A DISCUSSION WITH MCKINSEY & COMPANY EXECUTIVE
ELIE MAALOUF, SENIOR ADVISOR

Company:	McKinsey & Company, LLC Global management consulting firm
Respondent:	Elie Maalouf, Senior Advisor Formerly President and CEO of HMSHost Corporation, with approximately $3 billion in sales and 34,000 employees in 14 countries.
Interviewer:	Andrew C. Wicks

BACKGROUND

Background: Andrew C. Wicks (Darden School, University of Virginia) and Jeffrey S. Harrison (Robins School of Business, University of Richmond) asked seven executives from six major companies engaged in a variety of industries to read and then respond to an academic article they had published on measuring performance from a stakeholder perspective. The Harrison and Wicks paper is called "Stakeholder Theory, Value and Firm Performance." It was published in *Business Ethics Quarterly* in January 2013. The authors started the discussions with a list of questions, but then also asked follow-up questions and allowed executives to expand on topics in which they were particularly interested.

What follows is the transcript of one of the interviews in its complete form. Andrew and Jeffrey lightly edited the interviews and eliminated things not pertinent to the study (such as pleasantries) and they also allowed the interviewees to make clarifications prior to publication. The most interesting statements are in bold.

A related paper also included in this repository is called "A practitioner critique of a conceptual paper on measuring value and performance." That paper includes a more detailed examination and evaluation of what they found across all the interviews.

OVERALL REACTIONS

Wicks: Initial reactions to the paper, particularly whether you found the ideas compelling and whether they fit with your experience?

Maalouf: Here's what I would say: The subject in general I've given some thought to, the whole concept of CSR was starting to get a lot of traction. Some of the items that you wrote about, whether it's stakeholder perspectives or others, are similar. **I have, maybe, a slightly different view in the sense that I do believe that putting shareholders first is necessary in for-profit organizations. If you're a not-for-profit or governmental organization, that's a different game altogether. I do believe it's necessary and unavoidable. You may try not to, but it will get you eventually. The capital markets have changed. Ownership structures have changed significantly over the last 20 years; unless there's a family that owns 50.1%, sooner or later the capital markets, through activists, hedge funds, and others, will bring the pressure to put the shareholders first. But there are different ways to put shareholders first, and I could still agree with most of your argument that taking care of other constituents is part of putting shareholders first because long-term, it enables you to survive and succeed in your industry and to create more shareholder value.** But you wouldn't do it for other reasons. I think it's dangerous for organizations and for leaders to pretend that they have a duty to other stakeholders just for its own sake.

Wicks: **Irrespective of the impact on stakeholders?**

Maalouf: **Yes. Or even to put shareholders and stakeholders equal. I think eventually those situations unravel, and those organizations can't take care of shareholders or their stakeholders anymore at that point because they've lost the focus they need to have. I have this totally unscientific theory that all organizations exist in an ecosystem which has different constituents, and they're different by organization and certainly by industry. They may be common within industries, but they're certainly different across industries, so whether you're in mining, forest products, real estate, beverages, consumer products or finance, you have an ecosystem within which you need to interact that has some key constituents. I don't even know that they're necessarily stakeholders because the title 'stakeholder' starts to provide them with almost equity in your outcome, to provide them with entitlement. I think they're constituents, and the organizations that tend to succeed 50 years and beyond have had to change their business models. They have had to innovate their products, but it's very hard for them to succeed for 50 years and beyond if they don't have a certain harmony and balance within their ecosystem such that those key constituents eventually want them to succeed and survive because**

they are interacting with them in ways that are reasonable, that promote the ultimate success of both, despite tough negotiations and zero sum moments, and ultimately those constituents want that organization to succeed rather than fail.

So I think my view is compatible with yours, except I still believe that you can, and must, put shareholders first and make sure that stakeholders don't perceive a sense of entitlement to your organization, but a sense of shared outcome in your ecosystem.

STRENGTHS OF THE PAPER

Wicks: Is there anything particular that you liked about the paper? Any specific ideas? Any particular arguments?

Maalouf: I like the identification of those four or five areas—employees, customers, suppliers, shareholders, community. I think these apply to different degrees in different industries, and I think shareholders are always there. Employees are generally there, although there are some industries where employees matter a whole lot less, such as industries that are very automated, for example.

WEAKNESSES OF THE PAPER

Wicks: What about major weaknesses, highlighting places where you feel like the argument should've been structured differently or things we should've emphasized more?

Maalouf: **I'd go back to say that I maintain that shareholders need to come first and then there are building blocks towards that. I think that organizations that lose that focus are really miscommunicating to the other constituents – the employees, the customers, the suppliers, the communities. They may actually believe what you're saying – hey, we're all on equal footing here – and start to demand and require a different outcome, a different share of the pie, as you call it, because they see themselves on equal footing. That's not sustainable, and the system will just collapse. The market won't support that position, and then you're not taking care of anybody in the end.**

Wicks: But if you altered how you read the piece and you assumed that one of the things that employees, the customers, the other core groups want, is actually to see the firm earn the kind of returns that allows it to be competitive financially and financially viable, if that is built into the stake of each of these individual core stakeholders who are part of the value chain, does that address some of your concern?

Maalouf: It does. I think it's a challenge, frankly. Say you have an organization with 30 or 40 thousand people – it's a challenge to instill that capital markets understanding into each one of them. I did it to the extent that I could, communicating very simply: "Look, people, the way that we sustain ourselves and grow is we attract investor capital, and the way we attract investor capital is to produce returns, and the way to produce returns is to do these things, and if we stop this virtuous cycle, then we can't get capital, we can't get grow, and bad things happen versus good things." Most people will get it to some extent, but I think once they perceived that it is a stakeholder model and everybody's on equal footing, it's a different conversation, so I think it's important to explain to them that by taking care of shareholders, that then good things happen to everybody, and if we stop looking at that as our magnetic north, then eventually we will all suffer. I've seen organizations try pure stakeholder models.

I would say you have to make it clear that not all animals are equal in this kingdom. They're equal in terms of rights, but the purpose of a for-profit organization is to produce returns for its shareholders, and when it's doing it properly and legally and ethically, then generally good things happen to the others.

Now, the leaders of that organization who want to do it on a sustainable basis need to understand the value of having a balanced ecosystem because when you want that organization to go to the next level, to make sacrifices, to get through a tough time, to go beyond the ordinary—

Wicks: **The extra mile.**

Maalouf: **And beyond the extra mile, the extra mile running on broken glass – what I call walking on broken glass. When you want people to do that for you, that's very hard when you haven't treated that ecosystem properly and kept it in balance. So in good times you'll bump along and ride the wave with the market and go up in share or maintain share, but you're going to hit a bad time – whether you're Boeing or Marriott or whether you're American Express or whether you're Goldman Sachs, you're going to hit a really bad time, and if your employees and suppliers and customers don't think you're worth saving, they probably won't save you.** You become Lehman, where everybody said it was just a deal shop. There was no value system, no culture. It was all very mechanical and they let it go, but in other organizations that had something more to them, somebody stepped in.

Not the government. Somebody—the employees, some customers, some suppliers—stepped in and made a difference.

Remember Marriott in '90-'91, almost bankrupt, and the company I ran was a spinoff from Marriott, almost bankrupt, and some of their key suppliers stepped in with funding and in return, they got long-term agreements. But you know what, they thought it was worth saving and there were personal relationships there that they thought were worth saving, so I've seen it happen, and I think inspired leadership will maintain that balance and ecosystem for their own benefit and for their shareholders' benefit.

ARE FIRMS MOVING IN THE DIRECTION THE PAPER DESCRIBES?

Wicks: As you look at the business landscape, do you think that firms are moving in the direction the paper describes, even if it doesn't map it exactly onto how you read the direction?

Maalouf: **No, I think it's moving in the opposite direction.**

Wicks: How would you characterize business?

Maalouf: I think there's so much pressure on boards and on CEOs to think in the short term that I think, in terms of direction, there are more firms moving outside of balancing their ecosystem than to balance their ecosystem because they're saying, "if I don't make this next quarter, somebody else will." They'll find another supplier, another set of employees, which doesn't mean they don't have another choice, but not many leaders have the courage to maintain some balance in their ecosystem. Sometimes they have to tilt it. **Balance doesn't mean the same amount of light in every bulb all the time. You may dim one a little bit, but in general, you're not turning one off. But I think there aren't as many courageous leaders, and they're getting pummeled by activists and by information that can dissect their performance daily so they tend to drift away from balancing the ecosystem.**

IS YOUR FIRM MEASURING PERFORMANCE MORE BROADLY?

Wicks: Moving to your firm, would you say your firm is moving in the direction of measuring firm performance more broadly? Are you looking at some of the metrics that capture value for some of the key groups that you see as important beyond just traditional financial metrics?

Maalouf: You mean the firm I used to run or McKinsey? I'm an advisor with MacKenzie, a major consulting firm and I advise the firm. They're a strategic consulting firm, and I don't know that they're representative of an industry. They are a high class, high quality services consulting firm that does what they do very well, and I would say that they do very well in terms of balancing their ecosystem over the years.

Wicks: Do they measure performance in ways that go beyond strictly traditional financial measures? Do they look at some of these other notions about value creation?

Maalouf: I think they do, to be honest with you. I don't know that well, but I think they do. **I think they spend a tremendous amount of time measuring the progress and success and quality of their employees, which are their key resource. They have very close relationships with their customers and make sure that they're delivering value to their customers. [McKinsey] really doesn't have suppliers. Their suppliers are their employees.** It's the same thing. I don't think they're suppliers. The shareholders are also their employees, so they tend to have two core constituents, which are employees and their clients. It's easier to focus on them because they have two, but they're also very dependent on them. They don't have any hard assets or formulas or anything like that.

Wicks: Anything about your former company that you'd want to mention?

Maalouf: **I don't think they're doing it to any greater extent than when I did it and maybe to a lesser extent. It's not something the board will ever do. It's something that the CEO does; either he or she has the courage to balance things or they don't, and it's very hard to get several like that in a row. And so we hit a very hard patch when I was still running the company and during the financial crisis of '09, '10, and we had to make a lot of tough decisions, but you could've gone further in some of the areas with some benefit and probably a lot more cost. You would've gotten a little more headline in terms of cost saving, in terms of supplier renegotiation, in terms of customer renegotiation. You could've done that, but there was a moment when I had to sit down with the board and say that we can go to this other level but let me tell you where you might be two years from now when the recovery comes. You own this company, and tell me if that's where you want to be, because there will be a recovery. If we think the world will go on from the gloomy days of November 2008 to January 2009, if we think the world will come back from that, then let's imagine where we will be and where we want to be with our key customers, suppliers and employees and where do you want the value of your firm to be ultimately if some of it comes from these areas.**

HOW WOULD YOU HAVE WRITTEN THE ARTICLE DIFFERENTLY?

Wicks: What about the article would you have done differently? What did we miss that you think is important for people writing about business to better understand what's going on?

Maalouf: A three- or four-page introduction or executive summary that shapes the argument and its conclusions. **We're not in a world anymore where people want to read 30 pages to get the bottom of something.** I think some examples would be powerful. It's very hard today to make a point without some real life examples. **It's a much better made point when someone can say, "here's an organization that did it this way, and managed to succeed, and here's an organization that didn't and didn't succeed, and we think these are representative of our argument."**

Wicks: Would you use a company like Whole Foods as an example?

Maalouf: Yes, and I think when you listen to the CEO of Whole Foods (John Mackey) speak and write, he's very keen about what makes money, and so he's against having a unionized workforce and he's against the new health care plan and he's against a lot of mandates that would encumber his business from making money and from thinking on its own about how to treat its ecosystem, so he's not just a do-gooder for do-gooder's sake. **He understands that he's appealing to a certain demographic and that demographic feels better about shopping in his store when they feel like the whole ecosystem is being treated properly. They won't feel good about buying their organic lettuce if the organic lettuce farmer had been mugged in the process. So the people who are shopping there are thinking more broadly than just the health credentials of that individual product.** It's experiential, so he's doing it for his shareholders and very finely calibrating what goes into that formula to maintain that experience in the interest of the shareholder. Starbucks is another one.