

“Decomposing the Value of Corporate Culture”

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Motivation: Culture Matters

- Culture matters for firm performance and economic growth.
 - Intuitively, firms that are high performing, growing revenue, etc..., also have effective cultures.
 - Culture contributes to intangible capital, which drives economic growth (Haskel and Westlake, 2018)
- COVID-19 and other catalyst events have helped to expose different types of culture.
 - But what comes next? Advocates want to renegotiate and improve the social contract between employees and employers.
 - A prerequisite to improving culture is knowing where it stands and which methods for improving work.

Corporate Culture as an ESG Signal

- Corporate culture reflects aspects of ESG such as human capital, innovation, and customer-orientation.
 - Yet because culture tends to be more qualitative than quantitative, screening investments on culture has been held back until recently.
- A combination of alternative data, machine learning, and natural language processing techniques means culture can be quantified.
- Yet like other aspects of ESG measurement, the race to develop new measures means some show little connection to true concept.

Standard ESG Metrics Show Low Correlation

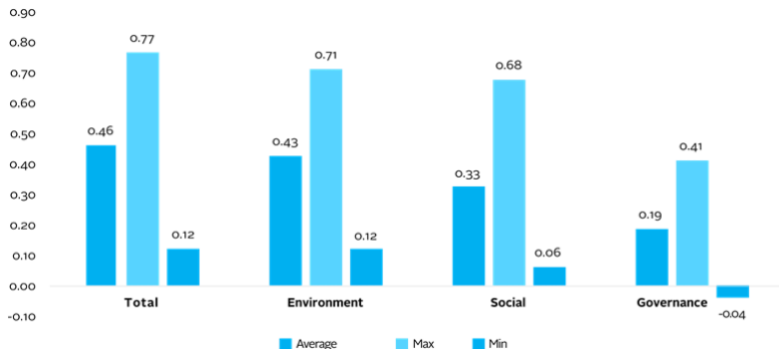


Figure 1: Average, minimum, and maximum correlations across providers

- Survey of 300 institutional investors shows ESG data confusion slows adoption of such strategies.
- Hundreds of organizations produce ESG ratings, which often disagree, even across top providers (Berg et al., 2019).

Woke Washing Is Only Going to Make It Harder

woke washing

term

#wokewashing is when a corporation, institution or individual says or does something that signals their advocacy for a social cause but also continues to cause harm to vulnerable communities. In this way, profit-driven companies prey on people's social awareness by cashing in on their idealism via progressive-oriented, purpose-driven marketing campaigns while deflecting questions about their own ethics or taking accountability for their own wrongdoings.

Source: The Guardian, [wokewashing.com](https://www.theguardian.com/uk-news/2019/sep/12/woke-washing)

**Slow Factory
Foundation**

What is culture? Where can we see it?

BANKING CONDUCT and CULTURE

*A Call for Sustained and
Comprehensive Reform*

“The events that precipitated the global financial crisis and the subsequent issues that have emerged have revealed a multitude of cultural failures.” –Group of Thirty (July 2015)

Culture Also Linked to Everyday Risks

Culture influences actions that are hard to contract on (ethics, creativity, or productivity). 85% of executives believe an ineffective culture increases the chances that an employee might act unethically or even illegally (Graham et al., 2019).

The State of America's Workplace Culture

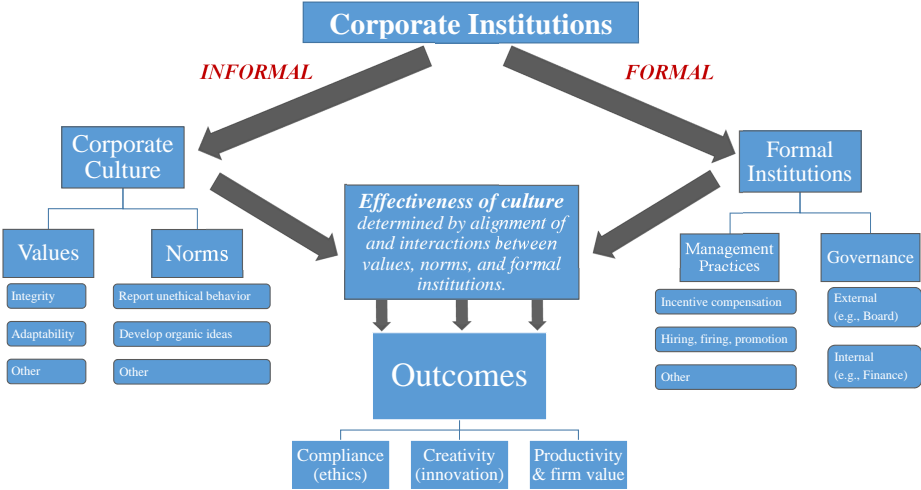
Increased Retaliation

This finding has doubled since 2013, from 22 percent to 44 percent of respondents who reported misconduct having experienced retaliation.

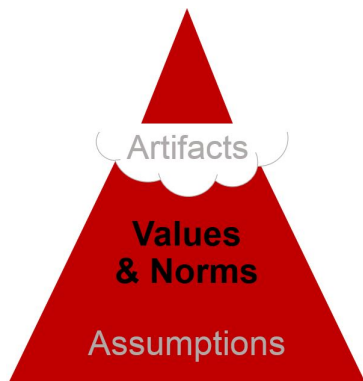
Pressure to Compromise Values

This figure has increased substantially in the last decade—from 10 percent to 16 percent of respondents feeling pressure to compromise their values.

Culture as an Informal Institution



Consistent with Schein's (1980) Culture Layers



- Why? Because values and norms are highly relevant for business outcomes; well-articulated unlike assumptions; and unambiguous unlike artifacts.

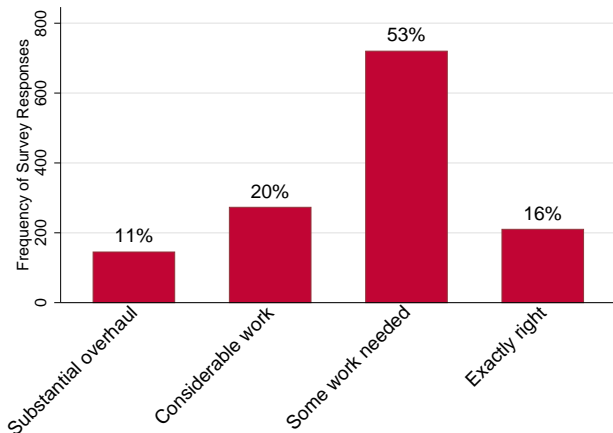
But Employees Disregard Cultural Values in Action



Judge's response: Words such as “honesty,” “integrity,” and “fair dealing” apparently do not mean what they say; they do not set standards; they are mere shibboleths. If Goldman’s claim of “honesty” and “integrity” are simple puffery, finance may be in more trouble.

Phenomenon Common Across Industries

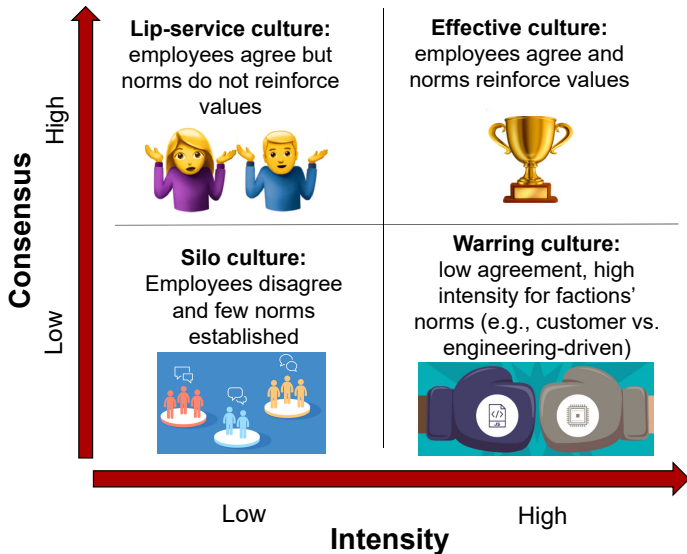
Survey of 1,348 executives: 84% thought their firm's culture is not exactly where it should be. Yet 52% indicate their firm's culture very closely tracks with their stated cultural values.



- 1. If there are aspects of culture that matter in addition to stated values, how best can this be measured?**
- 2. With measures of culture, can traditional valuation models be improved? can more effective ESG screens be put in place?**
 - Several theories argue for culture's prominent role in fixing contractual inefficiencies and reducing misconduct, but is it possible to show that it works out-of-sample.

Decomposing Corporate Culture

Using Consensus and Intensity to Categorize Culture



Approach to Quantifying New Measures

- Quantify cultural values and norms using text-based analyses.
 - Gather data from multiple informants: executives, employees, public relations, and equity analysts.
- Address the arguments that measures of culture need to reflect reality.
 1. Content – what are the cultural values? are they well-defined?
 2. Consensus – are cultural values and norms widely shared among employees?
 3. Intensity – is there willful blindness when day-to-day actions fail to live out the cultural values?
 4. Focus – what portion of cultural values are well-defined and intensely held?

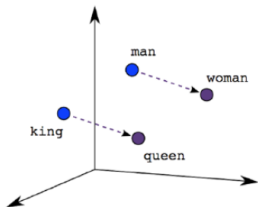
Use OCP to define values and norms

- 1 **Adaptability:** willing to experiment, innovative.
- 2 **Collaboration:** team-oriented, cooperative.
- 3 **Community-orientation:** respectful of community and diversity, inclusive.
- 4 **Customer-orientation:** listening and tailoring to customer needs.
- 5 **Detail-orientation:** analytical, precise, fact-checking.
- 6 **Integrity:** high ethical standards, honesty.
- 7 **Results-orientation:** high expectations, focus on goals, urgency.
- 8 **Risk-orientation:** unchanging, standardized vs. flexible, tailored, holistic approach to risk management.

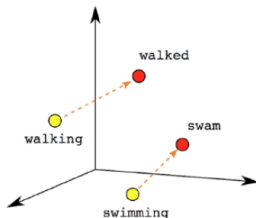
Gather texts for mapping from many informants

- **Employees:** analyze text of employee reviews from Glassdoor.
- **Executives:** analyze text of “Management Discussion & Analysis” sections of 10-Ks.
- **Equity Analysts:** analyze text of equity analyst reports and conference call transcripts.
- **Public Relations:** use wayback machine to evaluate cultural values espoused on websites over time.

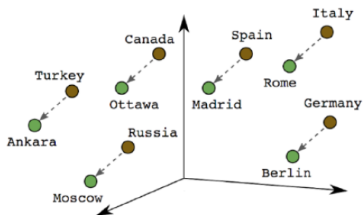
Create Mapping of Cognitive Synonyms via WordNet



Male-Female



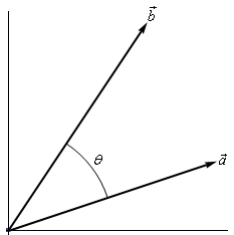
Verb Tense



Country-Capital

Use Synonyms to Map Into Culture

- Each measure is a cosine *similarity* between two vectors (e.g., employees text and collaboration synonyms text). This provides a mathematic interpretation as a correlation.
- High, positive values mean the firm displays more of that dimension of culture whereas low or negative values indicate less.



1. Content of culture

- **Content** identifies the extent to which stated cultural values are well-defined.
- To compute, I take the absolute value of the difference between executives' and employees' measure for each dimension. Then, I take the average across the eight dimensions. An aggregate value is 1 less the average difference.

	Adapt.	Collab.	Comm.	Cust.	Detail	Integ.	Results	Risk
Executives	0.0	-0.1	0.5	0.2	0.2	0.7	0.7	0.5
Employees	0.6	-0.2	0.2	0.1	0.6	0.6	0.3	0.3
Abs. Value of Difference	0.6	0.1	0.3	0.1	0.4	0.1	0.4	0.2
Average Difference	0.3							
Content	0.7	Values close to 1 indicate cultural content is well-defined.						

2. Consensus about culture

- **Consensus** identifies the extent to which there is agreement among the employees about the shared cultural dimensions.
- To compute, the text from employee reviews are not aggregated to an annual level. Instead, each entry is used. To simplify the space, reviews are split into 9 elements (8 fundamental values and other). Then, I calculate a *similarity* for each simplified vector against each other in a given year. Then, I take the average across all unique pairs.

	Emp. Rev. 1	Emp. Rev. 2	Emp. Rev. 3	Emp. Rev. 4	Emp. Rev. 5
Emp. Rev. 1	NA				
Emp. Rev. 2	0.20	NA			
Emp. Rev. 3	0.63	0.28	NA		
Emp. Rev. 4	0.87	0.23	0.20	NA	
Emp. Rev. 5	0.22	0.12	0.27	0.73	NA
Consensus	0.38	Values close to 1 indicate consensus about shared culture.			

3. Intensity for culture

- **Intensity** identifies how strongly held the cultural values and norms are.
 - Weakness is characterized by “willful blindness” that ignores day-to-day actions by employees that are not congruent with stated cultural values.
 - Strength is characterized by actions so powerful (e.g., sanctioning others for non-compliance and rewarding others for compliance) that even those external to the firm perceive the cultural coherence of day-to-day actions.
- To compute, the text from outsiders (i.e., equity analysts who have access to management) are evaluated for each dimension.

4. Focus of culture

- **Focus** identifies the amount of concentration across the cultural dimensions.
- To compute, convert content and intensity into indicator variables and construct a concentration measure that normalizes by the sum of the indicator variables.

Example #1	Adapt.	Collab.	Comm.	Cust.	Detail	Integ.	Results	Risk
Content	1	1	1	1	0	0	0	0
Intensity	1	1	0	0	0	0	0	0
Focus	0.28							

Example #2	Adapt.	Collab.	Comm.	Cust.	Detail	Integ.	Results	Risk
Content	1	1	0	0	0	0	0	0
Intensity	1	1	0	0	0	0	0	0
Focus	0.50	Values closer to 1 indicate more focus among cultural dimensions.						

Example #1: Governance-Culture-Value Link

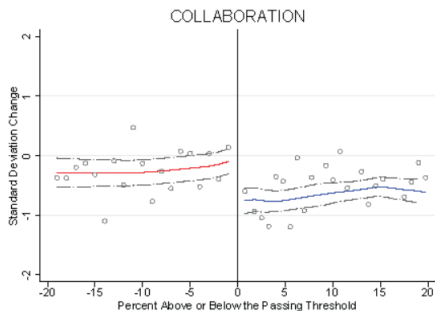
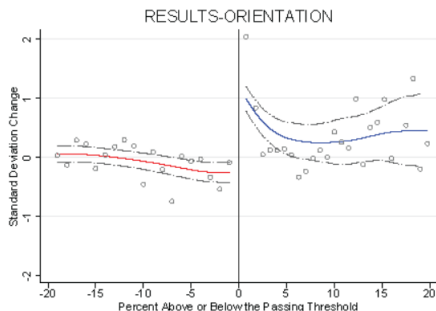
Does Governance Affect Value, and If So, How?

Is corporate culture a significant transmission mechanisms for the governance-value link?



Governance Changes the Content of Culture

- Compare firms just above to those just below passing threshold on close-call shareholder vote to analyze what would-have happened. Results-orientation increases, but collaboration, integrity, and customer-orientation decrease.



Intuition for Firm Value Comes from “Multitasking” Easy-to-Observe vs. Hard-to-Measure

“

There would be days where we would open 5 checking accounts for friends and family just to go home early.”

— Anthony Try,
former Wells Fargo employee



Overall Decline in Value through Culture Channel

- Short-term – significant increases in sales growth, profitability, and payout from stronger governance.
- Long-term – significant declines in intangible assets, goodwill, customer satisfaction, and brand value.
- The gains in easy-to-observe metrics erode and the losses from the harder-to-value intangibles dominate after a year.
- Aggregate decline of about 1.4% per year.

Example #2: Detecting Ineffective Cultures

Can Pinterests Be Detected?

- One of Pinterest's cultural values is “care with candor.”
- Former-COO reveals the opposite: Employees were not encouraged to share their ideas directly or respectfully; instead, transparency was met with backstabbing and retaliation.

**Put an end to all forms of
discrimination and
retaliation at Pinterest**



Campaign created by
Change at Pinterest



Lipservice Culture, Risk, and Persistent Policies

- Firms where there is low intensity about the values even though they are well-defined and agreed to is a lip service culture.
- Examine if a relationship exists between corporate policies and lip service culture (and other non-effective cultures).
- Use the multi-dimensional measures of culture to show that more effective culture is associated with lower volatility and better performance.
- The lower risk levels stem from adopting more persistent and less risky financial policies. Yet also, more efficient real risk-taking in terms of investment in innovation and intangibles.

Example #3: Culture and Unexpected Events

Communicating Culture Consistently

- Using historic versions of websites via WayBack Machine identified whether culture was communicated consistently across stakeholders (e.g., employees, investors, and customers).
- In theory, when something unexpected happens, employees rely on cultural values to guide them.
- Inconsistent cultural communication associated with lack of consensus about cultural values among employees.

Banks During the Financial Crisis

- Use the measure of inconsistent communication to examine both the cross-section of bank performance and within-bank variation.
- Convey the same message: inconsistent cultural communication is associated with significantly worse financial performance in terms of ROE. These results hold after controlling for various bank characteristics and time fixed effects.
- Examine private MBS vs. traditional loans and find strong support for culture mattering in moments of unforeseen events.

Future Research

- More simple screens
 - Less-is-more strategy – are firms that focus on few but well-defined values have a different risk profile than those that claim to do everything.
- More work linking standard ESG screens to real cultural outcomes
 - What is the correlate between diverse boards and effective community-orientation?
 - Does consensus around certain cultural values mean a firm is a better match for diverse board candidates or for beneficial intervention by activist hedge funds?

Conclusion

- **Novel measures** – combine many datasets to decompose measurement of culture into its psychological roots.
 1. Content – what are the cultural values? are they well-defined?
 2. Consensus – are cultural values and norms widely shared among employees?
 3. Intensity – is there willful blindness when day-to-day actions fail to live out the cultural values?
 4. Focus – what portion of cultural values are well-defined and intensely held?
- Show how these measures can be used to better understand corporate policies and valuations.