capital, information and people, their trajectories, and how countries compete to control these features for political advantage with an international and global dimension. Some respected analyses even view the 21st century tumult as cyclical. For example, as detailed in "The State of Globalization" by Steven Altman and Caroline Bastian (Harvard Business Review, April 12, 2022), "the fundamental drivers of success in global strategy remain unchanged."

Can we rest with this conclusion? Are we satisfied with this outmoded lexicon?

The Industrial Revolution Paradigm

In academia, we use intellectual map-making tools to guide inquiry. One prevalent tool is the concept of "Industrial Revolutions", introduced in 1837 by Auguste Blanqui, a martyr and leading figure of French radicalism, who was later popularized by Arnold Toynbee and Friedrich Engels. His construct helps in examining modern technology's influence on geopolitical and socio-economic transitions, beginning in the early 18th century with the invention of the steam engine and the subsequent transformation of Britain's textile industry. Subsequent "industrial revolutions" are defined by, secondly, mass production; the distribution of electric power; thirdly, electronic and IT systems as well as automation; and, fourthly, AI and cyber-physical systems

For both Toynbee and Engels, industrial revolutions increased national wealth at the expense of material and moral well-being, and has, to cite Toynbee, "led to a rapid alienation of classes and the degradation of a large body of producers".

Dates vary according to the expert, but the industrial revolution paradigm attributes a linear progression leading to our current fourth industrial revolution. Yet is our era unrelated and discontinuous to what has preceded it? Are we being presented features and a dynamic that we are unprepared to understand, assuming our historical analytical competencies are obsolete?

"Nothing makes you madder than wanting to defend yourself against something you can't even get hold of, something the human race is doing to you, but there's nobody you can grab by the throat." - Stefan Zweig (The Post Office Girl, published posthumously in 1982)

Standing before the abstraction of a digital landscape in 1989, Tim Berners-Lee envisioned the World Wide Web as a shared information space where we would work, play and socialize, using digital technology to analyze data and collectively participate in the making of meaning. Here we would individually yet expansively fit. The World Wide Web was to bolster the democratization of information. We'd find a shared purpose.

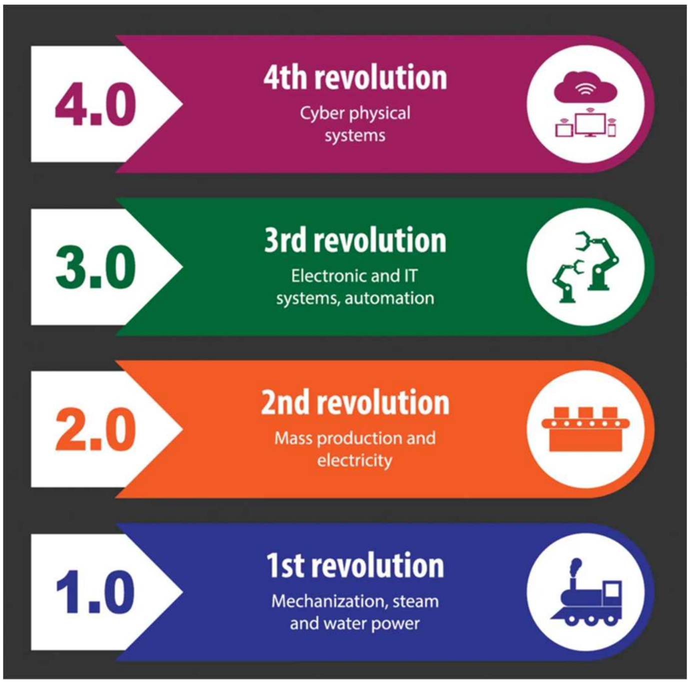
Our lived experience however, reveals something different from Berners-Lee's gaze. Today, the mobile web, data analytics and algorithmic applications fuel social media's trivialization and manipulation of news, sabotaging state sovereignty and even our sense of agency. These are the castigating allegations made by the EU which led to recent regulatory strictures defined in the Digital Services Act and Digital Markets Act. (The U.S. Congress, citing similar "Big Tech" issues, struggles to enact or even define comparable legislation). In this atmosphere, whether on a regional or global level, what then defines identity and allegiance, let alone understanding the complexities of geopolitics and globalization? These are not gratuitous questions, but a probing necessity if we agree that the Age of AI is ahistorical in terms of redefining the scale of industrial revolution disruption.

We work with basic assumptions that have proved reliable in the past. On one level the terms "geopolitics" and "globalization" suggest historically identifiable political and economic spheres of influence, anchored within the realities of China's economic transformation, global economic interdependence, European integration, Russia's irredentism, pandemics, and a potential catastrophic environmental crisis. We assume a base level of pragmatism and sane discourse as an a priori truth, requisite to avoid cataclysmic conflicts.

The Age of AI: Antecedents?

Even if we agree to assign preeminence to things digital, how can we understand the scope of this industrial revolution and accompanying reimagined industries and employment, as well as in its wake the arrival of unanticipated behaviors, norms, regulations, and political divisions? Does our very interpretation of "geopolitics" - in relation to this tumultuous era - deserve wholesale recalibration? Perhaps we interpret and apply Joseph Schumpeter's "creative destruction" as a catalyst to revolutionize our own sense making, to disassemble what is notional.

To agree upon the Age of AI context, consider the framework of the preceding three industrial revolutions. We study each "era" to identify and define the metamorphosing chain of economic, financial, political, psychological, philosophical, aesthetic, and societal changes.



Industrial Revolution

Graph depicting four Industrial Revolutions, in progression from the 18th century to the 21st.

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1. First Industrial Revolution: the advent of steam powered factories, incipient industrialization, and employment migration from agrarian to urban settings. Example: During this era in England, machines displace 98% of labor required to weave one yard of cloth.

2. Second Industrial Revolution: application of science, and electric power creates mass production and manufacturing. The advent of global telecommunications.

3. Third Industrial Revolution: Electronics and IT automated production: nascent digitalization

4. Fourth Industrial Revolution. Digital Technology innovation: robotics, Natural Language Processing, Machine Learning, computer vision, AR/VR, exponential increase in computing power, availability of unprecedented amount of data, zero marginal cost efficiencies, platform dynamics, network effects.

   Consider how AI will challenge geopolitical norms, blurring the lines between physical, digital and biological.

   - Connecting the world - **enfranchisement**
   - Fragmenting the world - **disenfranchisement**

- Decentralization of unprecedented processing power & storage capacity

Potential – long term

- Potential to raise global income levels and improve quality of life
- Supply side miracles: long term gains in efficiency and productivity
- Transportation and communication costs decrease (notwithstanding current fractures and rising inflation)
- Logistics and global supply chain more effective (again, even acknowledging the preemptive implosion in freight infrastructure)
- Cost of trade diminishes (absent punitive tariffs and political brinkmanship)

Darker Potential – near and long term

- Greater inequality (falling share of income and wealth)
- Disrupted labor markets (If we agree that cardinal underpinnings of capitalism are optimization and scale efficiencies, then automation and accompanying worker displacement are the rule, not an exception. Only the scale of unemployment is to be debated)
- Exacerbate gap between returns on invested capital and returns on labor
- "Deglobalized" supply chains, as a splintered internet and AI innovation is tied to nationalist ideology
- Middle class being squeezed, or disappearing altogether
- Worldwide surveillance capitalism, appropriation of an individual's data

AI as an ahistorical phenomenon

The Fourth Industrial Revolution incites dynamics that no other industrial revolution introduced, especially when direct access to the technology is measured. The list of examples is lengthy, but consider the speed of transmission.

- Never before has there been a communications network, used daily in the form of mobile devices by 66% of the world's population (6.6 billion), functioning at essentially unimaginable speeds (electrons move at the speed of light, 300,000 km/sec). In essence, information transmission is instantaneous and ubiquitous. Latency is dusty history.

As of June, 2022 the world's population is approximately 7.9 Billion. The reality: unprecedented access and use of communications technology, specifically the mobile web. Is income and wealth inequality coincidental or an irrefutable result?

- In Sub-Saharan Africa there is greater access to the Internet than to reliable electricity
- 58% of the world population (91% of mobile phone user base) use social media platforms, *daily*
- 95% of social media use is via mobile phone
- The average amount of time (each day) that internet is used by persons 16-64 years of age:
  - Internet: approximately 7 hours
  - Social Media: approximately 2.5 hours
- The poorest half of the global population barely owns any wealth (2% of total)*
- 10% of world's population holds 76%% of worlds total wealth

***World Inequality Data Base, January 12, 2022;** Sources and series: wir2022.wid.world/
methodology, Bauluz et al. (2021)

Benefits and trade-offs

The era of AI is defined by dominant technology throughout practically every industry and segment of society, supporting a more interconnected world with its corresponding advantages and efficiencies providing welcomed benefits.

But with benefits come trade-offs, examples being the commodification (and exploitation) of personal data fueling corporate behemoths, data oligopolies, and state architectured industries. As Shoshana Zuboff explains in "The Age of Surveillance Capitalism", the most highly valued companies in the world thrive upon an economic rationale built upon digitalization and an ever-expanding industrial infrastructure, where everything is deposited into data sets, surveyed, interpreted as behavioral data, and funneled through the supply chain's production facilities known as AI. Where is value created? Who captures the value? What authority reigns? The answers are self-evident. Simply look at the market cap of the largest ten largest companies, globally. What industry category dominates ?

AI: an accelerant of dispossession

Hannah Arendt writes in " The Origins of Totalitarianism" (1951) that we live not only with the outcome of the disintegration of the traditional nation-state (resulting from the pursuit of raw political power and disregard of material and utilitarian considerations), but in a world where societies are vulnerable to ideological seduction, filling the void created by "...the experience of not belonging to the world at all, which is the most radical and desperate experience of man."

Digital technology, whether social media or alchemical algorithms, drive the densest layers of neural networks that support predictive outcomes, nurturing divisive categorization. facial recognition, public square surveillance, natural language processing, AR, VR, blockchain and Web3, support a place to find a community and paradoxically an unrelenting accelerant of dispossession and loneliness.

The more we are consumed in and by digital worlds, the more cut off, the more non-belonging translates as seeing the world as more and more hostile, hopeless, deserving of our scorn, or worse. A tragic example: a US National Center study detailing increases in teenage depression and suicidal behavior over the past two decades coincides with the advent of social media. The World Health Organization details that suicide is the leading cause of death among adolescents (10-19) in low- and middle-income European countries, and the second leading cause in high-income countries. The statistics are coterminous with the average time spent online by this cohort: 7 hours/day. (Statista: January 2022)

Living in fantasy land

As described by social psychologist Jonathan Haidt in "The Righteous Mind", digital technology, particularly social media, diminishes a sense of participation, challenging what it means to be a citizen. We are not even required to inhabit the real world for we engage with our communities online. QAnon and the dark web are communities, writ large, of conspiracy fantasy; communities gifted with access to an alternate reality more powerful than actual life itself. How can we make sense of geopolitics and globalization if we acknowledge the appeal of a population that abhors "facts" and belief in anything visible, defining values and life itself according to the influence of ephemeral and fictive digital artifacts? Essentially, we are invisible, not only to others but to ourselves as we create fictional digital identities.

Conclusion

For the economist and political scientist evaluating the interrelated characteristics of industrial revolutions and geopolitics, the traditional disciplines focus on such pertinent issues as production, consumption, distribution of goods and services, and allocation of capital and human resources. These are valid standard assessments; however, they may ignore deeply psychological considerations, an existential ambiguity accompanying artificial intelligence's unrelenting force of change.

Consider 'geopolitical' issues as a philologist might well approach such an imposing term. The protean word "geopolitical" endures ongoing change in shape and proportion, influenced by historical circumstance. There is the traditional definition joining geography with politics; the postmodern usage in the sense that geopolitics is itself politics; a third perspective where any definition is lacking unless we include the critical sensibilities of science, technology (aka digitalization), finance, philosophy, sociology, aesthetics, and psychology. Essentially all social and natural sciences, as well as the humanities, are relevant in the pursuit of clarity.   This « sensibility » is not imaginary; it is put into practice, for example, in MIT's Science, Technology, and Society (STS) curriculum.

In using our understanding of artificial intelligence to revise the concept of geopolitics, consider that the study of science, especially for Europeans, includes philosophy, history, psychology as well as the natural sciences, for artificial intelligence does not think; at least not in the way "thinkers' think." The influence of AI and the all-encompassing technological age, challenges our pedagogy, challenges how we conceive our language, our imposition of geopolitical heuristics, and how we grasp dominion over the earth as well as our capacities for good and ill.

As we assess 21^{st} century geopolitics and the overriding industrial influences of our century - digital technology and artificial intelligence – consider Levi Strauss who maintained that in assessing modern economy, technology, and society, we are essentially mythmaking. Examining geopolitics in an era of AI is a way of explaining ourselves to ourselves.

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Business and civil society join forces for the social good: The case of the conversion therapy ban in the UK

Ken Chan*

ESCP Business School

Abstract

Companies should not ignore socio-political issues given the increased attention to environmental, social, and governance (ESG) imperatives by consumers, shareholders, and civil society. This paper discusses a recent example where business and civil society joined forces to tackle a discriminatory social policy issue, specifically, the UK government's decision to exclude gender identity from the conversion therapy ban. The policy led to criticism from LGBT organizations and resulted in their withdrawal from the government's global 'Safe To Be Me' conference. Businesses followed suit by refusing to sponsor the event – in essence becoming political actors. These actions by LGBT organizations and companies sent a strong political message to policymakers, resulting in the conference being cancelled. However, the actions did not trigger a policy reversal. This paper posits that companies could do more to advance this issue as part of their ESG agenda. When they join forces to champion progressive environmental and social issues, their collective voice can significantly influence and shape government policy-making for the better.

Keywords: Corporate Political Activity, Diversity, ESG, Inclusion, LGBT

*Global Executive PhD Candidate, ESCP Business School

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When business and civil society join forces to advance the social good, their capacity to influence ESG-friendly government policies is strengthened. This paper explores a recent example in the UK where LGBT organizations and companies were aligned on their responses to a problematic socio-political issue or, more specifically, conversion therapy.

The UK government announced in early 2022 its intention to partially ban conversion therapy, a longstanding practice condemned by LGBT communities and health experts. However, gender identity was excluded from the ban. This exclusion led to criticism from LGBT organizations and their subsequent withdrawal from the government's first global 'Safe To Be Me' conference. Companies followed suit by also refusing to take part in the event. The government eventually cancelled the conference due to the absence of key stakeholders, including businesses.

By refusing to participate in the high-profile government conference, business organizations sent a strong message to politicians about their haphazard policy on the partial conversion therapy ban. In so doing, they became political actors, whether by choice or by happenstance. Do they stop there? This paper discusses how companies can use their influence to advance inclusive social policies as part of their commitment to corporate social responsibility (CSR) and equity, diversity and inclusion (EDI) through corporate political activity.

The Example: Boycott of the 'Safe To Be Me' Conference

Conversion therapy is a practice aimed at changing a person's sexual orientation or gender identity. Stonewall, a leading LGBT advocacy organization in the UK, has been calling on central government to ban conversion therapy. LGBT advocates argue that conversion therapy stigmatizes LGBT people as it assumes they have a mental illness that needs to be cured. A report by Stonewall found that 5% of LGBT people in Britain had been pressured to undergo therapy to change their sexual orientation when accessing health services, while the number is four times higher for trans people (Stonewall, n.d.) Health organizations have long argued that conversion therapy is harmful and unethical. Over a dozen countries including Brazil, Canada, France, and Germany have banned conversion therapy. The UK government proposed banning conversion therapy only for sexual orientation, thereby excluding gender identity (BBC, 2022). LGBT organizations argue that the exclusion of gender identity from the conversion therapy ban is discriminatory and falls short of addressing the health concerns of the trans community.

In May 2021, the UK government announced the hosting of the 'Safe To Be Me' conference, "the largest event of its kind", which would take place in June 2022 to coincide with the 50th anniversary of London Pride. This global conference would focus on addressing discrimination and ensuring equal access to public services for LGBT people (Government of the United Kingdom, 2021). To signal their opposition to the government's exclusion of gender identity from the conversion therapy ban, over 100 other LGBT organizations signed a statement issued by Stonewall withdrawing from the conference (Consortium For Stronger LGBT+ Communities, n.d.). Their position was that a government which excludes trans people from the conversation therapy ban has no moral authority to host a global LGBT rights conference.

The conference provided the government with an opportunity to partner with business to improve global LGBT rights, and companies were invited to be sponsors. In return for their sponsorship, companies would be entitled to use the 'Safe To Be Me' branding in their marketing campaigns. Their financial support would also be amplified across government social media channels. The sponsorship marketing materials stated:

> We are looking for corporate sponsors who can lend their resources, commitment and expertise to making the conference a success, helping to deliver positive international action on LGBT+ rights. We are particularly interested in hearing from companies whose values are aligned with the themes of the conference and can demonstrate their commitment to championing LGBT+ equality and inclusion (Government of the United Kingdom, 2022).

Due to the controversy surrounding the conversion therapy ban policy, the UK government was unable to secure corporate sponsorships, with companies that included Vodafone, BP, Virgin Media, NBC Universal, and OVO Energy, refusing to sponsor the conference. LGBT organizations were not alone in criticizing the partial conversion therapy ban. For example, an OVO Energy spokesperson chastised the government's track record on trans issues and affirmed the company's commitment to stand with LGBT organizations on this matter (Hunte, 2022). The government suffered another setback when a high-profile LGBT leader resigned from its ranks because of the partial conversion therapy ban controversy. A private sector executive was appointed as the UK Government's LGBT Business Champion in 2021 to help drive equality and reduce discrimination in the workplace (Government of the United Kingdom, 2021). On the same day the LGBT Business Champion resigned, the UK Government announced it was cancelling the conference (Parry, 2022).

Continuing the Advocacy Journey

While the boycott led to the cancellation of the 'Safe To Be Me' conference, it has yet to result in a policy change. As LGBT organizations continue to advocate for the inclusion of gender identity in the conversion therapy ban, additional support by companies could propel the cause forward. In refusing to sponsor the conference, companies made a political statement on the issue. Companies can thus use their influence with politicians to lobby for the extension of the conversion therapy ban to trans people. This show of further support for LGBT people, including their employees, customers, and shareholders, is consistent with their EDI priorities and commitment to ESG principles.

Social policy has traditionally not been a focus for companies, unlike economic and regulatory policies that can negatively impact business operations, competitive advantage, and profit margins. However, a commitment to ESG principles means companies need to reframe their geopolitical engagement. For example, companies that market themselves as LGBT-friendly but fail to stand up against discriminatory practices affecting this community may have their motives questioned (Chan, 2021). While companies, especially those that are politically dependent, have a vested interest in maintaining good relations with governments, they need to consider the potential impact when public policy collides with stakeholder interests and ESG values. It is thus extremely important to strike the right balance.

To go back to the 'Safe To Be Me' example, when presented with an opportunity to support a signature government initiative that is also aligned with a company's CSR and EDI priorities, we can quickly see the benefits of signing on. Despite the best of intentions, however, sponsoring the conference would have been tone-deaf and sent the message to trans employees, customers, and shareholders that they are not valued. Companies would have faced justifiable criticism from LGBT organizations in view of their public stance on the issue. Further, the use of the 'Safe To Be Me' branding would have created reputation issues for the companies due to the controversy.

Companies must consider how their decision could be perceived. Did they refuse to sponsor the conference because of their genuine commitment to LGBT rights or because of the need to avoid damaging their reputation with the LGBT market? What they do next can provide clarity to the LGBT community regarding their motives.

As companies already invest significantly in corporate political activity, they could use their influence and resources to advocate for inclusive policies as part of their EDI and corporate social responsibility initiatives (Chan, 2021). Government relations experts could collaborate with their EDI colleagues to develop a strategy on how to address this issue with policymakers. For example, companies can make the case for inclusion, anti-discrimination, and health equity for LGBT people, including their own employees and customers. Further, the funds that would have otherwise gone to supporting the 'Safe To Be Me' conference could be diverted to LGBT organizations to help with their advocacy campaigns.

There is precedence for corporate political involvement in support of the LGBT community. For example, over 500 major companies in the US are members of the Business Coalition for the Equality Act, a group advocating for federal legislation that advances legal protections for LGBT people (Human Rights Campaign Foundation, 2022). A similar approach could be taken in the UK, where businesses proactively work with LGBT organizations to advocate for the inclusion of gender identity in the conversion therapy ban.

Conclusion

Given the enhanced focus on environmental, social, and governance (ESG) imperatives by consumers, shareholders, and civil society, companies cannot turn a blind eye to socio-political issues. The example in this paper highlights how the parallel but complementary actions taken by business and civil society sent a strong message to government that discriminatory policies are unacceptable. There is a growing list of government policies in many countries that are hostile to LGBT people. Companies can thus use their economic clout to champion equality for LGBT people. While there are those who criticize corporate involvement in social policy, the commitments made by companies to EDI initiatives and ESG principles provide them with a strong incentive to stand up against discriminatory policies.

This issue is one example that showcases the potential for social good when business and civil society work together to advance the ESG agenda. When they join forces to champion progressive environmental and social issues, their collective voice can truly influence and shape government policymaking for the better.

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Uncompensated risks: Russian invasion of Ukraine and the impact on state-owned investors' ownership of commercial real estate in gateway cities of Europe

Aaron H. Kim*

ESCP Business School

Abstract

Commercial real estate (CRE) in the gateway cities of Europe represents one of the largest investment categories, which in turn attracts one of the largest real estate investors, namely, state-owned investors (SOIs), The notion of real estate being a safe asset class is now being called into question, especially in light of geopolitical risk stemming from the Ukraine conflict and associated known risks such as market risks and operational risks. One such operational risk is the absence of an appropriate appraisal methodology and thus the invisibility of fair market value. In addition, there are unknown risks that are unique to SOIs such as foreign policy and national security objectives that can interfere with timely commercial decision-making. The Ukraine conflict magnifies all known risks, especially SOIs' lack of control of risk management visibility due to conventional appraisal methods that only indicate a theoretical estimation, when in reality the value at risk includes total loss due to the theoretical expansion of kinetic military actions. This article sheds light on SOIs' risk exposure during the prevailing Ukraine invasion.

Keywords: geopoliticalrisk; state-owned investors; real estate investment; appraisal methods; foreign policy

*Global Executive PhD Candidate, ESCP Business School

Uncompensated Risks: The Russian invasion of Ukraine and the impact on state-owned investors' ownership of commercial real estate in gateway cities of Europe

The Sense of Safe Assets – "a fallacy"?

On March 7th, 2022, Ukraine's Minister of Finance, Sergii Marchenko, sent a Letter of Intent to the International Monetary Fund seeking financial assistance for his country to offset the economic impact of the Russian invasion (Marchenko & Shevchenko, 2022), As was widely expected following the war rhetoric leading up to the actual invasion, all risk measurement indicators such as VIX shot up sharply after February 24th. The Ukraine geopolitical risk Index (GPR), a country-specific GPR index, had risen to 9% by early March. The GPR index is informed by a geopolitical text search and its frequency in 15 English-speaking newspapers (Caldara & Iacoviello, 2018). A geopolitical risk spike has a lasting impact on economic activities and investment. However, despite the rise in the GPR index and shifting global macroeconomic indicators, real estate has seen little change either in price or investment flow, although this may in part be related to the lagging nature of the industry.

Ukraine's conflict has global macro-economic implications. It is one of the largest producers of agricultural commodities - from wheat to various types of seed oil which are being held back, causing supply chain disruptions. Futures contracts have priced in the volatility. Rising energy prices such as crude oil and gas have a direct impact on manufacturers, especially in the Eurozone, leading to growing inflation even after GDP is expected to slow. Before the Ukraine conflict, the Eurozone inflation rate had risen to 5%. Despite the Ukraine conflict, on March 10, the ECB set a more hawkish-than-expected narrative on monetary policy (Holz, 2022). At the point of writing, Eurozone inflation is at 7.5%. Capital Economics expects a first rate hike of 25 bps in December with two further hikes in 2023 (Holz, 2022).

Rising policy rates are unfavorable to real estate investment for several reasons. They not only impact financing costs, but also valuation. Discount rates, which are derived from the cost of funding, have greater gearing in discounting the underlying operating asset's cash flow streams, ultimately curbing performance while increasing risk. This in turn has an impact on the yield landscape and thus on allocations into a critical real estate investment strategy or avoidance of real estate overall in favor of another asset class. A natural outcome is a flight to safety where capital is allocated to other regional markets in which the risk-reward balance tilts toward reward. Spread between the German Prime offices (core) and the 10-year German government bond (Bund), yields are the lowest they have been in 8 years. The real effects of war on fixed real estate transactions lag due to the lengthy origination process - a vital part of real estate sales (Leahy et al., 2022). €20 billion has been invested by non-Eurozone investors in Q12022, but this is likely to slow down. As seen in the volume of forwarding sales, an indicator of investor confidence in the future outlook for all real estate types reached €10 billion, dropping from €40 billion for the same quarter in the previous year (Leahy et al., 2022). Western-backed sanctions on Russia are expected to have a minimal impact on Europe's real-estate market given that its average size was just $330 million a year (Leahy et al., 2022). Central and Eastern Europe (CEE) accounted for 5.3% of all European transaction volume for the same quarter (Leahy et al., 2022). Poland, a neighbor of Ukraine, saw a capital inflow of €1.66 billion in Q1 this year, with a significant majority from non-domestic investors (Doyle et al., 2022).

Even to a casual observer, the paradox between the economic downturn and capital inflow into the European CRE markets despite the rising GPR environment is apparent. Unlike stocks or bonds where the sentiment of fear and risk is instantly priced in, GPR is not part of the valuation matrix in fixed real estate. Real estate appraisal practice does not truly reflect the prevailing reality, especially when the value is at risk and even the chance of total loss stemming from kinetic war activities is remote but realistic. This does not affect CRE valuation movements. A case in point is during the 9/11 attacks on the World Trade Center, when both rental rates and absorption rates, reflecting real-estate demand, declined by 22% in downtown Manhattan compared to midtown, while the absorption rate fell by 4.98% after the terror incidents (Miceli, 2014). When it comes to prolonged armed conflicts and their impact on urban real estate, we need look no further than the state of Israel. During the Second Palestinian Intifada, Gilo, a neighborhood in East Jerusalem, came under gunfire attacks. This resulted in a substantial downfall in housing prices that lasted for up to two years before prices began to normalize (Arbel et al., 2010). The same study showed that after a 10%-12% downfall in housing prices 6 months after the one-period shooting events, 18 months were needed to fully recover (Arbel et al., 2010). In simulated prolonged gun violence, a 17% decline was evidenced 10 months after the initial outbreak, extending the price erosion for 14 months. Even though this study was done on residential housing prices, it illustrates the effect of kinetic military action involving active warfare, including lethal force on residential properties. In commercial real estate (CRE), the issue lies mainly with appraisal practice since the sales comparison approach, a real estate appraisal method that compares one property with comparable or other recently sold properties in the area with similar characteristics, says little about the value during the holding period. In a sales comparison appraisal method, pricing occurs at closure. In the absence of mark-to-market pricing, holders of CRE such as SOIs do not have visibility over unrealized capital gain or loss during the entire holding period (Fisher, 2005). The Ukraine conflict reminds us of the stark reality of total loss of properties, and how valuation must account for a realistic value for risk management purposes, an essential aspect of SOI operations.

State-Owned Investors' challenges

To clarify, SOIs are classified as government-owned entities that invest their capital overseas. This definition includes various forms of legal structure and types of entity including Sovereign Wealth Funds (SWFs) and Public Pension Funds (PPFs) (López & Brett, 2022). SOIs are the largest investors with current Assets Under Management (AUM) of US$ 32 trillion worldwide. This is expected to grow to US$53.7 trillion by 2030 (López & Brett, 2022). The main challenge with SWFs is the sheer size of the operations. While asset allocation for real estate investment has remained mostly unchanged, AUM has increased significantly in the most recent five-year period. For instance, while allocations into total real estate investment remained static at 6% from 2016 to 2021, in the same time period, AUM grew from

$7.5 trillion to $ 10.5 trillion. A similar situation is true for PPFs AUM which grew from $14.5 trillion to $21.4 trillion, while allocations grew from 6% to 7% (López & Brett, 2022). As 77% of SWFs currently allocate up to 9.9% of their AUM in real estate, 93% of all SOIs have a target allocation of between 5% and 14.9%. At regional level, 90% of North America-based SWFs invest in real estate, while this figure is 76% in Asia, the Middle East, and North Africa (Laren Mason et al., 2015). In a world of finite high-quality properties of institutional quality, the growing AUM of SOIs means increasing real estate allocation, which in turn presents SOIs with a number of challenges. Allocation pressure requires a constant stream of deal origination and thus price competition as there are many big guys chasing after a limited number of good deals. This in turn leads smaller players to shoulder more risk in the form of greater leverage and credit facilities just to participate in the same deal, although the market will consolidate in the long run.

With the emergence of behemoth investors, there are looming and unforeseen issues aside from macro-economic forces and real estate market dynamics. Extended geopolitical tension may bring to the surface issues that are unique to SOIs, such as operational issues, management issues, and foreign policy and national security interest issues.

Motivated by factors at home such as policy changes and an overcrowded domestic property market, investors are attracted to cross-border investments in order to diversify their investment portfolio, but also find attractive returns elsewhere (Devaney et al., 2019). In an institutional cross-border investment, the country of origin places considerable importance on identifying target assets and their classification (Devaney et al., 2019). International investors prefer gateways cities, Central Business Districts (CBD), and prime office towers. Then there is also the pull of following investment trends (Devaney et al., 2019). While it may not constitute an exhaustive list of investment objectives, this anecdotal observation is plausible as real estate transactions rely on an ecosystem of professional service providers from transactional broker agents to lawyers, appraisers, and accountants. To an international investor, especially for a new market entrant, convenience is as important as transaction cost. Gateway cities have that convenience factor, and because of options in terms of price competition between professional service providers, prices tend to be fair. Gateway cities have an implied reduced liquidity risk due to a higher absorption rate, low vacancy rate, and an active local economy. For CBD office towers with master leases in place, there tends to be a concentration of investment holdings of SOIs as they want to hold long-term assets, both for profit and the income generated by the underlying asset.

An additional important aspect that limits SOIs' flexibility in real estate investment is locality. Local markets are dominated by local dynamics that shape the market, including property history, local tax laws, and real estate regulations. Not all SOIs can establish an onsite presence while competing in deal sourcing, making it impossible to obtain total control of the process from deal sourcing to deal management. However, ownership of all pieces of this real estate lifecycle is associated with high costs (Nam, 2014). These are operational issues that many SOIs face in their internal management and operations when considering cross-border investments.

Korean SOIs, for example, such as National Pension Services (NPS), the Korean Investment Corporation (KIC), Military Mutual Aid and Association, and others make up the world's largest investment syndication. In the case of Korean SOIs, beyond the portfolio benefits from a higher sharp ratio and higher risk-adjusted real estate returns, their main concerns are with real estate risk management, valuation, and accounting practices. Given the two separate components of income gained from the asset's cashflows and capital gains during the holding period of such an asset, a clear estimation of the perceived value or fair value versus book value is arbitrary, and regulators allow the use of book value for all alternative asset classes (Nam, 2014).

Another operational issue is remuneration and talent retention within SOIs. This is a well-published operational issue at NPS. While the base salary of a government employee remains low compared to the private sector, NPS managers' remuneration is linked to Key Performance Indicators (KPI). From a managerial perspective, fund managers' KPIs are measured according to short-term performance, which is immediate, and tangible. The nature of real estate involves long-term investment, however, and is therefore ambiguous when giving credit for KPI performance (Nam, 2014). Furthermore, investors are deterred from real estate investments as real estate appraisal methods lack accurate information and the market value is therefore merely an estimation, a significant issue with respect to portfolio risk management (Nam, 2014).

Perhaps the most extraneous and overlooked problem of SOIs investing in European real estate is foreign policy. This includes the perception of national security risk by the recipient country and leveraging the influence of SWFs for economic policymaking. In an open society with liberal markets, attempting to co-ordinate anti-protectionism is a key issue that arises in recipient countries when vital infrastructure assets or even a landmark trophy property of national importance is acquired by an SWF. The perception of SWFs is that they either pursue an overt objective or are tacit in their investment pursuits (Cohen, 2009). This intervenes in investment goals to the benefit of foreign policy goals. Some market analysts and regulators even fear that SWFs have enough leverage to shift power from developed industrial nations to more authoritarian or capitalist governments in the developing world (Drezner, 2008). Top-down government interventions into SOIs' investment decisions to hold or to divest may include seizing assets, government-imposed sanctions, or an embargo on repatriation of gains. These all form part of the arsenal of risks specifically associated with SOIs, which naturally tilt back the advantages of real estate investments' risk-adjusted return.

Conclusion and Future Research Avenues

SOIs are government-tied investors comprising SWFs and PPFs. Their AUM has grown significantly, making them the largest investors in real estate globally, especially in Europe. The unfolding of the Ukraine conflict presents SOIs with known and unknown risks. Known risks encompass geopolitics, macro-economic and investment management, and operational risks - all aspects of internal management. Opaque and estimation-prone appraisal methods not only lack the up-to-date information needed for dutiful reporting on asset performance but also hinder a crystal-clear overview of total portfolio risk management involving multiple asset classes. At a time of rising geopolitical risk, prevailing kinetic war activities not only have a reverse effect on commercial activities but also on asset pricing and risk management. With the few owning the most, SOIs' growth in AUM and allocation into the real estate asset class will make SOIs significant players, but also the greatest bearers of systemic risk concentration. The role of foreign policy and national security interests and the implications of SOIs' investment objectives represent another interdisciplinary field where further investigation could provide several opportunities for academic contributions.

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Putin's Invasion of Ukraine and its Geo-Economic Consequences

Jörg Himmelreich*

ESCP Business School

Abstract

Putin's invasion of Ukraine will trigger a new type of Cold War situation for decades to come, with a new kind of Iron Curtain falling in a once again bi-polarized world between Western democracies and autocracies in Russia and China. This has already had, and will continue to have, far-reaching consequences for the global markets and global trade. The delivery of natural and mineral resources and food has become a currency of power in this global conflict accompanied by trade sanctions and protectionist economic policies. De-globalisation worldwide looks likely to be the geo-economic consequence.

Diversification, friend-shoring, and abandoning the fixation of profit as the exclusive goal of business should more than ever be the guiding principles for Western states and companies to protect their vulnerable supply chains in times of long-term global economic turmoil.

Keywords: Putin, global polarization, geo-economics, diversification, friend shoring

*Ph.D. Student, ESCP Business School

Putin's invasion of Ukraine marked a unique turning point in history

The following considerations aim to demonstrate the extent to which Putin's war in Ukraine will ultimately lead to worldwide de-globalisation, forcing companies to protect their vulnerable and sensitive supply chains.

Putin's invasion into Ukraine on February 24th, 2022, marked a unique turning point in history. It is the largest war in Europe since World War II, destroying the building blocks of peace in Europe that were established by public international agreements with the former U.S.S.R., like the Helsinki Accords in 1975 which guaranteed the inviolability of state borders, signed by 35 states including the U.S.S.R.; the Paris Charter of 1990, the Budapest Memorandum of 1994, when Russia, the U.S., France, and the UK guaranteed the territorial integrity and sovereignty of Ukraine, and the UN-Charter's prohibition of the use of force.

1. A scenario for future global international relations

As difficult as it is to foresee how this war will play out in military terms and how it will end, it seems fairly likely that the political, economic, and military confrontation will continue, even if in varying degrees of intensity.

As a result, we are likely to see, at least in the next 15-20 years (Putin is constitutionally entitled to stay in office until 2036), an ongoing fundamental conflict with Russia, alternating between more aggressive and more cold war periods. Putin cannot give up his objective to annex and occupy the whole of Ukraine. And even this will not satisfy the imperial goals of his future long-term strategy. Only recently he compared himself to Tsar Peter the Great who retook Sweden for the Russian empire following the Nordic war which lasted 20 years. Even if Putin might eventually offer an armistice, it would have to be considered as simply a pause in the war to give him time to replenish his military and personal resources. When his military, personal, economic, and financial resources allow, he might eventually attack other regions of the former USSR empire, such as Georgia and Moldova, or even the Baltic states. Putin is driven by a century-old political culture of Russian imperialism and the notion of the superiority of the chosen Russian people above all others, with Moscow being the "Third Rome", assigned to defend the true values of mankind against the decadence of the West which, as a permanent foe of Russia, does everything in its power to try to destroy Russia's greatness and its orthodox mission.[36] Even without the deep influence of state propaganda on the mindset of the Russian people, there is strong support for this political and orthodox notion of the Great Russia by the majority of Russians. That is why, in principle, this Russian imperialism and proselytization drive will not end with Putin's departure. Both are deeply engraved in the Russian self-identity. The former U.S.S.R. basically followed the same principles, where the ideology of communism was only a temporary replacement for orthodox proselytization in the long Russian history. When communism replaced the orthodox faith as an ideology,

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[36] Walter Laqueur, Putinism: Russia and its Future with the West, New York 2015, p.91.

it only served as the other side of the same coin to legitimize autocratic governance and imperialistic expansionism.

As a result, we are going to see a relatively fundamental long-term conflict between Russia and the West (the EU and NATO) in Central Europe, with an "Iron-Curtain"-like division between both, although this conflict differs in many regards from that of the Cold War (1945–1989).

Major international stakeholders will not decisively join the Western camp but will pursue their own national agendas as far as possible. Following its usual non-alignment policy to stay on good terms with Russia, India, for example, will do everything possible to avoid getting involved in the conflict. China will support Russia, at least outwardly, and might even profit economically from the conflict and any potential future gas and oil embargos by the EU. We are likely to arrive at a more global conflict in the near future between two somewhat polarized blocks, in other words, between autocracies and democracies, which will differ from the ideological confrontation between communism and liberal democracies with global free markets during the cold war. Many states like India and others will probably once again manoeuvre between both blocks as in Cold War times.

2. Geo-economic consequences

What does this scenario of international political relations mean for international trade and the global supply chains of Western international companies? More than ever, economic globalization will be burdened by this conflict. Economic trade and finance, the global availability of resources like gas, oil, rare metals, and food such as wheat, have become a currency of power, more so than ever before. Thus, existing trends in trade protectionism and economic sanctions will accelerate and continue to undermine the principles of free trade and GATT. The original idea that an increasingly interconnected global economy, trade, and global business will lead to a more peaceful, harmonious world order has failed.[37] The underlying theoretical assumption that states with close trade relations would not wage war against one another has been disproved by the political reality. We are already seeing the beginning of "de-globalisation"[38] as a new era turns away from the former acceleration of globalisation. According to a recent survey, 46% of German companies receive significant inputs from China, and of those, almost half are planning to reduce their dependency on the country. [39] The German Minister of Economic and Climate Policy, Robert Habeck, did not extend the German state

[37] This theory was already once disapproved by the political reality in the decade before the First World War, when improving trade relations between Great Britain and the German Reich under Wilhelm I did not prevent both from becoming enemies in the First World War. Cf. Charles Kupchan, How Enemies Become Friends – Sources of Stable Peace, Princeton 2010, pp.187.

[38] "Das Ende der Globalisierung, wie wir sie kennen" (The end of globalisation as we know it), Frankfurter Allgemeine Zeitung, 27.05.2022.

[39] Baur, A. and Flach, L. (2022), "Deutsch-chinesische Handelsbeziehungen: Wie abhängig ist Deutschland vom Reich der Mitte?", (German-Chinese Trade Relations: How dependant is Germany on the Middle Empire", ifo Schnelldienst, No 4, 31 March.

guarantee for VW investments in China's Uigure province.[40] Instead, VW's top management recently announced an investment offensive in the U.S., framed as "strategic resilience". [41]

As the politically driven reduction in European gas, oil, and coal imports from Russia have become Putin's currency of power in the conflict, European states and companies are being forced to look rapidly for alternative energy delivery partners outside of Russia, together with alternative energy resources. The new push for the production of alternative, non-fossil energies in general will trigger a run on metals like lithium, zinc, nickel, copper, and cobalt, all needed for batteries, electric cars, solar panels, and electricity grids. These metals are mainly found in a few autocratic states: China was estimated to control over half of the global rare earths mining capacity in 2020, and 85% of rare earth refining[42], while Congo-Kinshasa controls 70% of cobalt. according to the International Energy Agency (IEA), this will, to some extent, shift the West's fossil energy dependence from Russia to dependence on such metals from other autocratic regimes.[43] To what extent these states will use such dependencies as a currency of power, like Russia today, remains to be seen. In addition, according to the European Commission, imports for 34 products that Europe relies on are highly exposed to supply chain disruption given their low potential for diversification and substitution inside the Union. [44]

3. Conclusion

This fundamentally new political and economic situation of global markets and trade will present international companies with profound challenges for decades to come. The global economy and international trade and supply chains have become and will remain far more politicized, if not militarized, as currencies of power.

Thus, Western states and companies need to be far more aware of their import dependencies than in the past. To avoid again falling into an import trap in their trade relations by becoming over-dependant on imports of resources from autocratic states, the trade policy of Western companies must become: diversification, diversification, diversification![45], diversifying both global trade partners and global supply chains. Like many other companies, BASF, the German chemical industry giant, blindly ignored the state of Putin's policies and naively went along with Putin's gas trap. Now BASF has to write off all of its Russia investments, with investment in Nord Stream 2 alone worth 1 bn euros.
Many other leading Western companies (MacDonalds, BP, et al.) have had to shut down and write off their production in Russia and are leaving their investments to the Russian state.

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[40] "Habeck verweigert VW-Garantie für China-Geschäft" (Habeck refuses to grant a federal German state guarantee to VW for its China business), Deutsche Welle 28.5.2022.

[41] "Volkswagen prepares for a de-globalized world", Wall Street Journal, March 27, 2022.

[42] The White House (2021), "Building resilient supply chains, revitalizing American manufacturing, and fostering broad-based growth", June 2021.

[43] The Role of Critical Minerals in Clean Energy Transitions, International Energy Agency, Flagship report — May 2021.

[44] European Commission (2021), Strategic dependencies and capacities, Commission Staff Working Document, 5 May 2021.

[45] Christiane Lagarde, A new global map: European resilience in a changing world, Keynote speech by Christine Lagarde, President of the ECB, at the Peterson Institute for International Economics, Washington, D.C., 22 April 2022.

In addition to this business policy, it would be wise and more secure for Western companies to trade with states and their companies that adopt a mutually comparable set of fundamental values and norms. Friend shoring means the commitment to work with countries that "have strong adherence to a set of norms and values about how to operate in the global economy and about how to run the global economic system", as U.S. Treasury Secretary Yellen recently argued.[46] "Globalisation is out, friend shoring is in" is the talking point in Western financial institutions. As a consequence, it is crucial to realize that profit alone should not be the only goal of Western companies. "Freedom is more important than free trade. The protection of our values is more important than profit," as NATO General Secretary, Jens Stoltenberg, said at the World Economic Forum in Davos.[47]

Following these three principles – diversification, friend-shoring, and abandoning the fixation on profit as the exclusive business goal –, Western companies could find themselves better prepared to stabilize their trade relations and supply chains in times of de-globalisation and geo-economic turmoil.

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The changing geopolitical landscape adds to the complexity of the Global sustainability agenda

Wioletta Nawrot

ESCP Business School

Tomasz Walkowicz

Abstract

Russia's invasion of Ukraine and its geopolitical impact have created new challenges that need to be confronted by policymakers in different countries across the world. They include securing the continuity of energy supplies by importing countries, addressing the effects of interruptions to the global food supply chain, and implementing measures to counteract the cost of living crisis and economic slowdown. The challenges are significant and have the potential to undermine the global sustainability agenda. We also see a risk that in order to ensure the continuity of energy supplies, some countries may have no choice but to undertake actions reversing progress towards net zero achieved to date through new investments in 'dirty' fuels.

At the same time, the recent UN IPCC report leaves no reasonable doubt that the climate agenda should not be delayed if the world is to avoid a humanitarian crisis on an unprecedented scale. In the present circumstances, the threats to implementation of the global sustainability agenda cannot easily be neutralised in the short run. At the same time, it remains critical that policymakers across the globe remain committed to the pro-environment agenda. This paper discusses some optimal solutions that can help respond to the new threats that have emerged as a result of the war in Ukraine and are compliant with the environmental agenda. The measures include increasing the role of nuclear power, a focus on initiatives to reduce the use of energy, continued investment in renewable energy technologies, and rethinking taxation of energy producers.

Keywords: UN IPCC, global sustainability agenda, net-zero target, war in Ukraine

The Changing Geopolitical Landscape Adds to the Complexity of the Global Sustainability Agenda

New global threats could push climate protection down the policymakers' agenda

The invasion of Ukraine by Russia and the subsequent sanctions imposed by the West have created significant new challenges that need to be addressed by policymakers in many different countries across the world. These challenges have the potential to seriously undermine the global sustainability agenda.

An immediate challenge arising from Russia's invasion of Ukraine is securing energy supplies by energy-importing countries dependent on Russian oil and gas. The continuity of energy provision, a core factor in sustaining the economies and industries of energy-importer countries, has been called into question by the inclusion of Russian oil and coal in the sanctions packages, and Russia's retaliatory actions, casting doubt on its continued provision of fossil fuels.

Russia and Ukraine are among the world's largest food exporters, accounting for close to a third of global wheat and barley exports. The war between the two countries has critically hampered supplies, contributing to a substantial rise in many food commodity prices observed in 2022. The extension of the conflict represents a threat to the global food supply system in the medium term. According to the World Bank, the price of food commodities is likely to remain at very high levels until at least 2024. As the main Ukrainian seaports are under Russian occupation and Russia appears to be deliberately blocking food exports from both countries, many developing nations, including 60 of the least developed countries in Africa, face the risk of an interruption of food supplies, which in extreme circumstances could lead to famine.

The Covid-19 pandemic has substantially weakened several sectors of the global economy and led to a strain on public finances in the majority of governments. Following a recovery in 2021, the conflict in Ukraine has triggered a further challenging period for the global economy, raising the prospect of a major slowdown and rising inflation. The main impact of the conflict on the global economy is channelled through the energy, metals, and food commodity markets, where supply constraints have led to a surge in prices. This in turn has generated a cost-of-living crisis, putting pressure on low-income households in particular. In the corporate sector, the economic slowdown combined with a rise in the cost of credit is likely to weaken business investment and could lead to an increase in corporate defaults. The impact of the Russian invasion of Ukraine is even more visible in emerging countries due to substantial capital outflows to safe heavens, putting additional pressure on their currencies and increasing the risk of problems in servicing their debt.

The cost-of-living crisis has already forced governments in various countries to introduce measures aimed at mitigating the impact of energy and food inflation on poorer segments of the population. In May 2022, the G7 Presidency and the World Bank Group created the Global Alliance for Food Security in a bid to prevent the unfolding food shortage crisis.

Despite various actions pursued at international and national level, we see a risk that the measures fail to substantially offset increases in food and energy prices, especially since public indebtedness has been substantially stretched by the COVID-19 pandemic. Consequently, there is also a risk of social unrest.

While far from comprehensive, the above list of serious threats faced by governments worldwide means there is a substantial danger that actions aimed at achieving the climate protection goals set under the Paris Agreement slip down the policymakers' agenda.

Risk of dwindling progress towards net zero

We see a risk that policymakers, in order to assure the security of energy supplies, might have no choice but to undertake actions reversing the progress towards net zero achieved to date. More specifically, countries most exposed to energy shortages might be forced to accept contracts for supplies of dirty fossil fuels, expanding their harmful impact on the environment. Another concern is that, as part of the reduced dependence on Russian oil and gas, fossil fuel producers in other countries might increase investment in the extraction capacity of dirty fuels. Such actions could directly reverse the progress made in emission reductions towards the targets set out in the Paris Agreement. In just one such example, the 'Jackdaw' project, rejected by oil and gas regulators in 2021 on environmental grounds, but approved by the UK government in 2022, is expected to account for 6.5% of total gas output from the UK North Sea from 2025.

We also see a risk that global coordination actions in favour of climate protection and realisation of the Paris Agreement goals could be weakened by growing hostilities between some of the major global powers over the Ukraine conflict, and growing tensions around Taiwan. Achievement of the net zero targets by the world is conditional on the coordinated implementation of pro-climate policies by the US, the EU, China, and other leading world economies. Withdrawal from the coordinated global effort towards achieving net zero by any leading economy would lead to failure in the fight against climate change.

Combining the environmental agenda with the response to new threats

While Russia's invasion of Ukraine has created new threats to the global environmental agenda, the latest UN Intergovernmental Panel on Climate Change (UN IPCC) report warns that the climate has been changing more rapidly than anticipated, and that the effects of interference to the global climate system are more worrying than previously thought. According to the UN IPCC, failure to adopt the strict and far-reaching recommended climate policies in a very timely manner will backfire, resulting in a humanitarian crisis on an unprecedented scale that will lead to massive loss of human lives, famine, and immense material losses as a result of extreme weather conditions, to list but a few of the predicted outcomes. The UN IPCC report leaves no doubt that the window for coordinated global action to stabilise the climate is closing fast, and that any delay will be detrimental to the planet.

In the present circumstances, the threats to implementation of the global sustainability agenda cannot be easily neutralised in the short run. At the same time, it remains critical that policymakers worldwide remain committed to the goals of the Paris Agreement. Consequently, it is of utmost importance to find practical solutions that can address both pressing matters simultaneously: i.e., the effects of the current geopolitical tensions and the requirements of the global sustainability agenda, searching for synergies where achievable. Several courses of action seem appropriate for international organisations, governments, businesses, and societies.

While not without risk, **reinstating the nuclear power agenda** could help to address potential issues, with the continuity of energy supplies in the near to medium term without resorting to a build-up of additional dirty fossil fuel capacity. This would require the return of several reactors in the EU that need maintenance and safety checks to ensure safe operations. The delayed closure of operations in a few other reactors such that the plants' safe operations are ensured would also help to address energy shortages.

For some time now, the International Energy Agency (IEA) has been advocating an increase in the role of nuclear power in the global energy mix so as to facilitate the transition to net-zero targets. However, some policymakers and non-governmental organisations have opposed this solution. In the face of a major disruption of the global energy market in the aftermath of Russia's invasion of Ukraine, other stakeholders might decide to reconsider their opposition to the nuclear power option. Globally, R&D is making constant progress towards new nuclear reactor technologies that use closed fuel cycles or self-breeding fuel concepts that minimise the production of high-level radioactive waste ('Generation IV reactors'). These reactors have the potential to substantially contribute to the goal of decarbonising the planet and can significantly support the global climate agenda, while remaining operationally safer than previous generations.

The benefits of nuclear power have recently been acknowledged by the EU that sees it as *part of the future energy sources in a number of Member States,* and *as part of their decarbonisation efforts.*[48] Consequently, the EU has finalised its position on nuclear power in the sustainable finance taxonomy, a guide to governments, businesses, and investors in the area of green investments. The Taxonomy includes climate neutral and renewable investment, although it also allows other economic activities that could, under strict conditions and for a limited time, facilitate the transition towards a sustainable energy system, nuclear power being one of these. The Commission Delegated Regulation of 9.03.2022 provided the legal basis to link nuclear power with sustainability and net-zero targets.

According to various expert forecasts, high energy prices could remain a burden, adversely impacting households and businesses in the medium term. In such an environment, awareness campaigns could help to **reduce the consumption of fossil fuels**.

[48] Commission Delegated Regulation of 9.03.2022 amending Delegated Regulation (EU) 2021/2139 as regards economic activities in certain energy sectors and Delegated Regulation (EU) 2021/2178 as regards specific public disclosures for those economic activities, C/2022/0631, par. 10.

Periods of energy shortages and rising energy prices send a signal to consumers and businesses that it is judicious to cut down on their use as long as it does not impact on basic needs. Russia's invasion of Ukraine added an ethical reason for reducing energy consumption, based on awareness that use of Russian oil or gas helps to finance the Russian war machine.

One example of an awareness-raising initiative advocating the reduction of energy consumption is the nine-point plan entitled '*Playing My Part: How to save money, reduce reliance on Russian energy, support Ukraine and help the planet*', issued in April 2022 by the EU in collaboration with the IEA. The campaign urges citizens to drive less and to use vehicles more economically, to use public transport, prioritise trains instead of planes, and work from home in order to reduce energy consumption[49].

Obviously, this helps to address energy shortages caused by Russia's invasion of Ukraine as well as the climate agenda, but other similar awareness actions are needed worldwide if it is to have a significant impact. These need to be taken at local level to reach a wider public.

Maintaining **incentives for investment in renewable energy** development remains hugely important in terms of the environmental agenda. Before Russia's invasion of Ukraine, the IEA highlighted four key measures that can help us reach the targets recommended by the UN IPCC: (1) a massive additional push for clean electrification; (2) significant boost to clean energy innovation; (3) continued emphasis on energy efficiency; and (4) a strong drive to cut methane emissions from fossil fuel operations[50]. To account for the drastic changes in the geopolitical landscape following Russia's attack on Ukraine, these measures need to be stepped up even more.

While the problem of energy shortages is unlikely to be resolved in the near future through additional investment in green energy, the present geopolitical tensions, which underscore our dependence on fossil fuels, could be used as a tailwind to reenergise the renewable energy development agenda. Consequently, a growing consensus that dependence on Russian energy should be reduced represents a window of opportunity to advance the transition to green energy. Governments must step up their support for green energy industries and some of such actions have been taken in recent months. One example is easing of a trade dispute by the Biden administration through allowing tariff-free imports of components for US solar installations from some Asian producers. Another significant step taken by the US policymakers has been to invoke the Defense Production Act to boost the US solar panel manufacturing.

Accelerating the green energy agenda could help to dynamize economic growth in many countries during the upcoming slowdown, helping to improve social support for the climate agenda as result. In order to overcome the challenges linked to the

[49] 'Playing My Part: How to save money, reduce reliance on Russian energy, support Ukraine and help the planet, EU and IEA, April 2022, https://www.iea.org/reports/playing-my-part.

[50] The World Energy Outlook 2021, IEA, October 2021, https://www.iea.org/reports/world-energy-outlook-2021.

availability of public finance that has been weakened by the COVID-19 crisis, funding for investment in the green energy sector could benefit from closer collaboration between the public and private sector and cross-country initiatives.

The high price of energy, underpinned by Russia's invasion of Ukraine and by the subsequent economic sanctions, boosted the profits generated by energy producers. Governments across the globe should carefully consider changes to taxation on energy producers (such as windfall taxes). While these have the potential to bolster government finances, they could also undermine energy producers' investments. In order to maintain the sustainability agenda, governments need to create a **fairer burden-sharing** system through taxation by giving producers the incentive to invest in carbon removal technologies and changing the fuel mix in favour of renewable energy.

As the UN IPCC considers carbon removal as a key part of the climate agenda, involving energy producers in the process would be highly beneficial. Recent research from the Universities of Oxford and Edinburgh proposed a 'carbon takeback obligation' to prevent the fossil fuels industry from contributing to global warming. Since their activities generate a considerable amount of carbon dioxide, fossil fuel extractors and importers would be required to dispose of a gradually rising percentage of CO^2 both safely and permanently. According to this proposal, the percentage in question would need to increase to 100% by 2050[51].

We believe that incentivising investment in carbon removal technologies and solutions as an alternative to the windfall taxes currently being considered in several countries would be highly beneficial to society in the longer term.

Conclusion

Russia's invasion of Ukraine and its geopolitical impact have created new challenges that need to be addressed by policymakers in different nations across the globe. At the same time, the recent UN IPCC report leaves no reasonable doubt that the climate agenda cannot be delayed if the world is to avoid a humanitarian crisis on an unprecedented scale. Even if, in the present circumstances, threats to the implementation of the global sustainability agenda cannot be easily neutralised in the short run, it remains critical that policymakers everywhere remain committed to the pro-environmental agenda. Several solutions are available which allow us to respond to the new threats that have emerged as a result of the war in Ukraine and that correlate with the environmental agenda. The measures include increasing the role of nuclear power, developing initiatives that focus on the reduced use of energy, continued investment in renewable energy technologies, and rethinking the way energy producers are taxed.

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International sustainability reporting standards: Competition or complementarity between different organizations and approaches?

Christopher Hossfeld
Martin Schmidt
Francesco Venuti

ESCP Business School

Abstract

Sustainability, globalization, geopolitics, and climate change are all issues that strongly affect every business and, consequently, should be transparently depicted in company reports. These issues often have an impact not only on a company's figures ("the bottom line") but require broader nonfinancial disclosures in order to inform both the company and the stakeholders about the risks and opportunities arising from sustainability matters. The need for common standards that ensure high quality, transparency, and comparability in sustainability reporting has become quite urgent. Legislators and organizations worldwide are currently working on new sustainability reporting standards, of which two main sets of standards and approaches stand out.

The first is led by the International Sustainability Standards Board (ISSB), founded in November 2021. In its proposals for a global baseline for sustainability-related disclosures, the ISSB has adopted the so-called "single-materiality" approach.

The second was recently introduced by the European Union. The European Financial Reporting Advisory Group (EFRAG) was assigned the project to develop European Sustainability Reporting Standards (ESRS), whose use will be required by European firms based on the revised EU CSR Reporting Directive. The ESRS proposes adopting a "double-materiality" approach.

These two sets of standards could thus impair the drive for a universal set of sustainability standards, opening debate on the two different materiality approaches in particular and the overall approach to sustainability reporting in general. Will this "competition" promoting a wider and more in-depth debate on the topic result in complementary approaches (building block approach) or will it lessen its effectiveness by polarizing positions and reducing international comparability in sustainability reporting?

Keywords: CSR, ESG, ESRS, sustainability reporting, nonfinancial disclosure

International sustainability reporting standards: Competition or complementarity between different organizations and approaches?

Introduction

Financial reporting regulations can be considered as "harmonized" across the globe: International Financial Reporting Standards (IFRS) have been adopted in over 140 countries. Several other countries have committed to a transition to align their financial reporting standards with IFRS. Only a very few countries maintain "national" financial reporting standards for publicly traded ("listed") firms.[52] The situation for sustainability reporting, previously also called non-financial or ESG (Environmental, Social, Governance) reporting, is fundamentally different.

Indeed, the current sustainability reporting landscape is characterized by a multitude of guidelines, frameworks, and standards that differ in terms of:

- originator: NGOs, investor-led organizations, regulators/legislators, multinational, international or national organizations (e.g., UN, GRI, ISSB, EU), multi-stakeholder organizations, auditors, etc.
- type of regulation: guidelines, frameworks, standards, voluntary or mandatory, etc.
- content of rules: themes, principles, indicators; management processes, indicator measurements, etc.
- subjects: environment & climate change, ESG, human rights, labour practices & safety, anti-corruption, responsible supply chains, gender, diversity, etc.

The voluntary adoption of sustainability reporting began in the 1980s and, until recently, three major sustainability reporting frameworks were largely dominant globally: the Global Reporting Initiative (GRI) Standards, the International Integrated Reporting Council (IIRC) Framework, and the Sustainability Accounting Standards Board (SASB) guidelines. In the last three years, there have been considerable advances in sustainability disclosure regulations, with different "actors" making significant progress, but not always in the same direction or in a coordinated way (Pronobis and Venuti, 2021). As presented in more detail below, the IFRS Foundation established the International Sustainability Standards Board (ISSB), consolidating other organizations and institutions. The European Union is working on significant expansion of its rules in the context of its Corporate Sustainability Reporting Directive (CSRD) and Sustainable Finance Disclosure Regulation (SFDR), while the US Securities and Exchange Commission (SEC) is also reviewing its climate disclosure rules.

Inevitably, this regulatory jungle hampers the development of comparable, high quality sustainability reporting and makes it difficult to "read" and "evaluate" companies' strategies, policies, targets, and performance measurement, as well as their risk exposure and impact regarding sustainability. It also allows companies to cherry-pick from the different standards to a certain extent, and to apply those that

[52] Countries that do not require IFRS for domestic public companies include Cuba, North Korea, Sudan, and the United States of America (as of May 2022).

best suit their objectives, thereby potentially facilitating green-washing or the misleading depiction of sustainability issues. Given that sustainability information is becoming increasingly important, especially in a globalized world, the harmonization of sustainability reporting requirements – just like financial reporting – has become a necessity. At present, two major harmonization standard-setting efforts are concurrently ongoing: the ISSB is seeking a globally applicable baseline, while the European Financial Reporting Advisory Group (EFRAG), tasked by the EU Commission, is working on harmonizing sustainability reporting at EU level. After providing some background to these initiatives, we will discuss one fundamental difference: the way they define materiality, and the consequences of this difference for sustainability reporting in particular and sustainability politics in general. Based on this discussion, we assess whether the two initiatives are in competition or complementary.

The ISSB as a global initiative

The International Accounting Standards Committee (IASC) was formed in 1973. It was the predecessor of the IFRS Foundation, which has governed the International Accounting Standards Board (IASB)'s work since 2001. Thus, this international organization has, for decades, been devoted to developing high-quality, understandable, enforceable, and globally accepted standards for general purpose financial reporting. The IFRS issued by the IASB are intended for (potentially) worldwide use. For many years, the IFRS Foundation restricted itself to financial reporting, refusing to engage in sustainability reporting (Hoogervorst and Prada, 2015). However, after growing demand from international investors for worldwide harmonized sustainability reporting and following a public consultation, the IFRS Foundation formed a new standard-setting board in November 2021, the International Sustainability Standards Board (ISSB), as a "sister organization" to the IASB. The purpose of the ISSB is to define "high quality, transparent, reliable and comparable" reporting standards for climate and other environmental, social, and governance (ESG) matters to enable investors and other market participants to make informed economic decisions[53].

To make use of the varied expertise, accomplishments, and technical work of organizations around the globe and to increase its legitimacy in the field of standard-setting for sustainability reporting, the IFRS Foundation included several pre-existing sustainability standard-setting organizations, such as the Carbon Disclosure Standards Board (CDSB) and (as of June 2022) the Value Reporting Foundation (VRF; see figure 1). The latter is the result of a 2021 merger between the International Integrated Reporting Council (IIRC; created in 2010) and the Sustainability Accounting Standards Board (SASB; created in 2011). The (planned) ISSB standards architecture is also consistent with recommendations by the Task Force on Climate-Related Financial Disclosures (TCFD). In addition, in March 2022, a "Memorandum of Understanding" was signed with the Global Reporting Initiative (GRI), one of the oldest and most widely used sustainability reporting standard-setters. The ISSB and the GRI have expressed their intention to coordinate their work programs and standard-setting activities to ensure the compatibility and interconnectedness of sustainability information.

[53] https://www.ifrs.org/groups/international-sustainability-standards-board/

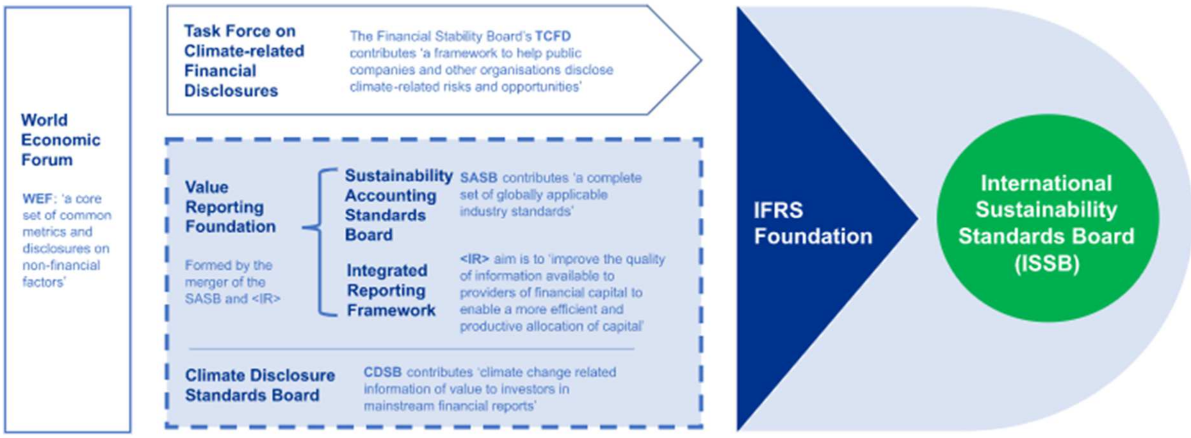

Figure 1: integration of existing sustainability reporting standard-setting initiatives into the ISSB (KPMG, 2021)

On March 31, 2022, the ISSB issued (its first) two Exposure Drafts (ED) of Sustainability Disclosure Standards: "IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information" and "IFRS S2 Climate-related Disclosures". These two Exposure Drafts (ED) are open for comment until the end of July 2022. The date of application of these standards has not yet been fixed.

Sustainability reporting in the European Union

One important step toward sustainability reporting in the EU is the Non-Financial Reporting Directive (2014/95/EU), passed in 2014 and applied for the first time in 2017. In 2021, approximately 11,700 large European public-interest companies were required to publish a sustainability report, formally labelled "non-financial statement" (EU Commission, 2021). This directive was followed by disclosure guidelines on non-financial reporting (2017), on climate-related information (2019), and by the Sustainable Finance Disclosure Regulation (2019/2088/EU) for financial market participants. The EU Green Deal, a strategy including legislation to make the EU more sustainable, was presented in December 2019. Six months later, the taxonomy regulation (2020/852/EU) was adopted and, in April 2021, a proposal for a Corporate Sustainability Reporting Directive (CSRD) was adopted by the EU Commission to replace the Non-Financial Reporting Directive. The CSRD – in its current proposed form – would extend the number of companies subject to mandatory sustainability reporting in the EU to an estimated 49,000 (EU Commission, 2021). The CSRD would also require external sustainability information assurance. In preparing their sustainability reports, companies would be required to apply the European Sustainability Reporting Standards (ESRS), currently being developed by EFRAG.

IFRS need to be formally adopted into European law (by way of a so-called "endorsement process"), which involves various parties: the European Parliament, the Accounting Regulatory Committee (with representatives from EU member states), as well as EFRAG. EFRAG's role in this endorsement process is to provide the EU Commission with "technical advice".

Unlike IFRS, ESRS would be adopted not by an endorsement process, but directly by delegated acts of the European Commission. EFRAG's role would not be to provide technical advice, but rather to adopt the role of a standard-setter. In initiating a project task force (PTF) as requested by the EU Commission in May 2021 (dissolved in April 2022), EFRAG became a standard-setter. It has adjusted its structure accordingly and now has two legs: EFRAG's Financial Reporting Board (FR Board) in an advisory capacity in the EU's endorsement process (and the IASB's standard-setting due process) and EFRAG's Sustainability Reporting Board (SR Board) as a sustainability reporting standard-setter (ESRS).

Preceding the formal creation of EFRAG's SR Board, the PTF published its working papers from January through March 2022. In April 2022, EFRAG's PTF published no less than 13 draft ESRS for public consultation (e.g., EFRAG, 2022a). The comment period ends 8 August 2022. Time is pressing, since the proposed effective date of the CSRD is 1 January 2023, including application of ESRS in its annual report 2023. However, the final CSRD is likely to postpone the application date by one year due to the negotiations between the EU Commission, the EU Council, and the EU Parliament ("Trilog") (EU Parliament, 2022).

The different materiality approaches and consequences

Materiality is an important concept in financial as well as in sustainability reporting. Basically, it determines which information "matters" and is important enough for a company to include in its report. As far as financial reporting is concerned, standard-setters, together with preparers, capital providers, and auditors have been discussing questions of materiality for decades. Despite ongoing debate regarding new accounting issues or company-specific aspects, there is a widely accepted common understanding of the concept of materiality in theory, based on qualitative and quantitative indicators. The application of the materiality concept, however, is often a matter of considerable judgement.

At the same time, there is no common understanding of the materiality concept for sustainability reporting yet, even on a theoretical level, making the currently discussed approaches even more interesting. The definition of materiality in the context of sustainability reporting will significantly impact the future boundaries of sustainability reporting.

Financial reporting focuses on a group of primary users of the information provided in the financial report: i.e., (financial) capital providers. From a sustainability perspective, the intended users are more diverse.

One view would extend providers of (financial) capital to include society as providers of nature-related capital (air, water, other resources). Companies' activities use these resources by polluting the air, producing climate-change-inducing greenhouse gases, impairing biodiversity, and generating waste. Reporting, including the materiality concept, would be geared toward measuring the sustainability profit or performance of a firm, based on a broader concept of resources, capital, and capital providers (sustainability reporting).

Another view further extends the intended users to include society, not only because the latter effectively acts as a provider of nature-related capital to companies, but because organizations have to consider corporate social responsibility under international agreements in areas such as avoiding corruption and bribery, and safe and fair working conditions (e.g., responsible supply chains, fighting child labour, gender and diversity management, etc.). Figure 2 illustrates the extension of the materiality concept taken from financial reporting adapted to include other capital providers and stakeholders (CSR reporting).

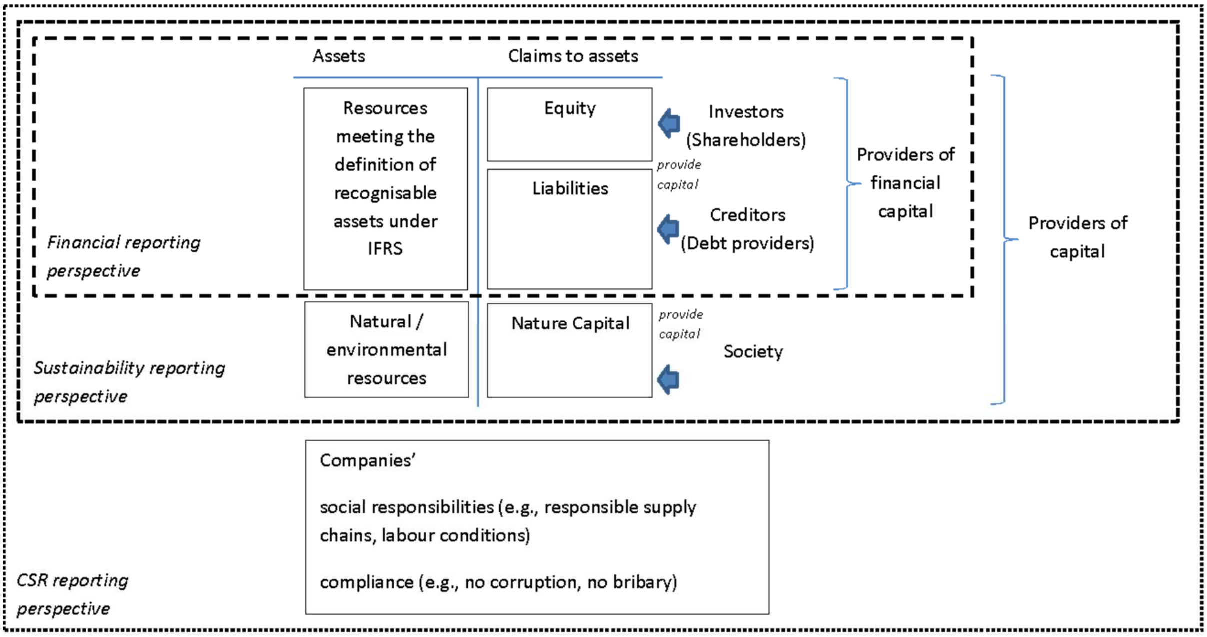

Figure 2: Extending the materiality concept from financial reporting to other capital providers and stakeholders

Companies therefore perform a "materiality analysis" to identify, estimate, and classify the sustainability elements which might impact a business and its stakeholders. The results and data from the materiality analysis are usually synthetically represented in the so-called materiality matrix in which companies showcase sustainability issues by generally referring to two dimensions: the degree of the issue's importance for the organization and the level of importance for the stakeholders.

Single materiality as the ISSB's approach

The ISSB proposal focuses on *financial* information. This focus results from the objective to disclose information that is useful for "primary users" of a company's general purpose financial reporting in order to assess the firm's enterprise value and decide whether to provide financial capital (equity, debt) to the company itself. According to ED IFRS S1, enterprise value "reflects expectations of the amount, timing and uncertainty of future cash flows over the short, medium and long term and the value of those cash flows in the light of the company's risk profile, and its access to finance and cost of capital" (para 1-7). Primary users are defined as the providers of (financial) capital, and materiality is assessed from the following perspective: if an issue could impact the company's ability to create value for the financial capital providers, then it must be relevant to the providers of financial capital, could thus influence their decisions based on the financial reporting information, and becomes reportable. As a result of this concept, entities are required to identify and disclose information about sustainability-related risks and opportunities to which the company is exposed, provided these risks and opportunities have a bearing on the company's financial performance and/or company value. This concept is therefore sometimes referred to as an "outside-in" (or single materiality) perspective as it is concerned with "outside" matters that could impact the company ("internal").

The advantages of this (narrow) concept of single materiality are that the user group (and their information needs) are relatively homogeneous and easy to identify. Consequently, its adoption could improve the clarity and focus of the report, with more straightforward, linear, and easier to compare disclosures. This narrow concept of materiality is also more closely linked to the materiality concept traditionally applied in financial reporting, which helps to foster consistent application in practice.

Double materiality

The European Union, EFRAG, and GRI favour a broader understanding of the materiality concept by combining the investor focus (identical to the ISSB view) with a broader stakeholder view. This second stakeholder view could be described as an "inside-out" perspective as it is concerned with the company's activities' ("inside") impact on the "outside". This impact is to be assessed based on scale, scope, and 'remediability'. The combination of these two views is commonly referred to as "double materiality", and it may substantially extend the matters that are considered material and thus, reportable. Although commonly described as combining the two concepts ("and"), it should not in fact be understood as an intersection (a mathematical "and", $\cap$), but as a union (a mathematical "or", $\cup$). Hence, a topic/matter is reportable if it is material under the "investor perspective" *or* the impact perspective.

An example of this broader concept of materiality is the GRI's definition of material topics (= reportable topics/matters). A material topic "reflects a reporting organization's significant economic, environmental, and social impacts, or substantially influences the assessments and decisions of stakeholders." (https://www.globalreporting.org/how-to-use-the-gri-standards/questions-and-answers/pre-2021-gri-standards-system-faq/materiality-and-topic-boundary/; last accessed 26 May 2022).

At first glance, the first part of this definition draws on what EFRAG refers to as the "impact materiality" (see figure 3), while the second part resembles the "financial materiality", extended from financial capital providers and their decisions to include other stakeholders and their assessments. A view that broadens the group of capital providers to include society (as providers of nature capital) in addition to financial capital providers is also consistent with this definition. If, for example, the environmental impact of a company's activities is so severe that society assesses the company's business model as *unsustainable*, then society may decide to impose restrictions on the company, which is equivalent to society no longer being willing to allow the company use of (no longer willing to provide) the nature capital. Alternatively, society can decide to price the usage of nature capital. An example would be CO_2 emission certificates. Pricing helps to reduce externalities and shifts returns from providers of financial capital to society as the provider of nature capital. Corporate income tax has a similar effect but pricing the usage of resources has the advantages of transactional taxes: companies with high usage of natural resources (and thus, relatively less sustainable business models) will be required to pay higher transactional taxes.

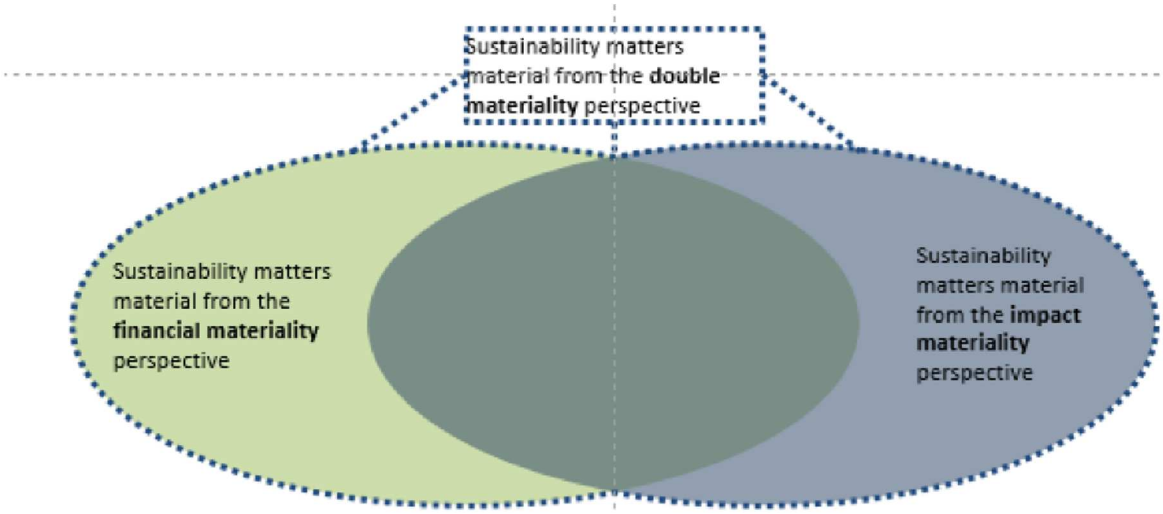

Figure 3: Double Materiality (EFRAG (2022))

While the double-materiality model might seem more complete, broader, and more inclusive (as it considers the perspectives of multiple stakeholders), it might involve a risk of excess complexity and a flood of information, which could potentially reduce the legibility and clarity of the disclosure.

ISSB's building block approach

One of the explicit objectives of the ISSB is "to facilitate the addition of requirements that are jurisdiction-specific or aimed at a broader group of stakeholders" (https://www.ifrs.org/news-and-events/news/2021/11/ifrs-foundation-announces-issb-consolidation-with-cdsb-vrf-publication-of-prototypes/, last accessed 26 May 2022).

By working with standard-setters from different key jurisdictions to address specific jurisdictional reporting requirements such as those outlined in the current EU proposals, a "building blocks" approach (see figure 4) could thus be adopted so that standards would "provide a globally consistent and comparable sustainability reporting baseline, while also providing flexibility for coordination on additional jurisdictional and multi-stakeholder reporting requirements." (ISSB, 2022)

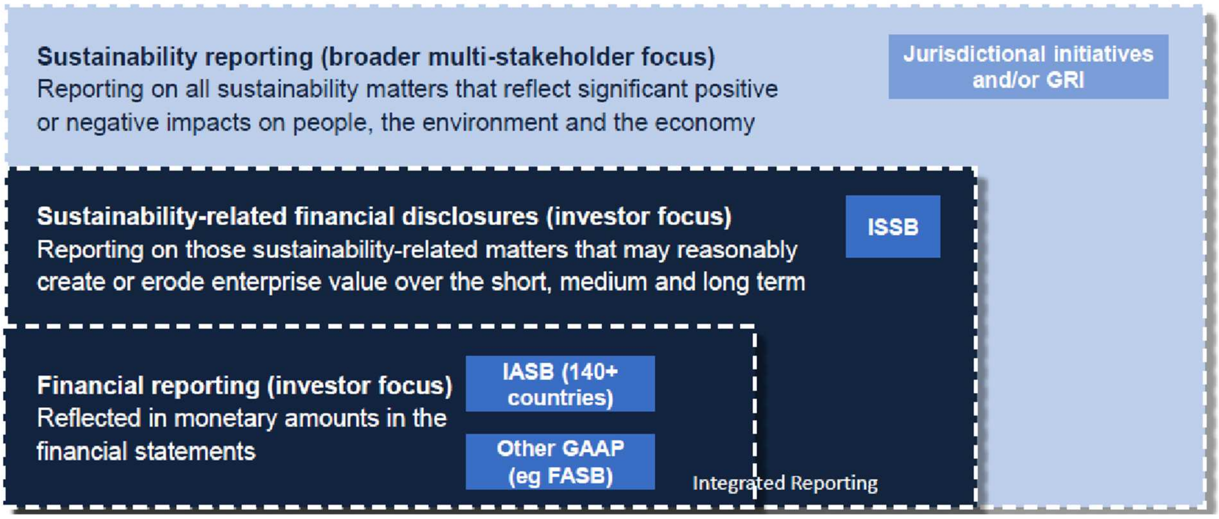

Figure 4: The building blocks approach (ISSB, 2022)

The ISSB recently formed a working group composed of representatives from several jurisdictions actively engaged in standard-setting in the field of sustainability disclosures. The working group will discuss the compatibility of the standard-setting initiatives. Members of the working group include, for example, the Chinese Ministry of Finance, the European Commission, EFRAG, and the US Securities and Exchange Commission. In addition, to ensure geographic diversity within the ISSB, three members must be from Asia-Oceania, three from Europe, and three from the Americas, one member from Africa, and four members may be from any area.

Discussion and Conclusion

Apart from the obvious issue that two different concepts of materiality (one narrow, one broader) impair comparability of reported sustainability information, there is the imminent danger of a “race to the bottom”. If some companies/countries apply the (narrow) ISSB single materiality concept, while others the broader double materiality concept, then this divergence may create pressure to move to the single materiality one. In that sense, the materiality approaches compete with one another.

On the other hand, we might ask whether there can be information that is material only under the “impact perspective” (and thus, under the double materiality concept), but not under the investor-oriented “financial perspective”. In times of accelerated climate change, with societies in many countries beginning to experience the consequences in their daily lives, is it possible that a company or business model with a severe negative impact on the environment will be tolerated in the long run? Or can we expect societies to be less and less willing to accept this impact and its associated externalities that shift wealth from societies to individual shareholders? If this is considered unlikely, then ultimately *all* topics/matters that are material from an “impact perspective” will become material under the “financial perspective”.

However, there could be a timing issue: there may be topics/matters that are only a focus for other stakeholders and parts of society initially. Only when the general public (society at large) becomes more aware of these topics/matters will they become material under a “financial perspective”, as customers consider the impact, for example, or because society considers legislating/regulating the impact, and only then will such topics/matters impact the company’s financial performance and/or value.

It is at least debateable whether the decision to report on these matters should be left to the discretion of companies. This decision is not left to the discretion of companies in the financial reporting domain and for good reason. Financial reporting standards, not the reporting firms, define what resources should be recognised as assets, and how changes in net assets are to be calculated to arrive at a profit.

Consequently, the ISSB’s single materiality approach might be easier and faster to implement in the short term. It may also be useful internationally, as many countries and jurisdictions have to (first) experience mandatory sustainability reporting. In the EU, however, the ISSB’s single materiality approach may only serve as a building block as part of the EU’s strategy to become more sustainable fast, based on the broader double materiality concept. Following this line of thought, we could say that the two materiality approaches are complementary over time.

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ESCP Impact Paper No.2022-19-EN

European open banking regulations: do they really favor innovation? Evidence from a cross-regional comparison between Asia and Europe

Matilde Guilhon*

ESCP Business School & Square Research Center

Abstract

The Open Banking concept emerged in Europe with the implementation of the PSD2 EU directives in 2013. A similar ruling was issued in the UK by the Competition Market Authority in 2016. These regulations were designed to promote innovation in banking services by opening the sector to new entrants (e.g., Fintechs, start-ups) and providing third parties with access to banks' customer data and functionalities. In this way, data sharing and market entries were supposed to increase competition and drive innovation towards new value propositions for banking customers.

However, the European banking sector is struggling in its transition towards Open Banking models. In Asia, where the Open Banking concept emerged later, the banking sector is nonetheless experiencing significant transformation thanks to greater intensity and a faster pace of innovation. One of the main reasons for these cross-regional differences lies in the regulations. In this impact paper, we analyze Open Banking regulations in Europe and Asia to explain differences in the cross-regional performance of banking service innovation.

Keywords: Innovation, Regulations, Open Banking,

*Ph.D. Student, ESCP Business School

European Open Banking regulations: do they really favor innovation? Evidence from a cross-regional comparison between Asia and Europe

Introduction

Open Banking is characterized by major regulatory reforms and competitive structure reconfigurations, with new entrants offering novel value propositions through innovative business models. It is a banking system where individual and corporate clients authorize their banks or financial service providers to use their financial data via APIs (Application Programming Interfaces). Open APIs enable third parties (developers) to access and exploit financial data to create new services and financial solutions. The underlying idea is to guarantee better financial transparency for account holders (Wewege & al., 2019), to promote competition in the retail banking sector and to enhance clients' experience. Open Banking regulations were initially introduced to promote innovation in the banking sector. Together with regulatory mutations and technological changes, the emergence of open business models represents a significant change in values and practices, paving the way for a new paradigm in the retail banking sector (Omarini, 2018).

However, the European banking sector is struggling in its transition towards Open Banking models. In Asia, where the Open Banking concept emerged later, the banking sector is nonetheless experiencing significant transformation thanks to its greater intensity and pace of innovation. One of the main reasons for such cross-regional differences lies in the regulations. In this impact paper, we analyze Open Banking regulations in Europe and Asia to explain differences in the cross-regional performance of innovation in banking services.

What can European regulatory institutions and banking executives learn from Open Banking initiatives in Asia? How can they enhance innovation in the European banking sector?

While acknowledging cultural, political, and economic characteristics between and within these two regions, the aim of our paper is twofold. First, we take stock of Open Banking initiatives in Europe and Asia by examining their regulatory and commercial underpinnings. Second, we analyze banking incumbents' responses to such evolutions. The paper examines differences in Open Banking regulatory approaches in Asia and Europe to draw lessons that can help promote innovation in the European banking sector.

Open Banking Regulations in Europe

Digital and technological advances have resulted in major changes in the way individuals share their personal data, search for products and services, and buy and consume them. However, for many years, few regulations addressed data-based and digital business interactions, giving rise to considerable security issues for individuals. In the banking system, where compliance regulations were reinforced following the 2008 crisis, European regulators took the lead to protect bank consumers in the digital age and to guarantee financial stability. Second, while, for many years, the European banking system suffered from inertia from the customers' perspective, European regulators also attempted to provide greater impetus for banking system innovation (Wewege et al., 2019). Their principal objective was to "invite the financial services industry to embrace the potential of new technologies by introducing legal certainty to previously unregulated services" (Omarini, 2022: 138).

The revised Payment Service Directive (PSD2) was adopted in 2015 and came into force in 2018. Its main goal was to transform the European banking landscape into a more open and innovative sector. It included several objectives: establishing banking and payment service standards across the European Union (EU), opening up the banking sector to novel entrants to enhance competition, and reinforcing security for banking customers in a context of digitalization. From a technical perspective, PSD2 exhorts incumbent banks to provide application programming interfaces (APIs) to third-party providers (TPPs), such as financial start-ups, Fintechs, technology firms, and banks, in order to share data upon customers' consent.

In the EU, Open Banking guidelines and recommendations are issued by the European Banking Authority (EBA). Another piece of legislation, the General Data Protection Regulation (GDPR), was introduced in 2018 to protect consumer data in the context of digitalization. Together with PSD2, GDPR contributes to the development of regulatory guidelines that serve as building blocks for Open Banking in the EU (Omarini, 2022). As for the United Kingdom, the Competition and Markets Authority (CMA) has published several recommendations following the logic of PSD2 directives to establish Open Banking standards regarding data sharing and APIs (Zachariadis & Ozcan, 2017). Both the CMA and the European Commission pursued the objective of unbundling banking services and opening up the banking sector to create "a more level playing field" through the implementation of novel regulations (Ozcan & Zachariadis, 2021: 2).

However, implementation of Open Banking in Europe has stalled for several years, and incumbent banks have found it difficult to take advantage of the new environment and to innovate.

Open Banking in Asia: towards a market-driven approach

A 2018 Accenture survey[54] indicates that almost 75% of European banks and 60% of banks across Asia Pacific were planning to introduce Open Banking initiatives. What are the drivers of these initiatives in Asia? South-East Asian countries are well advanced in terms of Open Banking. While the driver of Open Banking in Europe is mainly regulatory, the motivation in most Asian countries is largely commercial.

The most extreme illustration is China, where regulators have not enforced any legislation or limited BigTechs such as Alibaba and Tencent in their attempt to expand into financial services. These giant platforms have been able to create super-apps that operate as fully-fledged ecosystems, offering their users financial and extra-financial solutions. For instance, Alibaba offers multiple services in its WeChat Pay app, encompassing mobile payments, online banking, a BtoB

[54] Accenture (2018). *Accenture Open Banking for Businesses Survey 2018 – It's Now Open Banking.*

marketplace, a monetary fund, wealth management services, social scoring, fractioned payment, and consumption credit.

In countries where banking systems are closer to European ones, such as Hong Kong and Singapore, regulations exist, but they are less constraining than PSD2 and those of CMA, and are mainly motivated by market development factors. The Hong Kong Monetary Authority (HKMA) decided not to define standards for data exchange, for instance. Leaving this option to large incumbents, HKMA introduced the Fintech Supervisory Sandbox, enabling banks and Fintechs to share their data and to conduct pilot innovation projects. In addition, based on consultation with incumbent banks, and learning from Open Banking initiatives conducted abroad, HKMA launched an industry-wide Open API Framework that involves four phases of development. HKMA has thus adopted a more progressive approach to Open Banking regulations than European regulators.

In Singapore, the government backs Open Banking initiatives by providing API or Banking-as-a-Service reports as well as a list of APIs available in the financial industry. Although these guidelines are not compulsory, Singapore's banks have been very dynamic in terms of data exchange through APIs. For instance, DBS developed the world's biggest banking API platform, with over 200 APIs addressing 21 categories, such as cards, loans, online payments, and sales opportunities.

A similar approach was adopted in Japan. The Japanese government supports innovation through the entry of Fintechs and aims to promote competition by providing standards and a regulatory sandbox for Open APIs. In 2018, for instance, the Banking Act was amended to establish open API architecture and promote exchange between banks and Fintechs.

Our paper distinguishes between the legislation-based Open Banking model, adopted by countries or groups of countries such as the UK or the EU, and a market-driven Open Banking model. In the first model, it is mandatory for banks to open their data to third party providers upon customers' agreement. In the second model, which corresponds to a liberal approach, regulators leave the field relatively open for Open banking initiatives to connect different actors, i.e., financial institutions, Big Techs, developers, Fintechs, and firms belonging to non-financial sectors. In the legislation-based model, Open Banking corresponds to an imposed innovation, where pressure from non-market stakeholders (i.e., European regulators) is high, while the economic incentives to implement this innovation are relatively low (Radnejad & Osiyevskyy, 2019). In the aforementioned Asian countries, the incentive to engage in Open Banking is associated with high expectations in terms of competitiveness and profitability.

What lessons can we learn from regulatory differences between Asia and Europe?

Contrary to other sectors where regulators set the rules after new technologies and innovation have emerged, Open Banking regulations in Europe have preceded innovation, leading to several challenges for existing actors.

On the one hand, since they are ill-adapted to the reality of the context, Open Banking regulations lack clarity and precision in addressing key issues such as legal liability in collaborative arrangements between banks and third parties (Ozcan & Zachariadis, 2021). The pan-European regulations failed to take national specificities sufficiently into account. Although such regulations were designed to provide consistent standards at European level, their lack of clarity together with the characteristics of national banking systems resulted in diverse types of implementation and limited success. Inadequate adaptation to national financial landscapes, for instance, led some countries, such as France, Germany, and the UK, to delay implementation of the PSD2.

On the other hand, regulators' discourse aimed at boosting innovation and competition in the retail banking industry by putting pressure on dominant positions. In other words, the aim of the regulators was not to frame and set standards for an industry where incumbents compete with new entrants, but instead to explicitly encourage these new actors by promoting their innovative offers and setting them against traditional banking services. Regulators thus adopted a hard standpoint with regard to traditional banking. Together with technological innovations and the emergence of digital consumption, these regulations contributed to the shift from a supplier-oriented retail banking system dominated by incumbent retail banks to a market-oriented banking sector where incumbents' positions are increasingly contested (Omarini, 2022).

When the regulations were first adopted, Open Banking was perceived by incumbents as a threat more than an opportunity to create a competitive advantage. Radnejad and Osiyevskyy (2019) noted that the ability of incumbents to develop an effective response to an imposed innovation strongly depends on the perception of the innovation as either a threat to the entire industry or as an opportunity to create a competitive advantage. Incumbent banks perceived the threat clearly but lacked a vision of the potential competitive advantage they could generate in this context. This led incumbents from the very beginning to adopt a an attitude of defiance towards Fintechs and start-ups, rather than explore the opportunities for collaboration. For instance, figures on external operations (e.g., partnerships, equity investment, acquisitions, and joint ventures) between traditional French banks and Fintechs show that the number of operations gradually increased between 2013 and 2019 (Coeurderoy & Guilhon, 2022).

Our analysis of the regulatory differences observed between Asia and Europe enables us to determine four major limitations of European Open Banking regulations from an incumbent perspective.

First, the cumbersome and ambiguous guidelines provided by the European Commission and the CMA explain the limited results of Open Banking regulations in Europe. Almost three years passed between the adoption of PSD2 and its implementation. During these years, traditional banks spent a great deal of time deciphering the burdensome regulations and attempting to comply with them rather than developing an appropriate innovation strategy. Incumbents' hesitation towards their future value creation models and the herding effects observed in the external operations they conduct illustrate this observation (Coeurderoy & Guilhon, 2022).

Second, complying with regulations preceding the innovation itself is difficult and costly given the yoke of a complex IT legacy in incumbent firms, and the considerable time pressure imposed by the regulators. Historically, banks' technological infrastructure was designed to operate in isolation. Opening up these siloed infrastructures as technology evolves forces incumbent banks to deconstruct a system built up over decades.

Third, since they perceive novel entrants more as a threat than an opportunity, European banks cannot take full advantage of the Open Banking environment. Successful positioning could be achieved by integrating Fintech-style options with banks' existing products. The Singaporean bank, DBS, has gone one step further by collaborating with Microsoft on a Global Hackhathon, a model for developing next generation Fintech solutions based on the Microsoft Azure platform. The project provided a unique opportunity for talent and product development, and for collaboration between a bank and a BigTech.

Fourth, in addition to the Open Banking regulations, antitrust regulations are particularly stringent in Europe, discouraging initiatives like those taken by DBS which has developed strong ties with dominant players in other activity sectors, such as electricity and mobility. Such collaboration in Europe could be difficult to achieve as banks must abide by antitrust regulations, restricting them from creating such conglomerates.

Conclusion

It is true that regulations represent a catalyst for Open Banking. However, market factors such as consumer habits, competition, and technology, are equally important drivers of innovation in the context of Open Banking. Nevertheless, our analysis of regulatory differences between Asia and Europe provides evidence that in the case of strict compulsory regulations, banks passively attempt to comply with imposed innovations without appropriating them or viewing them as an opportunity.

From the clients' perspective, what is happening today in the European banking sector is not very satisfying since incumbent banks struggle to develop a customer-centered approach as interesting as those offered by platforms. Moreover, regulations that open up industries with higher consumer inertia to competition might inadvertently favor BigTechs, thereby recreating a monopolistic situation in the long term (Ozcan & Zachariadis, 2021). BigTechs have no interest in aggressively entering highly regulated financial markets. However, this does not mean that strict regulations effectively discourage them from expanding into financial services. BigTechs are likely to move forward in disguise on the fringes of regulations.

In this respect, we advocate for greater coordination between regulators so they can provide a fruitful environment in which incumbents can innovate. We also encourage Open Banking regulations to adopt a more progressive and market-driven approach in Europe. Obviously, the aim is not to maintain a dominant position at the expense of consumers. However, in our view, with their decades of experience in data security and expertise in financial services, incumbent banks must remain at the centre of the financial system in order to ensure its stability and to guarantee consumer protection.

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The French government's (re)location plan: relocation or reindustrialization?

Fabienne Fel

ESCP Business School

Abstract

The Covid-19 pandemic, followed by the war in Ukraine and numerous recent lockdowns in China, has relaunched the debate on the importance of relocating offshored industrial production to France to reduce French dependence on foreign, and in particular Chinese, supplies.

A (re)location plan was launched in France in the summer of 2020. But, contrary to its name, an analysis of the winning projects shows that it is not really a reshoring plan, but rather a reindustrialization and competitiveness plan. Securing supply chains will not be achieved by reshoring currently offshored production, but rather by producing new generations of products in France that will make foreign supplies obsolete, by increasing the performance of factories and implementing Industry 4.0 technologies. This competitiveness plan is based on France's potential for innovation and R&D.

Keywords: France; governmental plan; relocation; reindustrialization; competitiveness

The French government's (re)location plan: relocation or reindustrialization?

Supply disruptions: temptation to relocate

From the beginning of the pandemic, many sectors experienced disruptions, starting with the health sector (shortage of masks, protective equipment, respirators...), soon followed by other sectors. This was due to lockdowns around the world, border closures, and suppliers who had to supply their national market as a priority. These shortages are not over yet; car factories have been slowing down for the last 2 years due to the lack of micro-processors, we are also witnessing shortages for many raw materials, recently aggravated by the war in Ukraine as well as new lockdowns in China. While some researchers had previously highlighted the risks associated with fragmented supply chains, due to possible political risks or natural disasters, the risks seemed to be localized, and no one had envisaged global consequences.

The Western world has now become aware of its dependence on distant supplies, particularly from China. As early as March 2020, the mainstream media in various Western countries raised the need to relocate industrial production; this was supposed to be the only way to ensure continuity of supply in the event of a new pandemic. In France, this theme has had a particular resonance as the 2022 presidential election approached.

What do researchers say?

The academic literature published since the beginning of the pandemic is more nuanced, however; reshoring (i.e. relocation) would make companies more subject to the turbulence of their local economies. Moreover, it will not be possible to relocate everything, as many companies are dependent on raw materials that are not available in their geographical area. Finally, while reshoring will ensure better local sourcing, it will make foreign sales more expensive. In conclusion, reshoring would imply significant switching costs, without improving the resilience of the supply chain (Strange, 2020). Strange's solution is to source from more suppliers in more countries.

For their part Barbieri, Boffelli, Elia, Fratocchi, Kalchschmidt & Samson (2020) observed isolated reshoring initiatives implemented already by some European companies while indicating that reshoring will not solve the problems encountered by some industries during the covid-19 pandemic in the long term. They conclude that a better solution would be the near-reshoring of entire supply chains, at the level of a geographical macro-region (Europe, for instance) and not of a country. However, they point out that this is a long-term policy (preparation is needed), and that it will require government incentives.

Finally, a recent study commissioned by the European Parliament (2021) shows that the reshoring policies undertaken by the UK, the US and Japan have only produced modest results, and advises limiting reshoring to a few sensitive sectors (medical, solar with a view to the energy transition). For other sectors, this report recommends better resilience through better risk management and stockpiling.

In conclusion, contrary to the mainstream press articles that present reshoring as 'the' solution to the dependence of European supply chains on distant supplies, the few academic articles dealing with the topic are much more nuanced and recommend other solutions to improve the resilience of supply chains.

However, as Strange (2020) wrote, *'the evolving geopolitical context and rising protectionist sentiments worldwide are likely to be the critical drivers*' and plans to help companies to relocate are already being implemented in some countries. This is the case in France, where the mainstream press continues to stress the urgency of reshoring.

The French (Re)localization governmental plan

The French government has noted '*the industrial and technological dependence of the French economy, and the fragility of certain global value chains*'; in September 2020, it launched '*calls for projects to localize and relocate critical industrial activities*' supported by a €1Billion budget. These projects are aimed at five sectors considered critical to France's autonomy, resilience and sovereignty: (1) health, (2) agri-food, (3) electronics, (4) essential inputs for industry (chemicals, materials, raw materials, etc.) and (5) 5G telecommunications.
Since the launch of this 2020 recovery plan, called 'Relaunch France ', a total of 407 projects labelled 'relocation' ones were supported by the end of October 2021, after 5 waves of announcements. These projects represent a total industrial investment of € 2.7 Billion, of which € 729 Million is supported by the State.

Project analysis

As part of a recent research (Fel, 2022), we analyzed these 407 projects to establish an overall typology of the winning projects, and to determine whether the French plan is rather a plan for relocation or a plan for reindustrialization, or even competitiveness.

The project descriptions are detailed in the data table compiled by the Ministry of the Economy, Finance, and Recovery (https://www.data.economie.gouv.fr/explore/dataset/plan-de-relance/table/), which lists all the winning projects since the summer of 2020. The winning projects of the *'(Re)locate measure in critical sectors'* were recoded as:

- In-house reshoring operations (return to French territory of previously offshored manufacturing to a foreign subsidiary)
- Reshoring for insourcing projects aiming to propose alternatives (partial or total) to foreign supplies, and more specifically to Asian supplies.

- Other projects, aiming to improve French competitiveness or sovereignty, often through the development of innovative products and/or processes, allowing in some cases the creation of new sectors.

The first two types of projects were considered as reshoring projects, based on the typology proposed by Gray et al. (2013): the first type of project corresponds to cases of '*In-house reshoring*' (production was previously offshored to a foreign subsidiary), the second type to cases of '*Reshoring for Insourcing*' (production was previously outsourced to foreign suppliers). In both cases, the production will be relocated internally.

The other types of projects cannot be qualified as reshoring projects, in the sense that they are either:

- Projects to develop new products or new processes, aimed at ensuring France's competitiveness or sovereignty. Insofar as these are new activities, no offshoring has ever been carried out. We have differentiated 2 categories within these projects:

  -Projects that particularly refer to the development of new technologies belonging to the field of Industry 4.0. In some cases, these may involve the building of a new factory 4.0.
  - Projects that set up new factories, without any reference to Industry 4.0.
- Projects aiming at increasing production capacity to maintain or develop industrial employment in France, without reference to any reduction in foreign inputs into manufacturing.
- R&D projects, without immediate industrial benefits.
- Development projects for business consulting, especially for innovative 5G technologies.

The typology of winning projects

A low number of reshoring projects (13%)

At first glance it appears that reshoring projects, whether in-house reshoring (6%) or reshoring for insourcing (7%), represent only a very small share of the winning projects of the (Re)location plan, which may seem surprising in the context of a plan called (Re)location. In fact, this plan supports many other modes of reindustrialization in France.

A significant number of new factories (40%)

These projects represent almost 40% of the winning projects. In most cases, the aim is to build new industries to manufacture innovative products that will eventually replace those currently on the market (new generations of electronic components, medicines or medical equipment, or even food products). About 40% of the descriptions clearly indicate that these projects will help to establish France's sovereignty in their field, by reducing dependence on foreign suppliers. Although this is strictly not reshoring, in the sense that these companies are not going to internalize production currently made abroad, these projects are nonetheless participating in an indirect reduction in the share of foreign supplies of future French production. We can associate these projects with 'competitive development relocations' (Mouhoud, 2020); thanks to innovation, a company that was sourcing its supplies abroad will stop importing and will produce a new generation of products locally.

Industry 4.0 projects (14%)

Industry 4.0 is seen by the winning companies as a way of developing the competitiveness of French companies, and therefore to sustain employment in France. Concerns about sovereignty are expressed by only 10 companies out of the 56 that have a project referring to Industry 4.0. The objective here is to reindustrialize France through the implementation of 4.0 technologies, which does not specifically aim to reduce dependence on foreign suppliers.

Capacity increase projects (13%)

These projects aim to increase existing production capacities for the purpose of competitiveness and increased market share, thereby maintaining employment in France. Here again, the aim is to reindustrialize, without reducing dependence on foreign suppliers.

R&D projects (18%)

R&D projects, which have no immediate industrial impact but are intended to prepare for the future, account for a significant share of winning projects. These projects are supported by all sectors, but particularly by the 5G sector, where they represent 68 out of 70 projects, probably because of the sector's infancy.

Conclusion

Despite its name, the French government's (re)location plan is not a plan focused on reshoring, which remains marginal. Companies are not going to reshore their current production to France, which has been offshored to low-cost countries, particularly in Asia. Closing a factory abroad to rebuild it in France is expensive, raises the question of production costs, as well as the acceptability of higher selling prices. Since production costs are higher in France than in the emerging countries where production has been offshored, reshoring is not consistent with the usual strategies of companies.

France's (Re)location plan is mostly a localization and reindustrialization plan based on capacity increases, within existing plants or through the construction of new plants; it is also a plan to modernize industry through the development of Industry 4.0 and R&D projects. Many projects, relying on France's strong innovation potential, aim to develop new innovative sectors, rather than reshoring existing production. Relocations will tend to be 'competitive development relocations' (Mouhoud, 2020) where the next generation of products manufactured in France will replace current foreign supplies, which will have become obsolete.

France’s (Re)localization plan is not, therefore, ultimately a reshoring plan - contrary to what its name suggests, perhaps overly influenced by the general public's expectations. It is rather a plan to improve French competitiveness, taking advantage of France's high potential for innovation and modernization.

This plan will not solve all supply difficulties, especially for supply chains dependent on raw materials which are neither available in France or in Europe. However, we can think that with a stronger France in terms of industry, capable of manufacturing innovative products in productive factories, using 4.0 technologies, the next shock of global disruptions will be lessened, at least in the 5 sectors concerned by the plan. However, the problem of French dependence on foreign supplies remains unresolved in all other sectors, which are considered less strategic.

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ThisGenEU

Jérôme Creel
Gonçalo Pina

ESCP Business School

Abstract

The recent geopolitical events in Eastern Europe represent an important challenge to the European project. As most European economies are still recovering from the pandemic economic shock, the escalation of the Russian invasion of Ukraine has increased both fuel and food prices. Proposals to raise tariffs or ban fuel imports from Russia have been met with resistance by the leaders of certain European economies, in particular those that are dependent on Russian energy products. Is there a new role for EU solidarity? In the last two years, the pandemic response increased integration and coordination within the EU and led to the NextGenerationEU program, a stimulus package with long-term goals that included an unprecedented amount of EU debt issuance to finance loans and grants to Member States. Faced with new military and energy supply threats, the EU could use the policy impetus associated with NextGenerationEU to address these issues at the European level for the current generation. This essay highlights how the EU could develop programs to tackle the geopolitical challenges that we are experiencing right now, a ThisGenerationEU programme.

Keywords: ThisGenEU, NextGenEU, EU solidarity, budget, economic policy

ThisGenEU

Introduction

The escalation of the Russian invasion of Ukraine on February 24th 2022 poses a significant challenge for European economies and for the European Union (EU). Just as European economies were recovering from the Covid-19 pandemic economic shock, with inflationary pressures already building up worldwide, the military conflict further increased energy and food prices. It also destroyed a significant part of Ukraine's economy, and brought economic sanctions on Russia. Together, these factors are impacting European economies negatively. Crucially this impact is asymmetric. Some European economies are more exposed to trade with Russia and Ukraine, both in terms of exports and more importantly in terms of energy imports, and are therefore suffering relatively more from this economic shock.

The Russian invasion of Ukraine has produced a European-wide economic and political shock. Political decisions, such as a full embargo of Russian energy imports or punitive tariffs, are best left to democratic decision making. Meanwhile, we believe that the war shock requires a more systematic policy response at the European level. We therefore highlight some economic mechanisms that may limit the costs of the current shock and facilitate political decision making. One concern is that because the shock is so asymmetric, the distribution of costs associated with these political decisions fall more heavily on a few countries. Because European political decisions are taken unanimously, this asymmetry has hindered political decision-making and may even prolong the conflict as well as the economic shock for the EU as a whole. European solidarity, once again, is crucial.

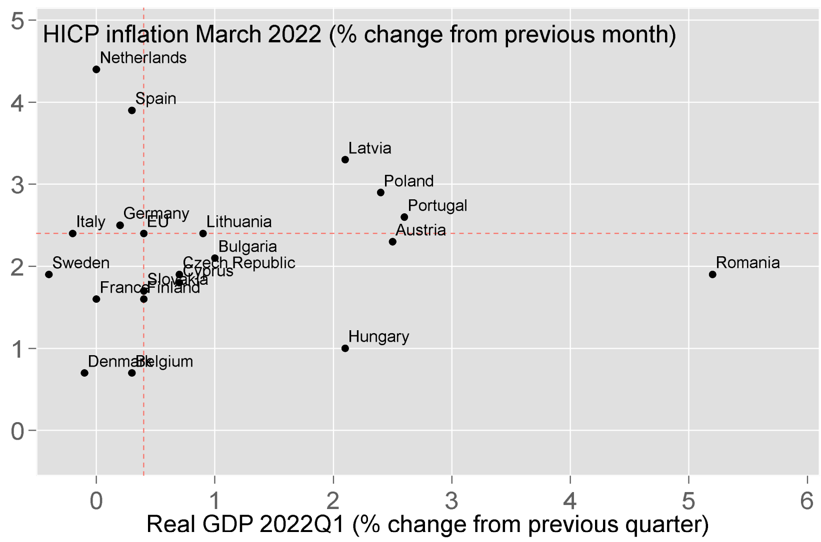
The paper is organized as follows. The first section highlights the economic costs of the war on European economies. The second section draws a parallel with the pandemic crisis and its European management via the creation of a new programme, NextGenerationEU (NextGenEU), and a new facility, the Recovery and Resilience Facility (RRF). The next section outlines how to spend European funds to tackle the asymmetric shocks associated with the Russian invasion of Ukraine and the sanctions levied as a result of the invasion, a ThisGenerationEU (ThisGenEU). The final section outlines how to pay for increased European level expenses, in particular, how to develop a mechanism that funds the European Commission in a way that Member States contribute to the European budget in a state-contingent manner, therefore minimizing negative consequences for their own debt sustainability.

The macroeconomic impact of the Russian invasion of Ukraine

To investigate the impact of this economic shock on macroeconomic outcomes within the EU, we can look at the two most tracked macroeconomic outcomes: real GDP, a measure of economic activity, and inflation, a measure of the growth in prices. Figure 1 shows available Eurostat estimates published on May 17th for the percentage change in real GDP in the first quarter of 2022, relative to the last quarter of 2021 on the x-axis, together with estimates of inflation rates for March 2022 relative to February 2022 on the y-axis. These data are computed as percentage change from the previous period, instead of the traditional approach of percentage change from a year ago, to better capture the effect of the invasion in the presence of base effects related to the pandemic. Because the pandemic hit different countries at different times, variations in output and prices from a year ago may be contaminated by country-specific experiences.

Looking at Figure 1 it is possible to see that there is substantial heterogeneity in terms of macroeconomic outcomes. The dashed red lines represent the European Union (EU) values for real GDP growth and inflation rates. Some larger EU economies are experiencing lower GDP growth and higher or equal inflation relative to the EU average. These include the Netherlands, Spain, Germany and Italy. Others like Sweden, France, Denmark and Finland are experiencing lower inflation than the EU average but also lower real GDP growth while Latvia, Poland and Portugal saw higher inflation than the EU average, but also higher output growth. The remaining economies experienced lower inflation and higher output growth than EU averages.

Figure 3: ASYMMETRIC SHOCKS WITHIN THE EU IN 2022 Q1 (Source: Eurostat)



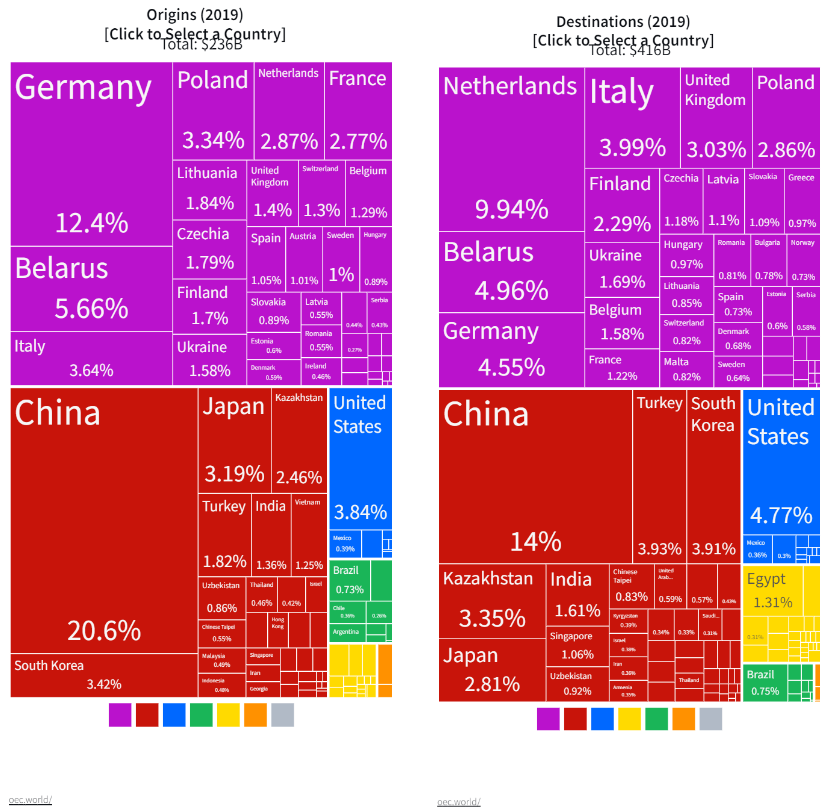
These data represent the first, crude, measured macroeconomic effects following the escalation of the Russian invasion of Ukraine. To estimate the full impact on macroeconomic outcomes one would need to compare realized macroeconomic outcomes with counterfactual outcomes without the conflict. A rough comparison can emerge from the differences between economic forecasts made in the autumn of 2021 and in the spring of 2022. While differences encompass other unexpected outcomes, such as the resurgence of the pandemic in China and subsequent supply chains disruptions, it gives a measure of the macroeconomic impact of the geopolitical tensions. According to the European Commission, inflation rate in the euro area measured by the increase in the harmonized index of consumer prices is expected to almost triple in 2022 and to double in 2023, with regards to the autumn of 2021 forecast at 2.2 percent and 1.4 percent respectively. Moreover, the euro area GDP growth rate in 2022 would be 1.6 percentage points lower, at 2.7 percent, than the autumn 2021 forecast.[55] Germany's economic forecast would decrease by 3

[55] The economic forecast for 2023 is only barely impacted.

percentage points, Italy's by 2 percentage points and France's by only 0.6 percentage points.

It is clear that one crucial element determining the economic impact of the war is the exposure to Russia. Figure 2 shows the main import and export markets for Russia for 2019, the last available data before the pandemic. Unsurprisingly, countries like the Netherlands, Italy and Germany, are very exposed to Russia through international trade, both in imports and exports, and have been experiencing relatively high inflation and lower real GDP growth during the first quarter of 2022. However, there is substantial uncertainty about the final economic outcomes of the war, in particular whether imports of energy products from Russia will be subject to an embargo or punitive tariffs, and when. Additionally, the economic effects of the war are not limited within country borders. Countries in the EU trade substantially with each other, leading to second round, external effects, even for countries that are not directly exposed to Russia, which may materialize over the next quarters.

Figure 4: Imports (Origins) and Exports (Destinations) for Russia 2019 (source: Observatory for Economic Complexity)



European solidarity: the experience of NextGenerationEU

One straightforward solution for overcoming these difficulties is to employ European solidarity. There are different options and levels of solidarity though, which can tackle specific issues. For example, Germany was reluctant to stop imports of Russian oil, which arrive through a pipeline to Germany, as its ports could not accommodate enough oil brought by sea from elsewhere. This lack of alternatives was pointed out by German officials as an example of the extreme dependence on Russian energy that would make an embargo impossible.[56] However, this lack of substitutability holds only when looking at Germany. On April, 26th, Robert Habeck, Vice Chancellor of Germany and Federal Minister for Economic Affairs and Climate Action, announced a solution to substitute Russian oil where non-Russian oil is shipped to Germany by pipeline from a port in Gdansk, Poland. These intra-European logistical solutions represent one option for dealing with asymmetric dependency on Russian energy. However they will nevertheless impose asymmetric economic costs, as existing infrastructure which imports energy from Russia still provides the cheapest source of energy.

Another option would be to build on NextGenEU and RRF and transform them into a permanent fiscal capacity. The economic and social costs stemming from the pandemic have urged the EU Member States and institutions to devote €750bn (at 2018 prices) to fostering recovery and resilience with a country-specific funds allocation and temporary European-debt financing. The question of the reimbursement of EU debt by new EU resources has been left to future political decisions. NextGenEU adds to the EU budget and has therefore a multi-annual (7-year) perspective. The pandemic has shown that it is possible to develop an integrated and coordinated EU response to a deep crisis, including unprecedented moves like the issuance of substantial European debt to finance a stimulus package with long-term goals. NextGenEU represents a significant leap in European wide policy in response to a crisis; in this case, targeting the pandemic recovery and transforming European economies and societies, making them healthier, greener, and more digital. Nonetheless, the unrolling of the RRF is still ongoing. By the end of 2021, hence more than one year after the pandemic started, only €100bn had been tapped. As a consequence, the impact of RRF on EU economies remains unknown to date. For this reason, it is difficult to argue for an immediate shift to a permanent facility.

Moreover, part of the RRF is made of loans, not grants. Although the entire amount for grants has been requested by Member States during the European Semester of 2021 (with the exception of the Netherlands), as of May 2022, €200bn of loans had not been yet requested. EU Member States still have until August 2023 to request these loans and therefore tap RRF funds entirely.

It is likely however that the funds available in NextGenEU will not be sufficient to achieve its dedicated policy goals. According to the European Commission (2020)[57], additional *annual* investment would need to increase to €1,040 bn on average (at 2015 prices) to achieve the goal of net-zero greenhouse gas emissions in the EU by 2050. While not all that amount would have to be funded collectively (at the EU level), it makes a sharp difference with the 7-year amount of NextGenEU which is dedicated to climate change for at least 37 percent of the total amount.

In contrast with the former option of turning NextGenEU and the RRF into permanent policy instruments, another option may be to create a new temporary

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[56] See Wolfgang Schmidt, Germany's Federal Minister for Special Affairs and Head of the Chancellery, making the case against substitutability here https://youtu.be/7S-V1EcsY28?t=1559, [Minute 26:23].

[57] See also Creel et al. (2020) for a more ambitious EU recovery programme.

programme. In the face of current challenges, including a tendency towards deglobalization, political disintegration in the EU and within EU countries, as well as new military and energy supply threats, the EU could use the impetus associated with NextGenEU to address such issues at the European level, building upon a new dedicated programme. Let us call it ThisGenEU programme as it would be mostly dedicated to the EU's immediate challenges.[58]

ThisGenEU: for what purposes, or how to spend it?

The pandemic crisis has prompted a budgetary reaction by the EU Member States that surprised many observers. The issuance of European public debt instruments delegated to the European Commission to fund a kind of European fiscal capacity was judged impossible a few years or quarters before. With monetary policy stuck in the liquidity trap and at the zero-lower bound, active fiscal policy is back in policy and political agendas. Furthermore, the discrepancies in available fiscal space between Member States to manage the economic and social consequences of Covid urged a common fiscal reaction.

Collective and coordinated spending reactions by the Member States have also stemmed from the exogenous nature of the health shock. In contrast with the former European debt crisis, this time was extremely different: it could not be argued that Member States and their governments were directly responsible for the shock. This certainly accelerated the involvement of Germany and the frugal countries, e.g. the Netherlands, to endorse NextGenEU and RRF.

The two above-mentioned arguments that are at the origin of NextGenEU and RRF have not lost their relevance. First, two years after the pandemic erupted, European public finances are still not in order and public deficits are very different from one country to another: Greece, Italy, Latvia, Malta and Romania had deficits above 7 percent of GDP in 2021, whereas Denmark, Luxembourg and Sweden achieved public balance or a surplus. Moreover, Belgium, Cyprus, France, Greece, Italy, Portugal, and Spain had a public debt to GDP ratio above 100 percent in 2021, whereas Germany was 10 percentage points above the 60 percent threshold and the Netherlands 10 percentage points below. Member States maintain uneven fiscal spaces. Second, the geopolitical and energy shocks are exogenous to the EU. Circumstances for a collective reaction at the European level are thus met (see also Pisani-Ferry, 2022).

There are at least two other conditions to fulfil before expanding collective spending. First and foremost, the multiannual budget of the EU must be balanced every year, unless some exceptional circumstances occur. The Russian invasion of Ukraine can easily be thought of as such an exceptional circumstance requiring exceptional reactions. Second, the EU rests on the subsidiarity principle: a policy decision must be taken at the political level (local, national or European) where it is the most efficient at fixing the problem it is meant to solve. According to the subsidiarity principle, one can argue that policy decisions with negative or positive spillovers are better handled at the European level. This is certainly true for the transition towards an EU carbon-free economy that requires common regulations

[58] For an opposing view, see Sapir (2022).

and a shared impetus to be achieved. The target of the RRF towards green investments is adequate in this respect.

The current energy and geopolitical crisis will prompt a common budgetary reaction along the same arguments, if and only if the targeted investments are prone to generating positive spillovers (or to limiting negative spillovers) in an emergency. In contrast with NextGenEU, the common fiscal impetus may be targeted towards those currently living in the EU and who face new risks for their security, for their purchasing power and for their ability to offer solidarity to new migrants.

Accordingly, the ThisGenEU programme may involve the acceleration of the means allocated to the European defense agency (EDA). The priority of the EDA is to support the development of defence capabilities and military cooperation among the Member States. With war at the EU borders, and in connection with the disruption of supply chains, securing the EU territory and goods' supply may be a necessity.

The uncertainty of oil and gas supplies and the substantial rise in energy prices require an acceleration of energy input substitution via renewables. This situation modifies the forecast about the transition towards a net-zero greenhouse gas emissions in the EU in that it *accelerates* the requirement to achieve this goal and substantially reduce the EU's dependence on Russian energy. Moreover, it has had uneven effects on inflation between EU Member States. In some states, the issue of purchasing power loss will be more acute as domestic fiscal space is limited. Reliance on European funding would alleviate the social tensions posed by surging inflation and contribute to European and social cohesion.

Finally, the EU has been facing a new refugee crisis. According to the UNHCR and as of 29 May 2022, more than 4.5 million Ukrainians had fled their country, with most arriving in Poland, Slovakia, Hungary and Romania. This puts a heavier weight on these countries that are still substantially below the EU average EU GDP per inhabitant.[59] Again, fulfilling social cohesion requires some mutualisation of the economic and social costs arising from the refugee crisis at the level of the entire EU.

ThisGenEU: how to pay for it?

To make the allocation of ThisGenEU possible, it will be necessary to increase the funding of the European Commission. The European Commission has access to different revenue sources. Although it is possible that new European-wide taxes will be developed, we argue in this paper that, as the residual element among the receipts of the EU budget, the Gross National Income (GNI) contribution is both the most natural and the best way to finance ThisGenEU. The GNI contribution already represents around 70% of EU funding. This contribution has tripled since the late 90s, so it increased substantially without significant political opposition. How should this financing be structured?

[59] According to Eurostat, in 2021, the real GDP per inhabitant of these 4 countries ranged between 33 and 56 percent of the EU average.

One option would be to ask member-states for an immediate GNI contribution and to implement the program through grants. This strategy would remove the fears of larger EU debt, but would be more demanding of member-states in the short run at an economically challenging time. Because the costs associated with the Russian invasion of Ukraine are asymmetric, the benefits from grants may be concentrated, which may make it politically challenging to finance with immediate contributions.

An alternative would be to reproduce the large debt issuance with postponed member-state payments, as in the RFF framework. In this case, the GNI contribution would only occur in the future. Crucially, it would have some desirable properties for member-states. This is because grants financed by EU debt with future GNI contributions by member states to service debt are equivalent to projects financed with state-contingent debt at the member-state level, even if as a whole the EU debt is non-contingent. This EU debt would likely be cheaper for member-states with costly domestic debt (although more expensive for member-states with cheaper domestic debt). Furthermore, judging from current EU borrowing under this mechanism, and examples of member-state state-contingent debt like the BTP Futura in Italy, the EU state-contingent borrowing would likely be substantially cheaper.

To make the role of state-contingent debt clearer, note that most government debt issued is non-contingent; that is, the payment on debt does not depend on economic conditions. That means that when the economy is doing poorly, payments are unchanged, which can make debt unsustainable. State-contingent debt has been proposed as mechanism to avoid these situations (Pina, 2020). However, state-contingent debt is still relatively rare (Pina, 2022). Crucially, a ThisGenEU programme made up of grants financed by EU debt to be paid by future GNI contributions shares some features of state-contingent debt for member-states and it would therefore limit the negative impact on debt sustainability coming from this new debt (Gros, 2020). Given that member state contributions to the EU budget depend on their future GNI level, economies that are doing better than expected pay more than expected, and the contrary happens for countries doing worse than expected. For example, between 2008 and 2016 the GNI of Greece fell by 44%. This reduced Greece's contributions to the European budget compared to countries that saw smaller decreases in GNI. Other economies that would experience substantial economic growth would see their GNI increase, and with it, their contributions to the EU budget to pay for EU debt. Therefore, the postponed GNI contribution somewhat stabilizes member-state debt ratios following economic shocks by making payments to the EU budget a function of economic conditions for each member-state, a property that is shared with state-contingent debt.

Conclusion

The current geopolitical crisis has renewed interest in a European policy impetus to develop a European defense force, collective actions to shield European economies from the rise in energy prices as well as mutualising the social and economic costs of the Ukrainian refugee crisis. Rather than a permanent NextGenEU programme, we argue for a new temporary programme, ThisGenEU, dedicated to the three afore-mentioned objectives. This enlarged EU budget would allow the EU to deal with asymmetric shocks that require EU-level responses.

As for funding, we propose two options. One would contrast with EU debt issued for NextGenEU and would give rise to immediate GNI contributions by the EU Member State. Another would be an extension of the debt financing used for NextGenEU, and would be financed by postponed member-states contributions based on GNI. Both the immediate or postponed financing of ThisGenEU would represent a move towards more quasi-fiscal transfers within the EU through the EU budget. Better-performing economies would contribute a bit more than the under-performing countries, ensuring that European solidarity is used to tackle the issues affecting this generation of Europeans.

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A new rationale for small tariffs

Michael Troege

ESCP Business School

Abstract

While free trade is always optimal with perfect competition, recent research by Amir, Jin and Troege (2022) demonstrates that under imperfect competition, the welfare of individual countries as well as the world can always be enhanced by well targeted small government interventions such as tariffs or subsidies. While these findings cannot be used to defend large tariffs that interrupt or severely reduce international trade, they provide new justification for limited restrictions on trade that attempt to offset the increasingly harmful effects of oligopolistic market structures.

Keywords: free trade, welfare, import tariffs, export subsidies, production subsidies, consumption tax

A new justification for small tariffs

Free trade is only optimal in perfect competition

Most economists agree that competition is good and tariffs bad. After all, in his famous book "On the Principles of Political Economy and Taxation", published in 1817, David Ricardo demonstrated that in an ideal world with perfect competition, free trade maximizes world welfare.

Unfortunately, competition is almost never perfect. Much of today's international trade is conducted by oligopolies (Head and Spencer, 2017). Even in markets such as agricultural commodities where producers and consumer can be considered atomistic, trade is managed by a small monopoly of commodity traders. This situation seems to be worsening rather than improving. There is increasing evidence that over the last few decades, competition has continually declined across the globe and across industries (Philippon, 2019, De Loecker et al., 2020).

Now it appears that our economic intuition about free trade is wrong if markets are oligopolistic. While, in perfectly competitive markets, government interference with trade will always make things worse, in imperfectly competitive markets, government intervention can often improve the economic outcome. The fact that this kind of counterintuitive effect is possible in specific cases has been known for a long time. For example, Brander and Spencer (1985) constructed a highly specific model in which export subsidies can increase global welfare. In a recent paper, Amir, Jin and Troege (2022) demonstrated that far from being an exception, this type of situation is actually very common. They showed that with imperfect competition, it always possible to improve the welfare of individual countries and even world welfare with either a small subsidy or a tariff.

From a general economic theory perspective, these findings are not new. Lipsey and Lancaster (1957) already showed that multiple distortions in markets do not need to add up, but can also partially offset one another and improve the original situation. It is therefore not surprising that well-targeted trade distortions can increase efficiency if markets are inefficient due to imperfect competition.

Different economic mechanisms can explain why government intervention in trade flows can improve welfare in oligopolistic markets. A very simple effect that explains why subsidies in particular are often good for welfare is based on the fact that subsidies will normally lead to lower prices. Since prices are higher than marginal costs in an oligopoly, this will generally improve welfare.

Another reason why tariffs can improve world welfare, for example, is that in an oligopoly, inefficient firms will produce too much and efficient firms too little, leading to a costly waste of resources. A small tariff that shifts production to more efficient firms, but does not increase overall prices too much, will thus improve overall economic efficiency.

Still another mechanism relies on the different levels of competitiveness in different countries. An import tariff introduced by a very competitive country will not affect prices there very much but might lead to a price decrease in another less efficient exporting country, resulting once again in higher production and welfare overall.

Today's trade policy is at odds with these insights

While very high tariff barriers that interrupt trade between countries exist, they are somewhat rare. In contrast, small tariffs and subsidies are actually surprisingly common. For example, in 2016, 34.8% of US imports were subject to tariffs averaging 3.11% (Leibovici, 2018). Similarly, in the EU, the trade-weighted average of import tariffs in 2015 was 3% (WTO, 2015). Subsidies are equally common, as in agriculture where international trade is dominated by oligopolies (OECD, 2016) or in the high-tech sector. However, to date, the argument that these relatively small tariffs can be optimal in an oligopoly has not been used in policy discussions about trade.

In addition, much of the current trade policy is not consistent with the oligopoly fighting rationale for trade distortions. To generate simple policy implications, Amir, Jin and Troege (2022) ranked the effect of different government interventions such as tariffs, export subsidies, production subsidies, and consumption taxes in a world with imperfect competition. They showed that consumption taxes are always detrimental to welfare. This is surprising since they are usually not even considered as a part of trade negotiations and are instead viewed as an efficient way to raise government revenue (Keen and Ligthart, 2002). In fact, tariffs often turn out to be a more efficient tool to raise government revenue than taxes. In contrast, Amir, Jin and Troege (2022) showed that subsidies are generally beneficial for welfare. This contrasts with the fact that subsidies are increasingly targeted in trade disputes. For instance, export subsidies are explicitly prohibited by the WTO and have been a major cause of the blockage in the Doha Round. Similarly, production subsidies play an increasingly important role in trade conflicts, as in the legal battles between the EU and the US over Boeing and Airbus, or the US-China trade war. The WTO classifies these subsidies as "actionable", i.e., to be prohibited if proven harmful to other countries (WTO, 2006).

Admitting that small tariffs can be useful is not protectionism

Economists have long been reluctant to highlight the potentially positive effects of trade restrictions, fearing that these arguments might be misused by "illiterates in economics incorrectly welcoming me as a new champion of protectionism" (Dixit et al., 2005). However, this position has become increasingly detached from reality. Today, large segments of the population on both the left and the right of the political spectrum share a negative view of free trade, views that were translated into political actions such as Brexit and Trump's trade war. As a result, over the last decade, world trade declined from 60% of GDP in 2011 to 51% in 2020, the first prolonged period of decline since 1945. The Covid-19 pandemic and the ongoing war in Ukraine will likely accelerate this trend. In this context, policy advice limited to arguing for a reduction in trade frictions is unrealistic and could end up being counterproductive (Rodrik, 2017).

Accepting certain types of identifiable small distortions does not contradict with a policy of dismantling major trade barriers and may help to focus the effort of free traders on truly relevant goals. In particular, subsidies should probably be less targeted in trade debates, a relevant insight in a world where many countries need to stimulate their economies following structural damage, supply chain interruptions, and sluggish demand after the shocks triggered by Covid-19.

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Challenges with the rise of superstar firms

Diego Abellán Martínez*
Pramuan Bunkanwanicha

ESCP Business School

Abstract

Over the past 20 years, markets have become increasingly concentrated and have been more intangible-intense. These market conditions have enabled a handful of very large firms, known as 'superstar firms' such as Google, Apple, Facebook, Amazon, and Microsoft (GAFAM), to exert excessive market power and generate massively abnormal profits. Although this winner-takes-all market has clearly generated extraordinary returns for shareholders, other stakeholders have growing concerns. Recent studies show that the increased market power of superstar firms has significantly reduced market competition. As a result, this lack of competition could not only harm consumers from a higher price markup, but also exacerbate income inequality due to lower income share of employees. Lastly, the rise of superstar firms can raise another geopolitical concern for governments. We argue that governments should put more effort into strengthening market competition to deal with these challenges rather than promoting political-driven national champions to compete with superstar firms.

Keywords: Market concentration; Competition; Superstar firms; Inequality

*Global Executive PhD Candidate, ESCP Business School

Challenges with the rise of superstar firms

I. Introduction

Globalization has changed the basis for competition. Nowadays, most firms compete in global markets. Firms implement global strategies to sell their products, acquire raw materials and intermediate products or services, allocate resources, and optimize costs in global markets to be more efficient. Also, governments, under the premise of improving competition, have implemented reforms, including tariff reductions, industry deregulation, and antitrust prosecution. Two trends are currently attracting the attention of stakeholders (investors, governments, and consumers): 1) The increase in market concentration across industries; and 2) the move to a more intangible-intense type of economy (Autor et al., 2020; Ayyagari et al., 2019; Crouzet and Eberly, 2019; Grullon et al., 2019; Lev, 2017).

Both trends are highly observable in the U.S. economy. Over the past two decades, there has been evidence of a significant increase in market concentration with adverse effects on competition. Grullon et al. (2019) analyze whether U.S. industries are becoming more concentrated and find that the Herfindahl-Hirschman index (HHI[60]) between the late 90s and 2014 has increased in more than 75% of the industries, with an average increase in the concentration of 90%. The authors find a positive correlation between the increase in concentration and profitability, mainly driven by firms' ability to extract higher operating margins through higher markups.

The second trend is related to technological change. Technology has become one of the main factors in many industries to achieve competitive advantages. Lev (2017) finds that the association between financial variables and market values was increasingly lower starting in the 1990s. One of the reasons for this dis-association is that intangible assets such as information technologies, R&D, or brands play a significant role in firms' operations but with little presence in accounting. Corrado and Hulten (2010) show the increasing relevance of innovation-related intangibles in recent years as drivers of the growth of the U.S. economy.

This environment has been favorable for the rise of the so-called superstar firm. Superstar firms are those firms that dominate their markets in terms of sales, profits, and returns. Researchers have used alternative definitions of superstar firms. Autor et al. (2020) define superstar firms as the most productive firms in each sector, with above-average markups and below-average labor share. In line with this definition, Ayyagari et al. (2019) distinguish between star and superstar firms. They define star firms in a given year as those firms classified in the top 10% in terms of ROIC, and superstar firms as those firms able to keep these top performances over a long period of time (5 or more years). Other researchers define superstar firms based on market values (Gutierrez and Philippon, 2019; Tambe et al., 2020). Superstar is the appropriate term for Apple, Google (Alphabet), Facebook (Meta), Amazon, and Microsoft. Today, most consumers have an iPhone and use Apple mobile software, use google as their search engine on the internet, Microsoft Windows operating system to run their computers, Facebook for social media, and buy products online

[60] HHI is commonly used to measure market concentration. It is calculated as the sum of the squares of the market shares of the companies in an industry.

with Amazon. Figure 1 presents the evolution of the market to book ratio of the superstar firms compared with the market median.

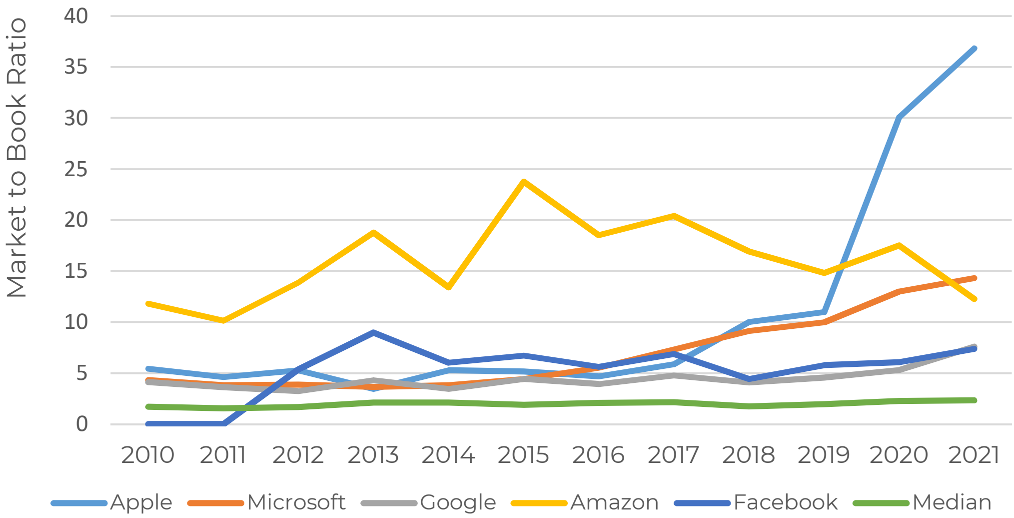

Figure 1. Market to Book ratio for U.S. Superstar Firms – 2010-2021

Source: Compustat. The market to book ratio is calculated as the market capitalization at year-end (Compustat items prcc_f*csho) divided by the book value of common equity (Compustat item ceq). The Median is calculated as the median of the market to book ratio of all listed firms in the NYSE, Amex, and NASDAQ stock markets in a given year. We have deleted firm-year observations with negative sales, total assets, and the book value of equity.

These tech superstars have combined annual revenues of $1.4 trillion, a market cap of $9.2 trillion, total assets of $1.6 trillion, and 2.17 million employees (Amazon has a workforce of 1.6 million, and the remaining four companies 560,000 employees) [61]. Figure 2 shows the dominant positions of these corporate giants in their respective markets. To reference the size of these superstars, the aggregated market capitalization of the Spanish Stock Market is $1.2 trillion[62] (7.7 times lower than the superstars' capitalization), and the Euronext, with a pan-European presence operating the regulated exchanges of Belgium, France, Ireland, Italy, the Netherlands, Norway, and Portugal with around 2,000 listed companies, has an aggregated market capitalization of $7.3 trillion[63]. As an additional reference, the last available estimate for worldwide market capitalization for listed domestic firms (year-end 2020) from the World Bank is $93.7 trillion[64].

[61] Source: U.S. firms Accounting and market data are obtained from Compustat at end of March, 2022. Employee figures are obtained from the 10-K at year-end 2021.

[62] Source: https://www.bolsasymercados.es/esp/Estudios-Publicaciones/Estadisticas. The stock market capitalization includes SIBE , Outcry System, BME Growth, and Latibex.

[63] Source : https://www.euronext.com/en/about/media/euronext-press-releases/euronext-announces-volumes-for-april-2022. Market capitalization at end of March 2022.

[64] Source: https://data.worldbank.org/indicator/CM.MKT.LCAP.CD?end=2020&start=2000&view=chart
Market value is calculated as the number of shares outstanding multiplied by price per share. The sample includes shares of listed domestic companies; shares of foreign companies which are exclusively listed on an exchange (i.e., the foreign company is not listed on any other exchange); common and preferred shares of domestic companies; and shares without voting rights. Investment funds, unit trusts, and companies whose only business goal is to hold shares of other listed companies are excluded.

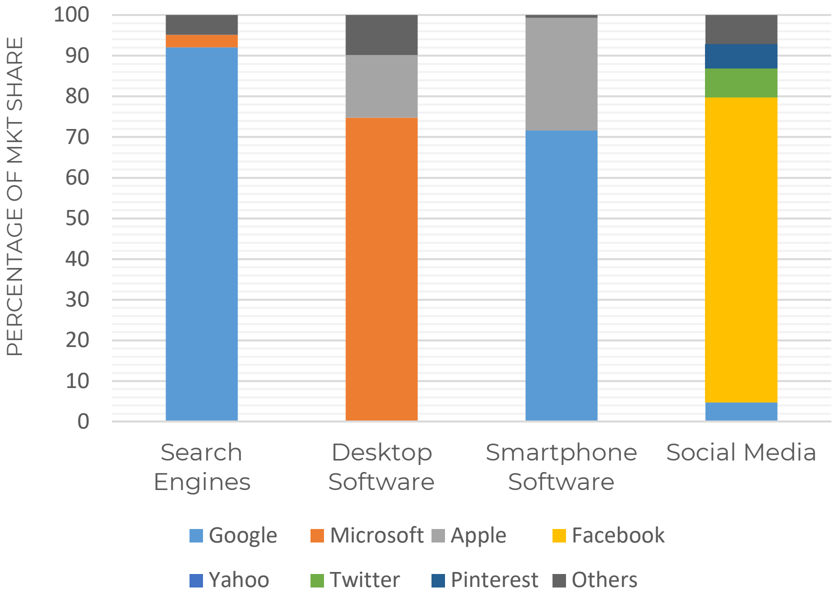

Figure 2. Worldwide Market Share of Selected Markets - %
Source: Statcounter. Market share at April 2022.

There are potential adverse effects associated with a high market concentration in a small number of firms. Bae et al. (2021) analyze three decades of data from 47 countries to study whether stock market concentration negatively affects the economy. The authors find that stock market concentration disincentivizes firms' innovation and slows economic growth. The extreme case is the superstar firms, in which one company or a few control almost the whole market. The extreme market concentration and the growth of revenues at a much higher level than their workforce generate an increase in inequality. In addition, firms with market power search to maintain it in the long term. The interaction between economic and political power creates an additional risk in which superstar firms modify the rules of the game to keep performing as monopolies. Governments need to implement new mechanisms and increase supervision to generate higher competition in those markets.

II. The effects of the superstar firms

a. Superstar firms and market concentration

Superstar firms are an extreme phenomenon of market concentration, dominating their markets almost as monopolies. Market dominance is not new, and there have been previous concentration waves in the economy. The main concern of market concentration is that those firms exercise their bargaining power with customers, suppliers, and employees to obtain extraordinary profits. An additional effect of high concentration is the reduction of investments in innovation. In industries strongly dominated by a leader, laggard firms have low incentives to invest in innovation due to the higher risk of failure (Aghion et al., 2005). Those giant corporates disproportionally dominate the stock market and make it difficult for young start-ups to raise funds. This situation stops the ideal competition cycle, in which firms search for competitive advantages through innovation and generate sustainable economic growth.

This massive market concentration, which is almost a monopoly in each market segment, has generated extraordinary returns for shareholders of the winners rather than enhancing the whole economy. Blonigen and Pierce (2016) analyze whether the net effect of M&A activity generates a welfare gain or loss. In M&A transactions, there is a tradeoff between improvement in efficiencies that generate a welfare gain and market concentration, which produces a welfare loss. They find that M&A manufacturing transactions in the U.S. increase markups but find little evidence of efficiency improvements. Grullon et al. (2019) study whether U.S. industries are becoming more concentrated. They find that higher profits in concentrated markets are attributable to higher markups instead of efficiency improvements. Gutierrez and Philippon (2019) analyze the evolution of the superstar firms in the U.S. economy over the last 60 years. They find that superstar firms have been less productive since 2000 and argue that decreased competition and rising barriers have cut investments and innovation.

Overall, the evidence shows that concentration has increased in the last three decades with an increase in markups, resulting in a reduction in investment in innovation. The superstar effect is widening this gap.

b. Superstar firms and the labor market

Extreme market concentration also affects labor markets. As firms become larger, they increase their bargaining power and can push wages down. Employees have fewer options to move onto other companies when market concentration increases. Powerful firms can also impose restrictions on free labor movements, such as non-compete agreements in which employees have to wait for a specific period before moving to another firm considered a competitor. In recent decades, it is well documented that there has been a fall in the labor share of GDP in many countries. This labor share reduction has interacted with the emergence of superstar firms. Barkai (2020) analyzes the decline of labor and capital shares in the U.S. market. He finds that, since the 1980s, firms have decreased both labor and capital costs and increased pure profits, and this decline is due to market concentration. The decline in labor share and the increase in pure profits, increase income inequality in society, and superstar firms are exacerbating this situation. An alternative explanation of the reduction of labor share is that superstar firms achieve their size through efficiencies, technological improvements, and innovation. The rise of the dominance of superstar firms generates a redistribution of income from employees to shareholders due to these efficiencies (Autor et al., 2020).

c. Superstar firms and political power

The revenues of these superstar firms can rival governments. With the emergence of superstar firms, a massive concentration of economic and political power is in a few people's hands. Zingales (2017) argues that these large firms have enough power to affect the rules of the game, and the interaction of economic and political power is a threat to the well functioning of the free market economy. The interactions between economic and political power are not so harmful when markets are fragmented and competitive, while it is a concern with a massive concentration of market power in a few firms. Superstars have strong incentives to exert their power to obtain long-term abnormal profits by influencing the rules of the game through the political system, suppressing new businesses, and limiting their access to funding to perpetuate their advantages (Braun and Raddatz, 2008; Rajan and Zingales, 2003). Firms can find several ways to exercise their political power. Companies lobby government officials to obtain benefits such as more favorable regulations to allow them to continue exercising their market power or receive government contracts. Lambert (2019) analyzes the relationship between lobbying and regulatory enforcement actions in the U.S. financial sector. He finds that banks obtain a relational power with the regulator through lobbying and benefit from a preferential treatment: Lobbying reduces the probability of being subject to severe enforcement regulatory actions by 44.7%.

d. Summary

Superstar firms have achieved a dominant market position obtaining competitive advantages through innovation and efficiency improvements. For example, Apple has innovated and improved the iPhone's functions and launched the iPad, Microsoft has added new functionalities and made the Office software more friendly, while Facebook has improved users' experience. Once they achieve almost monopolistic positions in their markets, they are incentivized to exercise their monopolistic power with customers, suppliers, and employees to maintain their extraordinary profits. The adverse effects of such a high market concentration are decreased investment in innovation in their industries and lower economic growth. These corporate giants have incentives to employ their political power to perpetuate their dominance at a high cost to society. It is hard for start-ups to emerge, raise funds, and compete with the leaders in these unleveled industries. The concentration of power in a few firms has produced a rise in income inequality, with a high return for shareholders at the cost of a decrease in labor share.

III. Challenges with the rise of superstar firms

a. Risk of extreme concentration

Competition pressure and the threat from new entrants lead firms to set prices with low markups, improving welfare. In markets with no competition, profit-maximization firms with high market power set prices to obtain extraordinary profits. In addition, market power increases firms' bargaining power with employees, reducing the labor share, dampening capital investments, discouraging laggard firms from investing in innovation, and making start-up fundraising difficult. De Loecker et al. (2020) study the evolution of market power in the U.S. economy and its implications. Consistent with the superstar firm evidence, they find that the upper-tail U.S. listed firms experienced an increase in both markups and profitability between 1980 and 2016, while most firms in the market did not raise markups. They also find evidence that profits and market values of upper-tail firms have gone up with markups, providing support for the argument that market power is the cause of the reallocation of the economic activity toward larger firms with low labor shares, resulting in a net negative welfare effect.

Under this framework of increased market concentration, there is an intense debate about protecting local businesses by creating national champions. In order to facilitate the emergence of national champions to compete with superstar firms, governments may use state aid or subsidies, give them preference in government contract biddings, or create artificial barriers, making it difficult for international companies to enter the local markets. These national champions can even be state-owned companies. The final goal of creating national champions is to promote innovation and economic growth, but it can generate adverse effects related to lack of competition. Examples of these national champions are the Chinese companies Huawei, the top global player in telecom equipment, and CRRC, the largest rolling stock manufacturer worldwide. In Europe, there is a debate on whether state policy should be more flexible to allow the creation of European champions. So far, the antitrust regulation in the E.U. has been strict. One example of this, is the opposition to Siemens' proposed acquisition of Alstom. The merger would have created a European champion in the railway industry, but the E.C. supported the idea that this merger would harm competition in the signalling and high-speed markets, as both companies were dominant players in these segments.

Companies with market power use their bargaining power to extract rents by increasing markups and reducing labor share. The increase in markups severely affects the poor, who overpay for the goods without benefitting from these extra profits and capital gains. The increase in market concentration is generating greater inequality. Ennis et al. (2019) analyze whether market power contributes to increasing wealth inequality using a sample of eight OECD countries by comparing the current levels of market power with an alternative scenario of competition enhanced. They find that market power can contribute significantly to inequality by increasing the wealth of the 10% richest group by an average between 12% and 21% and reducing the income of the 20% poorest group by 11% or more.

The lack of competition in markets where the winner-takes-all exacerbates income inequality due to extraordinary capital gains to shareholders at the cost of employees and the concentration of those capital gains in the wealthiest compared to the poor groups.

b. *Risk of an increase in political power*

The main concern associated with superstar firms is monopolistic power. Supersize firms can generate artificial barriers to entry, limiting competition to maintain extraordinary profits. Zingales (2017) highlights that three factors make the market power problem worse: 1) the dominant position of superstar firms is larger, increasing their bargaining power with consumers; 2) regulation is too complex, which allows powerful firms to shape the rules of the game to their benefit; and 3) the anti-big business Democrat party's ideology has floundered so that you are no longer castigated being close to supersize firms. In economic terms, political power is affected by firm size and market concentration. Corporate giants are the main driver of the cities where they are located and are one of the central employers in the area. These firms are in an optimal position to receive tax subsidies and other benefits and are able to pressure governments in obtaining their corporate goals. Superstar firms are extreme cases of market concentration and firm size.

One example of the monopolistic power exerted by superstar firms is described in the European Commission ("E.C.") antitrust filing against Google. In 2016, its search engine's share in almost all EAA markets was above 90%. The E.C. concluded that Google abused its dominant position by providing an anti-competitive advantage over competing services to another Google product, the Google comparison shopping service. The Commission imposed a record fine of $2.7 billion. In May 2018, the La Quadrature du Net initiated a collective legal action against Amazon, arguing that the targeted ad system uses personal information without free consent. In July 2021, the Luxembourg National Commission for Data Protection ("CNPD") imposed a fine of $887 million on Amazon for breaching the E.U. General Data Protection Regulation ("GDPR"). Amazon disclosed the information in its quarterly financial statement report ("10-Q")[65].

IV. Conclusion

During the last twenty years, most industries have experienced higher concentration. In this environment, superstar firms have emerged in industries where the winners take all (or most), resulting in a few companies with an extremely high market share, high markups, and high profitability. Superstar firms have developed their competitive advantages levered in technological improvement and innovation, augmenting sales at a much higher rate in relation to workforce increase. This effect has generated wealth creation for superstars' shareholders at the cost of the labor force, increasing inequality. This unequal structure in which superstar firms are far from the laggard firms will continue penalizing labor share and generating inequality. Regulators need to look for tools to improve competition within these industries, such as facilitating access to funding for start-ups and reducing regulatory and artificial barriers to competition. Otherwise, inequality will continue to increase.

In order to encourage market competition, governments need to break down barriers artificially created by firms with such economic and political power. Powerful firms can seek to maintain their dominant position through acquisitions. They can also wedge on market dominance to extend their power to other markets. The antitrust objective is the protection of competition to benefit consumers. Antitrust enforcement must be strict about disincentivizing powerful firms from searching for market power. A necessary condition for antitrust bodies to properly monitor market power is to have access to transparent disclosure of corporate activities.

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"Dancing in the dark": Regulatory reforms and incumbent banks' evolution towards new value creation models in the process of open banking

Regis Coeurderoy
Matilde Guilhon*

ESCP Business School

Abstract

Recent major regulatory reforms within the context of Open Banking have triggered the rise of technology-driven firms in the financial services sector. Consequently, they have encouraged banks to rethink their value creation models. Banks may shift from pipeline and vertically integrated value creation models towards platform ones. However, in highly uncertain environments, when radical innovation resets the counter to zero, incumbents cannot just do business as usual. They need to reinvent the way of doing business and thereby redefine the foundations of legitimacy. This article explores towards which platform value creation model banks are currently moving and examines what underpins banks' choices. Using hand-collected data covering the largest French banks, we investigate how banks strategically use external growth operations to chart the course towards new value creation models. We shed light on key salient features in the choices made by banks toward these new platform models. We particularly notice that, when "dancing in the dark", the incumbents facing radical uncertainty tend to develop mimical actions in order to maintain their space of legitimacy–what we call a herding effect.

Keywords: platforms; value creation models; retail banking; open banking; incumbents; external growth operations

*Ph.D. Student, ESCP Business School & Square Research Center

“Dancing in the dark”: Regulatory reforms and incumbent banks’ evolution towards new value creation models in the process of open banking

Introduction

In recent years, advances in technologies have enabled the rise of digital platforms that address a wide range of activities in most sectors and challenge incumbent firms (Parker & al., 2016). The banking sector, which seemed to be spared because of high barriers to entry, is nowadays facing this rise of technology-driven innovations as well as the emergence of new players benefiting from new regulations (e.g., Fintechs, start-ups). While traditional retail banking models are weakening, generating less profit, and facing increasing competition from new players, banks are searching for new value creation models. In this context, banks are moving towards platform-based business models that are more customer-oriented and offer seamless and user-friendly services. These models enable the unlocking of new sources of supply and value creation and remove ineffective control processes which tend to make incumbents more complex, reducing their capacity to innovate (Parker & al., 2016). The platformization movement we observe in most sectors refers to a “*shift from individual products/services to platforms as intermediaries for transactions and for organizing value creation processes*” (Nambisan & al., 2018:355). In platform ecosystems, the platform owner acts as market intermediaries between multiple groups of users. It aims at fostering the formation of ecosystems of complementary firms that offer their products and services within the platform, thus creating value for both its users and the platform owner (Nambisan & al., 2018).

Adapted to the banking sector, this move towards novel banking models implies the opening up of banking core technological infrastructure, the integration of new services and the building of a platform to offer such services. We observe the emergence of two distinct platform banking models: Banking-as-a-Platform and Banking-as-a-Service. Banking-as-a-Platform for a bank consists of integrating offering new services provided by third parties, that cover both financial and extra-financial products. As for Banking-as-a-Service, it depicts a model in which a financial institution (generally an incumbent bank) makes its core technologies and infrastructure available to unlicensed players on a white label basis via APIs. While both models correspond to platform-based banking models, they differ in terms of value creation and structure. For incumbent banks, the development of such business models requires open service infrastructures enabling this intermediation, which is challenging in terms of their IT legacy and organizational complexity (Hornuf & al., 2020). Moreover, the extension of products and services offered by incumbent banks raises the question of banks’ legitimacy to deviate from their core activities. Following this logic, banks are more inclined to develop interactions with external firms, including the very start-ups and Fintechs that threaten them.

But, in times of technological disruption and competitive uncertainties, the incumbents cannot benefit anymore from traditional landmarks to make decisions and have no choice other than reinventing a way towards new value propositions. As a reaction to the ongoing changes that threaten traditional models, banks respond by using external growth operations (partnerships, equity investments, and acquisitions) to foster the transformation process. In this paper, we investigate how banks use partnerships and external growth operations to find out which value creation model (Banking-as-a-Platform or Banking-as-a-Service) banks are moving towards.

Digital transformation of the banking world

Multiform developments lead to a high uncertainty in the banking sector

Technological innovation and digitalization have created new challenges for incumbent banks by creating new market standards and modifying their competitive landscape. Digitalization is changing consumers' expectations and uses. Banking customers have developed novel expectations: they are now looking more for tailor-made solutions adapted to their specific needs instead of standardized banking products. Moreover, users want to manage their finances wherever they are, without any delay or friction. Baranov (2019) summarises the new expectations of banking customers with the acronym TIPS: transparency, immediacy, personalization, and simplicity.

In Europe, the recent regulations implemented by the Competition Market Authority in the UK and the Payment Systems Directive (PSD2) in the EU have opened the banking sector to new players (Fintechs and start-ups) by shifting the intellectual property on data from banks to their clients. Since when, banks must provide authorized third parties access to customer and payment account information. These third parties can now use the data made available by banks to define new value propositions. These changes have paved the way to a new model, called 'Open Banking', that is a reconfiguration of the competitive structure with new players offering new value propositions based on innovative value creation models. Open Banking is a banking system in which retail and business customers allow their banks or financial service providers to use their financial data using APIs (application programming interfaces). Open APIs enable third parties (developers) to access and exploit financial data to create new services and financial solutions. The underlying idea is to guarantee better financial transparency for account holders (Wewege & al., 2019), in order to promote competition in the retail banking sector and to enhance clients' experience.

Together with regulatory evolutions and technological changes, the emergence of value creation models represents significant changes in values and practices corresponding to a paradigm shift in the retail banking sector (Omarini, 2018). In short, banks in the European Union must comply with PSD2 directives which force them to open their data to third parties. They could either choose to drag their feet regarding the application of these rules or try to take advantage of them. In the latter case, opening its data and partnering with the third parties would be a means to diversify banks' revenue streams, adapt their value propositions to changing demand and improve their technological abilities.

Legitimacy challenges arising in the banking sector

In addition to the regulatory and technological evolutions, as well as the changes in demand, banks currently face legitimacy challenges. Banks' legitimacy depends very much on stakeholders' confidence in their ability to properly act as an intermediary between economic agents to finance economic operations. It is based on their ability to serve customers' interests, to guarantee the security of their funds and the return on their savings, and to optimize the use of their money. Historically, banks were seen as actors behaving positively for the economy, enabling firms and individuals' transactions, ensuring their proper economic development.

However, the rapid rise of new entrants (e.g., neo-banks and Fintechs) who are developing novel value propositions, is evidence of changes within audiences' perceptions of how banks should behave and what they should be offering their customers. For instance, the rise of neo-banks offering cheaper banking fees in exchange for no-direct access to advisors, proves that the ability of banks to guide investment decisions through advisors is no longer a determinant of their legitimacy. The multiple economic crises since the 1980s, and especially that of the 2008 crisis that shook the global economy, demonstrated banks' weaknesses in ensuring economic stability and in satisfying common interests. The legitimacy of these banks has therefore been altered, resulting in lower customer loyalty and a decrease of confidence within audiences. Nonetheless, banks remain an unavoidable key player in the financing of the economy.

In addition, perception by customers of a certain inertia in incumbent banks is affecting their legitimacy to transform their business models by investigating new fields of activity and proposing innovative value propositions (Benner, 2007). Therefore, banks are facing a dilemma: trying to regain some of the legitimacy they have lost, while retaining their existing legitimacy in their core business. By extending their activities to customers' renewed needs, banks tend to put customers back at the heart of their strategies, and in order to regain a market legitimacy that they seem to have lost through past crises. However, this differentiation could be perceived as illegitimate regarding the expectations of audiences towards banking activities. This is what we call the strategic challenge of "dancing in the dark".

Experimenting with a new value creation model using external growth operations

External growth operations deployed by banks take the form of partnerships, product co-developments, joint ventures, equity investments and acquisitions. From the perspective of developing novel business models, these operations enable firms to develop novel competitive advantages while protecting their core business (Hagedoorn & Duysters, 2002), and to facilitate the adaptation process (Cozzolino & al., 2018). Specifically, in the case of platform models development, external growth operations are frequently used to build the technological capabilities and the foundations of the platform ecosystem. These past few years, incumbent banks have increased their external growth operations with new players, especially Fintechs and start-ups. Banks perceive Fintechs as a solution "*to create value at the core of the bank's financial-innovation activities through agile digital transformation*" (Wewege & al., 2020: 29). This type of collaboration enables banks to achieve cost and scope savings by exploiting similarities and complementarities with Fintechs. Second, banks form external growth operations with start-ups and with more established firms that are developing activities in multiple non-financial segments. This is an opportunity for banks to develop new sources of value in extra-banking segments and to meet their customers' renewed expectations, by offering integrated and comprehensive solutions rather than a portfolio of individual services.

Focusing on the the fifth largest French banking groups (Société Générale, BPCE, Crédit Mutuel Arkéa, Crédit Agricole, and BNP Paribas), which represent 76% of total assets in the French banking sector,we hand-collected extensive data of external growth operations conducted by thanks banks and their subsidiaries. We focused on external growth operations carried out between 2015 and 2021. Our sample consisted of 188 external growth operations conducted by five banks and their subsidiaries. We observe a steady and continuous increase in the operations conducted by our sample banks since 2013. From 2019 onwards a clear acceleration for these active banks has been noticed.

Key salient features of recent operations

Salient feature 1 – the rush towards Banking-as-a-Platform model

As mentioned by a banker during our interview, "*banks have been designed in a closed ecosystem, and therefore, they are the opposite of Open Banking*" (verbatim). The transformation towards a platform-based business model is particularly challenging for banks. This explains why banks develop their new platform models gradually, following an iterative approach based on test-and-learn. Indeed, there is no clear and explicit strategy communicated by banks regarding Open Banking. Banking-as-a-Platform operations are numerous compared to other strategies : the share of external growth operations corresponding to a Banking-as-a-Platform strategy is 72%, while 9% correspond to a hybrid strategy.

Banking-as-a-Service strategy represents less than 9% of the total number of operations. Banking-as-a-Service is the most difficult to characterize as this model has not yet reached its final form. With the notable exception of Société Générale which claimed its willingness to be a Banking-as-a-Service pioneer, other French banks are relatively more cautious. Banking-as-a-Service models constitute a lever to capitalize on banks' core IT by monetizing its infrastructure and its services. However, the development of such models is complex for several reasons. As evoked by an interviewee, the deployment of Banking-as-a-Service model could be technically challenging: "*you might have the best product,but if your Information Systems are not able to be easily visible or interconnected, you can't do anything. That is the tragedy of some banks, they don't have Information Systems that were designed to be open*" (verbatim).

Salient feature 2 – A strongly diversified exploration in new universes

Through their Banking-as-a-Platform operations, banks expand in multiple universes of needs. This trend is relatively stable from one bank to another, which reveals banks' preference for a cross-universe Banking-as-a-Platform strategy.

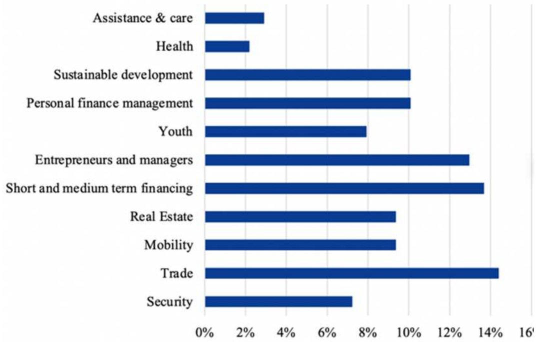

Figure 1 - Distribution of Banking-as-a-Platform operations by Universe of needs

A greater number of operations relates to universes close to core banking services (e.g., trade, short- and medium-term financing, services to entrepreneurs and managers) compared to universes far removed from banking traditional activities (e.g., real estate, mobility, youth). This raises the question of banks' legitimacy to explore market segments far from their traditional activities. Offering a plethora of extra-banking services to their clients might increase the added value banks bring to their clients. However, going beyond their field of banking expertise can damage their legitimacy. A bank's field of expertise is limited, and extending a platform strategy that is too far from its initial competencies can make it be seen as an illegitimate player investing in this economic field. The first Banking-as-a-Platform strategies can therefore be seen as a way of experimenting a banks' legitimacy to be present in certain market segments. The number of banking operations in universes far from their core business[66] has accelerated since 2019 : 47% have been conducted between 2019 and 2022.

Most banks have conducted operations in universes close to their core business, as well as in trade, health, and security. However, we found that these banks made different choices when it comes to exploring universes far from their core business. For instance, Crédit Agricole has carried out the most operations identified in the sustainable development universe. Operations related to youth were mostly realized by Société Générale; the bank has created a platform dedicated to 18–24-year-olds and develops partnerships, enhancing the portfolio of extra-banking services offered. As for mobility, this universe has raised banks' interest in recent years. Société Générale has been a pioneer in the universe, closely followed since 2019 by the other banks.

Meanwhile, in mutualist banks, the parent company conduct significantly less operations than its subsidiaries. For instance, the operations of Crédit Mutuel Arkéa are carried out mainly by their subsidiaries, which are federations with a strong regional footprint. In contrast, the two largest capitalist banks – BNP Paribas and Société Générale – develop their operations mostly through their parent company according to group strategy.

Salient feature 3 – Ally rather than buy!

Banking-as-a-Platform operations are mostly deployed through partnerships, which are more flexible than equity investments and acquisitions, and require a low level of integration. Banks widening their range of activities are likely to prefer partnerships with external partners, especially when they explore value propositions far from their core activities: "*If it is too strategic to do it with an external partner, we do it internally. But this happens in rare cases and even less so when you are outside the banking business.*" (verbatim)

When banks aim at internalizing new technologies and capabilities, their operations naturally take the form of incubation or investments, be they minor equity investment or full acquisition. Hence, banks can often obtain representation in the target's board, enabling them to drive the target's strategy towards its future interests and have full control over the resources of the target.

Salient feature 4 – Banking-as-a-Platform exploration through strategic partnership; equity investment for the others

We found a relationship of dependence between the strategy pursued by a bank for a given operation and the nature of this operation. There are more Banking-as-a-Platform operations using strategic partnerships than would be expected if there

[66] i.e., « Security » « Trade », « Mobility », « Real Estate », « Entrepreneurs and managers », « Youth », « Sustainable development », « Assistance & Care », « Health »

were no association between the strategy corresponding to the operation and the nature of the very operation.
Our results also show that Banking-as-a-Platform operation corresponds to a market-driven approach. These operations enable banks to enter new markets by developing interactions with non-financial firms and thus enriching their offers. Indeed, banks could benefit from the existence of a nascent ecosystem around banking services that could renew customers' experience, enhance their value propositions, and generate more profit since the bank positions itself as the central actor of the platform.

Salient feature 5 – Banks' strategic choices: a herding effect
Since there is no guarantee about the profitability and long-term viability of the two platform models – Banking-as-a-Platform and Banking-as-a-Service -- banks are navigating in a highly uncertain environment. The herding effect describes a social dynamic in decision-making in which actors follow the actions of their peers (Bikhchandani & al., 1998). In the absence of rationality and sufficient information, it becomes rational for managers to imitate the decisions of other managers. Banks can easily track the ongoing operations led by other banks through banks' official releases and public announcements. We use cumulative number of operations per universe as a measure of herding. This measure reflects banks' collective assessment of a certain universe of needs. We argue that banks as a whole exhibit herding behaviour if the cumulative number of aforementioned banks positively impacts the decision of other behaviour. We found concrete proof for the existence of herding behaviour in banks' decisions of collaborating with external partners and Fintechs. For instance, Société Générale collaborated early on with mobility actors, and after 2019, this universe was also being investigated by other banks.

Conclusion

Using a hand-collected dataset of 188 operations carried out among the five largest French banks, we found that banks have mostly opted for the Banking-as-a-Platform model. Our findings show that this strategy generally aims at expanding into new market segments, while the motivations underlying Banking-as-a-Service operations are less clear.

Banks are facing paradoxical pressures between conformity to their core activities in which they are perceived as legitimate, and differentiation that could help them renew their competitive advantage. This dilemma, referring to the "optimal distinctiveness" paradox, constrains incumbents in their transformation projects (Zhao & al., 2017). Developing partnerships appears to be a solution to overcome this dilemma in this very context. We also provided evidence of the existence of salient features in the development of incumbent banks' platform models. We can interpret this result regarding the high level of uncertainty characterizing the Open Banking context, as inducing herding effects among incumbent banks.

In highly uncertain environments, when radical innovation resets the counter to zero incumbents cannot just carry on business as usual. They need to reinvent the way of doing business and consequently their foundations of legitimacy. But it can be like dancing in the dark near a precipice. So, what do you do in such a case? You dance as the others do, hoping that where you are all dancing is the dance floor – what we call the herding effect.

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Implications for investor portfolio choice of salience shifts regarding geopolitical risks and sustainability issues

Houdou Basse Mama

ESCP Business School

Abstract

I examine the extent to which temporal shifts in the salience of geopolitical risks may impact investor portfolio choice with a specific focus on sustainable investing. Specifically, I seek to bridge research on issue salience, geopolitical risk, and the burgeoning but rapidly growing literature on sustainable investing. Indeed, casual observations support the view that geopolitical shocks, such as the ongoing Russia-Ukraine conflict, not only reveal flaws in sustainable investing but also most likely significantly weaken the argument of genuine salience of sustainability issues in investor portfolio choices.

Keywords: portfolio choice, responsible investing, geopolitical risks, issue salience.

Implications for investor portfolio choice of salience shifts regarding geopolitical risks and sustainability issues

The fragile rise of responsible investing

Estimations of the Berlin-based Mercator Research Institute on Global Commons and Climate Change (MCC) suggest that the atmosphere can absorb no more than 1,060 gigatonnes (Gt) of CO_2 if the objective of policymakers is to stay below the 2°C threshold. If true, keeping current emissions of CO_2 at a constant level, the available global carbon budget would be exhausted in about 25 years[67], making it clear how urgently concerned decision-makers need to take action. Notwithstanding that undoubted urgency and the fact that over 80% of the CO_2 emissions can be associated with industrial pollution, so far there have been few incentives for corporations to internalize the social costs associated with the impact on the natural environment (Basse Mama & Mandaroux, 2022). This manifest inaction has prompted most countries to establish a number of schemes meant to curtail corporate greenhouse gas emissions. However, countries differ considerably in how (successfully) they tackle this climate change challenge (e.g., Koch & Basse Mama, 2019).

Given half-hearted commitments of major global emitters of greenhouse gases (especially the United States and China) to curb emissions as well as corporate procrastination, it appears that the burden of fighting against the degradation of the natural environment eventually rests on daily decisions of environmentally-conscious citizens and corporations (Shive & Forster, 2020). In this vein, the last two decades have been characterized by a steadily growing public awareness of climate change and potential adverse effects of greenhouse gas emissions on, for eample, cognitive functioning, the hazard of deadly diseases, or risk aversion. As a result of both the growing awareness and the various environmental regulations underway, investors not only increasingly require that environmental, social and governance (ESG) factors are incorporated in investment and security analysis (Amel-Zadeh & Serafeim, 2018), but they also influence their investee firms' ESG choices (e.g. Dyck et al., 2019). However, critical observers contend that over time, the ESG movement has "transitioned from doing good to doing well and from plow-minded investors to banner-minded and pseudo-ESG investors" (Statman, 2020, p. 16).

Regardless of whether or not investors are using the label of sustainable investing as a fig leaf, a question of paramount interest is whether we would be right to assume that the level of salience of environmental issues in investor portfolio choice is constant over time. To address this question, we start by relying on a few empirical accounts.

Research shows that the financial value of firm-level social and environmental responsibility has substantially increased following the 2008/2009 global financial crisis. As would be expected, financially motivated investors have started asking their investee firms for more environmental and social activities following the financial crisis (Dyck et al., 2019). Similarly, exploiting the 2008/2009 global financial

[67] https://www.mcc-berlin.net/fileadmin/data/clock/carbon_clock.htm (Accessed 1 June 2022). The same source estimates that, in the scenario of 1.5°C, the global carbon budget would be exhausted in even less than 8 years from now.

crisis as an exogenous shock to the salience of corporate sustainability, Basse Mama and Fouquau (2022) find that the marginal investor would assign far too low a market valuation to corporate environmental innovation in the period up to 2007 compared to the valuation attached to corporate environmental innovation post-shock. That is, the financial crisis may well have sharpened awareness on ethics and the degradation of the environment in the financial industry.

I build on the foundations of institutional theory to assess the extent to which and how abrupt a shock to the sixteenth social development goal of the United Nations (UN SDG 16), in casu the Russia-Ukraine conflict, might have affected the propensity of institutional investors to make investment decisions in accordance with the principles for responsible investment.[68] Institutional theory posits that when confronted with demands from heterogeneous stakeholder groups that are far too incompatible, real decision makers (e.g., corporations, governments, and investors) will respond to these external pressures based on perceived issue salience (Bundy et al., 2013). This in turn depends on the perceived urgency and legitimacy of the issue at hand. In any case, if, when, and the degree to which real decision makers will respond to stakeholder pressures, hinge upon the perceived costs of benefits of mobilizing and committing resources (Durand et al., 2019).

Shaky salience of sustainability issues in the financial market amid geopolitical shocks

Clearly, the current geopolitical context shifts public and investor attention towards the political and economic developments of countries in which the firms operate, yet investors care to a larger extent about potential reputational risks arising from their investments in companies that operate in/with the countries in conflict. As a result of restrictive sanctions against Russia from the United States and the European Union (EU), there has been a generalized surge in the political risk exposure of firms that operate in an international setting. It thus comes as no surprise that the Russian military aggression against Ukraine makes continued engagement of corporations in Russia a source of looming reputational risks. However, seen through the prism of Western corporate withdrawal from South Africa in the 1980s, the current seemingly 'voluntary' withdrawal of a number of corporations from Russia[69] can hardly be viewed solely from the angle of the willingness of the respective firms to promote peace. Actually, we have been witnessing a radical shift in sentiment in the EU on defense spending, with, for example, Germany planning to massively increase military spending by €100 billion. At the same time, some governments in Europe (e.g., Germany and the United Kingdom) are planning to diversify the portfolio of their energy suppliers moving steadily away from Russia toward such countries as Qatar, Saudi Arabia, Iran, and Venezuela (all countries whose records on human rights and social issues are poor). In Germany, the change in the diversification strategy even includes (1) mulling over an extension in the lifetime of the last three nuclear remaining power plants that

[68] Please, access the following link to see the six principles: https://www.unpri.org/about-us/what-are-the-principles-for-responsible-investment (Accessed 1 June 2022).

[69] https://som.yale.edu/story/2022/almost-1000-companies-have-curtailed-operations-russia-some-remain (Accessed 1 June 2022).

were initially planned to be phased out by the end of 2022[70], and (2) temporarily increasing the use of domestic coal reserves.

The severity of the invasion and the extensive press and analyst coverage of the massive destruction with nearly 7 million Ukrainian refugees in just a few months has sparked a sense of urgency, prompting public outcry, reminding the international community of the need to rapidly take appropriate actions.[71] In addition, it should be emphasized that Ukraine is a key global exporter of commodities such as corn, sunflower oil, and wheat. Thus letting the war wipe out a substantial portion of the harvest might lead to pronounced global shortages, higher food prices, and famine especially in the developing world. These aforementioned arguments attest to both the relevance and urgency of the issue at hand. Notwithstanding, firms and investors might not directly draw from this urgency an obligation to act; this will only occur when there is a sort of legitimacy in doing so.

The fly in the ointment in the observed sentiment shift is that, for example, the current German government is a coalition of social-democrats, liberals and Greens. While sustainability-focused investors would typically shun stocks of firms making revenues from weapons or products with a high carbon footprint, the observed historic shift in the sentiment in the EU and the United States about national security allows the question of whether the Russian invasion of Ukraine has rendered investment in stocks of corporations operating in the defense, oil, and gas sector, suddenly socially acceptable even by sustainability-focused investors. The same question applies to making business with countries known to not particularly care about human rights and product responsibility. The EU might have indirectly legitimized increased reliance on natural gas and oil by clearly choosing to include US export of liquefied natural gas (LNG) in their new energy plan, which jeopardizes the objective of the attainment of a carbon-neutral and inclusive economy by 2050. Investors may even draw legitimacy in sustained investments in fossil energy given the revitalization of the sector (in Africa) by governments of developed nations such as Germany and Italy.

As a result, institutional investors have strong incentives to gain, maintain, and defend their legitimacy by responding to the normative pressures arising from the ongoing Russia-Ukraine conflict. If true, I anticipate that even sustainability-focused investors might be tempted to deceptively derive saliency of investing in non-Russian fossil energy stocks, in stocks of weapons and small arms manufacturing corporations. However, there might be cross-sectional variations in the responses by corporations and institutional investors around the globe given that grand societal challenges are in essence "value-laden and socially constructed" (Voegtlin et al., 2022, p. 13).

To the extent that at this time of writing, we only can rely on anecdotal evidence of the (in)ability of the current geopolitical shock to induce a shift in investor portfolio choice, an interesting line of research would relate to addressing this research

[70] FAZ online: https://www.faz.net/aktuell/wirtschaft/die-gruenen-streiten-ueber-atomkraft-und-energieversorgung-17849568.html (Accessed 5 June 2022).

[71] This link provides an overview of the sanctions by the EU: https://ec.europa.eu/info/strategy/priorities-2019-2024/stronger-europe-world/eu-solidarity-ukraine/eu-sanctions-against-russia-following-invasion-ukraine_en (Accessed 2 June 2022).

question within an international setting; the international setting is necessary if putting an end to the Russia-Ukraine were to qualify as a grand societal challenge. An ancillary but related research avenue would be to investigate the determinants of the differential responses of corporations to the heightened normative pressures arising from the conflict. Why should some firms exit, some curtail operations, while some would be continuing operations in countries under embargo? Most importantly, has the conflict revealed the limits of the sustainable finance initiative of the EU? This question is embarrassing as the answer seems to be in the affirmative. Therefore, the EU would need much more energy and effort to convince other players on the salience of sustainability in the financial sector. To put it in an intentionally provocative way, the way policymakers have responded to this shock in terms of diversifying energy sources and suppliers shows that ecological sustainability might come well after social sustainability. Is there any primacy left in the ESG-acronym? For the moment, the EU seems only to have focused on the "E", but is this choice warranted?

Conclusion

Geopolitical shocks such as the Russia-Ukraine conflict reveal the shaky foundations of the salience of sustainability issues in the financial industry. Unfortunately, the sustainable finance initiative of the EU relies so heavily on the financial industry (that it makes them?) redirect capital from polluting industries towards those industries meant to be environmentally sustainable. Amid the current conflict, it appears that attainment of such sustainability in the financial industry is much more tedious than assumed so far. An important 'shady' side of the response of major governments to the conflict with its attempts to reduce its dependence on Russian gas (for example, Germany is striving to develop natural gas fields with Senegal) raises the questions of double moral standards: Why develop fossil energy in developing countries when the goal is to increase renewable energy sources at home? To me, such ambiguous signals of the public hand are counter-productive in convincing the financial community about the salience of sustainability in the financial industry.

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From counting to giving account: Citizens auditing the 2022 Hungarian parliamentary elections

Mariann Györke *
Zsuzsanna Vargha

ESCP Business School

Abstract

Against the backdrop of fake news and distrust in electoral processes, what is the value of citizen ballot-counting? We take the case of ballot count volunteers on behalf of opposition parties in Hungary concerned about voting fraud by what they saw as an increasingly authoritarian regime, amidst the uncertainty of war in neighboring Ukraine. Analyzing volunteers' publicly shared audit stories as acts of accountability, we found a surprising result. The quantitative and control-driven auditing task spilled over and generated qualitative knowledge about the "countryside", a newly discovered social reality for urban volunteers. They reported unexpectedly harmonious cooperation during potentially controversial audit tasks, as well as "getting along" with the dominant party's officials. However, they were dismayed by what they perceived as the voters' shocking living conditions and political ignorance. In an audit of society, the rich ethnographic descriptions helped volunteers to account for the sweeping victory of Fidesz. Counter-accounts have criticized the volunteers' discoveries for their condescending depiction of voters, closing the circle of accountability. These field observations from a "popular" process audit suggest that ethnographic experiences are part of any formal audit, contributing to collective knowledge-making about the subject of the audit, in this case, the election result.

Keywords: Audit, accountability, elections, fraud

*Ph.D. Student, ESCP Business School

From counting to giving account:
Citizens auditing the 2022 Hungarian parliamentary elections

"It was a huge eye-opener for me as a young student in Budapest.
These people live in unimaginable depths."
Ballot count volunteer, public Facebook post

Introduction

The war in Ukraine was quickly translated into a stark political message during the electoral campaign in neighboring Hungary in early spring 2022. According to Viktor Orbán, the country's prime minister, "the stakes [of the parliamentary elections] are war and peace"[72]. The illiberal head of state meant that voting for his Russia-friendly Fidesz party would preserve peace, while voting for the coalition of opposition parties that spoke out against the Russian invasion would draw the country into war. This black and white message was highly contested by the coalition of left and right-wing parties that arose to challenge the increasingly entrenched government.

The political landscape in Hungary has remained largely unchanged since 2010 when Fidesz obtained a two-thirds majority in parliamentary elections, despite repeated attempts to reduce its majority by opposition parties. Following reports of suspected voting fraud and a vastly uneven campaign landscape in previous elections[73], new organizations assembled tens of thousands of citizen-volunteers to audit the voting process at every polling station, monitoring voting and performing the local vote count as representatives of the opposition parties.

The ballot count volunteers produced striking reports about the fairness of the election, which they shared on social media. Surprisingly, their reports contained very little about numbers, voting irregularities, or the voting process. Instead, the factual descriptions gave way to bewilderment at seeing first-hand how "the other half of the country" lives. The largely urban, educated and progressive-minded volunteers described the conditions they encountered across the country with ethnographic detail, expressing shock and talking about a transformational experience.

In the following, we interpret this unexpected turn from a quantitative mission into a qualitative experience of socio-economic difference. First, we introduce our empirical setting and discuss ballot count monitors through the lens of audit and accountability, then analyze our data collected from publicly posted narratives. Based on our preliminary results, we argue that while intending to hold the state accountable, the ballot counters shifted to an "audit of society", for which they in turn were held accountable in a "circle of accountability". We conclude by reflecting

[72] https://magyarnemzet.hu/belfold/2022/04/orban-viktor-a-haboru-es-a-beke-a-tet-2

[73] https://www.osce.org/odihr/elections/hungary

on the nature of audit work, and on how societies exist within societies in a post-truth political environment.

The volunteer movement for a balanced vote count

One lesson drawn from reports on preceding elections was that the local voting process was insufficiently monitored as opposition parties did not have volunteer delegates in half the polling stations and could not verify how the votes were counted[74]. In response, civic organizations emerged in advance of the 2022 elections to organize ballot-counting volunteers, most notably 20k22. Citizens were called on to "hold the state accountable in the name of democracy"[75]. A total of 28,000 citizens volunteered, 19,700 of whom completed the rigorous online training course and qualified as ballot count delegates. The movement's success meant that at least one opposition party counter was delegated in 99% of polling stations to complement elected and Fidesz officials.

A process audit

On election day, members of the Electoral Count Committee (including the volunteers) had to be present from 5:15 am until the count was completed and declared closed after full documentation, usually past midnight. Their tasks were threefold:

1. participation in the voting process (registering voters, giving out ballot sheets, checking ID cards, accompanying the mobile ballot box) and in the ballot count (sorting invalid and valid ballots, manually counting the votes on paper sheets, recounting)
2. observation and assurance of the lawful conduct of the voting process and the ballot count
3. checking for and reporting on anomalies.

The task was completed by sending the official minutes to the delegating NGO (20K22 or SZAM), and filing an official report of any misconduct.

To qualify as a ballot count delegate, citizens were trained in a disciplined and highly structured process which prepared them for the audit task. Their e-learning course consisted of 8 modules, with a grade of 80% required in each module. Upon completion, they were assigned to one of 10,285 polling stations, and bore all costs of travel. The Handbook of Volunteer Ballot Counters[76] details the procedures for the main tasks above. Training materials also described examples of voter and vote count manipulation and fraud. They contained precise instructions on the election official's appropriate behavior and the official process for reporting any unlawful activity[77].

[74] Political clientelism has factored into electoral corruption in Hungary (Mares and Young, 2019); robust election monitoring is seen as necessary to understand the extent of foul-play in electoral processes.

[75] SZAM: https://szamoljukegyutt.hu/ and 20K22 https://20k-www.vercel.app/kik-vagyunk

[76] https://szamoljukegyutt.hu/wp-content/uploads/2022/03/Kisokos_2022-0317_16-00perces_KJ.pdf.

[77] The Fidesz government added a referendum on LGBTQ education in schools. We have omitted the findings on this aspect due to lack of space.

Auditing democracy

Distrust in the state and in the democratic process has been headlining politics in liberal democracies of the Global North, calling the legitimacy of elections into question, most notably in the United States under Donald Trump's presidency (Moynihan 2022). Most democracies have audit procedures in place to safeguard the fairness of elections. "Postelection audits" are required in nearly all US states. "When polls close on election day, election officials, along with bipartisan teams of election judges, work sometimes for 24 or even 36 straight hours processing ballots." (Jacobs and Choate 2022: 28) These audits were activated over and over in Trump's attempt to formally (and unsuccessfully) challenge the results of the 2020 presidential election. By then dismissing the ballot count results, Trump has continued to delegitimize and "undermine the U.S. administrative state" (Moynihan 2022: 36). In Hungary, popular distrust is not from the far right, directed against democracy and the state in general, but across the political spectrum directed against the state that has labeled itself "illiberal democracy".

Voting systems are traditionally the object of study by political scientists, whereas we mobilize research in accounting to approach the specific practical task of monitoring and auditing elections. This is relevant for two reasons. In concrete terms, winning elections by illegally tampering with the number of votes is akin to delivering returns to shareholders by "cooking the books". Second, beyond the risk of fraud, as Michael Power's influential thesis on the rise of the Audit Society describes, modern societies are increasingly permeated by audit-like practices: "The audit explosion was also driven by closely related political demands on behalf of citizens, taxpayers, patients, pupils and others for greater accountability and transparency of service providing organizations." (Power, 2000: 113).

Such an approach has several advantages. First, it highlights the importance of verification, confirming that a counting process has taken place correctly. Second, it highlights the motive of accountability and the concrete instruments and mechanisms by which actors hold each other accountable: "(...)audits are demanded in the context of relations of accountability between two parties and the existence of operational difficulties for one party to monitor the other" (Power 1997: 134). Third, it offers a comprehensive view of accountability: an audit "seeks to draw conclusions from a limited inspection of documents, such as budgets and written representations, in addition to *reliance on oral testimony and direct observation*." (Power, 2000:111, our italics). Fourth, auditors must, and do, draw inferences from their sample, including from observations of the audited organization. Finally, auditing goes beyond the individual's professional judgment and consists of "collectively negotiated settlements" (Power 1995 quoted in Power, 2000:111).

In an era of post-truth information bubbles, the physical act of counting votes took on special significance since many Hungarians did not trust the election results reported by the government-controlled media and suspected that the government was undermining the democratic process. For these ordinary citizens, being present where the election "really" happens was meaningful. They could verify the election—"I saw it with my own eyes and hands", as one ballot count volunteer commented—opening up the black box of election results and participating in its making. The numbers here were generated by the people themselves.

To understand how a fact-oriented task of counting votes and auditing that process developed into broad and diffuse accounts of "how people live", we must draw further on the notion of accountability mentioned above. Accountability involves an actor "giving account" of their actions to others (Garfinkel, 1967). Accounting techniques and auditing protocols are examples of organizational systems of accountability, situated within the broader practices of accountability, in other words, giving others an account of oneself on an everyday basis (Roberts and Scapens, 1985). People constantly engage in account-giving in the ordinary course of life, telling work colleagues about their weekends or explaining how to fill out a tricky online form. This broader view of accounting as accountability resonates with ballot counters' mixed accounts of factual vote count information and descriptions of countryside conditions.

Actors do not simply perform their actions but also simultaneously witness the situation in which they participate. While giving an account can be seen as integral to any ordinary action, it gains more importance when actors sense that a situation might break down. Giving account is an important act that remedies delicate situations, maintaining the social order (Garfinkel, 1967) and evoking the actors' underlying assumptions about what constitutes normal behavior.

In this sense, it is productive to conceptualize ballot counters' actions as accountability:

- driven by the desire to witness and account for the votes, creating the fact of a fair election in the situation by seeing and describing it
- moving from a strict sense of accountability as an election official towards a broader sense, accounting for society
- accounting for a situation that is abnormal in their eyes: why an overwhelming majority of other citizens vote for an unacceptable political choice, Fidesz.

We studied the posts and comments in the two main Facebook groups created by and for the ballot count volunteers. These groups were set up as *fora* where volunteers could relate their task experience and evaluate the fairness of the vote count. The posts were often anonymous. They do not represent all the volunteers' experience, but they do convey a typical experience.

Volunteers' "ethnographic" results emerging from their ballot count experience

We found two types of "expectation gap" among volunteers' reports of their auditing activities. First, those who volunteered to count ballots on behalf of the opposition party coalition expected to uncover fraud by witnessing how voting happened and how votes were tallied in the hard-to-reach polling stations across the country. The overwhelming majority of posts confirm the opposite: volunteers were almost disappointed not to find any fraud. Second, many volunteers also expected controversy within the ballot count committee between themselves and the government (Fidesz) delegates, but their accounts reveal that they collaborated well on the work task with their ideological opposites.

We argue that having discovered no wrongdoing in the election day process, the volunteer delegates felt empty-handed as auditors and could not account for the landslide election victory of Fidesz. The ballot count volunteers' underlying theory that the victory was only possible due to fraudulent practices was proven wrong. They had to adjust their accounting for the 'abnormal' result, and subsequently devise new accounts. The posts invariably proceed to ethnographic descriptions of the voting day and the voters, serving as hindsight justification of voter choice, and accounting for all the ways their fellow citizens might have arrived at casting their ballots in favor of Fidesz. Below, we discuss the major themes that appear in the volunteers' broader accounts of election day.

1) *Policing a fair election, the official task*

The posts have a pattern. They begin with a description of their jobs as volunteers, but interestingly, the election process and the vote count are not the focus or even the main section of the posts. Most descriptions start off with details of the polling station, the number of registered voters, and the time they arrived or opened up the premises. The tone is somewhat official and focuses on giving factual information, as if reinforcing the volunteers' legitimacy:

> *"1070 people were registered in the electoral district and 800 people came to vote"*

> *"Our committee consisted of the three elected members, two Fidesz delegates and two of us, and the secretary helped out when he could during the day."*

After "getting through" the monitoring and counting tasks, the narrators quickly move on to their main points: the other, qualitative aspects of what they witnessed.

2) *Audit work: reports of "getting along" with opposing party delegates*

The posts almost always describe the other members of the ballot count committee and mention the working relationship. Here, factual information is often mixed with qualitative descriptions of, for example, how it felt to work alongside representatives of the governing Fidesz party. In face-to-face interactions, controversy was rare, and reports abound of collegiality. Volunteers describe this aspect of the work that forged solidarity between people, glossing over political differences:

> *"Working together was smooth, tasks were rotated, there were no conflicts. If something came up, we were able to discuss it."*

> *"My counting partner was a self-confirmed Fidesz fan. He was a terribly nice guy. He was smart, we talked a lot, we teased each other, he was the most positive character in the whole story."*

These descriptions of cooperation reinforce the auditors' status as separate from the people and the environment audited and suggest that the issues were not with the other auditors.

3) Giving account of countryside life: a collective ritual that justifies the election results

It is at this stage that most accounts take a decisively ethnographic turn. The transition from an official report to a qualitative narrative occurs as volunteers evaluate the outcome of their audit, mostly confirming that they did not witness fraud despite their expectations:

> *"There were no irregularities in the counting, all decisions were unanimous. So the bottom line here is that I have no reason to question the fairness of the vote (in my own constituency)."*

And yet, even as they confirm the fairness of the elections, volunteers seem unable to comprehend what occurred before their eyes: a vast majority of people came to the polls and voted for Fidesz. The volunteers feel they must relate their experience to the community to account for both the work they did as auditors and for the election results, searching for causes as to what they witnessed. The volunteers start by expressing their incredulity with respect to the situation:

> *"There was no unexpected event, no need to record any mistakes or fraud.... really everything went well....and yet it didn't!"*

Hereafter, ethnographic descriptions lengthen. Their positioning in the posts makes it clear that these descriptions serve to justify the election results. A range of "ethno-theories" appears that are often blended within the same post. We can distinguish four main theories: the state holding citizens captive; the essence of the Hungarian People; individuals' physical-mental state; and the regions' socio-economic conditions that drive them to vote the "wrong" way.

First, many posts theorize that the voting process is not where fraud happens. They refer to larger issues already documented elsewhere, such as the government's near complete control of the media, which "leaves alternatives no chance" as one user observes; subsidies to help with the cost of living, and fearmongering communication:

> *"The election was not rigged in the electoral commissions, but before, on TV, on Kossuth Radio, with billboards... and scaring people with the war [in Ukraine]"*

Most typically, volunteers turn to ethnographic descriptions of voters and the countryside in an attempt to justify voters' choice, getting a glimpse of another world that is not theirs and which would explain the results:

> *"...the catastrophic physical and mental condition of voters. (...) There was no shortage of voters who could hardly move, could barely see, could barely sign [the electoral register], were rotting, or had basic hygiene problems"*

> *"100% extreme poverty. These people were penniless. They live in rickety, crumbling shacks at subsistence level...there is poverty and ignorance."*

> *"As people from this tiny, tiny village wandered in, I had to wake up to the fact that most of them really are incredibly stupid."*

As the volunteers could not "catch" Fidesz red-handed in their job as election officials, their attention shifted from the process and the state to an audit of society. The results of the counting process and the lack of documented fraud lent legitimacy to the elections, which could reinforce the legitimacy of Fidesz. This underlying realization may have been the turning point in the audit process: the audit's object became not the fairness of the state but the soundness of society.

Their underlying assumption was that voting for Fidesz was unacceptable. With the actors' "suspension of disbelief", adopted in order to operate in everyday life, the situation where such a morally abnormal event could happen needed to be accounted for and remedied. The volunteers thus generated accounts about voters to help "make sense" of the situation. Based on their audit of society, some posts did hold the state accountable for building a political-economic system which has become self-sufficient and keeps the government in power, even through legal elections. Mostly, however, they held society accountable.

4) Counter-accounts: "society" responds

After eight days of such posts, the first critical comments began to appear, questioning the ethical nature of the descriptions of the countryside, accounts of how "the other half lives". These counter-posts criticized the "ethnographic moment" for what they saw as the urban elite's shock at discovering what life outside their comfortable bubble looks like. They criticized the volunteers for taking a condescending stance towards the voters they encountered, for their ignorance, and their lack of prior empathy towards fellow citizens.

> *"Very good writing - it would be if it didn't ooze fundamental prejudice and the supposed "experiences" that seek to justify it... The superior, pompous bullshit of a metropolitan man, contemptuous of the countryside, bitterly resentful of electoral defeat, peers out from between the lines...based on these crumbs [of truth], a false stereotype of the countryside and rural people is neatly constructed."*

These newer accounts criticize the previous accounts, providing a different justification for the election results and holding up a mirror to the volunteers who, while declaring themselves to be the "heroes of democracy", cannot seem to accept that fellow citizens could vote for a party they dislike. The justification that emerges from these counter-posts is that as representatives of the opposition, the privileged urban volunteers should have tried to engage with other parts of the country earlier, suggesting that the fault lies with the leftwing coalition for alienating voters outside the urban elite.

Conclusion

The ballot counters were representing the "audit society", holding the state accountable on behalf of society. From the starting point of auditing as a process of democracy, however, they ended up with an audit of society, scrutinizing voters' way of life from close up to find the individual or societal "errors" that would account for a disappointing performance in the election. The ballot counters themselves were then held accountable by way of disparaging comments from other citizen-users for their allegedly unethical and untrue audit of society. A veritable "circle of accountability" emerged.

Audits spill into their environment as the auditors' activities are not completely and narrowly bounded. Auditors almost always become ethnographers. In our case this aspect was highlighted by the mobile ballot box, delivered by delegates to those unable to vote in person. The public and private sphere is blurred as election officials enter citizens' homes, but it nonetheless resonates with the corporate auditor experience. The audit process generates qualitative accounts, although these experiences are not usually formalized or accepted as valid in professional audits. The distance between "us" the auditors and "them" the auditee is constantly created and maintained through storytelling about the milieu. A favorite pastime of auditors is sharing stories about their clients. Instead of the corporate auditors' private and informal setting, the election volunteers shared their stories on a public social media platform which has no backstage (Goffman, 1959; relative to the frontstage of social performances). This is what enabled the circle of accountability to close.

Is it ever possible to conduct an audit without having an "ethnographic experience"? Is there an audit without the milieu? The auditor does not perform the task solely in its pure state but enters an organization, a world, which he/she observes and witnesses. Auditors produce unique and rich vernacular knowledge about the society and culture of the organizations with which they engage. The election volunteers' case affirms that audit procedures exist to produce reassurance and comfort, rather than critique (Power 2000, Power 1997), and shows that the ethnographic material produced by auditors is a venue for critical accounts with implicit theories about the organizations observed.

Finally, in the context of election results, public audit stories by volunteers fulfill a therapeutic function and constitute a social ritual. Taken together, the mass of posts quickly became a method of collective processing after the government's overwhelming election victory. Solidarity emerged from the election audit experience of "them", the Fidesz voters. The ethical issues of such *othering* or creating differences between the in-group and the out-group is what prompts other actors (citizens, journalists, politicians) who read the posts and thereby observe the election observers. Taking place on an interactive social media platform, the otherwise "backstage" social ritual of the volunteers is witnessed by others, challenged and constantly over-written. It is a social ritual that cannot remain self-contained and cannot provide closure. The accounts of the auditors and the audited are brought into conflict, with vastly different versions of the "truth" colliding, which may be reconciled or remain apart.

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Responding to paradoxical tensions in global supply chains

Philip Glynn*

ESCP Business School

Abstract

According to the Intergovernmental Panel on Climate Change (IPCC), human-caused climate change is exacerbating crises within the natural environment as well as human society. Responses to these crises are highly politicized and, therefore, sit at the center of many geopolitical debates. The activities of firms (and decisions taken by managers) will determine, to a large extent, whether society can possibly reverse current climate trends. A transition to a circular economy has been proposed as a way of meeting society's needs within our planet's resource boundaries. Management research in circular economy has focused on the technological tools and economic processes but neglected the impacts on people and society. The paradox lens equips management researchers with the tools they need to re-balance this critically important field by centering on its social aspects.

Keywords: Global supply chains, Sustainability, Circular Economy, Social Challenges, Paradox Lens

*Global Executive PhD Candidate, ESCP Business School

Closing loops without closing doors

According to a 2021 report from the World Business Council for Sustainable Development, a company's supply chain can produce more than 11 times the CO2 emissions as its core operations. Given this significant climate impact, sustainability researchers and sustainability managers must focus on global supply chain sustainability.

This focus is nothing new. Management has always been about sustainability. A traditional manager in a post-World-War-II enterprise viewed sustainability as a process of earning profits to keep the company afloat. A manager of a firm after the onset of the environmental movement viewed sustainability as a balance between what a business takes from and gives to its environment.

Many managers now speak not only of a sustainable company but of a circular economy.

Most of our global economy is linear. One can track a common product (as Maxine Bedat cleverly did with a pair of jeans in her book Unraveled: the life and death of a garment) on its farm, factory, shop, closet, landfill journey. In a circular economy that same pair of jeans would go through multiple cycles of renewal—generating new economic opportunities for stakeholders across a longer lifespan. A circular economy envisions, for example, eco-industrial parks in which firms co-locate so that the waste stream of one can be a productive input for another. Other topics in circular economy involve changing from a model of ownership to a model in which products are shared, repaired and re-used under new ownership and business models. This circular economy would prioritize the "effective and efficient utilization of ecosystem, economic and product cycles by closing loops for all the related resource flows (Alhawari, Khurrum, Bhutta & Ülkü, 2021)." Quite often, theorists suggest that geographic proximity between partnering firms can facilitate closing these loops.

What would it mean for managers if the global economy were to go circular? Imagine the Nations of the world responding to IPCC reports with clear, unified government policy. Imagine companies enthusiastically embracing the letter and spirit of these new laws. In doing so, more and more companies would be faced with the competing demands of economic and environmental sustainability on a daily basis. This would be a source of tension. And those tensions would not just be technological and economic, but social as well.

This transition would dramatically impact employees and customers of firms. It would result in major restructuring of inter-firm networks. It would profoundly re-order power relations between firms and the communities in which they operate. The transition would have deep social impacts. There is an ongoing and unresolved debate about the definition of social sustainability (Walker, Opferkuch, Lindgreen, Simboli, Vermeulen & Raggi, 2020). However, in general, the concept refers to systems that promote economic and social fairness. It is in this area of social sustainability, where managers will sooner or later have to place their focus.

Why should this be a priority for managers? Strong enterprises are built on strong relationships. Managers will have to balance increased economic and technological sophistication while continuing to build (or re-build) relationships with the enterprise's employees, partners and the communities where they do business. Managers will have to be on guard against the unintended, negative impacts of this transition on all of those stakeholders.

Otherwise, closing loops risks closing doors of opportunity for both people and communities.

The paradox lens in sustainability research

Implementing sustainability strategies confronts managers with competing economic, environmental and social demands. The transition to a circular economy will only increase the frequency of situations in which managers are presented with contradictory imperatives. In studying how managers react to such situations, researchers have developed the theory of the paradox lens.

A paradox exists for a manager when tension between "elements that seem logical individually but inconsistent and even absurd when juxtaposed" is sustained over time (Smith & Lewis, 2011).

"Paradox studies adopt an alternative approach to tensions, exploring how organizations can attend to competing demands simultaneously. Although choosing among competing tensions might aid short-term performance, a paradox perspective argues that long-term sustainability requires continuous efforts to meet multiple, divergent demands (Smith & Lewis, 2011).

When a manager realizes they are facing a paradoxical situation, that paradox can then be said to have become salient. The apocryphal apple landing on Sir Isaac Newton's head was a moment of salience. It is important for managers to think in terms of salience. This is how the forces that place elements in tension reveal themselves.

What kinds of events could make tensions salient? It could be a public policy or shareholder resolution. It could be a public statement by a senior manager in response to pressure from an external stakeholder. How tensions become salient can inform managerial responses.

Paradoxes can become salient within inter-firm networks such as global supply chains (Walker, Opferkuch, Lindgreen, Simboli, Vermeulen & Raggi, 2020). Paradoxes can become salient as firms react to the external force of public policy (Ozanne, Phipps, Weaver, Carrington, Luchs, Gupta, Santos, Scott & Williams, 2016). Paradoxes can also be made salient through practice and discourse within organizations (Hahn & Knight, 2021).

Viewing the world through a paradox lens does not allow a decision maker to simply choose between competing demands and then live with the trade-off. It requires organizational actors to experience the salience of tensions and then acknowledge the paradoxical reality they inhabit. The manager must then view this paradoxical reality not as some temporary problem to be solved, but as the very nature of their environment.

Managers whose portfolios include sustainability, deal constantly with the tensions between profitability and purpose. As the transition to a circular economy takes place, under-studied aspects such as social sustainability will come under scrutiny. Managers will need methods to think about this problem and talk about it with their stakeholders. The paradox lens may be the right tool for the job.

The paradox lens and the social aspects of the transition to a circular economy

This transition will not just burden managers with learning new technological and economic models. New calls from external stakeholders for social sustainability—from activist shareholders, NGOs, customers—will make the job even harder. But this shouldn't be surprising. The implementation of a sustainability strategy as comprehensive as circular economy within global supply chains won't just be a technological and economic process. It will also be a social process in which all stakeholders co-create a new reality (Hengst, Jarzabkowski, Hoegl & Muethel, 2020).

Social sustainability is an important element of the transition to a circular economy. Yet, the social aspect remains the least studied (Clubbe & Tennant, 2020). In those rare instances in the literature centering on the social aspect of the transition, the definition of social sustainability is highly contested. Sometimes social sustainability is simply defined as the ability of a system to create widespread, accessible employment. Sometimes it is defined by the degree to which a system can operate with limited negative health impacts to workers. Very rarely, however, is social sustainability analyzed in terms of social justice.

One study that sought to comprehensively map research into the social aspects of circular economy, found that "social justice and inclusion" were mentioned the least often in discussions of social sustainability (Mies & Gold, 2021). Managers who cannot speak the language of social justice, will have difficulty navigating proxy votes, public events and the daily back-and-forth of social media. This challenge will be even more pronounced for managers in a global context as social justice will be defined differently in different cultures.

Therefore, managers must question a foundational assumption: that if the world can overcome the technological and economic barriers to circularity, the impacts on people and society will automatically be positive.

Planning for success

To prioritize social sustainability, managers need to think ahead. They must project themselves into a future in which a successful ecological transition has taken place. After all, it is clear what will happen if humanity fails to address the climate and resource crises. Now managers must explore the opposite question. What will the firm, and as a result the world, look like if humanity succeeds?

Here, it is important to differentiate between two streams of thought in the circular economy literature. For certain researchers, the goal of a circular economy is to decouple resource use from economic growth. They think about how circular economy practices can be used to continue the economic growth required to support a growing global population while at the same time preserving the world's resources.

For others, the goal of a circular economy can only be achieved in an environment of de-growth. For these researchers, the question is how to meet human needs using alternative models rather than increases in gross domestic product.

Managers are more likely to be asked to adopt the first point of view.

Viewed through the lens of continued economic growth, several patterns emerge from the literature. A circular economy would depend on highly sophisticated coordination between firms within global supply chains—even leading in some cases to vertical integration (De Angelis, 2020). This coordination and communication will rely on large amounts of data concerning the use of water, material and energy by the firm, employee and even customer.

At first glance, this statement offers hope. Global supply chains have already demonstrated their ability to get diapers on their way to sleep-deprived parents while the mouse they clicked to order them is still warm. Could these systems not simply accommodate the demands of circularity, just as a piece of music written for acoustic instruments could be played with electric ones?

The problem with this view is illustrated by the other societal trends that have accompanied the development of these global supply chains. This supply chain development is intertwined with the centralization of wealth and power in the hands of a small number of focal firms—Wal-Mart, Amazon, etc. Workers within these enterprises have seen their purchasing and bargaining power erode as the major industrial economies—most notably the United States—have trended toward greater economic inequality coupled with a declining organized labor movement. These supply chains and their participating firms now rely on immense amounts of granular data on the work and life habits of employees and consumers.

Further centralization of corporate power; greater surveillance of and control over workers; enhanced collection and monetization of data mined from every area of daily life; these are not typically considered to be the hallmarks of a circular economy.

Paradoxical tensions become salient for different actors within networks at different times based on the power relations of that network (Jarzabkowski, Bednarek, Chalkias & Cacciatori, 2019). One can't simply assume that a transition designed and led by technological and managerial elites will automatically be good for all people.

Consider a potential example from the United States. Supply chains with a heavy presence in the U.S. often adhere to supplier diversity programs. These programs require focal firms to buy a certain percentage of their inputs from supplier firms that are owned by members of historically marginalized communities. UPS is a good example. The global shipping firm spends approximately $2.5 billion (US) annually in transactions with over 6,000 diverse suppliers according to its supplier diversity page (https://about.ups.com/us/en/our-company/suppliers/supplier-diversity.html). UPS executives tout how partnering with African American, Native American and other diverse suppliers benefits the business and promotes the "social justice and inclusion" referenced earlier.

Let's imagine these same supply chains being reoriented with the primary goal of circularity. In order to meet their supplier diversity goals, focal firms might buy inputs from a small, remote rural supplier. In order to meet their circularity goals, however, these same firms might need to abandon such a supplier in favor of a large firm in a central location. In this situation, the environmental goal of circularity would be in tension with the social goal of justice and inclusion. As this tension was sustained over time, it would become salient to organizational actors as a paradox.

The path forward

Without the paradox lens, a manager could be lured into a binary choice. Either choice would detract from important goals that strengthen the effectiveness of the supply chain system. The paradox lens does not offer an easy answer to the question of how to balance social and environmental sustainability, but it would at least help managers to ask the right questions.

What is a firm's interest in building a circular supply chain? What is a firm's interest in participating in a supplier diversity program? How should a firm react if these two interests come into tension?

Here is where the paradox research can help light the way. Managers can take an integrative view (Hahn, Pinske, Preuss & Figge, 2015). The first step in this integrative process must always be explicit acknowledgement of the paradox. Then a manager can choose from available strategies: opposition, separation and synthesis.

Opposition is a strategy of acceptance. Managers don't try to resolve the tension, but rather to live with it. The opposing poles of the paradox are kept separate and organizational actors use improvisation to work toward the opposing goals on a daily basis.

Separation and synthesis are strategies of resolution. Managers can separate the opposing poles in space or time and then directly address both. Or managers can identify the common elements of the opposing poles and use those as the foundation for a new strategy.

Suppose a manager's primary formal responsibility is the design of a circular supply chain. Then external stakeholders force the manager and their team to consider supplier diversity.

One opposition strategy might be to accept the tension between these opposing poles. The manager could allow for the formation of a voluntary team outside the reporting structure to brainstorm ideas about how to further the goals of supplier diversity. This would address the tension as the employee experiences it (balancing organizational imperatives of circularity with personal values of diversity) and as the manager experiences it (needing new ideas to inform responses). This strategy would seek to transform conflict into debate and create an environment from which new strategies might emerge.

Resolution strategies would more than likely bring formal changes to the organization.

A manager could respond with temporal separation (creating formal pockets of time-off for team members to volunteer with diversity organizations) or spatial separation (creating a sabbatical program for team members to work within diversity organizations).

Otherwise, a manager could make organizational changes that seek a synthesis of the diversity and circularity goals. A manager could change the reporting structure so that diversity and circularity officers could work together to design and implement strategies to resolve the paradox—advising on the formation of joint ventures or partnerships between diverse and non-diverse suppliers, for example.

Conclusion

The purpose of this impact paper was to discuss the salience of paradoxical tensions and the manner in which the paradox lens can help managers navigate the ecological transition. The paper hinted at negative externalities that could arise as a result of this transition. This is not to discourage practitioners or researchers who see the circular economy as the best model to ensure our "spaceship earth" safe passage into the future.

Researchers should seize the opportunity to center social sustainability in ongoing debates about the future of circular economy. This will help managers to add the paradox lens to the array of tools at their disposal to light the way forward.

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Deploying the power of corporate purpose (profitably) in emerging markets

Ivy Buche*

ESCP Business School

Abstract

While the topic of corporate purpose has gained significant attention in the developed world and among Western companies, it remains an under-researched area in emerging markets. My study seeks to address this gap with a focus on India, a country that displays characteristics representative of most emerging markets. Through two in-depth case studies of market leading companies in the financial services and FMCG industries, I explore how corporate purpose can be deployed in a unique way to create higher-order impact, thus becoming a source of competitive advantage for the firm. My research finds two strategic paths that companies can take to successfully target some fundamental issues afflicting these markets. First, by identifying and plugging critical institutional voids (e.g., establishing credit worthiness of the unbanked rural people), companies can create an entire business model that serves the unmet needs in under-penetrated markets. Second, by systematically pursuing inclusion to break the widespread inequality in people's income and their access to products/services, purpose-led companies can develop new markets as opposed to fighting for market share. By doing so, they not only create meaningful outcomes for multiple stakeholders, but also unlock profitable growth opportunities for themselves.

Keywords: Corporate Purpose, Emerging Markets, Purpose-led Strategy

*Global Executive PhD Candidate, ESCP Business School

Deploying the power of corporate purpose (profitably) in emerging markets

Introduction

Over the last decade, purpose has been the subject of an increasing amount of academic research and media interest, as well as corporate efforts. However, as with most management concepts, this attention has largely been focused on the Western world – US- and European-based companies as well as developed markets. Given the existence of the strong institutional foundations and regulatory frameworks that facilitate successful business in such markets, companies appear to be pursuing a higher-order purpose as a differentiator. But what about emerging markets? A 2021 IMF study has shown that the top 20 emerging countries account for 34% of the world's nominal GDP in US dollars, and 46% in terms of purchasing power parity (IMF Fiscal Monitor, 2020; Duttagupta & Pazarbasioglu, 2021). Having said that, these markets are characterized by complex socioeconomics, bureaucracy, red tape, corruption and poor infrastructure – all of which makes it extremely difficult for companies to succeed. Within this context, can corporate purpose play a unique role to overcome the contextual challenges and create new opportunities? How can for-profit firms deploy purpose to realize value not only for the company but also for multiple stakeholders? This gap in understanding the latent power of purpose in emerging countries deserves attention.

How For-Profit firms Deploy Corporate Purpose in Emerging Markets

Large companies in emerging markets typically give a cursory nod to purpose through sporadic CSR activities, philanthropic gestures and ESG initiatives, considering them peripheral activities. I have previously argued that companies must put purpose at the core of strategy to play two distinct roles – redefining the playing field and reshaping the value proposition – to create higher-order impact (Malnight, Buche & Dhanaraj, 2019). Extending this line of thinking, I believe that purpose can be brought to bear much more strongly in emerging markets. Where inequalities abound and the lack of access to basics is the norm, corporate leaders have an unparalleled opportunity to bring this purpose alive in more strategic and meaningful ways. By doing so, they can create much-needed outcomes for multiple stakeholders while unlocking new growth potential for themselves.

The emerging market in focus here is India, and the companies that have strategically deployed the power of purpose are: Mahindra and Mahindra Financial Services (Mahindra Finance) and Hindustan Unilever Limited (HUL). Having studied these companies, I find that they have successfully put purpose into practice by 1) plugging institutional voids and 2) pursuing inclusion.

Plugging Institutional Voids

Emerging and developing markets are fraught with institutional voids (Gao et al., 2017). Khanna and Palepu (2010) describe institutional voids as missing or inefficient market-supporting institutions necessary to complete transactions in an economy. When these voids exist, the business environment typically becomes turbulent, costly and unpredictable, which directly limits the strategic responses available for a company. This was the situation facing Mahindra Finance as it sought to evolve from being a captive financer to parent Mahindra & Mahindra's utility vehicles and tractors to becoming a diversified financial services company.

On the one hand, there existed a huge base of underserved customers in underpenetrated rural/semi-urban areas across the country, who would benefit from the availability all types of loans. On the other hand, structural deficiencies, inefficient judiciaries, ineffective regulatory systems, weak infrastructure and information asymmetries resulted in a highly complex and dubious financial exchange context. Rural customers were caught between banks that refused loans due to a lack of legitimate documentation and unscrupulous moneylenders who charged exorbitant interest rates. How could Mahindra Finance determine the creditworthiness of these potential customers? They were mostly poor, illiterate, unbanked, with no proof of identity, no collateral and irregular cash flows (severely impacted by monsoons). At the same time, the company had to live up to its corporate purpose encapsulated in a single word – RISE – and improve the livelihood and wellbeing of its customers.

Driven by its strong purpose, Mahindra Finance decided to create a socially inclusive "Earn & Pay" business model based on understanding revenue and operating surplus through the use of the vehicles/tractors. The customer's potential cash flow was plotted and a decision to lend was taken based on model viability. Moreover, the company's business operations were supported by completely new ways of working – decentralizing decision making for handling non-traditional loan design, repayment terms, customer approval mechanisms, as well as cash-based disbursement and collection systems (the preferred mode for these customers). In terms of the field force, the company consciously recruited employees at a local level, rather than appointing them from cities and sending them to rural branches. These local employees knew the dialects, were connected to the land and its people, and they understood the contextual challenges. Their insights enabled Mahindra Finance to anticipate market needs and respond with the right combination of products and solutions, which allowed it to progressively expand its offers to brand-agnostic farm equipment/vehicle financing, housing loans, insurance broking, SME financing and asset management services. An analysis of these value propositions reveals that the company has served rural customers throughout their journey – securing their means of livelihood (the tractor), the roof over their head, their life and future opportunities.

Today, Mahindra Finance is India's largest non-banking finance company and the only one from the country to be listed on the Dow Jones Sustainability Index in the Emerging Market Category. It has attracted the country's National Housing Board to take a 12.5% stake in the company's housing finance subsidiary, proving itself to be a trusted partner in driving the government's rural development goals. Moreover, in 2019 the International Finance Corp., a subsidiary of World Bank Group, announced a $200 million investment in Mahindra Finance to finance micro, small and medium enterprises (MSMEs) in low-income states (The Economic Times, 2019). Out of this fund, Mahindra Finance has earmarked at least $100 million for women-owned MSMEs in the country.

The above example illustrates that by plugging a fundamental institutional void – establishing the credit-worthiness of the rural poor – Mahindra Finance has authentically deployed its purpose, enabling its customers to RISE and better themselves. Consequently, it has created social impact by improving the wellbeing of farmers/rural workers (and their families); enhanced economic impact by supporting the earning potential of individuals/small businesses; and strengthened private-public relations for the overall prosperity of the rural and semi-urban areas where the company operates.

Pursuing Inclusion

Inequality, a global issue, is more markedly felt in emerging countries. According to the World Inequality Report, India stands out as a "poor and very unequal country, with an affluent elite," where the top 10% held 57% of the total national income in 2021 (The Economic Times, 2021). Although these numbers include the negative impact of the coronavirus pandemic, the country has always had massive inequality, evident in income levels, gender parity, rural-urban divides, as well as access to education, employment, and so on.

Unilever, a foreign multinational company that entered the Indian market more than 85 years ago, had to navigate this context. How did Hindustan Unilever (HUL), its Indian subsidiary, become the largest fast-moving consumer goods (FMCG) company in the country? The answer is encapsulated in a single sentence, "What is good for India is good for HUL." This approach has been the hallmark of the company's growth story while empowering it to drive its purpose – to make sustainable living commonplace.

HUL realized that millions of consumers occupy every level of the socioeconomic pyramid. Although the needs in each segment were different, every consumer had the same hopes, aspirations and dreams for a better life. This motivated HUL to focus on market making (rather than share taking) by serving the needs of all consumers. The resultant strategy described as "straddling the pyramid" took an inclusive approach to combatting the income-access-consumption inequality triad. The company carried out reverse engineering for product innovation, re-designed process technologies for low-cost manufacturing/ packaging and developed its supplier partnerships to deliver products at varying price points/formats that addressed the consumer pain points of affordability and accessibility. For example, in detergents, Surf Excel Matic catered to the machine-washing needs of urban consumers, Rin served the middle-income group and Wheel offered low-income families access to a value-for-money detergent. This inclusive approach resulted in nine out of ten Indian households using one or more HUL products on any given day.

HUL's purpose-led approach resulted in it further accelerating its growth in the mid-2010s through a strategy called "Winning in many Indias" (WIMI). The company recognized the inherent heterogeneity of the country, in which language, culture, tastes and preferences changed every few hundred kilometers, making the country a mosaic of markets – a common characteristic of many emerging markets. HUL decided to change its responsiveness by slicing and dicing the consumer needs in multiple ways. WIMI drove an organizational restructuring that segregated the country into 15 consumer clusters based on diversity of consumption patterns and stage of economic development in order to provide insights into product gaps and innovations. These clusters were supported by 16 country-category business teams (e.g., home care, laundry, hair care, skin care, etc.) that functioned as micro-organizations focused on delivering the customized products at pace. With this 15X16 matrix, localization became a key driver of the company's growth – peeling the layers deep down in the market with an intimate understanding of consumers' needs. Hence, it is no wonder that HUL has never been perceived as a foreign MNC. Harish Manwani, former chairman of HUL, aptly described the company as having the "soul of middle-class India," characterized by meritocracy, competitiveness, frugality and striving to doing something better for the next generation.

Being a house of brands, HUL has systematically brought the corporate purpose to the level of the brand, embedding it in specific ways. The brands take a purpose-led stance and deliver a consistent message that is tied to the product. Sanjiv Mehta, CEO and managing director of HUL explains, "We believe that brands with purpose grow, companies with purpose last and people with purpose thrive. With growing awareness and concern for the planet as well as societal issues, consumers are increasingly demanding brands that deliver more than just the functional benefit. They look for brands that have a higher purpose that resonates with them" (HUL Performance Highlights, 2018-19). For example, HUL's largest tea brand – Brooke Bond Red Label – has the credo of "celebrating togetherness" (over a cup of tea), irrespective of gender, age, culture, religion or ability. The brand has struck an emotional chord with consumers through campaigns aimed at bringing change in the societal outlook. Its most successful campaign has been the creation of India's first transgender band (6-Pack Band), which won the Glass Lion Grand Prix at Cannes in 2016. This is significant because there could have been a huge danger of a negative impact on the brand, given that Indian society has always stigmatized the transgender community. However, the brand was able to break that taboo with its positive stance against such age-old marginalization, inequality and injustice.

It is clear that by taking an inclusive approach, HUL pioneered the FMCG era in India and experienced exponential growth, in sync with the needs of the developing nation. In the last decade, the company has grown at about 9% compound annual growth rate (CAGR), its operating margin improved by about 800 basis points and market cap swelled from about $16 billion to $70 billion (Business Today, 2022). Today, HUL is parent Unilever's largest subsidiary by sales and the second largest in terms of value globally.

Conclusion

Large companies are being put in a position of great responsibility. According to the Edelman Trust Barometer 2022, worldwide, business is the most trusted institution, ahead of NGOs, government and the media. The public's acceptance of big business as a central pillar of society and an integral part of people's lives, leads to higher expectations for them to not only perform on financial metrics but also to create an enduring positive impact on society and the environment by doing business in the right way. In fact, large companies are well placed to do so; the strategic advantage of incumbency allows them to take a long- term view and leverage their trusted relationships to build a purpose-driven business and outcompete rivals (Malnight & Buche, 2022). In emerging markets, the role and impact of large companies is even more accentuated. They have the potential to develop people's thinking, create empowerment and bring change to the social, economic and environmental make-up of the market. Instead of being defeated by the inherent deep-seated challenges, companies can activate the power of corporate purpose to address inequalities and institutional voids, to not only survive but also to thrive. Embedding purpose at the core of strategy can go a long way toward enabling companies to do well by doing good in emerging markets.

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The impact of geopolitics on Business Schools

Léon Laulusa

ESCP Business School

Abstract

As the 21st century advances, we can observe a shift in higher education from the Global North to the Global South. At the same time, the world is becoming increasingly unpredictable, whether from the post-Brexit impact, the emergence of the Covid 19 pandemic, the urgent need to address climate change, the rise in populism and nationalism, economic and international rivalry between the United States and China, or the war in Ukraine.

In this perspective, we will first address the background to the globalisation of business schools and the issues specific to attracting international students. We will then explore the future of business schools in a changing geopolitical context.

Keywords: Geopolitics, Business Schools, Higher Education

The impact of geopolitics on Business Schools

As the 21st century advances, we can observe a shift in higher education from the Global North to the Global South. HESA (2022) reports that in 2018, 70,000 of 90,000 academic institutions now come from the Global South region, which includes Africa, Latin America, the Middle East, and developing countries in Asia. This region accounts for almost 72% of the world's students, which numbered 225 million in total. International student mobility accounted for 5.6 million individuals in 2018 (Campus France, 2021). These trends will accelerate given the composition of the world's population eligible for higher education in the near future (Calderon, 2018).

At the same time, the world is increasingly unpredictable, whether due to the post-Brexit impact, the emergence of the Covid 19 pandemic, the urgency of managing climate change, the rise in populism and nationalism, economic and international rivalry between the United States and China, or the war in Ukraine.

These geopolitical issues have an impact on the ongoing internationalisation of higher education (Strassel, 2018, Pareiro, Thomson, 2022) and on business schools in particular. We define geopolitics as the study of the interplay between geography, history, and international relations. In this regard, we first address the background to the globalisation of business schools and the issues involved in attracting international students. We then explore the future of business schools in a changing geopolitical context.

The pathway to globalising business schools

After the Cold War, internet technology and the increasing ease of international mobility and exchange between countries accelerated the liberalisation of the market and the internationalisation of the economy. The world became a global village, interconnected and interdependent.

In this context, business schools, faced with the globalisation of companies, needed to educate their managers and leaders to accompany their international growth (De Meyer, Harker, Hawawini, 2004). The case of Chinese firms is revealing. In 2002, only 10 Chinese companies were ranked among the Global 500 in Fortune magazine. By 2021, there were 135!

On the one hand, companies increasingly need managers and leaders who are cross-culturally savvy and are trained to work effectively with local nationalities in the regions where they work. Chinese government organisations and Chinese companies thus took the initiative to send their managers and executives abroad for management training in business schools. At the same time, faced with this growing demand, business schools adapted their curriculum to welcome more international students, and also began training local students for professional experiences abroad.

In this perspective, the dominant model for business schools is the Anglo-Saxon one, often referred to as the Big Four model (United States, United Kingdom, Australia, and Canada) characterised by a liberal market economy, with English as the lingua franca, an MBA curriculum, the inclusion of academic research in class, and learning input that encourages in-class interaction and students challenging the professor's knowledge. The influence of the Anglo-Saxon model is not new, however.

Soulas (2017) reminds us that the evangelisation of management education in China by Christian missionaries dates back to the 19th century following the imperial military defeats during the opium wars. Christian universities and colleges opened the first business schools in China, mainly in Protestant institutions supported by foundations based in the United States, like Lingnan University in Guangzhou, and then later in Hong Kong (Soulas, 2017). Following the introduction of the Chinese Open policy, many Chinese universities established business schools or schools of management, mainly based on the US model, launching flagship Master of Business Administration (MBA) programmes. The same fervour and trend regarding the launch of MBA programmes can be observed in other regions of the world. The increasing number of MBA programmes accentuated by globalisation required talented faculty to teach business and management in an international environment.

A crucial need to train the trainers then arose. Harvard Business School founded the International Teacher Programme (ITP) in 1958 to that end. This management faculty development programme is now headed by a consortium of leading business schools, namely, the International Schools of Business Management (ISBM) and the European Foundation for Management Development (EFMD). ITP's goal is to train talented young teachers and bring together business educators from around the world to share their practices and knowledge, and to develop the skills and competences needed to succeed in their international careers.

Competition with international programmes also grew. One illustration of this shift was the fact that non-Anglo-Saxon business schools offered English track course modules. Programmes called "Doing business in" certain countries or regions, like Doing business in China or Doing business in Europe, flourished. At the same time, business schools significantly strengthened international academic partnerships for student mobility and double degree programmes in areas where the economy was growing. Business schools also launched joint programmes abroad with local partners or international alliances. Some business schools like NYU and INSEAD decided to set up campuses outside their home country to offer their students a multi-campus experience and gain access to the local markets. ESCP Business School pioneered this practice by launching a multi-campus business school concept in Europe in 1973. Business schools and their influence thus moved from being international regional schools to being global schools.

Attracting talented international students

As the world is becoming more global, international student mobility is also developing, expanding from 2.8 million in 2005 to 56 million in 2018. Ten countries (United States, United Kingdom, Austria, Germany, Russia, France, Canada, China, Japan, and Turkey) account for 62% of the global incoming student mobility programmes, 1.8 million of which were hosted by/in the United States, the United

Kingdom, and Australia (Campus France, 2021). Higher education institutions in these three countries depend heavily on Chinese students. Due to the Covid-19 pandemic, Campus France (2021) reports that the number of newcomers dropped substantially by 63% in Australia and 43% in the United States in 2020. In addition, with the war in Ukraine, student mobility in Russia was suspended in March 2022.

In a highly competitive market facing unexpected situations, business schools have several key levers at their disposal, nevertheless, to attract the best international students.

First, international rankings constitute a significant indicator of an institution's global positioning and reputation. These are based on both Alumni feedback and school-provided academic data. They allow candidates to compare business schools based on important criteria such as the graduate remuneration package, salary progression, student employability, and academic research. The goal of such rankings is to highlight how higher education produces knowledge that serves society.

However, some higher education institutions prefer not to appear in international rankings, favouring their own development strategy. Renmin University in China, for example, recently renounced the international rankings strategy (Lemaitre, 2022).

Second, international accreditations such as the Association to advance collegiate schools of business (AACSB) and the European Quality Improvement System (EQUIS) are widely recognised and valued peer-review certifications of academic excellence, serving as a guarantee of high-quality standards for students in terms of research, pedagogy, teaching, student experience, societal impact, etc. Still, these accreditors could be perceived as westernised labels, which could potentially be challenged by the implementation of their Asian and African counterparts.

Third, knowledge dissemination certainly does not stop at the Bachelor and Master degrees. In fact, academic research and doctoral programmes are essential to influence and impact society.

The importance of permanent faculty researchers and publishing heighten the credibility of a business school. Indeed, the most prestigious accreditation institutes require a certain ratio of permanent professors publishing within the higher education institution. In terms of the geopolitical role of business schools, the retention and attraction of faculty members influences not only the image of the business school, but also that of the hosting country.

Fourth, scholarship policies are another incentive to recruit the best international students. In the United States, the famous Fulbright programme gave grants to 3,512 non-U.S. citizens to study, teach, and conduct research in 2018. France (via Campus France) annually offers over 700 scholarships for study programmes, internships, and research programmes. The Eiffel Scholarship for excellence aims to attract the best international students into France's Master and PhD programmes. The Chinese Government also offers many scholarships (CSC) to over 280 Chinese universities. In addition to these scholarships, China's top universities offer scholarships to outstanding students, such as the 160 Schwarzman programme grant at Tsinghua University and the 100 Yenching Academy programme grant at Peking University.

Fifth, online courses provide institutions with effective marketing tools to promote their programmes and attract international students. Harvard Business School's HBS Online, or Open Yale for Yale University, offers free economics and business courses online as a means of educational influence, serving as a new form of soft power, the oxymoronic concept coined by Joseph Nye, the former Dean of Harvard Kennedy School, in his 1990 book *Bound to Lead: The Changing Nature of American Power*. Soft power is the ability to attract and to co-opt, rather than coerce or use force, to get others to do something or to give money (Nye, 2017).

The future of business schools in a changing geopolitical context

Business schools can be viewed as an object and subject of geopolitics. As higher education institutions, they become part of the soft power influence, especially when globalised. In this perspective, business schools may embrace three evolutions in the future.

To begin with, the subject of geopolitical specialisations is now unavoidable. Although geopolitical topics are not new to business schools' curricula, the impact of geopolitics on business is cross-functionally more integrated in management and business disciplines. Business and geopolitics, or international diplomacy as it were, are intricately intertwined. That is why business schools now offer Masters of Science in Business and Geopolitics. As we prepare future responsible leaders, it is essential for them to understand and decode the complexity of international relations. Today's students need to be able to adapt and to manage various events in the uncertain future or in the VUCA world. With this in mind, future leaders will be able to make better, more informed decisions. The objective is to learn about contingency plans and risk management when uncertain events occur.

To analyse the impact on business over the next few years, Rosenberg (2017) offers an interesting geopolitical framework that considers 3 dimensions:

- fixed assets related to topography, history, geographical location, and natural resources,

- semi-fixed assets linked to the structure of government and civil society, types of people and economic wealth, international relations and agreements, infrastructures, industrial fabric and environmental degradation, and climate,

- current aspects and events related to the situation like international tensions and hot spots with a potential material impact.

It may be useful to approach the analysis of geopolitical issues and sustainable solutions with a multicompetence education. ESCP has given a name to this approach. Since 2016, ESCP's Master in Management programme offers an ABCDE (Art, Business, Cultures, Diplomacy and Engineering) education, giving students a multi-specialisation experience thanks to the expertise of its global academic partners.

Second, business schools are challenged by newcomers from the private sector. What if giant tech companies like Apple, Google, Amazon, Alibaba, or Tencent launch their own business schools? How will the existing ones react?

This new geopolitical environment may lead business schools to enter a *cooptition* alliance, namely cooperation and competition with related partners in certain joint projects. These projects could be knowledge development-based research for educational or pedagogical purposes.

Not only will co-creation deliver faster, but it is highly probable that the solutions will be even more comprehensive. Future partnerships would thus not necessarily just be between two global academic institutions but would also involve Edtech firms, education providers, corporate universities and/or consulting firms from different regions and historical backgrounds. Each partner would contribute financial, human, or material and immaterial resources. Such alliances might also give business schools an opportunity to gain access to markets.

Multi-partnerships will mostly rely on the existence of common, transparent regulations, mutual trust, and respect based on equal opportunities. This will also provide a way to get to know, share, and learn from each other, resulting in a convergence towards common goals. One mistake is to consider that one partner is superior, resulting in an unbalanced relationship. In such a configuration, each partner is tempted to influence the other. A micro-geopolitical game would be established between the different stakeholders.

Lastly, it seems that the future predicted by Davey et al. (2018) involves multifaceted impacts (curriculum, teaching and learning, research, cooperation, social engagement, institutional change, students ' mobility and recruitment, etc) on higher education before 2040.

Moreover, ABCDM (AI, Big Data, Cyber-security, Digital and Metaverse) technologies could well add a new geopolitical perspective and reshape the business school landscape.

New technologies will have an impact on educational and economic interdependence, student attraction, teaching approaches and access. Daily life will be filled with increasing, abundant, and interconnected data. Business schools together with many organisations will rely on big data and AI to find, crunch and optimise relevant data on international students in order to influence and attract them. Good data is strategic, hence its protection through an effective cyber-security platform will be crucially important. New technology will also enhance transnational business schools that transfer teaching activities across borders.

Virtual 3D mobility or hybrid mobility could be the standard in the future. The use of metaverse, for instance, could add another geopolitical dimension with new virtual territories to conquer or to influence via new pedagogical modes thanks to

3D gamified technologies and thus new educational models. The metaverse based on digital human technology would also speed up the learning process, allowing for an on-demand immersive course at foreign business schools.

Lifelong learning-on-demand (LoD) will be instantly accessible, 24/7: a student could take a virtual immersive course anytime, anywhere in one institution and then decide to pursue it in another partner institution. By obtaining the necessary course credits for the different modules, the student could obtain the diploma recognised by the alliance partners. The strategic focus would be less on transferring knowledge to students, since knowledge will increasingly be free of charge and rapidly obsolete.

Conclusion

Countries view business schools as a key success factor to leverage their economy, their innovation, and a high level of human capital, in other words, to create a better life and society. They also play an educational soft power role. To that end, business schools will certainly continue to share their values and produce knowledge that is relevant and implementable for skills, competences, and attitudes. The added value of higher education would be to offer unique, varied learning, bonding, and mentorship experiences.

The cards could be reshuffled with new ways of doing business, such as cooptition alliances, in order to seize the Global South market opportunity. Will the Anglo-Saxon educational model continue to reign supreme or will it see the emergence of a new model like the Asian model led by China, or a European university model led by France? The UK also has a clear vision. Minister for Tech and Digital Economy, Chris Philippe, announced during the Global Leaders Innovation Summit on 13 June, 2022, that UK universities will be more digitised to commercialise their programmes globally, and to welcome and attract world tech talent to the country by facilitating a fast-track visa.

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N'arrêtons pas le progrès

Frédéric Fréry

ESCP Business School

Abstract

La notion de progrès est indissociable de l'entreprise capitaliste, qui en tant qu'outil de diffusion des innovations techniques a permis d'atteindre les objectifs des Lumières. Cependant, cette aspiration est désormais contestée : par-delà la critique de l'entreprise capitaliste, même le progrès scientifique est de plus en plus souvent présenté de manière négative. Plutôt que la recherche du mieux pour tous, beaucoup prônent l'immobilisme, la frugalité, voire la décroissance. Cette négation de l'idée de progrès peut s'expliquer par l'épuisement des ressources naturelles, mais aussi par toute une série de travaux issus des sciences de gestion, de l'économie et de la psychologie. Pour autant, renoncer au progrès est à la fois dangereux et illusoire : brider l'élan collectif vers le meilleur sera liberticide et anti-démocratique. Nous ne devons pas arrêter le progrès.

Mots clés : progrès, entreprise, capitalisme, décroissance

N’arrêtons pas le progrès

Si nous devons l’idée de progrès à Francis Bacon (1561-1626), elle a largement été développée par les philosophes français des Lumières, pour qui la prospérité, la santé et l’éducation devaient assurer le bonheur de tous. Près de trois cent ans plus tard, le projet des Lumières est en grande partie réalisé. Comme l’a souligné Harari (2016) : « Pour la première fois dans l’histoire, plus de gens meurent d’avoir trop mangé que pas assez, et plus meurent de vieillesse que de maladies infectieuses. Le suicide fait plus de victimes que les guerres, le terrorisme et le crime combinés. » Ce constat fait écho au discours de Montréal de l’ancien président Obama (2017) : « Si vous deviez choisir de naître à un moment dans l’histoire, et que vous ne sachiez pas à l’avance qui vous alliez être - riche ou pauvre, dans quel pays, homme ou une femme - vous choisiriez aujourd’hui. » Selon les calculs de la Banque Mondiale (2018), depuis l’effondrement du bloc communiste, plus de 2 milliards d’êtres humains sont sortis de la misère et le taux d’extrême pauvreté a chuté de 75 %.

Pourtant, il semblerait que ce projet, une fois achevé, ne fasse plus recette. Si nous avons atteint l’idéal des Lumières (Pinker, 2018), beaucoup prônent désormais l’immobilisme, voire la régression, plutôt que le progrès. Dès 1987, Canguilhem a publié un article intitulé « La décadence de l’idée de progrès », dans lequel il souligne un glissement du principe de conservation vers le principe d’épuisement : métaphoriquement, la recherche d’un ordre supérieur a cédé la place à la lutte contre l’entropie. Depuis cette date, l’idée de progrès a peu à peu disparu du débat public, comme l’a très justement souligné Klein (2017) : le mot « progrès » n’est quasiment plus employé. Quand il n’est pas négativement connoté (dans les médias grand public, les progrès technologiques sont plus souvent assimilés à des menaces qu’à des promesses), il est remplacé par la notion d’innovation, qui délaisse l’aspiration à une finalité pour se cantonner à la simple nouveauté.

Or, face à cette crise de l’idée de progrès, les sciences de gestion et le point de vue qu’elles apportent sur l’entreprise peuvent apporter un éclairage spécifique, voire quelques pistes de renouveau.

L’entreprise capitaliste est indissociable de l’idée de progrès

Tout au long des deux derniers siècles, l’entreprise capitaliste a été le vecteur central du progrès : elle a permis la diffusion à très grande échelle des innovations scientifiques, que ce soient les avancées de l’industrie pharmaceutique, les technologies de transport et de l’information, l’amélioration des conditions d’hygiène et d’alimentation ou encore l’accès aux sources de financement, qui a permis à la très vaste majorité de la population d’en bénéficier.

Par sa recherche de l’efficience qui pousse toujours à améliorer les procédés, grâce à l’aiguillon de la concurrence qui stimule à la fois l’amélioration des offres et la baisse des prix, au travers de la notion d’investissement qui consiste à sacrifier des ressources aujourd’hui dans l’espoir d’un meilleur retour demain, ou encore du fait de l’irruption épisodique d’entrepreneurs schumpeteriens – de Henry Ford à Elon Musk – capables de régénérer de loin en loin les marchés arrivés à satiété, l’entreprise capitaliste est indissociable de l’idée de progrès. Grâce à elle, le prix d’une automobile d’entrée de gamme en France a baissé de près de 41 % entre 1978 et 2022, alors que celui d'un vol transatlantique baissait de 82 % et celui d'un téléviseur de 90 %, sans compter que la qualité et la performance de ces offres ont très fortement progressé depuis (Mirlicourtois, 2022) : les voitures sont plus sûres et plus économes, les vols transatlantiques plus confortables et moins énergivores et les téléviseurs toujours plus perfectionnés. Comme l'a montré la stupéfiante explosion du niveau de vie en Chine depuis l'autorisation – pourtant largement contrainte – de la logique capitaliste, l'entreprise est un des meilleurs catalyseurs de l'ingéniosité humaine, si ce n'est le meilleur.

Jean Perrin, Prix Nobel de physique en 1926 pour ses travaux sur la discontinuité de la lumière, affirmait en 1930, lors de la création de l'ancêtre du CNRS : « Rapidement, peut-être seulement dans quelques décades, si nous consentons aux légers sacrifices nécessaires, les hommes libérés par la science vivront joyeux et sains, développés jusqu'au limites que ce que peut donner leur cerveau. Ce sera un Éden qu'il faut situer dans l'avenir au lieu de l'imaginer dans un passé qui fut misérable. » Dans une large mesure, si l'on compare nos conditions de vie d'aujourd'hui avec celles de nos arrières grands-parents, notre longévité, ou le fait que nos outils électroniques nous permettent un accès inédit à la connaissance, nous pouvons dire que le rêve de Perrin est devenu réalité, sauf sur un point essentiel : nous ne sommes pas véritablement plus joyeux

Tout porte à croire que la prospérité, la santé et l'éducation n'ont pas abouti au bonheur : le désenchantement weberien, qui a substitué la science à la croyance et la modernité à la tradition laisse penser que le projet des Lumière est désormais dans une impasse. Outre le fait que la notion de progrès fait nécessairement polémique – car ce que l'on considère comme « meilleur » n'est pas unanime, et c'était d'ailleurs une des ambitions (très occidentale) des Lumières que de définir universellement le mieux – le progrès a toujours eu ses détracteurs. Baudelaire le qualifiait ainsi de « fanal perfide » et y voyait un déclin scientiste, médiocre et matérialiste, alors que Nietzche soulignait : « Lorsqu'on vante le progrès, on ne fait que vanter le mouvement », comme si là encore la finalité faisait défaut.

L'éclairage des sciences de gestion

Les sciences de gestion peuvent cependant contribuer à mieux comprendre cette crise de l'idée de progrès, au travers de plusieurs prismes.

Tout d'abord, on peut invoquer l'aversion à la perte de Kahneman et Tversky (1979), largement utilisée en sciences de décision, pour constater que la recherche de la prospérité porte en elle les germes de son propre épuisement : au-delà d'une certaine accumulation de richesses (estimée à 75 000 dollars de revenus annuels aux États-Unis en 2018), les individus sont plus inquiets de perdre ce qu'ils ont déjà qu'ils ne se réjouissent d'obtenir éventuellement plus (Jebb *et al.*, 2018). Le confort matériel finit donc par devenir une source d'angoisse plutôt que de bonheur.

De même, les travaux de Arthur (1983) et David (1985), devenus des classiques du management de l'innovation, montrent que la concurrence ne sélectionne pas nécessairement la meilleure solution. Le *design dominant* qui s'impose peu à peu dans une industrie (Utterback et Abernathy, 1975), peut se révéler sous-optimal, voire défectueux, à l'image du clavier QWERTY, conçu au départ pour ralentir la frappe des utilisateurs (afin d'éviter un blocage des machines à écrire) et devenu tout à fait contre productif sur les ordinateurs actuels. Selon cette approche, le darwinisme du système capitaliste et de la concurrence ne débouchent pas nécessairement sur un mieux, mais peuvent au contraire enfermer la société dans des systèmes médiocres, en contradiction avec l'idée même de progrès.

Par ailleurs, l'idée positiviste de progrès s'est heurtée à la prise de conscience que l'humanité a la capacité de se détruire et de détruire le monde, notamment par le déclenchement d'une guerre nucléaire, l'épuisement des ressources naturelles, l'érosion de la biodiversité ou le dérèglement climatique. Comme le soulignent un nombre de travaux croissant en sciences de gestion et en économie, l'entreprise capitaliste, en encourageant le consumérisme, a fortement contribué à cette dangereuse dérive. Il est donc compréhensible que certains la décrient.

Enfin, il convient de souligner, notamment à la lumière des travaux sur la complexité, notre incapacité croissante à comprendre les technologies qui forment notre quotidien et les connaissances scientifiques qui les sous-tendent. S'il était possible il y a encore un siècle pour un esprit bien fait de comprendre le fonctionnement d'une machine à vapeur ou d'un moteur à explosion, qui de nos jours est capable d'expliquer à la fois un smartphone (réseaux, caméra, écran tactile, etc.), un véhicule autonome (radar, lidar, intelligence artificielle, etc.), une blockchain ou un vaccin à ARN modifié ? Or, cette incompréhension croissante du quotidien encourage la méfiance : ne pouvant comprendre les avancées scientifiques et techniques qui sous-tendent le progrès, on commence par le subir et on finit par le redouter. Face à notre incapacité à expliquer nos outils du quotidien, l'avenir devient plus menaçant que prometteur. Plutôt que de changer le monde, on aspire à le sauver. Nous avons le sentiment que la prédiction de Jean Perrin ne s'est pas parfaitement réalisée : les choses se sont améliorées, mais mal.

Conclusion : il faut sauver l'idée de progrès

Pour autant, même si l'idée de progrès est attaquée, même si sa détestable antithèse, le principe de précaution, s'est imposée jusque dans la constitution de la république française, et même si elle n'a pas donné tous résultats escomptés, il est impératif de continuer à la défendre.

En effet, contrairement à ce qu'affirment les déclinistes et autres collapsologues, le progrès technique et économique, associé à l'entreprise capitaliste, est une des meilleures réponses à la menace environnementale (Shellenberger, 2020). En effet, non seulement la natalité s'effondre lorsque la richesse augmente, non seulement l'amélioration des conditions d'hygiène préserve l'environnement, non seulement l'accès à des modes de production d'énergie modernes permet de contenir les émissions de gaz à effet de serre, mais surtout toute une série de technologies prometteuses permettent d'entrevoir des réponses aux problèmes environnementaux auxquels nous sommes confrontés, de la captation du carbone à l'électrification des transports, de la fusion nucléaire à l'informatique quantique, et des aliments de synthèse aux bâtiments à énergie positive.

L'opposition au progrès est une idéologie réactionnaire, totalitaire et malthusienne, une anthropophobie selon laquelle les aspirations humaines à la prospérité, voire l'humanité elle-même, sont condamnables. Or, brider l'élan collectif de milliards d'individus vers le meilleur serait nécessairement liberticide et anti-démocratique

(Laget, 2021). C'est pourquoi il faut sauver l'idée de progrès et la revitaliser, en surmontant ses défauts et en dépassant ses limites. Les sciences de gestion, à leur modeste niveau, ont très certainement un rôle à jouer dans ce renouveau volontariste.

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Développer la résilience pour soutenir la performance : le pivot des stratégies D2C

Anna Souakri*

ESCP Business School & Square Research Center

Abstract

Dans un contexte d'incertitude désormais structurelle, la résilience est devenue l'objectif prioritaire des entreprises qui cherchent à maintenir leur performance et à faire face à leurs concurrents. C'est pour atteindre cet objectif que les stratégies D2C ont émergé et se sont multipliées au fur et à mesure que le degré d'incertitude augmentait, et particulièrement depuis la crise du Covid-19. Si elles ont réussi jusqu'alors et contribué à renforcer l'avantage concurrentiel des entreprises qui les ont utilisées, des premiers signes de faiblesses apparaissent. Il est à craindre que, sur la durée, à force de bouleversements toujours plus nombreux, les stratégies D2C ne parviennent plus à soutenir l'avantage concurrentiel et la performance. Il importe dès lors de comprendre comment et dans quelles conditions ces stratégies ont pu transformer les bouleversements en opportunités favorables.

Mots clés : résilience ; performance ; direct-to-consumer ; pivot stratégique ; différenciation

*Affiliate professor, ESCP Business School

Développer la résilience pour soutenir la performance : le pivot des stratégies D2C

Introduction

Depuis 2019, les bouleversements engendrés par de nombreux épisodes de crises sanitaires, de chocs climatiques et de conflits géopolitiques inattendus ont structurellement modifié les préférences et les comportements d'achat des consommateurs. Ceux-ci se détournent des canaux traditionnels et renouvellent leurs habitudes de consommation au profit de moyens plus directs, transparents et rapides qu'ils peuvent maîtriser et gérer en temps réel.
Ces mutations structurelles impactent la performance des entreprises dont les stratégies de vente traditionnelles se révèlent dès lors inadaptées. La divergence entre ces stratégies traditionnelles et les comportements des consommateurs a été exacerbée par la crise du Covid-19 : les ventes au niveau mondial ont chuté en moyenne de plus de 10% pour les trois-quarts des entreprises, et de 50% pour le tiers d'entre elles. En parallèle, le recours croissant au commerce en ligne, exacerbé par les restrictions sanitaires, ont conduit à une hausse de 57% des transactions exclusivement en ligne sur les périodes de référence pré et post restrictions.

Cette chute considérable de la performance a servi de déclencheur pour développer des stratégies plus appropriées, que certains acteurs avaient déjà anticipées. Ces acteurs ont été plus résilients face à la crise du Covid-19, et ont su s'en servir pour gagner en performance. Pourquoi ces entreprises ont été plus résilientes face aux bouleversements et comment le rester ?

Partant du constat que les entreprises les plus résilientes qui se sont adaptées rapidement à l'incertitude sont celles qui ont redéfini leur stratégie de vente en s'adressant de manière plus directe au consommateur, nous concentrons notre étude sur ces stratégies dites « Direct To Consumer » (D2C). Elles consistent à maîtriser la vente en s'adressant directement à l'acheteur final, et minimisent le recours aux stratégies Business To Consumer (B2B). Nous analysons comment les entreprises les ont utilisées pour générer un avantage concurrentiel différenciant.

1. La vulnérabilité croissante des entreprises : le déclencheur majeur de l'émergence des Stratégies DTC

Le contexte

Les bouleversements déclenchés par la crise sanitaire du Covid 19 et les chocs climatiques et environnementaux, ont engendré une mutation profonde et structurelle des comportements et des préférences d'achat. Les entreprises doivent dès lors s'adapter à ces nouvelles tendances pour maintenir leurs ventes et atteindre leurs objectifs de performance. Il leur faut redéfinir leurs modèles de vente au niveau de la chaîne de valeur, et réorienter leurs stratégies d'approche client pour être à la fois plus directe et plus différenciante. Il leur faut également considérer les conséquences que ces mutations d'achat des consommateurs peuvent avoir sur leurs stratégies B2B et leurs partenaires. En effet, ces bouleversements peuvent avoir porté atteinte à leur partenaire et questionner la pertinence du modèle B2C jusqu'alors établi étant donné que le B2B nécessite une intermédiation susceptible de cannibaliser de la valeur sur la chaîne de vente au détriment du donneur d'ordre.

L'émergence des Stratégies DTC peut dès lors se comprendre comme un enchaînement de causes à effets : les bouleversements d'ordres divers ont engendré des modifications structurelles du comportement des consommateurs qui ont rendu inadaptées les stratégies d'approche classique des consommateurs. Les entreprises ont, en conséquence, été poussées à pivoter leur business model et à redéfinir leurs stratégies d'approche. Les consommateurs cherchent désormais à maîtriser l'ensemble de leur cycle d'achat en temps réel, et à éviter les intermédiaires de manière à avoir plus de visibilité sur les opérations et les acteurs associés. S'y ajoutent les contraintes réglementaires exigeant plus de transparence et de respect de la RSE qui contribuent à redéfinir les modèles de vente pour s'y adapter.

Depuis lors, la boucle bouleversements – modifications structurelles - inadaptation business model - pivot continue de tourner en s'intensifiant.

L'émergence des stratégies DTC

La réflexion sur le besoin de plus de résilience car au cœur performance

Evoluant ainsi dans un VUCA world (Volatility, Uncertainty, Complexity and Ambiguity) qui a des conséquences sur sa performance, l'entreprise doit parvenir à élaborer des stratégies dans des temps très limités en réponse à des concurrents et à des défis inconnus. L'incertitude est accrue par une plus grande accessibilité aux informations, qu'il est difficile d'analyser rapidement, et par l'évolution des nouvelles technologies, qui rendent difficiles les positionnements des entreprises sur les marchés. Chaque décision stratégique est donc soumise aux aléas de l'environnement. La résilience suppose pour l'entreprise de pouvoir absorber ces chocs et de les traverser sans en être diminuée, mais renouvelée voire renforcée. C'est dans ce contexte de disruption que la résilience est placée au cœur des priorités stratégiques.

Il s'agit de renouveler en permanence l'entreprise, de développer de nouvelles options et opportunités avant que l'entreprise ne soit négativement affectée par une rupture, et c'est dans cette perspective que les approches DTC s'inscrivent comme stratégies adaptées à ces finalités. En effet, les organisations résilientes sont plus performantes que leurs concurrents en période de perturbations, et y parviennent en creusant quatre types d'écarts cumulatifs vis -à -vis des concurrents et qui génèrent une différence de valeur cumulative significative. Les stratégies DTC participe à construire 4 avantages :

- **Un avantage d'anticipation avec la maîtrise des données clients** : une stratégie DTC assure avec une vision dynamique, en temps réel, la collecte des données sur la consommation et des informations sur les clients qui donnent aux marques DTC une vision claire de qui sont leurs clients idéaux et des comportements d'achat futurs de ces derniers. Cela permet d'avoir une connaissance précise des clients (segmentation pointue) et de leurs comportements (activité média type recommandation, achat) qui dessine une trajectoire sur les comportements futurs en fonction des facteurs exogènes, et donc une adaptation en temps réel.

- **Un avantage lié à l'impact avec une ultra personnalisations des contenus** : Le contrôle des données des clients et du point d'achat permet aux marques DTC de créer des expériences immersives et sur-mesure qui conduisent à un avantage concurrentiel. Elles offrent la possibilité de créer des produits personnalisés pour les clients les plus fidèles, car ces derniers peuvent être prêts à payer davantage pour des produits personnalisés créés en fonction de leurs commentaires. Par exemple, Warby Parker a adopté cette approche pendant les fêtes de fin d'année 2018, avec des produits en édition limitée, au lieu de pratiquer des rabais pendant le Black Friday et le Cyber Monday. Au-delà des produits, les D2C permettent de personnaliser la publicité et la communication vis-à-vis des clients car chaque interaction avec le client peut être tracée et suivie. La personnalisation permet ensuite d'améliorer le service et l'assistance, de renforcer les relations avec les clients et de mieux les fidéliser, ce qui contribue à renforcer la fidélité à la marque.

- **Un avantage lié à la vitesse de récupération** : la capacité à se relever plus rapidement après le choc en identifiant les ajustements nécessaires pour revenir au niveau opérationnel antérieur. En effet, les marques D2C ont davantage de contrôle sur les prix et les remises, ce qui peut leur permettre d'ajuster leurs coûts et leurs dépenses qui sont principalement variables. Elles peuvent en conséquence obtenir des marges plus élevées et une meilleure perception de la valeur de leurs produits que leurs concurrents.

- **Un avantage en termes de résultats éventuels** : une meilleure adaptation au nouvel environnement post-choc. Les stratégies D2C permettent d'obtenir des informations instantanées et très précises de la part des clients sur les produits, l'emballage, le marketing. Les marques DTC peuvent tester les produits rapidement et récolter les réactions des clients avant d'investir dans de grandes séries de production, et donc s'adapter en temps réel pour en tirer profit.

Le pivot stratégique sur une stratégie DTC est donc pertinent pour conduire une stratégie de résilience. Voyons désormais comment peut se réaliser ce pivot avec l'exemple de marques D2C à succès.

Les Stratégies D2C : un pivot stratégique vecteur de résilience

Allbirds, marque de chaussures de sport, est une histoire à succès. Son succès a été le fruit de l'innovation de ses produits et d'une compréhension aiguë des valeurs de ses clients. L'industrie des chaussures de sport vaut 65 milliards de dollars, et ses acteurs y évoluent en général avec beaucoup de publicité, des logos proéminents, et une technologie avancée type applications mobiles et objets connectés. En revanche, les chaussures Allbirds sont basiques : le dessus des chaussures est construit principalement en fibres de laine mérinos, les semelles sont fabriquées à partir de matériaux qui remplacent la mousse pétrochimique par de la canne à sucre, et les lacets sont en polyester recyclé.

Les chaussures sont dépourvues de détails inutiles à la marche et leur prix est raisonnable : 95 dollars. Grâce à ses chaussures durables, abordables et confortables, Allbirds a réussi à établir un lien émotionnel avec les consommateurs sur cette industrie. Avec des ventes annuelles supérieures à 100 millions de dollars, elle est évaluée à plus de 1,7 milliard de dollars.

Les marques comme Allbirds sont des challengers natifs du numérique. Elles interagissent directement avec les consommateurs via les médias sociaux (y compris le Web3), elles construisent et affinent leurs produits en se basant sur les commentaires des clients, et elles s'appuient sur un service client de qualité pour les aider à promouvoir leur proposition de valeur. Les marques de D2C constituent un petit sous-ensemble des quelque 6 millions d'entreprises qui vendent leurs produits en ligne. Elles n'ont pas de présence au-delà du numérique : la marque est le canal, et le canal est la marque. C'est précisément cette exclusivité qui fonde sa valeur et, au contraire, la vente par l'intermédiaire de tiers (B2B) peut éroder le caractère unique et la valeur d'unicité associée à une marque D2C.

2. Les facteurs favorables aux Stratégies DTC

Les forces positives

Des forces majeures ont aidé ces marques à pénétrer leurs marchés respectifs. L'essor de l'Internet et de la téléphonie mobile, qui a coïncidé avec le changement démographique des Baby-Boomers aux Millennials, a révolutionné la manière dont sont utilisés les médias et les comportements d'achat. L'évolution démographique a également entraîné la croissance rapide des réseaux sociaux et des applications mobiles. Les jeunes consommateurs sont plus enclins à suivre les influenceurs sur Instagram et Tik-Tok.

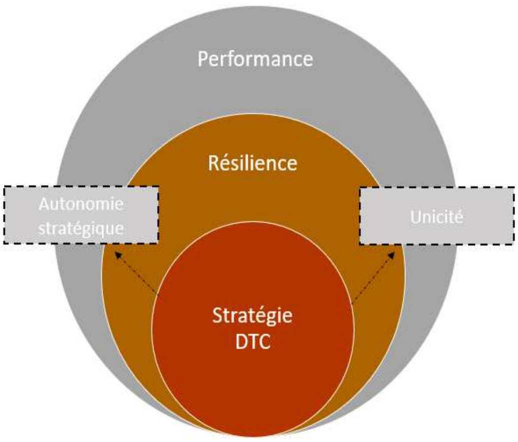
Dans le sillage de la montée en puissance des médias numériques au cours des 15 dernières années, les annonceurs ont réorienté leurs dépenses vers des canaux tels que Google, Facebook et Twitter, où ils ont pu de plus en plus cibler et réussir à micro-segmenter le marché, ce que les médias de masse n'avaient pas réussi à faire. Et lorsqu'un canal est devenu trop coûteux, ils se sont tournés vers d'autres canaux plus récents, comme Instagram, Snapchat et TikTok. Les nouveaux venus du DTC ont ciblé des marchés matures, notamment le rasage, les cosmétiques, les chaussures de sport, les lunettes et les matelas. Quelques acteurs dominants y appliquent une stratégie de sophistication avec des prix et des marges élevés. Avant que Dollar Shave Club et d'autres n'entrent sur le marché des rasoirs, par exemple, Gillette détenait une part de marché de 70 %, et de nombreux consommateurs se plaignaient du coût élevé des lames. Peu de R&D ou de conception de produits ont été intégrées dans les offres des nouveaux entrants. Mais leur stratégie a consisté pour beaucoup à optimiser la chaîne d'approvisionnement en localisant les usines susceptibles de leur vendre des stocks excédentaires et à ensuite proposer aux clients des produits à un prix inférieur à celui pratiqué par les marques traditionnelles dans la vente de détail.

Une autre tendance importante a été l'apparition d'options d'exécution évolutives pour faciliter l'expédition des commandes en ligne. Shopify et d'autres plates-formes de commerce en ligne en mode SaaS similaires servent de vitrine de vente. Les fournisseurs de services de paiement tels que Stripe et Plaid, et les entreprises de marketing par courriel comme Mailchimp, sont assurent la distribution et l'exécution à la demande pour une large variété de marques de D2C.

Lorsque les marques ont mis en œuvre cette stratégie, elles ont dévié des approches marketing traditionnelles et ont pris des raccourcis pour livrer les produits à leurs clients. Ces tactiques ont contribué à leur succès initial et à les rendre plus résilientes. C'est en réduisant leur dépendance à des tiers et en se différenciant radicalement des acteurs matures qu'elles ont créé leur résilience et en ont fait le fondement de leur modèle de performance.

Le besoin accru de résilience pour soutenir la performance : la résilience distinctive des marques D2C

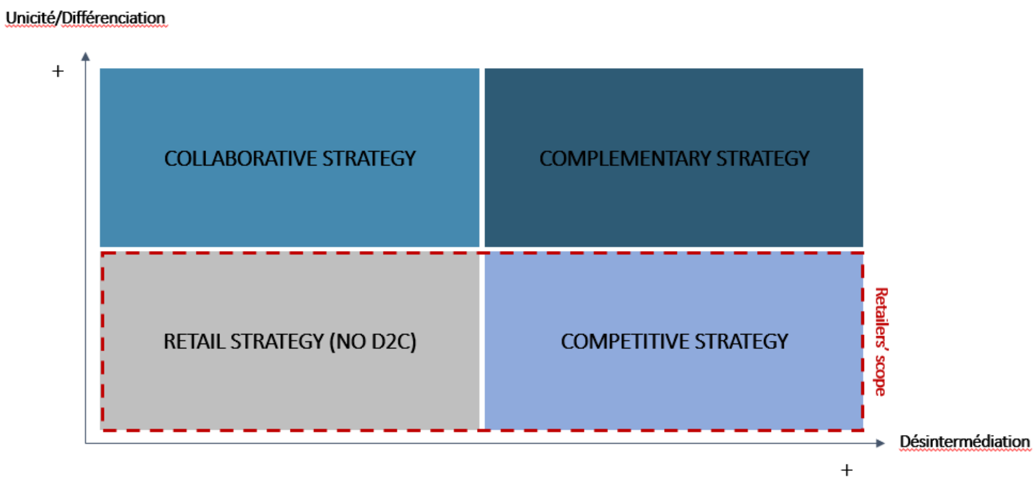
Modèle de performance instrumenté par une stratégie D2C



Au regard de l'instabilité croissante de l'environnement économique, les entreprises sont vulnérables et leur dépendance et faible degré de différenciation impactent négativement leur capacité à être performante. Les marques D2C sont précisément celles qui réussissent à préserver leur autonomie stratégique en réduisant leur recours aux intermédiaires, et à créer une valeur d'unicité qui les distingue radicalement de leurs concurrents. Ces deux caractéristiques clefs d'autonomie et d'unicité expliquent leur résilience et pourquoi elles sont plus performantes en cas de crise.

En effet, les marques D2C construisent leur résilience grâce à un moindre recours aux tiers permettant la rapidité dans la mise en œuvre des réponses, la rationalisation des frais, et la relance agile de l'activité par des opérations marketing grâce à un positionnement de marque unique et une segmentation des consommateurs très précise. Ces caractéristiques ont un effet positif et significatif sur la performance.

Stratégie D2C: concurrence, collaboration ou complémentarité avec le revendeur



Ainsi, c'est l'autonomie stratégique permis par à un moindre recours aux intermédiaires et l'unicité qui fondent la résilience des stratégies D2C et agissent comme levier de performance. Néanmoins, les stratégie D2C font face à de nouveaux challenges et les facteurs qui ont permis leur succès doivent être renouvelés afin d'alimenter la croissance et de créer davantage de performance sur le moyen et long terme.

3. Les limites des sous-jacents aux stratégies DTC actuelles à relever avec succès les challenges de la croissance

Lorsque les marques ont développé leur stratégie DTC en se positionnant sur des marchés matures, elles ont dévié des approches marketing traditionnelles et ont pris des raccourcis pour assurer la distribution. Ces tactiques ont contribué à leur succès initial et ont contribué à leur résilience en renforçant leur indépendance stratégique, mais elles ont causé des problèmes lorsque ces marques ont tenté de se développer dans une logique de croissance organique.

La négligence des étapes intermédiaires indispensables au succès

Le premier obstacle auquel elles ont fait face est celui de la "loi d'airain de la distribution" selon laquelle les consommateurs doivent pouvoir s'informer, voir, acheter et entretenir un produit quelque part dans la chaîne de distribution. Elle suppose que, même si les étapes peuvent être réorganisées (par exemple, le consommateur peut voir un produit dans un magasin avant d'effectuer des recherches en ligne, ou vice versa), toutes ces étapes sont nécessaires à la réussite finale.

Jusqu'alors, les marques de D2C ont toujours ignoré la loi d'airain de la distribution. Warby Parker, par exemple, a transféré une partie du travail de l'opticien au client – en demandant au client de mesurer lui-même son écart pupillaire, étape clef pour la réalisation de lunettes sur-mesure qui fait intervenir un tiers (dans ce cas, un opticien) dans les approches marketing traditionnelles. Des raccourcis comme celui-ci ont permis aux marques de D2C de réduire leurs coûts et de proposer des produits à un prix inférieur. Mais ils ne fonctionnent que pour les segments de clientèle qui n'accordent pas de valeur à la fonction supprimée. A titre d'illustration, Casper (marque de matelas) a réalisé avec le temps que les clients accordaient de la valeur au test des matelas avant de procéder à un achat et ont finalement ouvert des pop-up stores pour y procéder.

Dans l'ensemble, bien que les marques D2C aient fait preuve d'ingéniosité en trouvant des moyens de briser la loi d'airain de la distribution, elles l'ont fait à un coût non négligeable, et leurs lacunes en matière de services ont rapidement limité la taille de leurs marchés, si bien que nombre d'entre elles ont dû trouver d'autres voies de distribution pour soutenir la performance de leurs ventes (hybridation B2B et D2C notamment).

Une acquisition trop rapide

Un deuxième obstacle réside dans la faiblesse de leur proposition de valeur. Au départ, la stratégie D2C a consisté à combler rapidement et à moindre coût une lacune perçue sur le marché (« to relieve a pain and to bring a gain »), critère d'évaluation déterminant des investisseurs en capital-risque dans leurs décisions d'investissement. Mais cette approche est un substitut limité à la traditionnelle approche « STP » (segmentation, targeting, and positioning). Certains clients sont si faciles à atteindre par les canaux numériques qu'une première vague de ventes peut bien souvent se réaliser avant même que la marque ne comprenne véritablement les motivations d'achat et le profil sous-jacent des consommateurs.

L'approche D2C au stade initial et de manière très rapide ne permet pas de comprendre comment les clients perçoivent un produit et ses avantages. Ce n'est qu'après la première vague de ventes qu'une marque peut savoir qui sont ses principaux clients et pourquoi ils ont effectué un achat particulier. En d'autres termes, certaines marques de DTC en reviennent à devoir définir plus profondément, en amont de la vente, une proposition de valeur. Elles tendent à éviter l'effort et les dépenses de marketing initiales et les remplacent par une approche d'apprentissage par la pratique (learning by doing). Parce que les médias numériques sont initialement moins chers et plus précis que les médias de masse, cette approche conduit dans un premier temps à une acquisition efficace de clients et un avantage temporaire. Mais passé ce « first-mover » advantage et la rente associée au premier entrant, les concurrents rattrapent leur retard, car les opérateurs historiques ont pu consacrer leurs plus importantes ressources dans la publicité numérique et donc faire monter les prix, ce qui devient plus difficile à soutenir pour les marques DTC qui ont des ressources moindres et se retrouvent alors en difficulté pour poursuivre leur acquisition de clients par des moyens similaires.

La hausse multifactorielle des coûts

Concernant la hausse des coûts de manière plus précise, les coûts des publicités Facebook (aujourd'hui Meta) ont triplé au cours des deux dernières années. Warby Parker a été introduite en bourse avec une notoriété de 13%, et c'est l'une des entreprises D2C les plus connues. Avec des publicités Facebook à coût plus élevé, la lutte pour la reconnaissance du nom et la valeur d'unicité est encore plus difficile à assurer. En parallèle, les problèmes de chaîne d'approvisionnement ont renchéri les coûts d'importation. Le coût du transport d'un conteneur de la Chine vers les États-Unis est passé de 2 000 à 15 000 dollars entre le début et la fin de la pandémie et la situation se répète avec la guerre Russo-Ukrainienne, et ce coût est encore accru par l'inflation importée.

En parallèle, la mise à jour iOS 14.5 d'Apple a obligé les applications à se conformer à son cadre de transparence en matière de suivi des publicités (ATT), qui exige que les annonceurs demandent la permission aux utilisateurs pour suivre leur activité. Il est donc plus difficile de mesurer les performances des publicités Facebook et d'obtenir des données fiables. Enfin, la hausse des taux d'intérêt pousse les investisseurs vers les entreprises plus matures et rentables, ce qui n'est pas le cas de la plupart des acteurs D2C.

Globalement, les stratégies D2C présentent de nombreuses limites. Les concurrents les rattrapent et leur viabilité est menacée par le renchérissement du coût des publicités sur les médias sociaux qui rend l'acquisition des clients encore plus difficile. 98% des marques D2C ont fait faillite en 2021 par leurs lacunes sur la maîtrise des fondamentaux pour continuer à acquérir des clients à un coût accessible, et les investissements en capital-risque ne soutiendront pas une acquisition coûteuse sur la durée « growth hacking »).

C'est donc le développement et la croissance (« scale-up ») qui représente le principal challenge d'une stratégie D2C. Des analyses comparatives des marques D2C et de celles qui ont réussi et continuent à croître versus celles qui ont fait faillite, il en ressort des pratiques clefs à mettre en place qui permettraient de renforcer la résilience avec une stratégie D2C pleinement exploitée, et d'alimenter ainsi la performance de l'entreprise.

4. Renforcer la résilience de l'entreprise avec une stratégie D2C revisité pour accroître la performance

C'est en revisitant les principes fondamentaux du business et du marketing et en intégrant les leçons des dernières années des acteurs matures qui sont restés performants, comme des acteurs innovants, que les stratégies D2C pourront relever le challenge de la croissance.

1) *Concentrer les efforts sur l'approfondissement de la relation avec les clients et ne plus se limiter à un benchmark vis-à-vis des concurrents* :

Une stratégie D2C résiliente doit chercher à créer de la valeur tout au long du parcours d'achat, en commençant par sonder les clients lors de la phase initiale où ils perçoivent la marque comme innovante, puis poursuivre et consolider la relation après achat. De nombreuses marques D2C ne réalisent pas que l'étape initiale du processus consiste autant à connaître le client qu'à se différencier. Alors que les riches opérateurs historiques parviennent à faire baisser les coûts de production et d'acquisition de clients, les alternatives DTC se retrouvent sans identité de marque ni caractéristique de différenciation.

Approfondir la relation client pour se différencier sur une proposition de valeur plus ciblée serait donc une première solution.

2) Exploiter l'accès au client pour créer de la valeur au-delà de l'acte d'achat :

Parce qu'elles accompagnent leurs clients tout au long du processus de décision et n'ont pas recours aux intermédiaires, les marques D2C ont accès aux informations très variées sur leurs clients, ce qui leur permet d'avoir des contacts intimes et directs avec eux, point faible des marques matures aux approches traditionnelles.

Une stratégie D2C optimale doit pouvoir exploiter activement et sur la durée ces informations collectées et disponibles sur les clients réels et les clients potentiels pour stimuler l'innovation, renforcer la chaîne de valeur au-delà de la transaction initiale et satisfaire le client à chaque étape du parcours d'achat.

3) Utiliser une combinaison de plusieurs canaux :

Une stratégie D2C résiliente doit considérer des extensions de canaux pour combler les lacunes dans le parcours d'achat des marques D2C. Fournir des services clefs avant ou après la vente, tels que l'inspection, l'ajustement, la réparation ou la mise à niveau est complémentaire et contribue à la mission de la marque D2C. Les extensions omnicanales doivent s'inscrire dans une stratégie de performance nourrie par la croissance et la différenciation.

4) Consolider son marché actuel avant l'extension de produits :

Avant de chercher à croître par une extension de produits, les marques D2C doivent analyser le bénéfice qui pourra être apporté par les revenus supplémentaires potentiels générés par une extension versus les risques associés aux coûts d'approvisionnement d'une extension. Pour qu'une stratégie D2C soit performante, le marché doit être suffisamment grand et robuste sur le produit cœur pour ensuite considérer une extension.

5) Intensifier sa valeur d'unicité :

La valeur symbolique d'unicité associée à la plupart des marques D2C est un facteur clef de succès sur lequel les stratégies D2C ont su se différencier par rapport aux approches traditionnelles. Au fur et à mesure que les entreprises plus matures les imitent, les marques D2C qui jusqu'alors reposaient sur une interface exclusivement en ligne, doivent considérer des approches hybrides avec des enseignes physiques (« brick and mortar »).

En effet, c'est en assurant une expérience unique et différenciante que les stratégies D2C soutiendront la croissance. Les consommateurs utilisent majoritairement plusieurs canaux – online et offline – et ceux qui ont des comportements hybrides dépensent en moyenne 1.5 plus que les comportements exclusifs. Dans cette perspective, l'enseigne n'a pas pour but premier de finaliser la transaction mais d'offrir des services exclusifs et innovants sur les modalités pour tester les produits, découvrir des gammes exclusives, et personnaliser davantage leur achat.

C'est ainsi que Glossier, marque cosmétique D2C, vient d'ouvrir son deuxième magasin qui a accueilli plus de 35 000 visiteurs au cours de ses deux premiers mois d'existence. Il attire notamment par une sculpture de champignons que les jeunes clients valorisent particulièrement (des milliers de flux sur Instagram). Son autre magasin se concentre sur l'expérience de la rencontre avec un design façonné pour créer la rencontre et l'échange physique. De même, dans le suivi d'Apple qui avait déjà adopté cette stratégie hybride dès 2001, Meta et Google viennent également d'ouvrir leurs propres magasins pour offrir une expérience unique. Les visiteurs peuvent essayer les produits de réalité virtuelle et web3 (casque, lunette, assistant de voix, metaverse) d'une manière unique et non reproductible ailleurs, et c'est cette unicité qui peut soutenir la résilience et la performance de l'entreprise adoptant une stratégie D2C hybride.

Conclusion : Quel avenir pour les stratégies D2C ?

Les stratégies D2C resteront sur la durée. Elles innovent par rapport aux approches traditionnelles et viennent pallier les faiblesses de l'existant. En exploitant pleinement les informations riches et variées sur les clients recueillis à travers de fréquentes et directes interactions, les stratégies D2C ont réussi à suivre les évolutions des comportements d'achat en adaptant leurs pratiques pour servir leurs communautés de clients uniques. Les meilleures d'entre elles ont transformé cette capacité en un modèle économique rentable appliqué à plusieurs segments de clients.

Mais au fur et à mesure que les marques D2C deviennent plus matures, il leur faut évoluer pour soutenir la croissance et renforcer la résilience de l'entreprise sur le long terme. Elles doivent sonder les tendances du macro-environnement et les « patterns » de leurs clients afin de pouvoir saisir les forces favorables à leur croissance en renouvelant leur modèle, et minimiser leur exposition aux risques. Se concentrer sur l 'unicité et la fidélité des clients est indispensable pour pouvoir s'appuyer sur une proposition de valeur différenciante et innovante qui pourrait soutenir une future extension. C'est dans cette perspective que les stratégies D2C évoluent vers l'hybridation avec des magasins en propre offrant une expérience exclusive et unique, non reproductible.

Il importe que, sur l'ensemble de la chaîne de vente, du marketing à la production jusqu'aux services après-vente, les marques de D2C multiplient les points de contact avec le client pour renforcer leur indépendance et leur lien direct avec les clients dans tout ce qu'elles font. C'est cette relation client unique qui pourra soutenir leur autonomie stratégique, leur unicité et leur capacité d'adaptation permanente aux évolutions structurelles des comportements d'achat, au cœur de la résilience.

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Le recours aux cabinets de conseil dans le secteur public : Remettre en perspective, penser l'opérationnel

Eléonore Brouard*
Tristan Dupas-Amory*

ESCP Business School

Abstract

Les récents débats sur le rôle des consultants privés dans le secteur public ont revêtu une dimension géopolitique, en questionnant l'indépendance et la souveraineté de l'Etat face à des cabinets pour la plupart d'origine anglo-saxonne. Ils sont l'occasion de réfléchir sur les relations entre le secteur public et le secteur privé dans un contexte de globalisation des pratiques managériales. Fruit de l'expérience des auteurs dans plusieurs cabinets de conseil et au sein des administrations autant que de la mobilisation de travaux scientifiques, cet *impact paper* propose une prise de recul face à cette pratique controversée du recours aux consultants dans la sphère publique française, par-delà son récent surgissement médiatique. Il tâchera de dégager, après une mise en perspective historique, quelques enjeux terrains que posent les prestations de conseil à la fois pour les agents publics et les consultants.

Mots clés : Consultants, secteur public, perspective historique, pilotage de mission de conseil

*Ph.D. Students, ESCP Business School

Le recours aux cabinets de conseil dans le secteur public : Remettre en perspective, penser l'opérationnel

Introduction

En mars 2022, les sénateurs français ont publié un rapport dénonçant l'emprise « tentaculaire » des cabinets de conseil sur l'État, notamment sur la conception et le déploiement des politiques publiques. Ce rapport a alimenté des débats anciens, qui ont ressurgi à l'occasion de la crise du Covid-19, sur l'intervention de consultants dans des domaines jugés régaliens. Ce débat médiatique - l'un des derniers en date - met en lumière des phénomènes qui remontent aux années 1980 et qui s'illustrent de façon inégale en Europe. Les consultants interviennent par exemple plus largement auprès de l'État en Grande-Bretagne qu'en France (Saint-Martin, 1998). Toutefois, tant la sociologie que la conception de l'État diffèrent entre les deux pays et le débat prend une coloration singulière en France.

Aux côtés de l'administration, en France et dans d'autres pays, les consultants ont contribué à introduire la performance au cœur de la conception et de l'analyse des politiques publiques. A titre d'exemple, la Loi Organique relative à la Loi de Finances (LOLF) de 2001 a acté la mise en place de projets et rapports annuels de performance pour chaque politique publique, à laquelle sont associés des cibles et des indicateurs de réussite chiffrés. La mise en place de la LOLF et du système d'information comptable de l'État afférent a été accompagnée activement par des consultants. Amendé dans les pays précurseurs, remis en cause par de nouveaux paradigmes, le *New Public Management* continuerait cependant de se diffuser, notamment dans les pays où il avait initialement connu un succès relatif, comme la France (Abord de Chatillon & Desmarais, 2012).

Près de vingt ans plus tard, plusieurs éléments sont questionnés par les médias, par les élus, par les citoyens et par les chercheurs. Ainsi, l'utilisation de fonds publics pour rémunérer des sociétés privées avec des montants jugés importants est questionnée. Plus fondamentalement, la souveraineté de l'État se trouverait mise en cause selon certains, en raison de l'intervention jugée massive de consultants appartenant à des entreprises, qui pourrait menacer notre souveraineté intellectuelle. Ainsi, des enjeux géopolitiques ont animé les récents débats : la plupart des grands cabinets de conseil en France sont des cabinets d'origine américaine ou britannique (McKinsey, Accenture, etc.), bien que certains soient issus de fusions avec des cabinets français (Deloitte, KPMG, par exemple), et que d'autres soient d'origine française (Mazars). En outre, ils disposent presque tous de bureaux sur le territoire français depuis parfois plusieurs dizaines d'années. Plus largement, ce sont la forme, le rôle et la place de l'État et ses relations avec le secteur privé qui peuvent poser question.

Cet article s'appuie sur le point de vue de deux chercheurs – doctorants en management et comptabilité ayant travaillé au sein de plusieurs administrations en tant que consultants ou contractuels. Son objectif est de replacer la dimension médiatique du débat dans un contexte historique plus large et de souligner les enjeux opérationnels du recours aux consultants. Il nous semble notamment important de démontrer le rôle actif des donneurs d'ordre dans le pilotage des missions de conseil, tandis que beaucoup d'études se concentrent sur le rôle des consultants. Cet *impact paper* est aussi l'occasion de questionner plus en détail le fonctionnement d'une mission de conseil, les conditions de sa préparation et de son pilotage dans les organisations publiques, et de proposer des pistes de réflexion permettant de mieux appréhender l'intervention des consultants. Il nous semble opportun de prendre ce recul pour établir une réflexion sur le pilotage et les rôles respectifs des agents publics et des consultants.

Dans un premier temps, nous proposons un état des lieux historique du recours aux consultants dans le secteur public. Nous proposons ensuite quelques réflexions sur les enjeux opérationnels de la relation entre consultants et agents publics.

Remettre en perspective : éléments historiques sur le cas français

Le marché mondial du conseil représentait 178 Md€ en 2019. Les trois quarts de la demande sont concentrés en Amérique du Nord et en Europe (Jouan & Lemesle, 2021a). Le marché français du conseil en management occupe la troisième position sur le continent européen, avec un chiffre d'affaires total de 8,1 milliards en 2019, derrière celui de l'Allemagne (36,2 milliards) et du Royaume-Uni (12,9 milliards). Les banques et les services financiers représentent 30 % du marché en France, l'industrie 28%, et les services publics 9% (Jouan & Lemesle, 2021b). La part de l'administration dans le marché du conseil en France, bien que croissante, reste donc relativement modeste.

Au-delà de ces chiffres, comprendre ce qui se joue dans les débats actuels passe par une mise en perspective au long cours. Dans le prolongement de travaux qui ont mis en évidence l'opportunité de s'intéresser à l'histoire de la gestion et de la contextualiser, nous proposons donc dans un premier temps un retour aux origines du conseil en management dans le secteur public.

Les origines américaines

Dès les années 1880, des ingénieurs et des comptables américains inventent aux États-Unis les fondamentaux d'un nouveau métier : le consultant en management (McKenna, 2006). Leur influence - considérable - au sein des *boards* des plus grandes sociétés américaines s'accroît aussi auprès du gouvernement américain dans la période d'après-guerre. Ce dernier s'impose comme un acteur et client stratégique pour promouvoir leur vision des formes organisationnelles les plus « efficaces ». Des consultants supervisent la restructuration de la bureaucratie fédérale des Etats-Unis. McKenna évoque ainsi l'utilisation des cabinets de conseil pour des études réalisées pour la Marine pendant la Seconde Guerre mondiale par Booz, Fry, Allen & Hamilton, la réorganisation du pouvoir exécutif pour la Commission Hoover à la fin des années 1940 par Cresap, McCormick and Paget et Robert Heller & Associates, ou encore l'organisation initiale de la NASA en 1958 par McKinsey & Company.

Le recours aux consultants pour résoudre les problèmes organisationnels de l'État administratif américain est banalisé, institutionnalisé, et lui permet de maîtriser le nombre d'employés fédéraux tout en assumant des responsabilités administratives plus importantes. Cet « État contractuel » (McKenna, 2006) caractérisé par la contribution d'experts externes est devenu l'une des caractéristiques du gouvernement fédéral américain depuis 1945. Au milieu des années 1960, des critiques s'élèvent déjà pour critiquer ce « gouvernement fantôme » aux États-Unis. À la fin des années 1950, les sociétés de conseil mènent leur expansion en Europe et offrent leurs prestations aux acteurs privés comme publics du vieux continent. Dans ce contexte, la France a d'abord fait figure d'exception.

La pénétration des cabinets de conseil dans le secteur public français : un phénomène plus récent

La France s'est montrée plus imperméable au recours aux prestations de conseil dans le secteur public (Saint-Martin, 1998). Les idées managériales sont entrées dans la formulation des politiques publiques dans les années 1980 : la période 1982-1988 correspond notamment à une phase d'expansion, portée par la demande de certaines administrations publiques pour les prestations de conseil (Bezes, 2009). La loi-cadre sur la décentralisation en 1982 ouvre notamment les portes de certains niveaux d'administration locale aux consultants, et a facilité l'entrée des idées managériales à l'échelon local. La structuration du marché du conseil et les recommandations qui y sont prodiguées sont donc influencées par les réformes mais elles sont aussi susceptibles, en retour, d'influencer leurs contenus (Saint-Martin, 2004).

Lors de la première moitié des années 1980, les grands cabinets de conseil commencent à accompagner la réforme de l'État, comme l'analyse le sociologue Philippe Bezès. Les *Big fours* historiques de l'audit, polyvalents et dotés d'une réputation internationale solide, et les cabinets de conseil en stratégie, armés de leur prestige, tirent leur épingle du jeu (Bezès, 2009). Évaluation de politiques publiques, contrôle de gestion, ou encore analyse stratégique de l'organisation : ils proposent de nombreuses démarches managériales. Le développement de la discipline des sciences de gestion participe à la légitimation du recours à de nouvelles formes organisationnelles pour mieux administrer (*ibid*). L'administration est constituée en objet d'investigation et, simultanément, en objet d'interventions, enjeu politique et de politique (*ibid*). Dans le tournant des années 2000, la réforme de l'État « passe en mode industriel » et les échanges entre hauts fonctionnaires et cabinets de conseil, notamment à culture anglo-saxonne, se systématisent (*ibid).* Les réformes successives de l'État à partir de 2007 accentuent le recours à ces acteurs. Organisation de la transformation numérique de l'État, renouvellement des marchés publics, entrepreneurs « Govtech », les recours aux consultants se diversifient, au point que certains chercheurs remettent au goût du jour le terme de « consultocratie » pour désigner l'emprise des cabinets de conseil sur la transformation publique.

La « consultocratie » à l'épreuve de l'« énarchie »?

En Grande-Bretagne, des universitaires ont inventé le terme « consultocratie » pour décrire la manière dont l'entrée des idées des gestionnaires dans les politiques allait de pair avec la présence croissante des consultants autour de l'élaboration des politiques (Saint-Martin, 2004). Ce phénomène n'a pas été de la même ampleur selon les pays. Dans le cadre d'une comparaison incluant également le Canada et le Royaume-Uni, Saint-Martin suggère qu'en France, la haute administration publique a en partie freiné la montée d'une « consultocratie » française et retardé l'influence du « managérialisme » sur les politiques publiques. Le gouvernement a rapidement opté pour la création de son propre service de conseil interne car « les solutions proposées par les consultants internes sont en général mieux acceptées que celles des consultants externes marquées par une culture de l'entreprise privée » (rapport de la DGAFP, 1991). D'autres facteurs structurels français, comme la relative faiblesse du secteur du conseil et des idées managériales dans l'administration publique, font partie des raisons pour lesquelles la France se distingue, pour Saint-Martin, des cas britannique et canadien.

D’autres chercheurs, loin de se ranger derrière cette interprétation, insistent sur le fait que la proximité sociologique entre élites dirigeantes (décideurs, élus, consultants) constitue, au contraire, une variable clé de la pénétration croissante du conseil dans le secteur public (Gervais, 2012). Les thèses de la « consultocratie » sont critiquées car elles se centrent sur l'étude des cabinets les plus prestigieux, vraisemblablement dotés d’une légitimité plus importante que d’autres auprès des décideurs publics, politiques et administratifs (Poupeau et al., 2012). D’autres chercheurs encore, s’inspirant des travaux de Bourdieu, ont démontré que les élites travaillant pour le secteur public dans les cabinets de conseil et dans les administrations ont de nombreux points communs. Ces différentes études démontrent la complexité de ces groupes sociaux.

La prise de recul historique opérée dans cette première partie nous permet de mieux appréhender le phénomène du conseil auprès du secteur public. Notre démarche de chercheurs en gestion et de praticiens permet en outre de mettre en lumière dans la partie qui suit quelques enjeux stratégiques et opérationnels fondamentaux qui entourent le recours aux consultants dans le secteur public.

Penser l’opérationnel : préparer, piloter le recours aux consultants

Nous proposons ci-dessous d’aborder certains enjeux clés des missions de conseil auprès du secteur public, et notamment la question des marchés publics et l’importance de la préparation du recours des consultants pour les administrations.

Entre injonctions à la performance et nécessaire réflexion sur le rôle et les contours de la prestation de conseil

Comme évoqué précédemment, les différentes réformes du secteur public en France se sont largement inspirées du *New Public Management*. Ces réformes, entre autres, ont introduit des injonctions à la performance des agents publics et des femmes et hommes politiques, et ont accéléré le recours fréquent aux indicateurs de réussite des politiques publiques, médiatisés et utilisés comme outils de légitimation de l’action politique. Ces éléments peuvent limiter les temps et les espaces de réflexion sur le rôle de l’État et le recours à des prestataires extérieurs. Dans nos recherches, plusieurs fonctionnaires nous ont fait part de leur grande frustration de ne pouvoir consacrer du temps à la réflexion sur l’opportunité ou non de faire appel à des consultants.

Il ne s’agit pas ici de questionner le bien-fondé du recours aux consultants et de proposer une typologie des causes et modalités de recours, mais d’appeler à réintroduire des temps de réflexion (en amont) et de bilan (après la prestation) pour bien définir les contours, les opportunités, et les bénéfices (attendus et/ou obtenus) des missions de conseil. Bien sûr, ces missions font déjà l’objet d’une réflexion et d’une préparation par les personnes publiques. Toutefois, celles-ci nous semblent manquer de temps et de la possibilité de les questionner, tant les impératifs managériaux et politiques sont forts.

La passation d’un marché de conseil : une étape décisive qui fixe les bases du pilotage de la prestation

Préparer et passer un marché public pour une prestation de conseil prend du temps. L’établissement d’un dialogue soutenu entre les services demandeurs et les services des marchés est impératif et fonctionne plutôt bien. Il nous semble toutefois nécessaire de repréciser que la passation d’un marché public, exercice précis parfois jugé chronophage voire fastidieux, est une étape fondamentale pour le bon déroulement de la prestation à venir. Ainsi, une passation de marché peut prendre plusieurs mois, selon la procédure juridique retenue : en deçà de 40 000€ HT, les organisations publiques peuvent recourir sans mise en concurrence à des entreprises privées (d’après le code de la commande publique). Au-delà, c’est une obligation.

Tant l’identification du besoin, que sa formulation, puis la rédaction de pièces juridiques et le déroulement d’une procédure d’achat public sont des exercices qui permettent à l’administration de réfléchir à ses attentes quant au marché de conseil, mais également à son rôle dans la relation avec ses consultants. C’est aussi l’occasion de réfléchir aux modalités de déroulement et de suivi des prestations à venir. Nos interlocuteurs nous font parfois part de marchés qui sont trop peu suivis à leurs yeux, et ils nous semblent que ce suivi se prépare et s’intègre dès la passation du marché : prévoir une ou plusieurs personnes en interne qui pilotent la mission, prévoir de demander des points réguliers pour suivre la consommation du budget, etc. Pour les consultants également, ces éléments sont clés : une prestation dont les contours sont clairs, avec des interlocuteurs sensibilisés au fait qu’une mission de conseil va requérir de leur part un investissement personnel, un partage de documents, des échanges réguliers, permettent de mener une mission efficacement. Tant la préparation que le suivi de près permettront d’éviter les décalages budgétaires et de calendrier.

Il est ainsi intéressant de confronter les enjeux de la procédure avec les impératifs de performance et d’immédiateté mentionnés précédemment. Cela permet de comprendre dans quelle mesure une préparation et une passation bouclée dans des délais très restreints avec un périmètre plus ou moins défini peut avoir des incidences sur la réussite de la mission (tant dans son déroulement opérationnel, que dans ses conclusions et ses effets, et dans ses coûts).

Enfin, l’un des éléments importants du recours à des consultants privés dans le secteur public se situe selon nous dans la confrontation de deux types de fonctionnements et de cultures professionnelles, que les consultants et les personnes publiques doivent appréhender. Cette confrontation apparaît dès la conception et la préparation du recours aux consultants par les personnes publiques. En effet, nos recherches montrent que même si les personnes publiques font en sorte de choisir leurs consultants en toute indépendance, en ayant recours à des documents d’analyse standardisés par exemple, elles sont influencées dans leurs choix par les a priori qu’elles ont sur les consultants. Il peut s’agir d’a prioris généraux, liés à des représentations des consultants dans les médias, ou bien d’a prioris nés de leurs expériences passées avec certains consultants. Côté consultants, la réponse à des appels d’offres requiert des interprétations sur le cahier des charges et donc sur les attentes supposées des personnes publiques. La passation de marché constitue ainsi un dialogue indirect entre consultants et clients, où se nichent des représentations croisées de chacune des parties sur l’autre, et qui influence fortement la prestation par la suite.

En outre, la différence de culture entre les clients publics et les consultants requiert de la part des consultants une adaptation et une compréhension rapide des enjeux et fonctionnements spécifiques de leurs clients publics, qui est souvent déplorée par ces dits clients dans les échanges que nous avons avec eux. L'adaptation des méthodes, des propositions, et des livrables des consultants aux spécificités de leurs clients secteur public existe mais nous semble à renforcer. Au-delà de ce travail qui doit être effectué par les consultants, il nous semble intéressant d'approfondir les leviers dont disposent les personnes publiques pour encore mieux piloter la relation commerciale avec leurs prestataires de conseil.

Conclusion

La valeur du conseil : une quête de sens ?

Les missions de conseil ayant les plus grandes chances de réussite sont celles qui sont caractérisées par un engagement mutuel, réciproque et équitable entre le cabinet de conseils et le client dans la réalisation de la mission (Huczynski, 2006). La collaboration entre les agents publics et les consultants est au cœur des enjeux historiques et opérationnels autour de la valeur de la prestation de conseil. Le conseil a parfois été caractérisé comme une activité « entièrement tendue vers la production de sa propre valeur, faite de performances fragiles et contingentes que les consultants sont donc tenus de faire exister et reconnaître, en mettant sans cesse en avant leur contribution » (Bourgoin, 2017). La question que pose leur recours dans le secteur public est complexe : quelle est la valeur de leur contribution pour la société (*ibid*) ? Tous les agents publics susceptibles de piloter des prestations de conseil devraient y être formés, et tous les consultants être sensibilisés. Nos expériences montrent que le point commun entre le consultant pour le secteur public et l'agent public, c'est parfois une quête de sens, de sens social. C'est peut-être à partir de ce dénominateur commun qu'il faut construire une relation - équilibrée mais exigeante - entre administrations et prestataires privés.

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Une méthode conceptuelle pour la coordination des politiques de durabilité : une analyse macro-géopolitique

Amir Pirayesh
KEDGE Business School,
Bordeaux

Hamed Ghiaie
ESCP Business School, Paris

Nicolas Boisson
KEDGE Business School,
Bordeaux

Omid Fatahi-Valilai
Jacobs University, Bremen

Abstract

Les politiques de durabilité, qui deviennent de plus en plus vitales et incontournables dans le monde géopolitique pour protéger la société et notre planète, peuvent impliquer de nouveaux choix de matières premières, la modification des technologies de production et de logistique, ou encore la relocalisation des fournisseurs, etc. Dès lors, de nouvelles interactions industrielles peuvent émerger autour des produits et des chaînes de valeur existantes. Afin d'étudier l'impact de ces changements, une analyse macro-géopolitique pourrait être bénéfique. De plus, une telle analyse permettrait d'identifier la corrélation entre les politiques de durabilité et leurs compromis pour atteindre des scénarios optimaux. À ces fins, sur la base du modèle Entrée-Sortie (Input-Output) et en se concentrant sur un secteur industriel comme pilote, cette étude propose donc une méthode conceptuelle centrée sur le schéma économique du secteur cosmétique comme exemple.

Mots clés : Politique de durabilité ; économie ; chaîne de valeur ; modèle entrée-sortie.

Une méthode conceptuelle pour la coordination des politiques de durabilité : une analyse macro-géopolitique

1. Introduction

Depuis des années, les communautés internationales essaient d'adopter de nouvelles politiques « durables » telles que l'utilisation des matières recyclables ou la relocalisation des fournisseurs. Afin d'évaluer l'impact de ces politiques, plusieurs indicateurs sont utilisés comme le taux d'émission de CO_2 et les taux de consommation d'eau et d'énergie, ou encore le niveau d'investissements financiers pour la durabilité. L'impact individuel ou mutuel de ces politiques et la corrélation des indicateurs sont des sujets qui méritent d'être davantage étudiés. Ces sujets peuvent être très complexes lorsque plusieurs politiques ont été ou seront adoptées. Compte tenu des interactions industrielles, ces sujets pourront être étudiés d'un point de vue macro ou sectoriel. Ce travail vise, en conséquence, à illustrer de façon conceptuelle l'investigation des politiques durables et leur impact, selon une approche macro-économique basée sur le modèle Entrée-Sortie de Leontief. À titre d'illustration, cette étude se concentre sur le secteur de la cosmétique. Tout en confirmant les stratégies durables dans ce secteur, Buso (2021) et Focquet et al (2018) précisent que les industries cosmétiques orientent leurs leviers d'actions de durabilité vers les mécanismes d'éco-innovation. En outre, ce secteur a une certaine proximité avec les industries du plastique, des matières premières et de l'agriculture, largement concernées par les questions environnementales, et génère plus de 10 milliards d'euros de PIB en France. Les résultats de la méthode, sous réserve d'hypothèses prédéfinies, ont été présentés pour alimenter les réflexions ultérieures.

2. Durabilité et Modèle Entrée-Sortie

Dans le contexte d'une chaîne de valeurs, et notamment dans une économie nationale ou globalisée, l'approche macro-économique pourrait avoir une place importante. Cette approche peut permettre d'évaluer les politiques durables via une étude multisectorielle en considérant chaque secteur comme un composant unique d'une chaîne de valeurs globale (Vadvári et al, 2015). De ce point de vue macro, le concept de l'analyse entrée-sortie (E-S), initié par Potron en 1912, permet d'établir les interdépendances entre les différents secteurs de l'économie (Leontief, 1974). Ainsi, cette approche sera reprise par les travaux de Leontief, qui proposera le modèle entrée-sortie, lequel lui vaudra le prix Nobel d'économie. Leontief visualise notre économie sous la forme d'un tableau entrées-sorties (TES) formant une matrice carrée ayant pour valeurs les flux monétaires en dollars entre un nombre *n* de secteurs économiques à l'origine de la structure matricielle (n x n). L'économiste prend également en compte l'ajout en dollars de la demande finale pour les différents biens produits au sein des « n » secteurs. Amsyari (1992) souligne que l'établissement des liens entre les résultats d'un modèle MRIO et les piliers de la durabilité (environnement – social – économie) reste possible et important, même s'il est complexe. Certains chercheurs essaient même de relier les résultats du modèle MRIO avec des KPIs de durabilité. Par exemple, Voigtlaender (2002), après avoir estimé les flux financiers de l'industrie du transport aux États-Unis, a mis en place une méthode pour convertir ces données monétaires en tonnes de marchandises transportées afin de les valoriser à l'aide d'un taux d'émission de CO_2 imputable aux activités routières. Cette stratégie lui a ainsi permis d'estimer la pollution annuelle de l'industrie du transport aux États-Unis.

3. Méthode proposée

Dans la méthode proposée, à partir d'un secteur cible, il est nécessaire de définir les secteurs à l'origine des composants de sa chaîne de valeurs afin d'isoler une économie. Suivant le modèle de Leontief, et en partant des données sur les échanges industriels fournies par l'OCDE (Organisation de coopération et de développement économiques) pour l'industrie des produits chimiques et pharmaceutiques en 2015, qui pourrait avoir les mêmes caractéristiques que le secteur cosmétique par analogie, la matrice des coefficients (la matrice A dans le modèle de Leontief) est calculée. Ensuite, à partir de cette dernière et prenant en compte le PIB du secteur cosmétique, il a été possible d'identifier la part de sortie de chacun des secteurs intervenant spécifiquement dans la génération du PIB du secteur cosmétique, ce qui constituera la base du modèle pour les analyses des scénarios. Ensuite, en considérant le vecteur matriciel $X_{cosmétique}$ et le PIB du secteur cosmétique, il est proposé de déterminer l'émission de CO_2 de la supply chain de ce secteur (l'ensemble des secteurs concernés pour répondre à la demande du secteur cosmétique) selon le calcul suivant, où S_i est un secteur ayant des sorties pour le secteur cosmétique, C désigne le secteur cosmétique, et E est le taux d'émission de CO_2 par un dollar de PIB.

$$Émission\ CO2\ Cosmétique = \sum_1^i \quad Output\ S_i\ pour\ C * E_i + PIB_c \ * E_c \qquad (1$$

L'étape suivante consistait à définir des scénarios à analyser via une approche calculatoire qui vise à relier, sous différents critères, la planification quantitative de notre économie à des KPIs de durabilité pour arbitrer les résultats. Dans le cas illustratif, trois paramètres sont distingués pour construire la scénarisation : le recyclage des packagings des produits cosmétiques, les éco-innovations dans les secteurs en interaction avec le secteur cosmétique, et la relocalisation de l'approvisionnement. La dernière étape du modèle reposait sur une répétition des points précédemment décrits selon une base annuelle afin d'obtenir des résultats sous forme de séries chronologiques, de façon à proposer des projections des émissions de CO_2 des industries cosmétiques. De plus, la variation des différents paramètres tels que le taux de recyclage T, la part de durabilité P, l'efficience des éco-innovations E et la distance des fournisseurs des différents secteurs ont permis d'arbitrer les scénarios.

4. Illustration et analyses

Cette partie revient sur la présentation des résultats de l'application de la méthodologie au secteur cosmétique[1]. Pour les analyses comparatives, la situation actuelle est considérée comme le scénario I (témoin).

[1] *Approximations (hypothèses simplificatrices) : la nomenclature classique des produits cosmétiques est considérée pour identifier les secteurs de la supply chain cosmétique ; certains coefficients associés au secteur des produits chimiques et pharmaceutiques en France sont repris pour le secteur cosmétique ; la réduction du transport à l'amont, grâce au recyclage, est*

4.1. Cas du scénario II : éco-innovation soutenue par l'internationalisation

4.1.1. Éco-innovation unique ou mono-sectorielle

Dans ce scénario, s'agissant d'une éco-innovation unique, nous considérons la possibilité de recyclage et de réutilisation des packagings des produits cosmétiques et que cette action impacte seulement les secteurs de la supply chain suivants : métaux (verre), papier, plastique. En effet, et rappelons-le, ces secteurs interviennent directement sur la conception du packaging et le recyclage de ce dernier induit indirectement une réduction des outputs issus de ces trois secteurs précédemment évoqués. La notion de $Output\ Recyclabilité$ est notamment introduite via le calcul suivant selon une règle de trois :

$$Output\ Recyclabilité_{secteur\ i} = Output_{secteur\ i} - \frac{Output_{secteur\ i} * PIB\ Cosmétique * T}{PIB\ Cosmétique} \quad (2$$

Avec $Output\ Recyclabilité_{secteur\ i}$, la quantité d'outputs pour un secteur donné à apporter pour répondre à la demande « PIB Cosmétique » suite à l'application d'un processus de recyclage à un taux T. La variable $Output_{secteur\ i}$ renvoie, quant à elle, à la quantité d'outputs pour le secteur i issue de la planification économique de base. Plusieurs taux de recyclage (T) ont donc été testés à 30, 50 et 80 % de la demande globale (Y) en produits cosmétiques (voir la Figure 1).

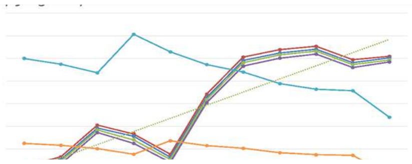


Figure 1. Impact de la recyclabilité des packagings sur les émissions de CO_2 de la supply chain cosmétique

4.1.2. Éco-innovation commune et multisectorielle

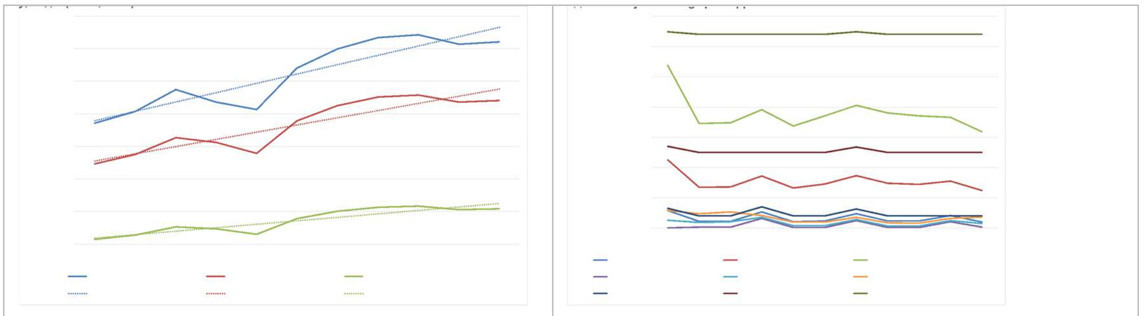
Dans ce sous-scénario, nous émettrons l'hypothèse que l'ensemble des secteurs à l'origine de la confection de produits cosmétiques sont capables de mettre en place les principes d'éco-logistique dans le périmètre national et que les mécanismes d'éco-innovation n'affectent pas les distances de transport. Dans un premier temps, pour chacun des secteurs de notre supply chain, deux paramètres ont donc été introduits avec P, la part d'outputs soumise aux éco-innovations (p. ex. 10 % agriculture traditionnelle) et E, l'efficacité de ces dernières pour réduire les indices d'émissions de CO_2. Dès lors, les calculs suivants ont été utilisés pour introduire ce second aspect.

$$Émission\ durabilité_{secteur\ i} = Output_{secteur\ i} * P_{secteur\ i} * Taux\ d'émission_{secteur\ i} * (1 - E_{secteur\ i}) \quad (3$$

$$Émission\ sans\ durabilité_{secteur\ i} = Output_{secteur\ i} * (1 - P_{secteur\ i}) * Taux\ d'émission_{secteur\ i} \quad (4$$

égale à l'augmentation du transport des matières à recycler/emballages recyclés ; le PIB du secteur cosmétique dans les prochaines années est estimé selon les données de l'Institut de la mode.

Avec $\acute{E}mission\ durabilit\acute{e}$, les quantités de CO_2 émises par les parts d'outputs du secteur i soumises au processus d'éco-innovation. Inversement, $\acute{E}mission\ sans\ durabilit\acute{e}$ renvoie aux quantités de CO_2 émises par les parts d'outputs du secteur i non soumises au processus d'éco-innovation, soit une situation analogue au scénario I. L'influence des éco-innovations est d'abord étudiée pour les secteurs « mineurs », ayant moins de 5M $ d'outputs pour le secteur cosmétique : les secteurs des métaux, du bois/papier et du plastique. Ainsi, la part d'outputs de ces secteurs soumise aux éco-innovations a été fixée successivement à 20, 50 et 80 %. En lien avec ces pourcentages, l'efficience des éco-innovations pour réduire les indices d'émissions a été paramétrée aux mêmes seuils (20, 50, 80 %). Finalement, l'application globale des éco-innovations a été étudiée (voir la Figure 2).



Éco-innovations appliquées à l'ensemble des secteurs

Variation des émissions de CO_2 (% de réduction) par rapport au Scénario I

Figure 2. Impact des éco-innovations sur les émissions de CO_2 de la supply chain cosmétique

4.2. Cas du scénario III : éco-innovation sans la possibilité d'internationalisation

Ce dernier scénario, comparé au scénario II, intervient dans un contexte où l'adoption globale des pratiques d'éco-innovation dans la supply chain cosmétique peut obliger les entreprises associées à travailler avec des fournisseurs d'autres secteurs qui sont plus éloignés. Les mécanismes d'éco-innovation sont encore configurés selon une approche globale à 20, 50 et 80 %.

Les étapes de calculs du scénario II ont été conservées pour illustrer la durabilité. Toutefois, le principe d'éco-logistique a été modulé pour éloigner les fournisseurs de nos différents secteurs par rapport aux sites de production cosmétiques. Étant donné que les tableaux E-S issus des bases de données de l'OCDE ne permettaient pas d'avoir des extractions multirégionales avec plusieurs pays, il a été nécessaire de procéder de la façon suivante. Ainsi, les outputs associés au secteur du transport pour générer la demande en produits cosmétiques ont été ventilés entre chacun des secteurs de notre supply chain, selon leurs poids respectifs, par rapport à la somme total des outputs, selon le calcul ci-dessous :

$$Output\ Tansport_{secteur\ i} = Output_{Transport} * \frac{Output_{secteur\ i}}{Output\ total} \qquad (5$$

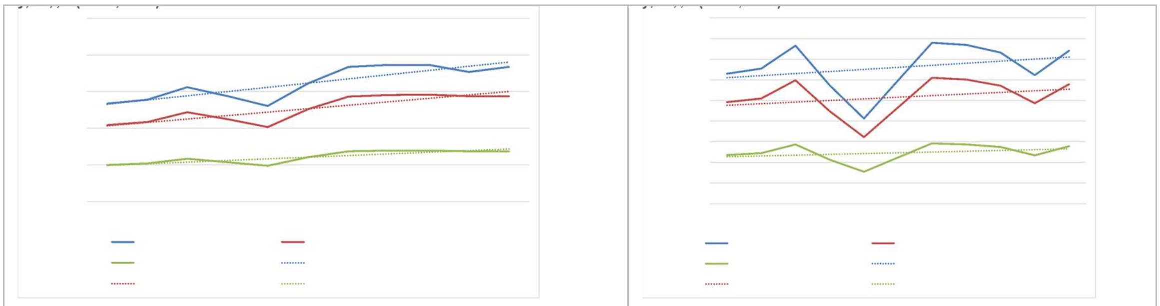
Une fois réparties entre les différents secteurs, les émissions des outputs de transports ont été déterminées en prenant en compte la distance des fournisseurs de la façon suivante, et en revalorisant les facteurs d'émissions de CO_2. Afin de réaliser cette étape, nous avons introduit une notion de variation notée ⊗ telle que :

$$= \frac{Distance\ fournisseur_{secteur\ i} * 0{,}1 - 20}{20} \qquad (6$$

Où 0,1 correspond aux émissions terrestres en kg/T/km selon le CITEPA (Centre interprofessionnel technique d'études de la pollution atmosphérique) et 20 au nombre de kg émis pour une distance de 200 km, que nous assimilerons à la localisation des fournisseurs de nos différents secteurs dans le cas du scénario II. Ainsi, en faisant varier le paramètre $Distance\ fournisseur_{secteur\ i}$, il deviendra possible d'appliquer le taux de variation au taux d'émission de CO_2 des transports qui a été estimé à 0,0272 kg/$ lors du scénario I. Cette contrainte permettra en conséquence d'évaluer les émissions d'output des transports selon les secteurs de notre supply chain et de prendre en compte la localisation des fournisseurs, selon ce dernier calcul :

$$\text{É}mission\ transport_{secteur\ i} = Output\ transport_{\ secteur\ i} * \ * Taux\ d'\text{é}mission\ transport \qquad (7$$

L'intégration de cette dernière procédure dans l'équation initiale permettra de déterminer les émissions totales de CO_2 de la chaîne de valeurs des produits cosmétiques. Par la suite, il est supposé que les fournisseurs durables (qui peuvent adopter l'éco-innovation) de notre supply chain macro-économique sont localisés à différentes distances par rapport aux sites de production cosmétique. À titre d'exemple, les données obtenues pour les distances de 500 et 8 000 km sont illustrées par la Figure 3.



Éloignement faible des fournisseurs (500 km) — Éloignement important des fournisseurs (8 000 km)

Figure 3. Impact des éco-innovations et relocalisation des fournisseurs sur les émissions de CO_2 du secteur cosmétique

5. Discussions et perspectives

Dans ce travail, une méthode macro-géopolitique est proposée pour analyser l'impact et l'alignement des stratégies sectorielles et des politiques de durabilité en prenant en compte l'ensemble des chaînes de valeurs d'une industrie ou d'une économie donnée. Les politiques étudiées dans le cas illustratif sont principalement articulées autour du recyclage des matières premières, de la durabilité des secteurs, et de l'emplacement des fournisseurs du secteur cosmétique en France. Sous réserve de certaines approximations et hypothèses simplificatrices susmentionnées, l'interprétation des résultats issus de la méthode permet, dans un premier temps, de mettre en avant la notion d'arbitrage des politiques de durabilité pour optimiser la réduction des émissions de CO_2, dans le cas des activités cosmétiques à l'échelle nationale (et par extension, dans d'autres contextes plus globaux). En particulier, s'il est important d'intégrer des éco-innovations chez les fournisseurs partenaires des sites de production cosmétique, l'arbitrage de leurs distances est tout aussi important étant donné qu'une localisation éloignée peut contrebalancer les efforts d'éco-innovation mis en place. Concernant les perspectives macro-géopolitiques de cette étude, il est, dans un premier temps, proposé de vérifier les données du modèle E-S du scénario I (témoin) et d'affiner le calcul des émissions CO_2 du secteur cosmétique en conséquence. Comme autre réflexion d'ouverture, une exploitation des indicateurs de durabilité, issus des deux autres volets (social et économique) intégrés au modèle entrée-sortie, est jugée pertinente pour apporter des réponses communes aux défis écologiques et socio égalitaires.

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