

Management and Morality – An Overview

Gustav von Hertzen

Summary

Depression and financial crashes are a plague of the market economy and always elicit calls for tighter control. Laws and regulations are indeed important especially in the financial sector. The rules define punishable actions, but they should also discourage irresponsible business decisions that are at the root of economic depressions. Basically the aim should be to set the scene for an equitable and fruitful plus-sum game. In the ideal case the profitability of a company should be proportional to its contribution to the common weal.

Yet no amount of laws and regulations, however astute, can approach this goal without access to sufficient moral capital among the principal agents. If the rules are right, the individual and public interest will converge. Our limited funds of morality can then keep short-sighted self-interest at bay, providing prosperity as well as stability. But we still have a lot to learn in minimizing the lure of foul play; free-riders and

wanglers of any hue must not prosper at the expense of honest players.

In any case, the basic moral imperative is to play a plus-sum game, to create value together within and without the enterprise. Honesty and openness are the critical values which support the trustful relations, essential for good cooperation. The accumulated moral capital is the prime asset of any organization, commercial or otherwise. It pertains to every aspect of management. The implications for public behaviour, organizational structure, strategy and leadership will be broadly explicated.

A candid plus-sum strategy cannot be pursued in a foul moral environment. It would work like a dream in the ideal case where the rules of the game are perfectly attuned to the public interest. But I maintain that our present democracies are close enough to the ideal for good morals to pay off handsomely.

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The moral aspect emerges at every juncture of managerial life

Introduction

It is generally assumed that management and morality do not mix well. In my opinion this is an unfortunate misapprehension. The moral aspect emerges at every juncture of managerial life. The following overview is based on personal experience, discussions with other executives and a sample of the relevant literature. For exemplification, I will mainly use Baltic Beverage Holding (BBH), a spectacular success story which is yet to find its way into the business case literature.^{1,2}

BBH was established in 1991 as a partnership between Hartwall and Pripps, the leading breweries in Finland and Sweden respectively. Starting up in Estonia, BBH rapidly established a dominant market position in the brewing industry in the countries of the former Soviet Union. By acquisitions, the half part of BBH was successively transferred from Pripps to Orkla of Norway and Carlsberg of Denmark. In 2002 Hartwall entered a merger with Scottish & Newcastle. As chairman of Hartwall, alternating chairman and vice-chairman of BBH and chairman of Baltika, the biggest brewery in the group (and in Europe), I could over the years follow the development of the company at close range.

Before going ahead, I want to declare my debt to several authors who have strengthened my conviction that morality is what matters most in business. I will only mention Peter Drucker and Jim Collins without trying to document their manifold contributions.

The moral capital

Morality is often perceived as a superficial element in management, an add-on which covers the hard core of real managerial competence. In this "realistic" view, the lack of morality is a sign of strength and affecting a moral stance is hypocrisy, plain and simple. This attitude is slowly receding and nowadays professorships in business ethics abound at the leading academic institutions. The mainstream view is that morality, after all, may have something to do with good management. Whether this is based on enlightened self-interest is a moot question. Anyhow I maintain that morals are not merely helpful but at the core of successful management in the modern world. Yet business morality must be rightly understood.

Let me first state what business morality is not. It is not:

- Giving money to charities or other good causes
- Appeasing stakeholders
- Bowing to national interest or political pressure
- Caving in to pressure groups (gender, racial, environment etc.)
- Pandering to political correctness

Those activities may make good business sense and polish the image of the company but they can indeed be deemed hypocritical window-dressing. In the worst case they amount to a kind of corruption by making unwarranted side payments to selected stakeholders who resort to extortion, political or otherwise.

This scepticism does not mean that basic humanity should be abrogated. Nobody, not even top managers, should be called upon to go against his or her conscience. To draw the line between human concerns and fiduciary responsibility can be an agonizing moral dilemma. The rationale for the core of business morality stems, however, from other sources. The categorical imperative is to play a plus-sum game, to manage the creation of value. This has profound implications.

Well-known zero-sum games, like poker, do not create value; the amount of money around the table is only changing hands but does not grow. In a zero-sum game, the main competitive weapon is deception or, at the very least, withholding information – ergo the proverbial poker face. In contrast, the decisive success factors for plus-sum play are honesty and openness, which creates and maintains the requisite trust between the parties. Thus the insidious temptation of the Prisoners Dilemma can be overcome. Business life has undeniable and unavoidable zero-sum aspects but it is, or at least it should be, mainly a plus-sum game, producing value for customers, employees, shareholders and the taxman. Consequently integrity and dependability become key elements of success.

Morality is the crucial minimum success factor in any organization. Everything else – capital,

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know-how, adequately trained people, even good managers – can be acquired but the morale must be certified by top executives, though it is free of charge. In short, the moral capital is the core resource of a viable business enterprise. The importance of this production factor in private enterprise has been understood for a long time, at least implicitly. Enlightened leaders in big companies have tried to enhance the return on the scarce moral capital by introducing decentralized organizational structures such as divisionalization, project management and outsourcing. Matrix organisations, on the other hand, call for an increase in moral capital and are an uphill battle.

The amoral marketplace

Before proceeding, let us have a look at the business environment. In a market economy, enterprises are participating in a web of value-creating games. Every market transaction by definition creates value. The goods or services rendered must be more valuable to the buyer than to the seller, otherwise there would be no deal. Added value is the driving force of commerce which thus constitutes a vast plus-sum game. But the division of the spoils is a zero-sum game which can give rise to time-consuming haggling, wasting part of the accrued added value.

A free and open market with many buyers and sellers is the appropriate remedy. It reduces but rarely eliminates the zero-sum component of trading. The marketplace is basically amoral. Every player has to watch out for himself and catch where he can. Competition is, or should be, the incorruptible referee of the market, and the formal morality of managers is limited to following the approved rules of the game. The market discipline is an efficient stand-in for the frail morality of man, but its effectiveness depends on the official and unofficial system of rules. Ideally the norms should promote long-term, fruitful plus-sum play.

This important problem falls outside the scope of the present study. Suffice to say that the aim should be that the profitability of a company should be proportional to its contribution to the public weal. In any case, the individual

company has to accept the existing laws and regulations as a given, their unavoidable imperfections notwithstanding. A new entrant can, however, strive to improve the existing rules of the market game.

In BBH we acquired existing breweries, guided by our consultants in SIAR³ which had established itself in the area prior to our appearance on the scene. The reconstruction of the plants and company structures was briskly implemented by dedicated project teams from the mother companies. Our policy was to be good corporate citizens and avoid involvement with shady organizations or practices. I cannot guarantee the absence of bribing but nothing has surfaced; internally one major fraud was detected whereupon the managing director was dismissed.

Bribing apart, collusion between competitors strikes at the very heart of a market economy. The temptation is always there and the legal sanctions have, for good reasons, become increasingly severe, although the target of perfect competition will never be reached. In mature markets, severe competition induces takeovers and mergers and we end up with oligopolies instead of the former cartels. This restricts competition but can still be the best possible plus-sum game.

Imperfect competition is the rule rather than the exception. Natural monopolies require extensive regulation and the abuse of dominant market positions must be restrained by public surveillance. The open market, too, is far from perfect. The market is always in the wrong but is incessantly correcting itself.

Managers in the public arena

For many reasons, good and bad, companies are often induced to engage in non-commercial activities. This presents distinct moral challenges. Public relations, for instance, is perceived as an exercise in clever media spin. Outright lying is of course unethical and usually counterproductive. Moreover, in a crisis honesty has been empirically proven to be the best policy. Dissimulation and procrastination only worsens the situation. Nothing is more devastating than the truth, dug up by eager journalists, one piece at a time.

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When Coca Cola met with quality problems in Belgium in 1999, the inclination of the top management was to play down the incident, but it soon engulfed the company. All Belgian production had to be stopped and the products recalled. The giant factory in Dunkirk was closed and products had to be recalled in France, too. Coca Cola systematically tried to escape the blame and was repeatedly overrun by events. The scandal contributed to the dismissal of Douglas Ivester, chief executive since 1997; Warren Buffett, a major stockholder and member of the board, called him "tone deaf". Arrogance is a bad adviser particularly in dealing with customers and the mass media. Humility is the best approach but ever so hard to employ.

Lobbying is an advanced form of PR focused on important politicians and public servants. The moral duty if not the prime objective should be to improve the rules of the superordinate political game. But the practice of politics is largely an adversary zero-sum game, a fight for a fixed amount of power, positions and budget money. Personal relations are often decisive and you have to find suitable allies. The important question is not what is right but who will gain and who will lose. Furthermore, public bureaucracies are usually permeated by procedural concerns and risk aversion, if nothing worse. The natural inclination is to postpone decisions, ask for additional information and clarification, concentrate on nitpicking – it cannot be a breach of duty.

Dealing with the authorities in the former Soviet Union countries is particularly challenging and in BBH it was left to the natives; foreigners made an appearance only at the behest of the local managers or consultants. The top executives in the acquired companies had excellent political connections – a definite asset in dealing with the local bureaucrats. In the rare dismissal cases, we took care to keep the former executives in the circuit by offering honorary positions and decent retirement terms.

Power without transparency creates a moral hazard. State and local bureaucracies are always open to the temptations of corruption. As a countermeasure, the division of responsibility and tasks are laid down to the letter, procedures are prescribed in minute detail and everything has to be documented, registered and filed away. In the favourable case, the proliferation of reports, directives, audits and policies can achieve bureaucratic probity which

is sufficient for public bodies. They cannot and do not need to be efficient or flexible. The absence of corruption and arbitrary decisions is, after all, the main point of such organizations. But an enterprise has to achieve a maximum of sustainable productivity and profitability. This is the challenge of business management which shall be our main concern henceforth.

The perils of growth

Companies are vehicles of strictly planned economy navigating the perilous seas of the market economy. They extract efficiencies from a seamless internal plus-sum game, reducing uncertainty and eschewing the costs and delays of market transactions. Size is a decisive advantage, if routines can be standardized and the success formula is duplicated in a huge uniform market. Spectacular growth can then be achieved by military style authoritarian management, model Wal-Mart. In such circumstances bureaucratic supervision and performance pay can to a large extent stand in for morality. But when flexibility and creativity are at a premium, tight control becomes counterproductive and the moral capital comes into its own.

Very small organisations have few internal problems. They are essentially one-man shows, and the chief is wholly dependant on his own business acumen. When the company expands, responsibility and power should be delegated and the internal plus-sum game must be supported by honesty and openness. Thus the demand for moral capital grows with the size of the organization. This basic relationship holds for all human organizations and communities but its strength depends on the challenges. Managing complex problems in a turbulent environment requires voluntary morality. Creative team work cannot be tightly administered, it can only be permitted.

When the company expands, the lines of communication are extended and bureaucratic control must be strengthened. Flexibility is diminished while motivation and innovation suffer. Staffs are mushrooming and responsibilities obscured while internal power games distort decision making. A morally responsi-

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ble manager will try to improve the rules of the game and nudge human effort into more constructive channels but the odds are stacked against the well-meaning reformer. I have examined this problem in a short treatise, *Cynics and Progress Motors*, originally published in 1974 in Swedish.⁴

In BBH we desisted from the early introduction of bureaucratic devices. Detailed budgets and profitability calculations were largely irrelevant in the turbulent environment of the fledgling BBH-companies. Their forced application would only have poisoned our relations with the local executives. Time and again these people demonstrated their business acumen by pushing for swift, bold but correct decisions, based on facts on the ground and the correct perception of business opportunities. Certainly some mistakes were made but they did not matter. Or rather they became ladders on a steep learning curve.

In general, we went against the conventional managerial wisdom. A key issue was the reliance on domestic brands, vigorously supported by the locals. To relinquish our own trade marks was not an easy decision. In the end, we did not fall for the old Soviet-style management maxim "I am boss, you are stupid" which has its adherents in the West, too.

In a politicized arena you have to run with the pack or lose out, which provides ample room for scheming cynics and self-indulgent free-riders but makes life hard for self-motivated progress motors. Top management relies mainly on figures and often lacks a real understanding of the business issues. The precious moral capital is slowly evaporating while the headquarters turns into a scene for destructive political infighting. This syndrome is all too familiar to anyone with experience of large organisations.

The bureaucratic instinct is to control everything and to avoid mistakes at all cost. The dangers of excessive centralization should be obvious but the temptation seems to be well nigh irresistible. For egomaniac executives, personal ambition and thirst for power gets the better of fair play and good judgment. Hierarchy trumps factual insight, self-importance and vain conceit prevail. In successful companies, arrogance can engulf the whole organization with dire consequences.

Large, profitable companies are the preferred hunting ground for psychopathic managers, *Snakes in Suits* as they are named in the eponymous book by Babiak and Hare⁵. These cynics, as I call them, are utterly devoid of loyalty to friends, associates or the company. They are great manipulators, winding their way through the organizational structure with a minimum of effort. Verbally gifted they can be extremely convincing, nimbly shifting merit and blame to their advantage. They leave a trail of betrayal, parasitizing on the good will of their team mates. Corporate cancer spreads in their wake.

The consoling fact is that in a competitive market, bad morale and internal infighting will sooner rather than later cause the downfall of companies; the bigger they are, the harder they fall. At least at a second look, the debacle of most large companies is related to a major moral deficit at the executive level. Unfortunately, the feedback is much slower for public bodies which can survive for decades or even centuries despite the moral decay.

Quick fixes

As in cancer, a prompt diagnosis improves the odds for curing the disease. The flamboyant lifestyle of top management can be an early warning signal. Bad personal conduct – drinking, divorces or extra-marital affairs – also correlate, albeit with some delay, with downturns in business fortunes. The same holds for an excessively high public profile. If a culpable top executive can relay on a good management team, the situation may still be in hand. But if the rot has become part of company culture the end is near.

Self-deception is the most insidious kind of dishonesty, breeding a false sense of security. Complacency at the top is often coupled to an indulgent managerial style and lack of innovation. It bodes ill for the company, as does the departure of good managers. High turnover of personnel is generally a sign of bad management. The way people speak about their company can also divulge bad morale.

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install a new managing director, often from the outside. He is in a better position to cut out the deadwood and the cynics, who at that point usually have revealed themselves and anyhow are looking for greener pastures. Most successful turnarounds are accompanied by a sweeping change at the top.

Even if the old management could change their ways, their credibility would be gone. People would refuse to follow the leaders who brought on the crises in the first hand by bad decisions or indecision. And personal probity is of no avail if a string of bad luck taints a top executive. We live in an unjust world.

Sustainable growth

Top management is pivotal, and moral stamina should weigh heavily in recruitment and promotions. Even so, the nomination of a top executive is always a gamble. The main challenge is to facilitate plus-sum play, but many successful managers are exceedingly self-assertive, exert meticulous control and leave little for their underlings to decide. They behave like executives of small companies and the attendant virtues – goal orientation, industry and perseverance – can carry them a long way by inducing fierce loyalty. But corporate growth will hit a ceiling, at the very latest when the top executive retires.

Whether the need to micromanage is rooted in some deep personal insecurity is another moot question. Worrying is part and parcel of managerial life but good management also calls for the courage to trust other people while carrying the responsibility for their mistakes. Without such risk-taking, you cannot attract or rear and keep capable leaders. Executive self-restraint calls for curtailment of the ego, which makes genuine teamwork possible. A symbiotic two-man team at the top can generate sufficient moral self-discipline and opens the way for spectacular growth.

The virtues of delegation and decentralization cannot be overstressed not least because relinquishing power voluntarily is a hard act to follow. No corporation can accept a personal empire within its bounds, but more often than

not tolerance produces a handsome payoff. Necessity can be the mother of good decisions.

In BBH we decided early on to give maximum responsibility to local managers while providing all possible support. At every major step we sought the advice of our consultants in SIAR. No expatriates were permanently placed in the daughter companies. When we considered a controller from abroad as a minimum precaution, the local consultant said: "Look these people have been cheating all their lives during the old regime. If they want to steal they will steal right under the nose of any foreign controller". We decided that trusting the locals was the only option. Their learning curve was very steep and they took great pride in their capability to run the business themselves. The spectacular success can mainly be attributed to these policies.

While BBH is an excellent example of the benefits of radical decentralization, another case shows that this is not an odd exception. During the Second World War, the US affiliate of Hoffman la Roche, a private pharmaceutical enterprise, was virtually cut off from its mother company in Switzerland. The forceful head of the American organisation took full control and in a few years catapulted Roche into the top rank of the industry. A humiliating experience for the Swiss bosses but they kept their cool.⁶

Sustainable growth cannot be achieved without delegation. Decentralization depends on trust but, most importantly, it fosters trust and enhances the funds of moral capital. In contrast, centralization weakens personal responsibility and initiative. Inexorably it drains the organization of crucial moral resources. Decisions should always be made at the lowest feasible level. Excessive decentralization is easily remedied while centralization is often irreversible.

Integrity at the top

Moral leadership is a key if not *the* key responsibility of top management. Integrity at the top provides a powerful example and creates the right atmosphere for a fruitful plus-sum game. Honest leaders attract honest people, fostering adherence to company values at all levels. Control, supervision and reporting can be slimmed down to the minimum. Hierarchical shackles are eliminated and self-organization is encour-

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aged, ensuring high flexibility and motivation. At best, the virtuous circle of decentralization produces the necessary conditions for its implementation.

Every creative plus-sum game carries a risk. A dispersal of responsibility can beget disorder, confusion and sundry inefficiencies. Cynics have ample room for their evil designs and free riders may just enjoy themselves. Lack of recognition might sap the self-motivation of the progress motors. Morality alone can not be relied upon to solve all problems. Old-fashioned discipline and organizational structure are still required. "Economize on love" says the Nobel laureate James Buchanan, meaning that the management of self-interest is still the mainstay of an organization.

In the early 1990s, the top executives in the BBH breweries had become substantial owners of their debilitated companies. This cemented their loyalty and motivation under foreign ownership when a brighter future was in sight. Managers and many employees, too, had become shareholders and everyone was happy to have a decent job. When rivalry between the daughter companies became a problem, the main actors were taken to the United States for a roundtrip to the Anheuser Busch breweries. The emulation of the American company was set down as an explicit strategic goal. It was essentially attained in 2006, when all Russian breweries were consolidated in Baltika and the market share approached 40 per cent.

Performance pay economizes on love, for sure, but is no substitute for morale. It can be a poison, particularly in a downturn, and must be handled with exquisite care. Morality is in any case an indispensable support, keeping our egocentricity in check and imparting sense, purpose and cohesion. The higher the morale the better; the moral capital correlates with efficiency, profitability and competitiveness.

The tremendous growth of many Japanese companies after the disasters of the Second World War is due to specific Japanese values. Confucian respect for authority is supported by unswerving samurai loyalty to the team and the company. The life-long employment policy of the major corporations reinforced these basic inclinations. The famed Toyota production system made a partial break with tradition by delegating substantial responsibility to subcontractors and down to the factory floor.

A lot can be done to facilitate the growth of moral capital. Relevant information should be easily accessible and actively dispersed – openness is after all a requisite condition for plus-sum play. An in-house management training program provides opportunity for top executives to indoctrinate the staff and meet managers in an informal setting. And, most importantly, personnel policies must be focused on promoting the real contributors to company success while weeding out pernicious cynics.

This is no mean task and the difficulties increase with company size. In general, the superior has the least knowledge of the true character and performance of an employee. The team-mates know much more but only the subordinates are truly informed. In small and middle-size companies, the grapevine provides much important information which gets lost in a big organization. One way or another, promotions (and demotions) as well as hiring and firing must come out right. They carry the true message of company values, overriding any amount of executive rhetoric or written policies.

Executive pay has caused much moral outcry and can be perceived as the ultimate moral challenge for management, but it is unequivocally the business of the company board. In any case, the interests of top management must be aligned to the long term prosperity of the company and its shareholders. This principal-agent problem is as old as the hills and must be resolved by the negotiating parties. Overpayment can be an affront to the public but to hire or to retain a second-rate executive is a much graver breach of good governance.

Strategic plus-sum play

Everyday operations are by necessity immersed in zero-sum play. For instance price and salary negotiations are essentially zero-sum games. Survival and short-term profitability dominate the goal-setting. But in the longer term, an obsession with the zero-sum perspective becomes destructive. The strategic aim of every company must be to minimize competi-

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tive pressure, securing a good return on capital. Strong brands, for example, are a common strategic goal, because they maintain a certain degree of uniqueness and avoid commoditization which implies strict comparability with competing products or services.

This overtly selfish aspect unexpectedly coincides with strategic plus-sum play. The governing principle should be that an enterprise must be different, representing a unique business idea within its market area. Otherwise it does not participate constructively in the division of labour and the plus-sum game of the market. Thus it will not provide any added value and cannot be successful in the long term.⁷ Learning from competitors is commendable but all-out copying is futile in the absence of a clear-cut cost advantage. The daily grind is dominated by zero-sum play but strategic competition requires a more creative approach in order to achieve sustainable profitability.

Evolutionary biology provides an illuminating analogy. If two or more species are confined to the same niche and pursue identical survival strategies, only one of them will survive. This causality is called Gause's Law⁸ after the Soviet biologist G.F. Gause (1910–1986) and applies equally to business economics. Diversity in nature and the economy spring from the same logic. Companies pursuing identical business strategies cannot coexist in the same market; only one of them can survive, barring artificial restrictions on competition. Cut-throat competition is the outcome of zero-sum based strategic thinking. Economic depressions can be traced back to similar shortcomings.

An innovative strategic approach always carries a certain risk but exaggerated risk-avoidance eventually buries a company for good. An enterprise must contribute by defining, developing and implementing a unique business idea with the potential to create added value for existing and presumptive customers. In marketing, morality is at least as important as in internal company relations. The trust of the customer can only be built over time but it can be lost in one, short moment. Contemporary corporations can be as particular about their reputation as medieval knights.

A favourable image is also an important asset in attracting gifted people to the company. Besides earning money and getting ahead, young men and women of the right calibre

want to participate constructively. For them, self-realization implies a measure of altruism. A most important task of top management is to make work meaningful for the troops. A genuine heart-felt company mission raises the game beyond trivial zero-sum play, and makes wonders for company morale. For good people, real satisfaction can be achieved only by playing a plus-sum game. And in business, good people is all.

Business networks

Networking represents the ultimate logic of plus-sum play. It has, of course, been around for ages; trade and industry has always depended on a network of more or less trustful connections. But customarily, business relations are contaminated by a sizable zero-sum component, which entails considerable costs and inefficiencies. Modern networking strategies aim at reducing this burden by cutting transaction costs all around. Additional long-term gains can be made by blurring the organisational barriers between the business partners and encouraging the open exchange of information.

Accordingly, formal and informal networking has become popular but a close collaboration must be preceded by the build-up of sufficient trust capital. This is best secured in a stepwise fashion. Subcontractors can for instance be brought deeper into production planning while customers are enticed to become partners in product development. Outsourcing of vital company functions, such as information processing, calls for a lot of trust but, given good morals on all sides, there are no limits to the scope of networking.

A joint venture is a very intimate relationship between two companies, albeit in a clearly circumscribed area. The partners assume joint responsibility for a well-defined project. Usually all important decisions require unanimity which opens the door for a stalemate or something worse. The joint venture approach utilizes the complementary strengths of the partners and diminishes the risks, but calls for substantial moral capital to maintain trustful relations between the partners. Otherwise the project will collapse.

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Over the years I have participated in a score of joint ventures besides BBH, most of them rather successful. In developing Xylitol together with Hoffman-la Roche we went through several difficult stretches which could be negotiated only in close cooperation with my counterpart at Roche. In the end, my company took over the project and finally brought it to fruition.

In BBH, differences in values, style and personalities produced a lot of argument and put considerable strain on the joint venture relationship. Early on I insisted on regular meetings between the boards of the partners, some of them at BBH locations, to forestall serious clashes. This was accomplished, but local management occasionally became bewildered and frustrated by conflicting messages, leaking through from the owners. In the final analysis, the sustained trust-building efforts of the Finnish side kept the venture afloat through thick and thin.

Basically, a joint venture is a contingent structure with a limited life span. Recently Carlsberg and Heineken made a successful bid for Scottish & Newcastle. The half part of BBH was the main prize. It was taken over by Carlsberg, who became the sole owner, and the joint venture era came to an end. The implied value of BBH was approximately 10 billion euros; in comparison the original investment was negligible.

In an open ended cooperative effort you cannot apply administrative power and you have to rely solely on good will and fair play. A man as good as his word then becomes an essential asset for the project, regardless of his position or localization in the collaborating organizations. Trust slowly begets trust while distrust spreads like wildfire. Among lower level managers the temptation to pull a fast one is hard to resist. The involvement of the top executives is therefore essential; without backing from the highest level, joint projects will founder.

In a broad perspective, business enterprises carry out vital tasks in a wider, politically coordinated network. The success of this overarching plus-sum game depends on the proper interaction of all key participants on the appropriate level – local, national or global as the case may be. Democratic societies sorely need moral capital to lubricate the wheels of this super-ordinate, self-organizing mechanism. The lack thereof causes destructive friction which seriously impedes our welfare and future prospects.

Conclusion and outlook

Like truth and love, moral capital belongs to a group of notions which cannot be closely circumscribed. These so called prospective concepts are linguistically indefinable but for that very reason they are all the more important. Honesty and openness, respect for the truth and for our fellow human beings are anyhow the basic values which maintain human plus-sum play and assure long term profitability in business. High intelligence, industry, frugality, fortitude and self-discipline are of course desirable qualities in a leader, but without personal integrity and a dose of humility they are worthless or may even serve self-destructive delusions.

Morality is the often overlooked ultimate source of sustainable success for an enterprise. But a caveat must be introduced. A candid plus-sum strategy cannot be pursued in a foul moral environment. As a young enterprising executive I was counselled by an Italian friend (from Milan): “Never do business south of Rome!” I suspect this is still good advice if you do not want to run with the pack.

Nevertheless, investment in a high-risk environment can bring spectacular rewards. When we in Hartwall went ahead with BBH in Russia, the decision stemmed from a sense of responsibility. The fall of communism was not only a major business opportunity. It was also a moral challenge to make a constructive move when Russia was heading for an economic, social and political breakdown. No calculations or business plans were made; fundamentally, we betted on the future of Russia. The happy outcome was a vindication of plus-sum oriented strategic thinking. Furthermore I believe that the positive externalities of the BBH activities are many times greater than the profits.

A business enterprise fulfils its moral obligations by making money, respecting the overt and covert rules of the game. This home truth has been repeated many times over but the intellectual underpinnings are wanting. Company culture and company values have been emphasized but the central position of moral capital has rarely been spelled out in so many words. The reduction of sustainable business success to a single factor – simple morality – is indeed a bold hypothesis. I hasten to add that it can hold strictly only in the ideal case where

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the rules of the game are perfectly tuned to the common weal. But I maintain that our present democracies are close enough to the ideal for good morals to pay off handsomely.

Primarily, my conviction concerning the supremacy of morality rests on deductive reasoning. The market economy is evidently a plus-sum game and elementary game theory tells us that honesty and openness are the necessary and sufficient success factors. This conclusion is supported by a lot of anecdotal evidence, but thorough empirical investigations are few and far between. There are good reasons for this lack of verification (or falsification). Moral capital is very hard to measure but empirical research in this area would be highly welcome.⁹ Otherwise we must resort to circular argumentation. Long-term success is the only dependable measure of morality!

What then can be done? Teaching morality is a futile exercise. Stamping out immorality might be more practicable. Competent psychiatrists can profile psychopathic personalities although they have been duped even by serially convicted jailbirds. If psychopathic managers could be exposed at an early stage, it would be a great boon. I have in passing touched upon a few other expedients which can be helpful in business organizations. While every company must look out for itself, our joint responsibility is to work for the improvement of the politically determined framework, the rules of the market game. This is part and parcel of the challenge of democracy, mapped out in a forthcoming book.¹⁰

Wealth is thus the fruit of morality, signified by postponement of material gratification. This bourgeois mindset has had many detractors but recently the virtues of money making have also received accolades.¹¹ The long-term preservation and expansion of wealth is above all a moral challenge. It has been an exacting problem for most families, companies, countries and even civilizations. Success leads to self-indulgence which degrades morality. The subsequent tribulations provide a chance to restore it but in the last instance we can only fall back on our remaining moral capital.

Our joint responsibility is to work for the improvement of the rules of the market game

Endnotes

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² BBH/Pripps: *Baltika: Det ryska ölet* in Martin Ådal and Oleg Anisimov *Att lyckas i Ryssland: Exempel från svenska framgångsföretag* Stiftelsen SIAR 2000.

³ The Scandinavian Institute for Administrative Research (SIAR 1965–97) pioneered the integration of research and management consulting. SIAR became the world leader of this methodology called Clinical Research.

⁴ Gustav von Herten *Cynics and Progress Motors: An approach to business morality* SIAR Dokumentation 1979, reprinted in 1991 by Fritzes. Swedish original *Organiserat entreprenörskap: Synpunkter på en företagarorganisation* SIAR Dokumentation 1974.

⁵ Paul Babiak and Richard D. Hare *Snakes in Suits: When Psychopaths Go to Work* ReganBooks 2006.

⁶ Personal communication.

⁷ SIAR developed the business idea concept in the early 1970s. See Richard Norman *Management for Growth* Wiley 1977; Christian Junnelius *Businessidea – The Cornerstone of Business Strategy* Tallinn Technical University Press 2000. See also Gustav von Herten *Att spela plussummespel* in R. Carlsson (ed) *Strategier för att tjäna pengar: Om affärsidén och andra SIAR-begrepp* page 238–267 Ekerlids förlag 2000.

⁸ G.F. Gause *The struggle for existence* 1934. New edition Dover publications 2003.

⁹ Behavioral game research offers an empirical method to measure the moral inclinations of people but it is hard to apply in test situations. See e.g. C.F. Camerer *Behavioral Game Theory: Experiments in Strategic Interaction* Princeton University Press 2003. For a recent contribution see Hermann et al. *Science* vol 319 7 March 2008, 1362–1367 *Antisocial Punishment Across Societies* and the commentary by Herbert Gintis *Punishment and Cooperation* on page 1345.

¹⁰ Gustav von Herten *The Challenge of Democracy*. The translation of the Swedish original *Demokratins utmaning* 2007 will be available from Amazon. In Finnish *Demokratian haaste* Gummerus 2007.

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Box 1 Creating value together

Basic statements

- The moral imperative is to play a plus-sum game
- The success factors of plus-sum play are honesty and openness.
- The moral capital is the most valuable resource of the company
- Growth is a moral challenge

The internal challenge

- The solidarity and trust within a group decreases with the size
- Accordingly, the demand for moral capital grows with the size and the complexity of the organization

The strategic response

- Resist the temptations of centralization
- Delegate responsibility to the lowest feasible level of the organization
- Look for the best return on the available moral capital

The external challenge

- If several organizations compete in the same niche with identical strategies, only one of them will survive (Gause's law)

The strategic response

- Play a plus-sum game
- Make a contribution, try to make a difference
- Create a unique business idea

Qualifications

- During the daily grind, zero-sum games are prevalent
- In zero-sum play, the success factors are with holding information or outright deception
- In a foul moral environment, the prospects are dim for long-term plus-sum play
- Plus-sum games are inherently risky. Zero-sum play is apparently safe but has no future.

Concluding remarks

- The basic principles extend to all kinds of communities
- Politically established rules of the game determine the openness of markets and the fairness of competition
- In the ideal case, when the rules are perfectly aligned to the common weal, honesty would reign supreme
- Most democracies are close enough to the ideal for good morals to pay off handsomely

Box 2 The BBH story – an outline

The business idea

- Investment in the brewing industry in the countries of the former Soviet Union
- The joint venture Baltic Beverage Holding
- Start in 1991 in Estonia

BBH highlights

- Maximum negative cash-flow 100 million EUR
- Present value around 10 billion EUR
- Dominant market share in Russia and the Baltic states
- Baltika brewery is biggest in Europe
- Baltika trade mark is number two in Europe
- About 15 000 employees

Strategy – acquisitions

- Loyalty between the joint-venture partners
- A sense of mission, good corporate citizenship
- Reliance on local consultants from SIAR
- Steering clear of the mafia
- Starting with 50 per cent ownership
- Top management retained with substantial shareholding
- Investment into reconstruction, not in paying off former owners

Strategy – operations

- Project teams from the parents to ascertain quick improvements
- Additional expansion mainly based on domestic cash flow
- Delegation of full operational responsibility to local executives
- No expatriates employed
- A minimum of reporting, control by results
- Total reliance on local brands
- Emphasis on personal relations and informal contacts

Strategic goal-setting

- Anheuser Busch in USA was set down as an explicit strategic goal



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