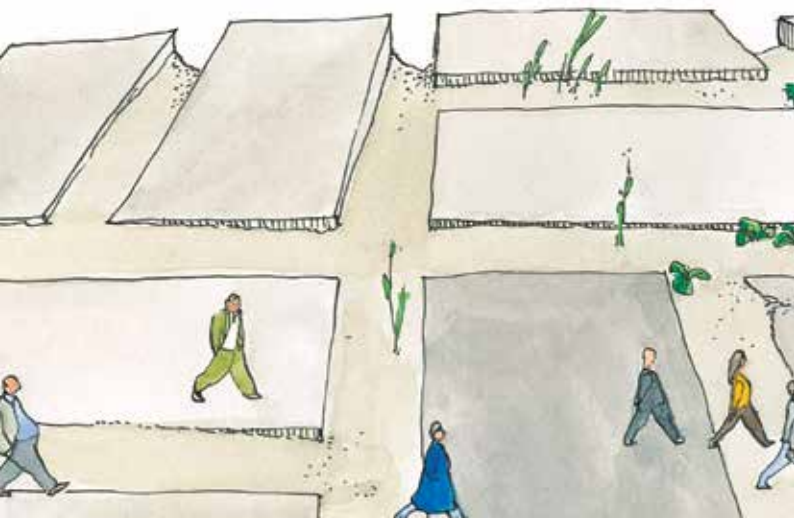


The European Enterprise Value creation for society

by Donald Kalff



*“Europes Liberal Democracies
deserve European Enterprises”*

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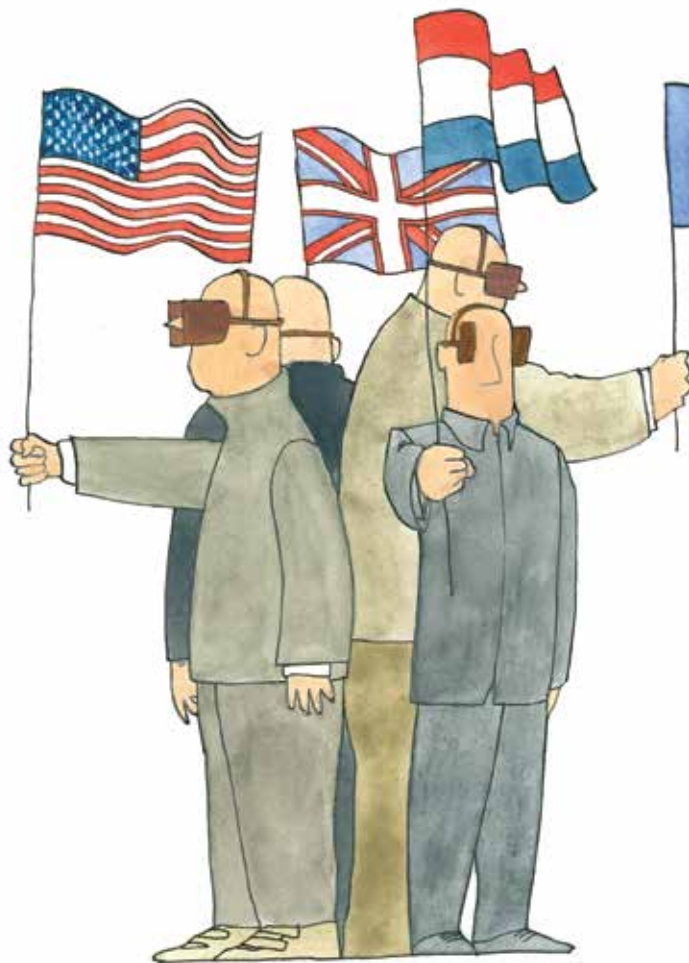
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I • Liberal Democracies under pressure

Liberal Democracies are challenged
whilst coping with legacy problems and
facing the need for structural change.



A world adrift

Geopolitical turmoil

Paralyzed political decision-making

Failing institutions and institution building

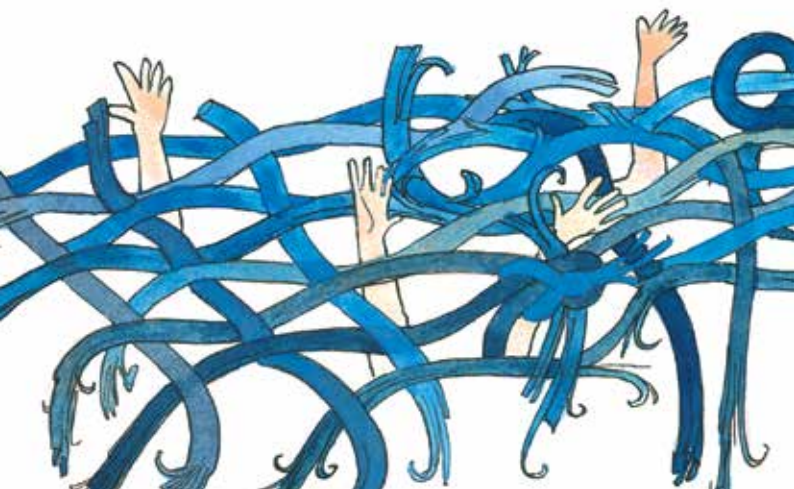
The demise of the middle class

Youth unemployment

Migration

The rise of inequality

... causing the rise of ethnic nationalism



The need for economic growth

To remedy global imbalances

To create a buffer to cope with new sources of instability

To finance investments in infrastructure, the environment and the energy transition

To create employment

To reduce inequality

...helping to restore the torn social fabric





Stimulation of economic growth is becoming ineffective

Central banks have reached the end of the road

Proposals for structural change are meeting increased resistance

Fiscal stimulus is constrained by high government debt

Declining world trade

Instruments to stimulate innovation lack effectiveness

... whilst the risks associated with these interventions are increasing



No apparent way forward

Economists profoundly disagree about remedies

The world's economic institutions repeat their mantras

Companies have withdrawn from the public debate

Politicians are at a loss

Citizens are confused and angry

... producing a harmful impasse



II • Exploring a different direction

An, up till now unexplored, explanation for the lack of growth is value destruction and insufficient value creation by large listed companies. Policies aiming to serve shareholders and stakeholders cause considerable macro-economic and social damage, both directly and indirectly. A turnaround will bring highly significant benefits.



Large enterprises fulfill an indispensable role

Providing economies of scale

Driving world trade

Contributing to R&D

Bringing innovations to market

Investing in large, high-risk projects

Selecting and developing talent

Providing employment, directly and, in particular, indirectly



Poor performance of large listed companies

Growth of investment lackluster

Return on investment shrinking

Export growth decreasing

Productivity growth sharply declining

Share of new products in total revenues stagnating

Scandals revealing structural shortcomings in governance and management

... whilst historically high margin and profit growth is not sustainable





Under extraordinarily favorable circumstances

ICT revolution served outsourcing, market access and marketing

Increased pricing power due to industry consolidation

A low and decreasing effective tax rate

Unprecedented low inflation and lowest cost of capital ever

Until recently, a de facto freezing of wages

Highly effective lobbying in defense of established (market) positions

Large incentives provided by competing cities, regions and countries



III • How value is destroyed and built

Value destruction and lack of value creation by large listed companies are not caused by adverse market conditions or geopolitical turmoil, but by a number of fundamental choices that shape corporate governance and management.



Flaws in the shareholder model

Serves financial markets, not the economy

Emphasis is on control and transfer of risk

Artificial investment hurdles

Harmful commercial doctrines

Suppression of innovation

Inadequate governance and management

Counterproductive organizational design and culture





Flaws in the stakeholder model

Serving special interests at the expense of the development of the enterprise

Steering clear of risk, avoiding and suppressing conflicts

Stakeholders exercise power without responsibility and accountability

Stakeholders defend established positions and depend on short-term successes

Stakeholders constrain innovation

Inadequate governance and management

Counterproductive organizational design and culture



The European Enterprise model

Operating license provided by society at large

Focus on economic profit, not on accounting profit

Creation of economic value by innovation, by investments and by productivity growth

Facing the future and embracing risk

Retaining control of the Enterprise by diversifying sources of capital

Engagement in partnerships to optimize value creation

Entrepreneurship built into governance and management to exploit all sources of economic value

The enterprise functions as a working community



Shareholder Model

Source of legitimacy	Shareholder
Worldview	Financial
Attitude to risk	Transfer and control
Modus operandi	Analytical
Overriding objective	Shareholder ROI
Steering variable	Profit per share
Principle source of finance	Stock market
Leadership	Individual
Culture	Competition among individuals
Management	By rule
Decision making	Procedure driven
Enforcement	Exercise of power
Control	Command and incentives

Stakeholder Model	European Model
Stakeholder	Society
Political	Economic
Steering clear	Facing uncertainty
Probing	Holistic
Eclectic	Creation of economic value
Multiple	Free cash flow
Banks	Diverse
Committee	Dispersed
Competition between units	Cooperation
By principle derived rules	By principle
'Horses for courses'	Quality driven
Building support	Corporate interest leading
Formal commitments	Professional standards

IV • Affecting Change

The tide is turning as a number of advanced European companies move away from the two established enterprise models, in the pursuit of enlightened self-interest and the interest of citizens, shareholders, employees, taxpayers and pensioners.

This provides a major opportunity for governments, institutions and the enterprises themselves to regain ground in the battle for legitimacy, demonstrating the resilience of liberal democracies.



Existing listed companies are difficult to turn around

Conspiracy without conspirators, appealing and shared world views held by those in power

Financial markets impose and preserve the shareholder model

Existing reporting requirements, bookkeeping conventions and personnel policies

Stock markets as conduits for imposing and preserving the shareholder model

Finely tuned and connected functions and systems

Resistance to change, even by disheartened employees

... yet, advanced enterprises, many of them nordic, show the way forward





What governments can do

Redirect fiscal and other facilities designed to boost profits to the stimulation of innovation, investment and productivity

Establish, and adhere to, long-term policies to provide frameworks for investment

Consolidate the myriad of equity funds and providers of subsidies

Stimulate R&D by providing and maintaining technical infrastructure

Stimulate innovation by prototype testing and by acting as launching customer

Control corporate lobbying geared to the defense of established positions

Help to prevent value-destroying takeovers

Reposition research and education in business administration





What institutions can do

Banks: evaluate clients and their plans on the basis of economic value added

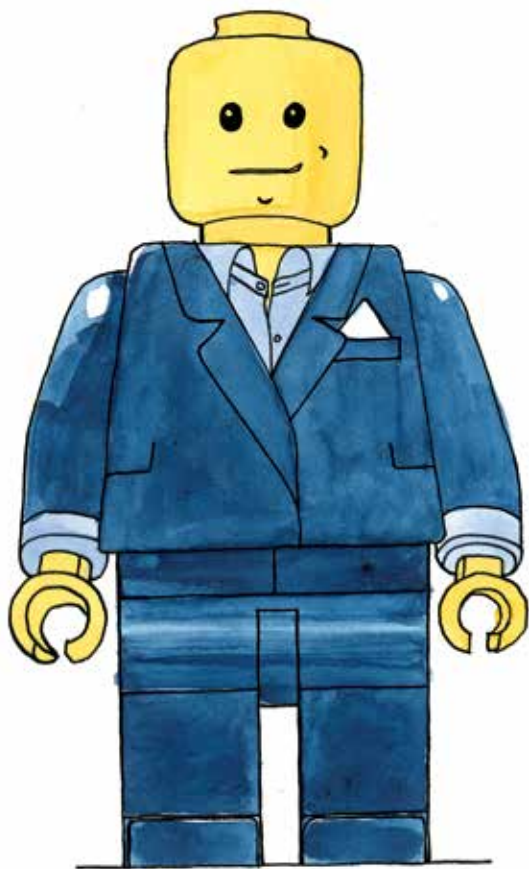
Investors: focus on present and future return on assets and productivity growth

Regulators: protect small enterprises, suppliers, partners and customers of large companies against abuse of power

Courts: protect the enterprise against shareholder and other special interests

Trade unions and work councils: engage in corporate policy re innovation, investments and productivity





What new and growing enterprises can do

Follow advanced and successful enterprises that focus on value creation

Turn the articles of association into the constitution of the company and build defenses against share- and stakeholders

Diversify the sources of capital to retain independence

Reduce organizational and financial risk by growing at a measured pace

Establish that all decision-making bodies and all managers and employees put the corporate interests central stage

Adjust governance and management to different stages of enterprise development

Capitalize on major disruptions such as mergers, takeovers and bankruptcies to change culture

V • The European Enterprise in context

The EU, after Brexit, is the natural home of the European Enterprise. It is well placed to take advantage of the many competitive advantages of the EU vis-a-vis other trading blocks.

At the same time the European Enterprise, with its emphasis on value creation, will contribute disproportionately to EU economic growth and well-being.

The EU advantages embedded in its Economic and 'Soft' infrastructures should inform the EU innovation and growth agenda. Enforcing what is strong is far more efficient and effective than seeking remedies for what is weak.



Economic infrastructure

Exposed to world markets and therefore highly productive in its heartland

The largest consumer market in the world

A sizeable and advanced manufacturing base

Strong positions in the world's business-to-business markets

A superior patent system

Competition law and its enforcement the envy of the world

Considerable untapped potential in terms of the integration of markets for energy, ICT, services and labor





'Soft' infrastructure

The member states and the EU serve the people and protect the common good

A long history of effective public/private cooperation in a variety of fields

Availability of a range of corporate legal entities accomodating very different companies in various stages of development

Civil law serving the public and the business community

An unprecedented network of trade agreements

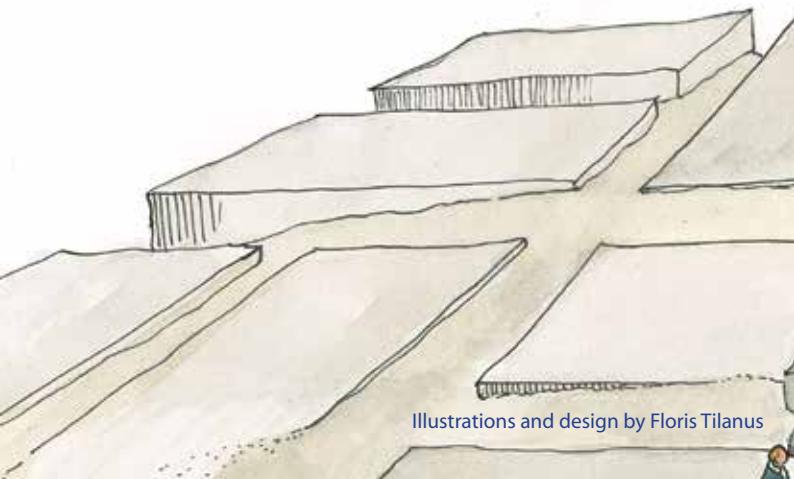
Mechanisms to cope with the social consequences of economic development already in place

About the author

After receiving his PhD degree from the Wharton School of the University of Pennsylvania, Donald Kalff spent most of his professional life as a manager at Royal Dutch Shell and as a member of the Executive Board of KLM, Royal Dutch Airlines. During the last 15 years he has co-founded AIMM Therapeutics, a biotech company, and three other companies working in the field of the diagnosis and treatment of tropical diseases.

He is also the author of three books and numerous articles on the governance and management of large enterprises. In the Fall of 2019 he and his co-author Andrea Renda published *Hidden Treasures, Mapping Europe's sources of competitive advantages in doing business*. This booklet provides the outline of a forthcoming book titled *The European Enterprise, value creation for society*.

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