

ENGAGING YOUR STAKEHOLDERS

12 Pitfalls to Avoid on the Path to Managing Reputational Risks

By WITOLD J. HENISZ

Whenever I ask executives in the programs I teach how much management time they wish to dedicate to engaging with external stakeholders, they usually answer in one of two ways: one camp emphatically answers "zero" while the rest say between 10 and 20 percent, though they often concede this grudgingly, and only insofar as it advances their careers. When I ask them why, most argue that stakeholder engagement doesn't create any obvious value. Besides, business people see themselves as managers, innovators or marketers, not as lobbyists or diplomats.

Yet when a crisis hits, what's the typical thing a business person focuses on? Damage control and reputation repair in the eyes of external stakeholders. If they play their cards well, they may even be able to transform that crisis into an opportunity, improving their long-term standing with their stakeholders and society.

So why do executives appear to ignore "corporate diplomacy," which in many ways is one of the best resources in the executive toolkit to help manage risk effectively?

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Becoming a Corporate DIPLOMat

In my book *Corporate Diplomacy: Building Reputations and Relationships With External Stakeholders*, I define six elements that are key to winning the hearts and minds of external stakeholders in support of an organizational mission. These six stack up to form the acronym DIPLOMat.

- **D** **DUE DILIGENCE:** conducting a thorough investigation of the stakeholder landscape.
- **I** **INTEGRATION:** incorporating those insights into core business systems, so as to identify profit-maximizing stakeholder engagement strategies.
- **P** **PERSONAL:** building personal, trust-based relationships with key stakeholders.
- **L** **LEARNING:** adapting your strategy to the dynamic evolution of the external environment.
- **O** **OPENNESS:** being transparent in deploying a communications strategy that reinforces trust by highlighting your actions to address stakeholder needs.
- **M** **MINDSET:** cultivating and maintaining an organizational mindset or culture that recognizes the importance of external stakeholders.

Corporate diplomacy differs from stakeholder engagement, external or public affairs and reputation management in its holistic and integrated design. The goals and demands of stakeholders are linked to the key performance indicators of the company. The interactions with stakeholders and media-based communication strategies emphasize the observable and core behaviors of the company, some of which have been modified to address stakeholder concerns. The entire system is dynamic, allowing for real-time monitoring and adaptation of any aspect of operations, marketing, technology, finance or corporate strategy. The culture of the company is transformed to bring external stakeholders into the discussion of every strategic decision.

When you frame corporate diplomacy this way, it becomes apparent that these are the essential means by which companies not only reduce risk and preempt future crises, but also generate value for stakeholders who subsequently become their advocates for business expansion. Once managers see the place where business, politics and society collide not as a source of nasty surprises or unexpected expenses but as a source of value creation for shareholders and society alike, they will begin to put their companies on the right path to success.

However, that path is strewn with traps. In trying to design and implement corporate diplomacy, executives are frequently stymied in their efforts. To do this job well, you need to be aware of the risks you will likely encounter along the way. Here I sketch out the 12 biggest pitfalls to avoid.

1 WE DON'T DO THAT

The first trap is complacency. Take Shell: It wasn't until 2008 that the company acknowledged that not only were its market capitalization and strategy influenced by political and social developments, but that it had a vested interest in influencing those developments and the ability to do so. How could Shell, of all companies, have persisted for so long under the illusion that it was *not* a political company?

There are clues on the company's website, which describes its mission in terms of using advanced technologies and pursuing innovation. It's clear that Shell's management prizes engineering. When this happens, anything else is seen as a distraction or a waste of money. As a result, engagement professionals are afforded little voice or authority, and their teams tend to be understaffed and under-resourced.

EXECUTIVE SUMMARY

Engaging with your external stakeholders is an essential means by which companies not only reduce risk and preempt future crises, but also generate value for shareholders and society alike. So why do executives appear to ignore "corporate diplomacy," which in many ways is one of the best resources in the executive toolkit to help manage risk effectively?

Drawing on his DIPLOMat framework, the author answers this question by showing the myriad ways that executives are frequently stymied in their efforts to maximize their stakeholder potential. He sketches out the 12 biggest risks to avoid. By identifying the main risks in the stakeholder environment, executives can mitigate their adverse impacts and seize their upside opportunity.

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If you find yourself in this position, simply arguing that external stakeholders matter is not enough. To change attitudes, the senior leadership team must commit itself to reshaping the organizational mindset such that every employee accepts, internalizes and acts on this argument. Without such a cultural shift, whatever efforts are made to develop systems, hire personnel and engage stakeholders will, at some point, run aground.

2 NICE TO HAVE BUT NOT CORE

The second most common trap is treating engagement as a peripheral, long-shot investment undertaken when resources allow. The fiercest critics view these investments as giveaways of hard-earned returns that management will come to regret. In companies where diplomacy is under development or, worse, under attack, cost pressure can trigger a counterproductive retreat. For example, as oil and gas prices plummet, investments in corporate diplomacy have been slashed.

A common pattern emerges: Managers begin with an overly optimistic forecast for a new investment that ignores the full range of concerns and potential costs associated with external stakeholders. The investment is approved. As the reality is slow to realize, necessary additional costs are borne and concessions made. When prices come under pressure and, especially, when new leadership arrives, these investments are viewed with growing skepticism. They are compared with the original plan, which promised far greater returns with lower up-front costs. No matter that the original plan was naïve in its assumptions and impossible to realize. The new manager wants to be seen as adept at righting the ship that has gone astray. Investments and staff in the corporate diplomacy function are slashed. While this may register a short-term improvement in the balance sheet, the long-term value prospects are reduced. By the time the true costs of this short-sighted strategy are revealed, managers will likely have moved on to their next position.

It is absolutely critical to guard against such a pattern. This means that any investment in stakeholder engagement must be presented in the same terms as other investments in operations, marketing or finance. As one analyst has noted, "A business case of words does not cut it. To get airtime, (you) must talk the language of commerce. Even if a general manager disputes the level of revenue upside, (you) will at least be able to engage in a debate on this basis. By making the case financially tangible, a dialogue becomes possible."

In order to survive business downturns, the corporate diplomat must abandon hopes of transforming or supplementing the existing systems that drive business decision-making, or convincing their peers of the virtues of corporate diplomacy as an end in and of itself. Instead, they must accept the dominant logics of their organizations, and embed their value proposition within them.

3 ARBITRARY BUDGETING

Another challenge involves resource allocation. Budgets are tight, and companies want to see returns on their investments. For the sake of expedience, people follow rules of thumb for budgeting, especially when dealing with activities that are not perceived as providing obvious financial returns. Managers will often allot a fixed revenue percentage of, say, 1 percent. The Indian government has gone further, mandating that companies spend 2 percent of net profits on social development.

Such fixed targets are damaging for several reasons. First, they bear no correlation with the potential returns from corporate diplomacy investments. Second, they perpetuate the perception that these activities generate

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no returns. Worse still, they preclude any anticipatory investment in stakeholder capital, because until a project begins operation, there's no revenue stream or net profits from which to allocate funds. That is why the previous point – about achieving integration into core business systems – is so important, as it enables managers to calculate the net present value of corporate diplomacy, which can then drive the allocation of resources.

4 INTERNAL DIVISIONS

Invariably, managers will disagree over which risks and stakeholder priorities deserve the most attention. These disagreements may be influenced by personal relationships and biases, internal political rivalries or the quest for status or power.

The key is how these disagreements are managed. If the process is not fair, employees may harbor resentment, leading them to attack the process, their peers or even the corporate effort more broadly.

Sometimes the biggest divisions are those where well-established practices are being challenged. Say your company operates in a dangerous country with a history of corrupt police. What's the best way of managing the risks: Hire more armed security guards? Fund youth soccer teams and health clinics to build social capital? Run public service media campaigns? All could be legitimate. But those who favor one approach versus another – especially when "we've always done it that way before" – may end up spending all their time squabbling over it, which is why being able to show the relative returns of a given choice can help to win the day.

As such, in addition to managing the risks "out there," corporate diplomats must devote time to their internal stakeholders, building personal relationships and trust with them, too. Sadly, those who espouse the need to recognize the perspectives and values of external stakeholders can neglect doing the same for their colleagues.

5 CHOOSING THE WRONG FRIENDS

An all-too-common shortcut is to hire or ally with a well-connected insider. Although this may avoid costly due diligence, the long-term consequences of doing this can be risky.

The trouble with this strategy is that an insider will make recommendations based on personal knowledge of a place and its players, but if this knowledge cannot be substantiated with data or analysis that can be examined and questioned by others, there are grounds to be suspicious. How does this person benefit? Who else might he or she be serving?

Even more problematic, you are not building your own relationships but relying wholly on those of your local champion. That means you inherit not just this person's allies but also his or her enemies. To the extent that your champion is part of a local coalition or clique, you, too, have joined, becoming a rival to his or her rivals. If the tables should turn, your sole ally may become the outsider and your

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It is far better to build your own understanding of the risk environment and its stakeholders, especially as the definition of "relevant" information and players depends on the issue at the time.

enemy the new authority. Even if this new leader chooses to be forgiving rather than exact revenge, the advantages of your initial ties depreciate rapidly.

In the long-term, it is far better to build your own understanding of the risk environment and its stakeholders, especially as the definition of "relevant" information and players depends on the issue at the time, in a rapidly shifting competitive landscape. You want to be the one making those critical judgments about what the key risks are, who the main players are, how they're connected and how they will affect your business – not leaving that to someone else's discretion.

6 ARROGANCE AND A DESIRE FOR CONTROL

Arrogance is an affliction that manifests itself as "Decide, Announce, Defend" and other paternalistic forms of management. When managers believe they have all the answers, they stop receiving vital input from internal professionals and the wider community that could signal important shifts or emerging risks.

No doubt, sharing control and decision rights with other functions of the business and external organizations with less capacity entails risk. But disabling internal and external stakeholders from directly and personally contributing their expertise and specialist knowledge poses a much greater threat, as the corporate diplomat can't be expected to know everything.

Working for a big multinational, Deji Haastrup of Chevron Nigeria notes the issue: "We are all well-read. We all believe we are intellectuals. We all believe we know a great deal, and therefore we know what's right for everyone. But we don't. One must be a little humble."

Sometimes the best answers reside with managers and operators in an outlying production facility or distribution chain. Deferring to these local stakeholders is important not just because it enhances your current position, but because it honors those stakeholders and their descendants who remain and who will have to manage their own risks long after your project is complete and your company has pulled out. Again, it's a matter of thinking long term, not just in terms of reducing the short-term costs and benefits that stakeholder risks represent to you today.

The Tintaya mine in Peru offers an example of this kind of capacity building. An arrogant approach would have involved the foreign managers negotiating the best deal for the mining company with no regard for local stakeholders who lacked sophisticated negotiating skills and business backgrounds. Instead, they trained their negotiating counterparts, helping their adversaries to secure a deal that represented their interests.

Ask yourself: which was the riskier option? The first one, expedient for the company but leaving people feeling manipulated or coerced? Or the second one, which involved giving up some control and short-term returns but was ultimately more sustainable?

7 LEARNING THE WRONG LESSONS

A denied permit. A double-crossing ally. Both can sting and cost plenty of money. But it would be wrong to conclude, from a single failure, that further investments in new capacities, personnel and analysis are without merit.

A company would not terminate its entire R&D program because one investment failed. Nor would it fire the entire sales staff if one client walked away. The difference is that R&D and sales are considered central to business performance. Corporate diplomacy, on the other hand, is often viewed as a cost center. Changing this mindset will take time.

Failures will happen along the way, as in every corporate endeavor. Where bad luck strikes early, or before efforts have delivered results,

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the backlash can undermine the future ability to attract resources, people and credibility.

But it's not just a case of "once bitten, twice shy." Early success can breed as many misguided attitudes as early failure. Having dodged the bullet, managers may feel that enough has been done already.

Regardless of the most recent outcome, one needs to look beyond the immediate result – the permit received or the risk averted – to the data on stakeholder issues. Which performed as expected? Which surprises emerged? How much did they influence outcomes, if at all? The more a company regularly reviews these processes, the more they begin to resemble R&D, sales and any other core business function.

8 GREASING THE SQUEAKY WHEEL

It's natural to pay attention to the loudest voice, the most persistent and outspoken critic, particularly if that person appears powerful. But if others see that whiners and bullies get their issues prioritized, they may mimic that behavior, and complaints and grievances will escalate.

John Ruggie, former United Nations Special Representative on Business and Human Rights, tells the story of how a community leader in Peru closed down the only access road to a local mine. His reason: "They paid no attention to us when we raised small problems, so we had to create a big one." This illustrates what happens when companies only pay attention to the big risks but ignore the seemingly smaller ones – until the simmering pot finally boils over.

Allocating resources to one set of stakeholders versus another needs to be done with reference to the extent it influences stakeholder cooperation and encourages fair dealing in the present and in the future. Rewarding bad behavior today encourages worse conduct in the future – leading to abuses of power or status, destabilization of once peaceful relations or, in extreme cases, violence.

Rio Tinto's mine in Bougainville, Papua New Guinea, is a case in point. In the late '80s, the company dealt with one vocal group of young men in a dispute over land rights. What the company failed to appreciate was that this was a matrilineal, age-stratified society, and the English-speaking group with whom they negotiated had little or no social legitimacy in an island rife with long-running ethnic tensions, territorial disputes, post-colonial resentments and a growing independence movement. The mine conflict sparked violent uprisings, which contributed to a 10-year civil war in which thousands of people were killed.

9 PROPAGANDA OVER SUBSTANCE

Given the complexity of accurate due diligence, of integrating that information into key business systems, of sharing and ceding authority and of adapting to changes, some practitioners argue it may be easier to just spin or sell a project than engage in such time- and resource-intensive processes. For spinners, stakeholders are stooges to be bamboozled with ads and photo ops. Their goal is to identify key influencers and use them to sell a project to other stakeholders. The problem here is that spinners do not believe in true engagement.

In an age of YouTube, Facebook and all manner of social media only a smartphone away, the ability to engage in propaganda, greenwashing and manipulation is increasingly limited. Perhaps in the 20th century, investors could rely on their power over mass media and the powerlessness of their competitors and opponents. Today, however, PR tools and tactics are accessible to all.

Multinational corporations operate amid sophisticated networks of activists, politicians and suppliers. It is safer to assume that the spotlight will shine on your misdeeds than

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to assume that you can selectively present your accomplishments and hide your failings. We live in a world without secrets. As such, the returns on propaganda, greenwashing and manipulation are increasingly ephemeral.

10 PERFECT IS THE ENEMY OF GOOD

Some specialists with expertise in data systems over-engineer corporate diplomacy and risk management by trying to build perfect data and reporting systems, capturing every possible piece of information about every stakeholder interaction. While a laudable goal in theory, such an effort can undermine progress.

In reality, the rollout of such a system can take years and require a big investment in information technology. In the meantime, engagement teams providing the data will still have to do their jobs, flying blind while the perfect machine is being built. Worse still, corporate diplomacy will end up like a vacuum, sucking in funds but providing little measurable benefit in return. This situation can backfire, especially if a new management team arrives.

The focus of data-gathering should always be on the rapid delivery of material benefits. The initiative should be well-designed but cannot stretch for more than a few quarters. Multi-year pushes involving major IT investments or external partnerships can continue in the background. But short-term successes are essential if corporate diplomacy is to prove its worth.

Skeptical internal stakeholders will expect more than promises of returns in two or three years from an optimal system. They will need to see short-term benefits. A competent team should be able to execute a stakeholder survey, analyze the financial returns of a number of initiatives, and design and implement new strategies, including a communications strategy and an internal culture-shaping component, within six to nine months, or one year at most.

11 TOO MANY GOOD INTENTIONS

Managers can also fall prey to excessive responsiveness. A common complaint among skeptics is that corporate diplomacy is just bribery in disguise, with all the same risks. In other words, instead of putting cash in envelopes, you build schools, community centers, parks and clinics. In the end, however, the recipients are never satisfied and keep asking for more. The budget increases but the social license does not. And if the budget does not increase, the social license withers.

I encountered a classic example of this problem at a hotel in Bali. The general manager there was struggling to build a stronger relationship with the residents of the community around the hotel. One of their major grievances was a lack of garbage collection by the government. The hotel initiated a "walk the block" event for Friday afternoons in which hotel staffers would walk the neighborhood around the hotel collecting and bagging garbage. They then took the trash to a landfill.

After the first week, the change in the neighborhood was striking. Community members appreciated that the eyesore and health hazard of the garbage had been removed at no cost to them.

But a problem emerged the following Friday. Instead of taking 10 employees two hours, trash collection took four hours, and the hotel staffers managed, in that time, to clear only half the block. The amount of garbage seemed larger. The next Friday, it was larger still. The hotel staff quickly deduced that the residents were receiving garbage from their friends and relatives elsewhere on the island, and that the hotel was becoming the de facto dump.

The general manager ceased the program and convened a meeting of the community at which he explained that he wanted to help but could not run a hotel as the island's trash hauler. He offered a new policy. The hotel would

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commit up to 10 workers and transportation to the landfill – but only if the community committed an equal number of people and the work was shared equally. He also involved the residents in a grassroots political campaign to get the relevant political authorities to take responsibility for the garbage clean-up.

The corporate diplomat is a member of an organization that has a goal. He or she seeks to engage with external stakeholders in support of that goal. The goal is not, however, to make everyone happy or to be everyone's friend. A company is neither a government nor an NGO.

Corporate diplomacy is a mix of tough analysis and gentler interpersonal elements in pursuit of a hard-edged objective. It involves weighing the risks and making difficult choices. Diplomats can be trusted – they should be trusted – but are rarely loved.

12 MORALISM THAT ANTAGONIZES AND ISOLATES

Personalities and internal politics matter. You have to choose the right evangelist for your corporate diplomacy effort.

In one recent case, I observed an organization with a high-level commitment to corporate diplomacy unleash a moralistic attack dog on various operational units. He lectured and iambasted colleagues for violations of process and law. He demanded investigations. Needless to say, his outreach was not well-received.

While extreme, this example is not unique. Given the typical lack of experience with corporate diplomacy, the status quo may outrage people trained in engagement. When they are finally empowered, they may see an opportunity to right injustices. But what these people lose sight of is the need to win over skeptics. Realistically, replacing these skeptics is unlikely. Instead, they must be persuaded. Change and learning are slow – sometimes too slow for the specialist.

Attacking insiders needlessly antagonizes. To avoid internal hostility, a diplomat should focus not on past failings but on future improvements. Certain violations will demand action, while others can be managed over time or deferred.

The same personal approach applies to finance, accounting, operations and other teams: Invest time in understanding your colleagues and learning the issues that matter most to them.

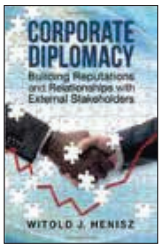
Dancing Free of the Traps

The path from the status quo to the forefront of corporate diplomacy is littered with the 12 traps described in this article, and potentially more. By learning the critical steps from firms on the front lines, managers can dance free and push forward the frontier of the art and science of corporate diplomacy.

In so doing, you are enabling external stakeholders to achieve their long-term goals while simultaneously pursuing the enlightened self-interest of your client or employer. You are building the dynamic capability to identify risks emanating in the stakeholder environment, mitigate their adverse impacts and seize their upside opportunity.

As the focus of global competition shifts to emerging markets, where politics are more fluid and social challenges are not well-addressed by governments, such risks and associated opportunities are increasingly influencing the outcome of global competition. □

TO KNOW MORE



- This article is based on the concluding chapter of *Corporate Diplomacy: Building Reputations and Relationships With External Stakeholders* by Witold Henisz (Greenleaf, 2014).

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