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CHAPTER 7

A Stakeholder Approach to Value Creation and Leadership

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Takeaways for Leading Change

This chapter builds on the notion that in contemporary societies, leaders need to pay attention to a broad array of stakeholders and understand how value is created in stakeholder relationships. Stakeholder research considers how firms can create value simultaneously for multiple stakeholders (Freeman, Harrison, & Wicks, 2007), and how value is created in stakeholder relationships (Myllykangas, Kujala, & Lehtimäki, 2010). The key message in this chapter is that organisations and their leaders need to understand value-creating stakeholder relationships. The chapter proposes the SVC model with an emphasis on joint interests, the ability to collaborate, and trust in stakeholder relationships. For those working in leadership positions, the SVC model provides a tool for considering value creation with and for a wide-ranging variety of stakeholders.

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This chapter argues that those working in leadership positions must understand that value is created in relationships with a broad variety of stakeholders. Beyond increasing the value of investment made by owners, business organisations must fulfil the needs and expectations of various stakeholders, such as employees and customers, suppliers and distributors, investors and local communities. Public organisations need to address and engage a variety of stakeholders including citizens, non-profit organisations and local authorities, to accomplish their mission. In this chapter, we introduce the stakeholder approach and describe what kinds of tools it proposes for understanding value creation.

The traditional view of value creation examines how companies create value by using resources to make products to be sold in the market. In the value creating chain, actors are subcontractors, vendors, employees, and sales agencies, to mention a few. The input of each actor continuously adds value to the product until it reaches the customer. (Porter, 1985.) This view of value creation sees companies as production machines between inputs from suppliers, investors and employees, and outputs to customers (Donaldson, 1995). The chief executive officer (CEO) acts as an agent of the owners who have invested their money in the business and expect returns on their investment. In other words, the owners hire the CEO to act as their agent in the company whose primary objective is to produce the maximum return on the money invested in the company. This view is also called the neo-classical view of the firm where the purpose is in maximising firm value rather than optimising collective value (cf. Bosse, Phillips, & Harrison, 2009; Donaldson & Walsh, 2015).

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The traditional view can be criticised along several lines. First, it may lead to serious malpractices resulting from individual benefit-seeking and short term profit maximisation by the owners and CEO. This comes at the cost of long term profitability. Corporate scandals such as the cases of Enron or Siemens illustrate this problem. In the Enron case, financial reporting and disclosures covered problems of corporate governance and

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leadership. Profit margins and the share price was manipulated from the late 1990s into the early 2000s. As a result, 4,500 employees lost their jobs, investors lost USD 60 billion, and trust in the American economic system was eroded. In the Siemens case, hundreds of employees gave bribes amounting up to EUR 1.3 billion to business partners and government officials between 1999 and 2006. The practice resulted in the dismissal of numerous top managers in the company, the payment of EUR 500 million in back-taxes, EUR 1 billion in investigation costs and repairing the damage to the company's reputation in the eyes of the public (Global Ethic, 2009).

Second, the traditional view allows and even encourages the exploitation of natural resources. For example, air pollution and waste are considered the unwanted but inevitable outcomes of economic activity. However, with growing scientific consensus on the effects of global warming, running a business to the detriment of the natural environment has become increasingly unacceptable in the eyes of the public. A recent Finnish example, the Terrafame mine case, illustrates this tension. While the company brought jobs and economic well-being to a remote and economically depressed region in North-Eastern Finland, it was nevertheless criticised for the damages its mining activities caused to the local environment.

Third, the traditional view does not sufficiently take into account the needs and expectations of various stakeholders in society. It justifies the focus on profit maximisation without paying attention to societal outcomes. We argue stakeholders such as employees, citizens as well as local and national authorities have a legitimate right to expect and claim socially acceptable and beneficial behaviour from organisations and their leaders.

The stakeholder approach is an alternative to the traditional profit maximisation view. According to Freeman (1984; 2010), stakeholders are groups and individuals that can affect or can be affected by an organisation. For private organisations, the argument is that business is not only about increasing the value of the investment made by owners, but about fulfilling the needs and expectations of various stakeholders. The theory argues that the reason for a firm's existence can and should be found in value-creating stakeholder relationships (Freeman, Harrison, Wicks, Parmar, & de Colle, 2010; Näsi, 1995a). Companies bring together employees and customers,

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suppliers and distributors, investors and communities with the purpose of creating new jobs, products and services needed and desired by various stakeholders. Value not only accrues to owners and investors, but to all stakeholders (Garcia-Castro & Aguilera, 2015). The collective value created reflects the value created in all stakeholder relationships (Bosse et al., 2009). For public organisations, organisational objectives are connected to stakeholders through joint activities. In this way, public organisations fulfil their mission and create value for all involved parties (Heikkinen, Kujala, & Inha, 2018).

Interestingly, the origin and evolution of the stakeholder concept can be traced to Scandinavian management literature dating back to the 1960's; the basic concepts and ideas of stakeholder thinking were developed by Swedish researcher Eric Rhenman (Rhenman, 1964; Rhenman & Stymne, 1965; see also Strand & Freeman, 2015). In the 1970s, the "stakeholder approach enjoyed an almost dominant role in the Finnish university management teaching" (Näsi, 1995b, p. 98). Among the promoters of stakeholder thinking was Finnish professor Juha Näsi. He was influential not only in international theory development from the 1970s to the 2000s, but also in advancing stakeholder thinking in the strategic management of Finnish companies.

Since R. Edward Freeman's seminal work in 1984, the stakeholder approach has gradually increased its importance in organisational studies worldwide. Over the years, the stakeholder approach has been established as an important approach in conceptualising the relationship between business and society. The approach has been used to examine multiple phenomena in various fields such as strategic management (e.g., Haksever, Chaganti, & Cook, 2004; Harrison, Bosse, & Phillips, 2010; Sachs & Rühli, 2011), corporate responsibility (e.g., Sachs & Maurer, 2009; Smith & Rönnegard, 2016; Strand et al., 2015), business ethics (e.g., Phillips, 1997; Purnell & Freeman, 2012; Wicks, 1996), international business (e.g., Lehtimäki & Kujala, 2017), and non-profit organisations (Heikkinen et al., 2018).

At first, stakeholder scholars were primarily interested in identifying the most important stakeholders and their interests; in other words stakes, in business (e.g., Clarkson, 1995; Mitchell, Agle, & Wood, 1997). More recently, the focus has shifted toward examining interaction between diverse stakeholders (Neville & Menguc, 2006), understanding

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stakeholder dialogue (Burchell & Cook, 2006; van Huijstee & Glasbergen, 2008), and learning from multi-stakeholder networks (Roloff, 2008). The interest lies in stakeholder interaction and the nature of stakeholder relationships (Evan & Freeman, 1988; Mitchell et al., 1997; Rowley, 1997). Advocates promote the idea that the interests of different parties in stakeholder organisations should be incorporated into the process of value creation (Freeman et al., 2010). Value, in this sense, is created not only for stakeholders but also with stakeholders (Freeman et al., 2010).

> In the long run, an organisation must operate in such a way that each stakeholder is satisfied with what they give and with what they receive.

The key argument in stakeholder theory that, in the long run, an organisation must operate in such a way that each stakeholder is satisfied with what they give and with what they receive, i.e. stakeholder interests must be balanced over time (Freeman et al., 2007; Näsi, 1995a). In business organisation, the stakeholder approach argues it is necessary to broaden organisational goals beyond profit maximisation and include the interests and claims of non-stockholding groups (Mitchell et al., 1997). One of the main arguments is that the development and maintenance of favourable and productive stakeholder relationships are essential in creating value (Post, Preston, & Sachs, 2002; Svendsen, Boutlier, Abbott, & Wheeler, 2002). Seeking to serve the interests of a broad array of stakeholders will create more value over time (Freeman, 1984; Harrison et al., 2010). As society changes, the stakeholder approach can help organisations and their leaders in determining what issues to address in order to facilitate the creation of new innovations and value (Harrison & Wicks, 2013).

In this chapter, we present two approaches to understanding stakeholder interests and firm-stakeholder relationships. First, we introduce the Responsiveness Approach in stakeholder management. It proposes that organisations operate in a stakeholder environment and proposes ways in which organisations can pit responding to stakeholder needs and interests at the core of its strategic operations. Second, we introduce the Stakeholder Value Creation (SVC) model in stakeholder management. This model

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views organisations and their stakeholders as interdependent. The SVC model highlights the importance of understanding how organisations pursue joint interests. We will conclude with a discussion on these two approaches and their impact on understanding how companies and other organisations operate.

The Responsiveness Approach

The key argument in the responsiveness approach is that organisations decide their societal engagement based on stakeholder needs and demands (Frederick, 1978; Wood, 1991). The strategic outcome is that organisations which respond to stakeholder needs and interests are better off in the marketplace and can gain a competitive advantage over organisations which do not pay attention to the views and expectations of their stakeholders. Since the early days of stakeholder theorising, the discussion has focused on the question of who stakeholders are, identifying their stakes and understanding the nature of stakeholder driven organisations. The responsiveness approach seeks to identify the most important stakeholders, analyse the interests and needs of these stakeholders, and measure responses to stakeholder expectations. Measures for analysing the connection between social responsibility and social performance have also been developed (e.g., Berman, Wicks, Kotha, & Jones, 1999; Kobeissi & Damanpour, 2009; Orlitzky, Schmidt, & Rynes, 2003).

Mitchell et al. (1997) made an important contribution to the stakeholder theory by defining the principle of who and what really counts in stakeholder management. They identified three attributes that serve as a basis for stakeholder salience: power of the stakeholder, urgency of the demand made by the stakeholder, and the legitimacy of the stakeholder demand. Their theoretical framework, the salience model, is one of the best-known models for the responsiveness approach (Figure 1).

In the salience model, power refers to "a relationship among social actors in which one social actor, A, can get another social actor, B, to do something that B would not have otherwise done". Legitimacy, in turn, is defined as "a generalized perception or assumption that the actions of an entity are

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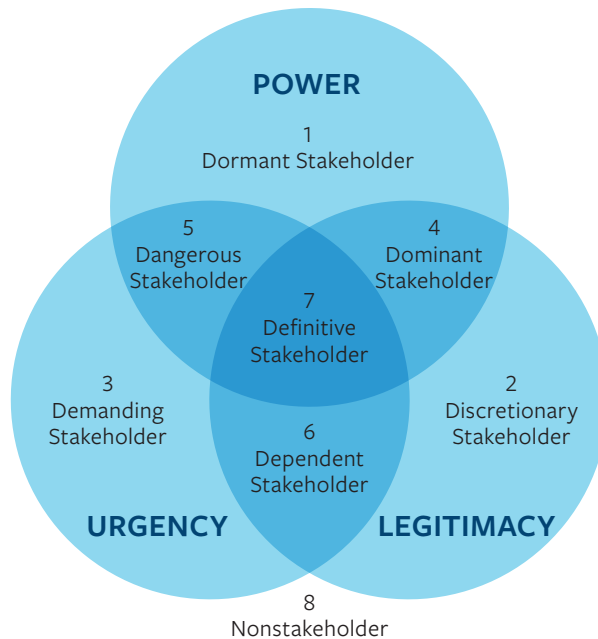A Stakeholder Approach to Value Creation and Leadership

FIGURE 1. The stakeholder salience model (Mitchell et al. 1997, p. 874)

desirable, proper, or appropriate within some socially constructed system or norms, values, beliefs, definitions." Urgency, as the third dimension of the model, addresses "the degree to which stakeholder claims call for immediate attention" (Mitchell et al. 1997, p. 869). According to this model, the more attributes a stakeholder claim has, the more salient it is. Salience is defined as "the degree to which managers give priority to competing stakeholder claims" and stakeholder salience analysis is argued to reveal the definitive stakeholders and provide a foundation for analysing stakeholder relationships (Mitchell et al. 1997, p. 869).

The stakeholder salience model has served as a tool for empirical analysis in previous research. For example, Myllykangas et al. (2010) used the salience model in a longitudinal study to depict stakeholder dynamics in strategic change of a company. The results of the study showed that over time, in the different strategic periods, the stakeholders both lost and

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gained attributes. With the salience model, they were able to show that stakeholder relationships are processes that change and evolve over time (Myllykangas et al., 2010, p. 68). The salience model has been also used to measure and assess stakeholder influence (Aaltonen, Kujala, & Oijala, 2008; Eesley & Lenox 2006; Neville & Menguc 2006; de Vries, 2009), to examine stakeholder prioritising (Boesso & Kumar, 2009; Harvey & Schaefer, 2001; Parent & Deephouse, 2007), and to study responsibility reporting (Weber & Marley, 2012). It has also been used to identify stakeholder management strategies in supply chain collaboration (Co & Barro, 2009; Magness, 2008), to create corporate stakeholder cultures (Jones, Felps & Bigley, 2007), and to analyse the dynamics of stakeholder relationships (Jawahar & Mclaughlin, 2001).

Despite the wide use of the stakeholder salience model in empirical analysis, many researchers have criticised the model for its limited understanding of stakeholder relationship dynamics (Friedman & Miles, 2002), the role of dependent stakeholders (Calton & Payne, 2003), and stakeholder interface and networks (Pajunen, 2006; Frooman, 1999; Rowley, 1997; Rowley & Moldoveanu 2003). Moir, Kennerley & Ferguson (2007) and Derry (2012) point out that the stakeholder salience model does not work because salient stakeholders change over time and managers need to tackle constantly changing stakeholder relationships. For this reason, a better understanding of how stakeholders influence organisations, how organisations should engage with stakeholders, and how to evaluate the impact of organisational activities on stakeholders is needed. According to Freeman (2010), stakeholder theorising needs to escape the trap of building trade-offs among stakeholders and move toward redefining how we think about value creation. In the next section, we discuss the mutuality and jointness of value-creating stakeholder relationships in more detail.

Stakeholder Value Creation

Stakeholder value creation is seen as the ability of an organisation to create enduring relationships with its stakeholders (see Dyer & Singh, 1998; Freeman, Wicks & Parmar, 2004; Goyder, 1999; Hillman & Keim, 2001;

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Wheeler & Davies, 2004). There are many ways to examine how value is created in interactions between organisation and its stakeholders and even among stakeholders themselves. Scholars have recognised that value is a complex concept with different dimensions. Mele and Colurcio (2006) identified five value dimensions: customer value, human resource value, shareholder value, firm value, and societal value. Lerro (2011) presented four stakeholder value dimensions: economic value, socio-cultural value, environmental value, and knowledge value. Harrison and Wicks (2013), in turn, identified four stakeholder utility factors representing the different kinds of value sought by stakeholders: stakeholder utility associated with actual goods and services, stakeholder utility associated with organisational justice, stakeholder utility from affiliation, and stakeholder utility associated with perceived opportunity costs. More recently, Garriga (2014) argued that instead of stakeholder utility, understanding stakeholder capability is sufficient to understand value creation in stakeholder relationships. She identified the following stakeholder capabilities as significant to value creation: being employable, being autonomous, being innovative, being entrepreneurial, being responsive, being socially integrated, being emphatic, being "green", and being healthy (Garriga, 2014).

The Stakeholder Value Creation (SVC) model focuses on the stakeholder relationship. It seeks to understand how value is defined in organisational relationships. It argues that instead of seeking to define what is valuable for whom, leadership should seek to understand value-creating stakeholder relationships and their characteristics. It is crucial, on the one hand, to recognise that different stakeholders have different expectations toward the firm, and on the other, to understand the importance of bringing stakeholder interests together over time (Freeman et al., 2006). There is a distinction between what counts as value for a single organisation and what counts as valuable in general (Donaldson & Walsh, 2015). An organisation will likely never be aware of all stakeholder interests

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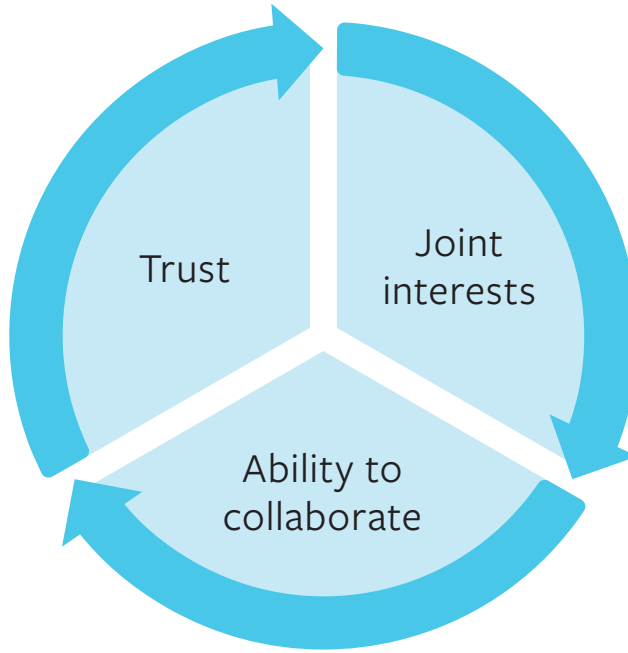
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FIGURE 2. Stakeholder value creation (SVC) model

nor be able to fully manage the social processes leading to value creation. The SVC model therefore highlights three attributes of value in creating stakeholder relationships: (1) joint interests, (2) ability to collaborate and (3) trust. These attributes are synthesised in Figure 2.

Joint interests create the basis for collaboration, interaction and development of a relationship. Joint interests build on shared objectives, aligned strategic goals and a sense of understanding between the organisation and its stakeholders. Joint interests between the focal organisation and stakeholders can be strengthened if strategic goals account not only for short-term economic outcomes but also for the long-term goals of stakeholder wellbeing and societal benefits. For Freeman (2010), the jointness of stakeholder interests is central to stakeholder theory. Common history, shared experiences and mutual objectives support joint interests in the relationship and quality of stakeholder interaction

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and also develop stakeholder dialogue (Harrison et al., 2010; Myllykangas et al., 2010). Dentoni, Bitzer and Pascucci (2016) argue that the capability to understand needs and demands and to recognise conflicting views among multiple stakeholders is an important part of joint interests. While sharing objectives is important in creating joint interests in a relationship, different stakeholders can have differing goals and still be willing to work together. Joint interests mean that the goals of different parties do not need to be the same. Instead, parties see value in collaboration and are willing to invest in it. For example, in a situation of organisational renewal, employee objectives may be to save jobs while management concentrates on the strategic outcome of improved efficiency. What is important in such a situation is that both groups are willing to work together to find solutions supporting organisational renewal which create value for all parties.

The ability to collaborate is the basic attribute of all relationships. The ability to collaborate is based on a mutual understanding of the importance of interaction and information sharing. Active participation and openness between the organisation and stakeholders are important aspects of the ability to collaborate. A strategic change can mean implementing new ways of thinking about collaboration, adopting new roles between the organisation and its stakeholders, developing new competencies, and learning new things (Myllykangas et al., 2010). The ability to collaborate means that both the organisation and its stakeholders see the opportunity to advance their own interests while also pursuing joint interests. Garriga (2014) showed that being responsive, being socially integrated, and being empathetic are relevant to the ability to collaborate. The capabilities to interact, learn and change are essential in stakeholder collaboration (Dentoni et al., 2016). Information sharing and learning transform relationships from transactional to collaborative (Svendsen, 1998; Myllykangas et al., 2010). The ability to collaborate also means commitment to interactions that construct solid relationships and make the co-creation of value possible (Myllykangas et al., 2010).

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Commitment manifests itself in stakeholder loyalty, the stability of stakeholder relations and the development of stakeholder networks. Commitment strengthens the relationships as it allows for attaining both separate and shared targets and appreciating different stakeholder interests (Cai & Wheale, 2004). Forerunners of stakeholder value creation are ready to invest in stakeholder collaboration and are able to create processes that support continuous stakeholder dialogue (Freeman et al., 2007). In committed stakeholder interaction, meetings, gatherings and negotiations are frequent and collaboration is intense (Myllykangas et al., 2010). In time, relationships become tighter and stronger. Commitment often increases in the collaborative process.

Trust is both an element of the relationship and an outcome of a successful interaction and collaboration. Commitment and fairness along with information sharing and learning build trust in a relationship (Cai & Wheale, 2004; Myllykangas et.al. 2010). Trust is the oil in the wheels of stakeholder relationships. Trust builds resilience and reduces strain on relationships in situations of change (Kujala et al., 2017). Trust is important in strategic change. Leaders who develop trust in stakeholder relationships will improve organisational performance (Wicks, Berman & Jones, 1999). The higher the trust between the organisation and its stakeholders, the easier it is for all parties to engage in joint value creation. Stakeholders who trust an organisation are willing to share information because they know it will not be used against their interests (Harrison et al., 2010). The SVC model brings trust, joint interest and the ability to collaborate together. It is therefore useful in examining stakeholder value creation.

Discussion

Over the years, stakeholder theory has developed into a promising approach which views organisational and stakeholder interactions from the standpoint of joint instead of conflicting interests. In this chapter, we have presented two models: the salience model, which focuses on stakeholders, and the SVC model, which views stakeholder relationships as central to stakeholder value creation. With these two models, we show that attention to both the

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attributes of stakeholders and the attributes of stakeholder relationships are needed when seeking to understand value creation in organisations.

The strength of the salience model is that it provides insight into identifying key stakeholders and the strategic impact of their interests; i.e., who and what counts. However, the salience model does not capture the co-operational nature of stakeholder relationships, where value is pursued together (Myllykangas et al., 2010). What is problematic is that the salience model treats stakeholder relations as transactional. It emphasises responding to short term problems instead of seeking to foster long-term stakeholder collaboration. As such, the responsiveness approach reproduces the neo-classical view centred on maximising economic value instead of generating collective value (cf. Bosse et al., 2009; Donaldson & Walsh, 2015). The responsiveness approach is one sided, as it sees stakeholder relationships predominantly from the focal organisation's point of view (cf. Davila & Molina, 2017). In order to foster dynamic stakeholder collaboration, stakeholder theorising needs to pay attention to both stakeholders and relationships. Recent literature has made a strong argument that stakeholder relationships are reciprocal (Bosse et al., 2009) and evolve over time (Davila & Molina, 2017).

Stakeholder interests need not be zero-sum games. The SVC model promotes the idea of stakeholder relationships consisting of joint interests and the ability to collaborate and trust. It directs attention to the ways by which value is created with and for stakeholders. Relationships of value creation are not considered to be built on inconsistency, rivalry and conflict. Rather, they are built on a search for mutual joint interest and collaboration. Instead of narrowing the relationship between an organisation and its stakeholders as a simple transaction-based exchange between parties focusing on economic returns, the SVC model provides an appropriate lens through which to consider the value stakeholders seek.

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