Managing Stakeholder Relationships

Lesson 1

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Stakeholder Context and Analysis

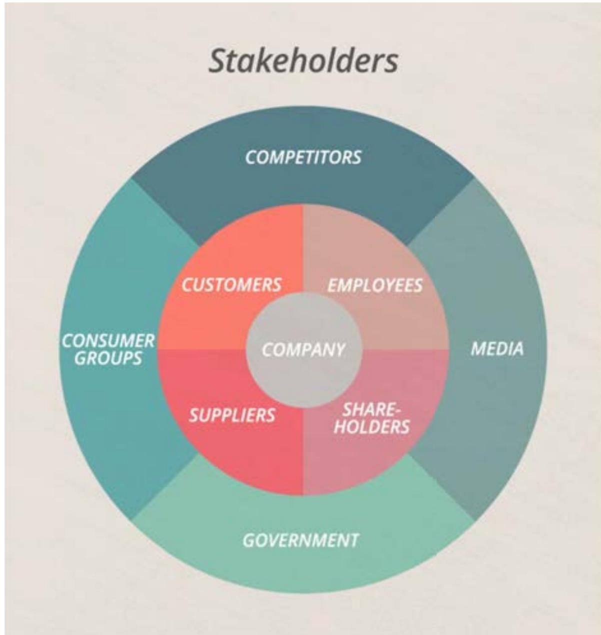
- Identifying different types of stakeholders
- The importance of building stakeholder relationships for organisations
- Stakeholder influence
- Challenges of working with stakeholders

Considering Stakeholders

To understand who stakeholders are, consider an organisation you know well - perhaps the one you work for - and the people or groups it deals with in the course of its activities.

The company's customers or clients, employees, and HM Revenue and Customs will almost certainly be on the list.

Depending on the organisation, there may be others it deals with in the wider community: local government, investors, or the media, to name just a few. Not all of these people or groups will be of equal importance at all times; however, they will affect, and be affected by the organisation's activities in ways large and small. They will therefore have an interest or 'stake' in how well it functions. This is the reason we call them 'stakeholders.'



Considering Stakeholders (cont.)

In the now classic text Strategic Management: A Stakeholder Approach, R. Edward Freeman defined a stakeholder as:

‘Any group or individual who can affect, or be affected by, the achievement of the organization’s objectives’.

Internal Stakeholders

So, for example, every organisation will count their own employees as stakeholders - after all, who has more stake in its objectives than the people who work there?

These people are collectively known as ‘internal’ stakeholders because they operate inside the organisation. Everyone from the senior leadership team to entry level workers will fall into this category.

External Stakeholders

An organisation will also have 'external stakeholders,' who operate outside it.

Who these external stakeholders are will differ depending on the size and sector in which the organisation operates. A business will count its customers and investors as stakeholders. A local community group will have donors or volunteers, and a government agency, such as HM Revenue and Customs will have stakeholders among the general public - in this case, tax payers.

A company may also include trade associations and regulatory bodies as external stakeholders, as they also interact with, and have a 'stake' in it.

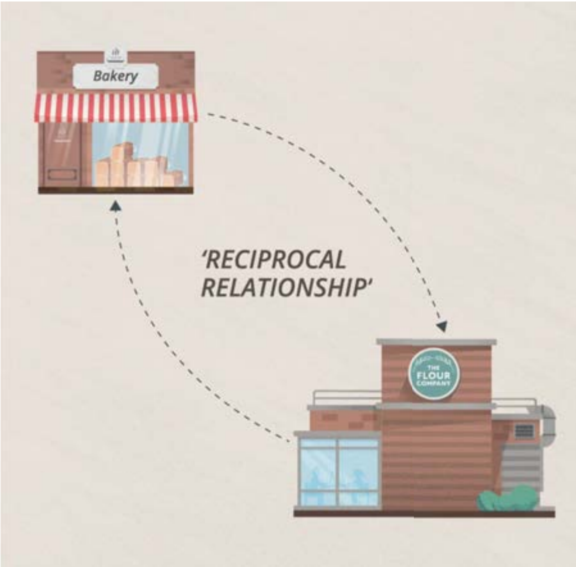
Stakeholder Interest

The importance of each of these relationships will depend on the level of interest the stakeholder has in the company, and vice versa. This will reflect the degree of impact the two entities have on each others' activities.

For example, the relationship between a bakery and its flour supplier is crucial to keeping both parties in business, therefore there is great emphasis on maintaining and developing the connection on both sides.

Reciprocal Relationships

The bakery and its supplier have a 'reciprocal relationship.' This is a two-way interaction, through which both parties give and receive information, goods or services at different times.



From his research, Freeman concluded that stakeholder relationships are by their nature reciprocal. He further argued that these relationships are critical for the success of the organisation, and therefore need to be proactively 'managed.'

Stakeholder Management

‘Stakeholder management’ is an umbrella term for all the tasks involved in identifying, analysing, monitoring and engaging stakeholders. In essence, it’s everything organisations do to maintain the relationship.

This is supported by an understanding of what each party needs and expects from the other, and therefore each relationship will be different. These needs may also change over time, affecting the interaction, and the balance of interest and influence of both parties.

Equal Relationships

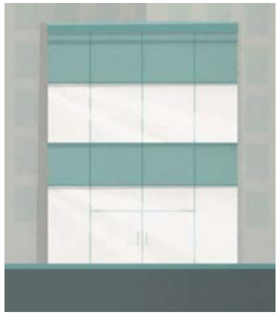
So the bakery and its supplier may initially have an ‘equal stake’ in the relationship. However, as the bakery grows it may need to expand its list of suppliers.

Given its more powerful position, it may even impose business terms that its original supplier finds difficult to meet. The supplier may find that the relationship is no longer an equal one, and its leaders will need to decide whether they can maintain it on the new terms.

Stakeholder Expertise

We've now seen that organisations have 'reciprocal' relationships with their stakeholders. In other words, there is a 'give and take' between them. The result of this give and take can be very beneficial to an organisation.

This benefit may come in the form of funding, which can be critical when the company wants to expand, or when it's affected by an economic downturn.



However, stakeholder assistance often extends beyond money. Management author Joseph Heagney identifies 'expertise' as an important form of non-financial assistance.

Stakeholder Expertise (cont.)

Stakeholder expertise can fill gaps in the organisation's knowledge base. This can influence the research and development of its services or products, leading to their overall improvement. The assistance may come from both external stakeholders, like suppliers or consultants, and internal ones, like employees.

However, the impact of reciprocal relationships varies depending on how strongly stakeholders can affect, or be affected by the company.

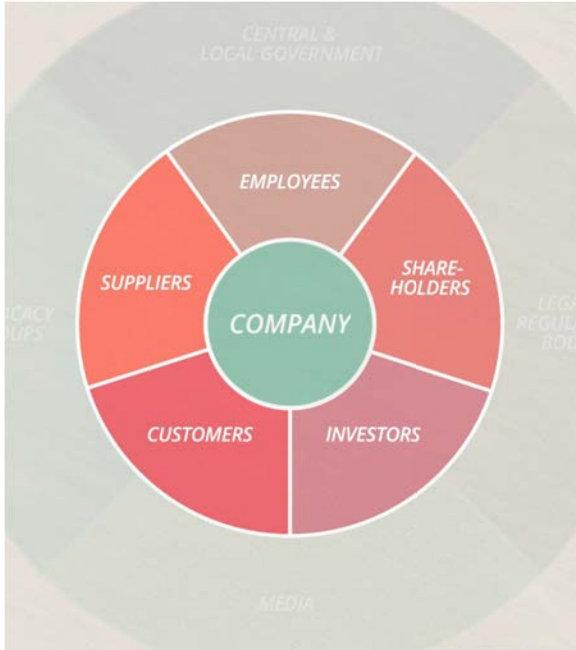
Primary and Secondary Stakeholders

Those who have a direct impact on the organisation, and are most heavily affected by it, are known as 'primary' stakeholders. Those who have an indirect impact, and are less affected are known as secondary stakeholders.

Both categories may include stakeholders who function within and outside the company.

Primary Stakeholders

According to the CMI, primary stakeholders are those who ‘define’ the organisation and ‘are vital to its continued existence.’



They may include:

- Employees
- Shareholders
- Investors
- Customers
- Suppliers

All of these groups have a strong impact on the organisation and its operations - we saw an example of this with the bakery and its supplier.

Primary Stakeholders (cont.)

Suppliers provide products or services which the company needs for its daily functioning. Customers bring essential revenue, and ultimately, profit. Investors and shareholders bring funds, and in some cases, guide the company's strategic direction. Employees bring skills and time to create the organisation's products or deliver its services.

Actions taken by primary stakeholders are often visible and the effects immediate, not only to the organisation, but to its other primary stakeholders.

Consider what happens when the employees of a rail company decide to strike. This action will have an immediate impact on the company's bottom line. But it will also strongly affect its other primary stakeholders - commuters.

Secondary Stakeholders

Secondary stakeholders, conversely, have an indirect impact on the organisation. They may not engage with it first hand, or be as strongly affected by its actions, but they will have a stake in how it operates.

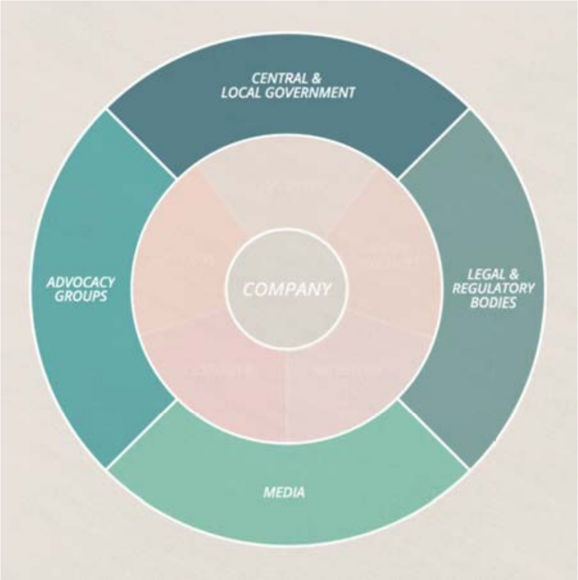
Depending on the organisation's sector, its secondary stakeholders may include:

- Central and local government
- Legal and regulatory bodies
- The media
- Advocacy groups

Secondary Stakeholders (cont.)

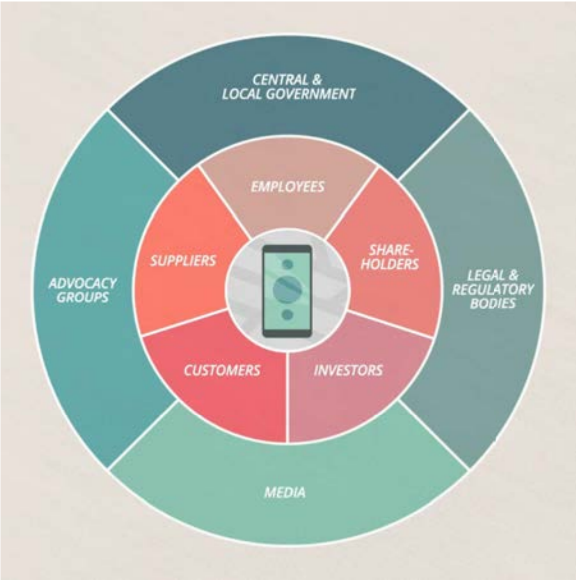
These entities can influence an organisation in different ways. Government may pass legislation that impacts how a company functions. Legal authorities, such as inspectors, may enforce this legislation. The media will report on the organisation, and social groups may pressure it to act in certain ways.

Secondary stakeholders may also influence the organisation through its primary stakeholders. For example, social groups may pressure investors or customers to stop supporting a company if they consider it to be acting unethically.



Primary and Secondary Stakeholders - Example

Consider the impact of the stakeholder network at a mobile phone company.



The company's primary stakeholders include the investors and shareholders who contributed to its launch, and continue to fund it, and advise its leaders. The company's financial success is critically important to these stakeholders.

Other primary stakeholders include customers who are loyal to the company's products and to its overall brand.

Primary and Secondary Stakeholders - Example (cont.)

Now imagine that the company manufactures its phones in factories which have a record of labour violations.

This may get the government and regulatory bodies to investigate it, which in turn may alert the media. News outlets will write articles that have a negative impact on its image, alienating its customers. This in turn may lead investors to rethink their relationship with the company, and withdraw some funding.

In this way, individuals or groups with a lower stake may influence those with a higher one, affecting all of a company's stakeholder relationships.

Stakeholder Power

So far we've seen that stakeholders can fall into several categories depending on their relationship with an organisation. They may be internal or external to a company, and may have a major stake in it, or a minor one.

However, we also noted that a stakeholder's power can be a factor in the relationship.

In this context, power can be defined as the degree to which the stakeholder can influence the behaviour of an organisation. This is true whether the stakeholder is internal, external, primary or secondary. For example, the government is an important stakeholder in all UK organisations, simply because it has the power to legislate their conduct.

Stakeholder Power (cont.)

We've also said that the importance of a stakeholder relationship is determined by the interest the two parties have in each other's activities. Interest is equivalent to 'stake' in the organisation; primary stakeholders tend to have higher interest than secondary ones.

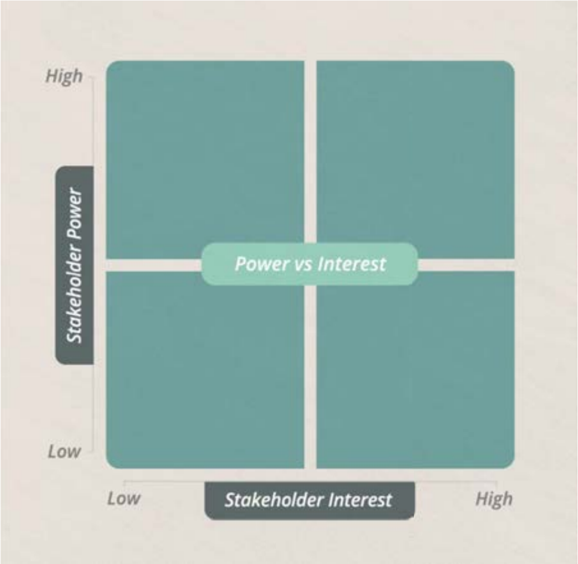
In order to manage stakeholders effectively, organisations must know how much power and interest different stakeholders have, and how these elements combine to affect the relationship.

Power vs Interest Grid

Management academics Colin Eden and Fran Ackermann developed a model to map stakeholders based on these criteria in the 1990s. It's known as the 'Power vs Interest' grid.

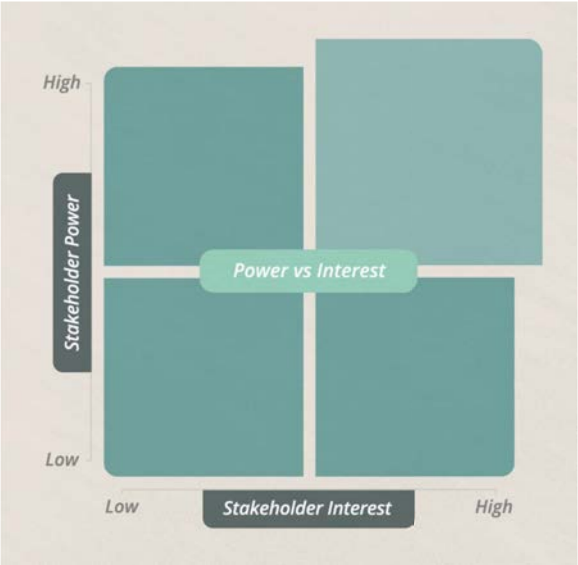
The model is set out across two dimensions: stakeholder 'interest' in the organisation, and stakeholder 'power' to influence it.

This forms a grid with four possible combinations.



High Interest, High Power

The ‘high interest, high power’ quadrant is occupied by stakeholders who have strong interest in the organisation and a great deal of power to affect its activities. For a public agency these will be government ministers. For a non-profit, they will be its trustees and major donors. For a business they may be the investors in the company.

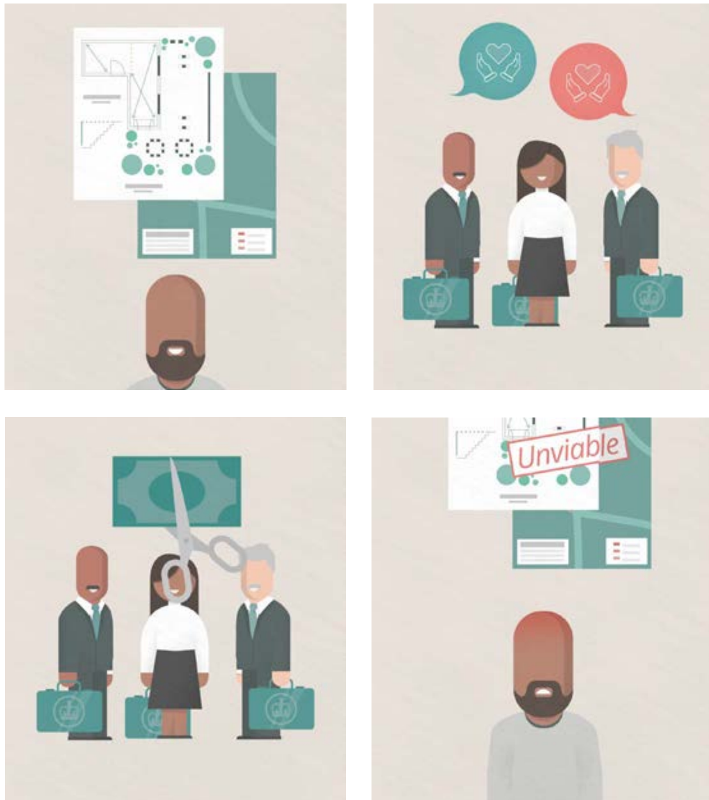


The people and groups in this quadrant are also sometimes known as key stakeholders.

High Interest, High Power (cont.)

According to author Graham Kenny, these are stakeholders with a disproportionate impact on the performance of an organisation - for example, its ability to meet production deadlines and make a profit. They often have the power to make or break a company's plans.

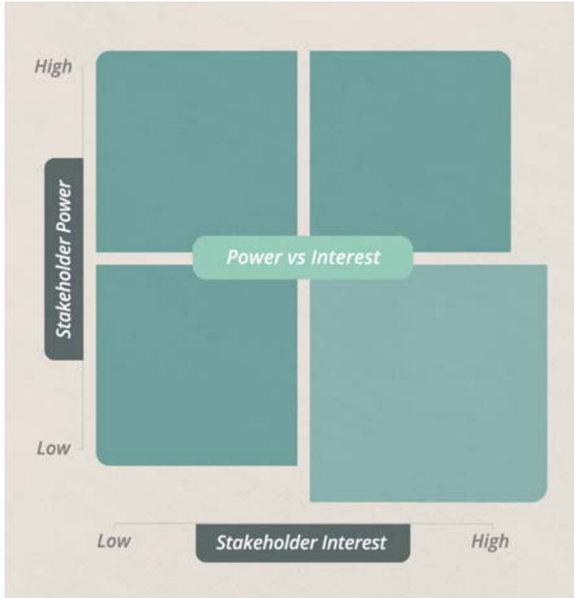
Consider a developer planning to build a retail park. The company's investors have a high interest in the project - they want to see a return on their investment. They also have the power to reduce or withdraw their funding if they judge the plans to be unviable. This will have a significant impact on the developer's ability to proceed.



High Interest, Low Power

Conversely, the 'high interest, low power' quadrant is occupied by stakeholders who have a high interest in the organisation's activities, but limited power to act on it.

This group includes the majority of an organisation's employees. Whilst not as powerful as the first quadrant stakeholders, they can gain power through external means, such as government and the courts. They can also increase it through collective action - for example, by joining a trade union.



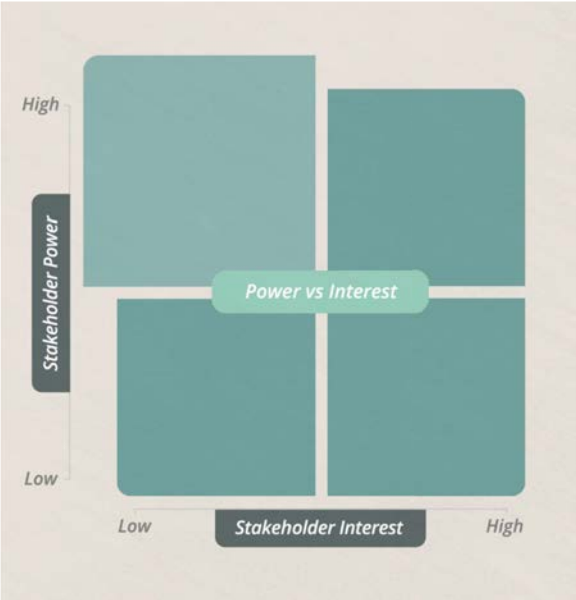
High Interest, Low Power (cont.)

The residents of the area where the retail park will be built would also fit this category. They might not have much power individually.

However, if they're opposed to the project they could increase their influence by protesting together, or lobbying their local MP.

Low Interest, High Power

On the other hand, the ‘low interest, high power’ quadrant is occupied by stakeholders who have little interest in what the organisation is doing, but do have a lot of power.

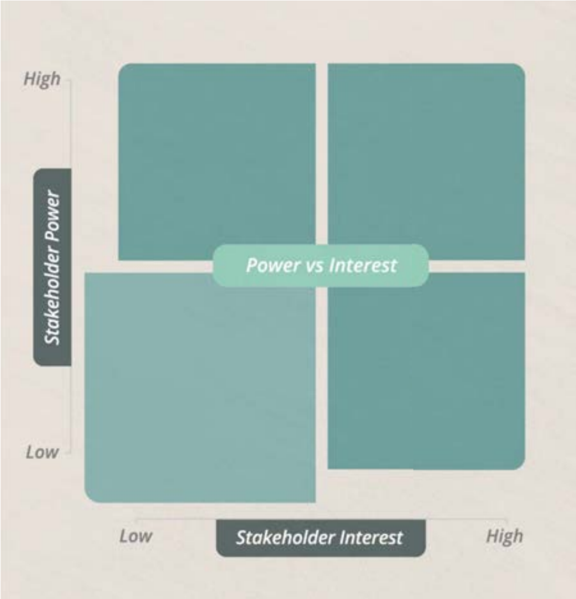


Government and professional bodies often fall into this category. They may not have a high stake in a particular company, but can exercise power over it - for example, by levying fines.

The retail park developer will also need to work within their rules - by getting planning permission for buildings and respecting transport restrictions.

Low Interest, Low Power

Finally, the ‘low interest, low power’ quadrant is occupied by stakeholders with little interest in the organisation, and little power to influence it. These may include less important contractors, or potential employees who don’t yet know about the company.



The prospective employees and customers of the retail park meet this criteria. Their interest and power is low right now - in fact, they may not even know about the developer’s plans.

Shifting Positions

However, it's important to note that stakeholder positions aren't static. The position of the employees and customers can move at any time - and will change once the retail park opens.

The Power vs Interest grid can help organisations determine which stakeholders will have the greatest impact on their objectives. Armed with this information they can form a strategy to advance their interests, and protect their position within the relationship.

Negotiations

Although power and interest are useful criteria by which to evaluate stakeholders, these aspects may change over time.

Some of these changes may be driven by the stakeholders themselves. For example, both internal and external stakeholders will seek to increase their power in the relationship by 'negotiating' better terms with the organisation.

A 'negotiation' is a dialogue between two or more parties that aims to reach a solution benefiting all sides. It's a natural part of reciprocal relationships, where both stakeholder and organisation have their own interests.

Contracts

The outcome of a negotiation will often be finalised in a ‘contract’ - a legally enforceable agreement between two parties. By signing a contract, both sides hope to protect their interests in the relationship.

Contracts exist within a larger framework of government legislation. For example, all employee contracts are subject to UK employment law; a contract that contravenes the law - say, by adding an illegal clause - is not enforceable.

Contracts are common in long term stakeholder relationships, especially those involving primary stakeholders.

Contracts (cont.)

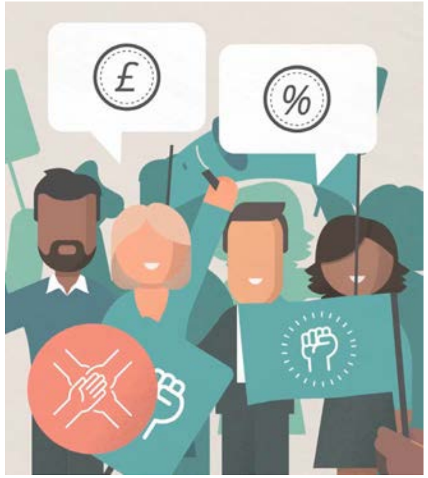
'Employee contracts' are standard for internal stakeholders. These cover both the expectations of the company and the employee regarding the terms and conditions of employment, such as working hours and days, the scope of the work, and payment, including any additional benefits.

The final terms will depend on the needs of the company, the position of the employee, and the negotiating skills of both parties.

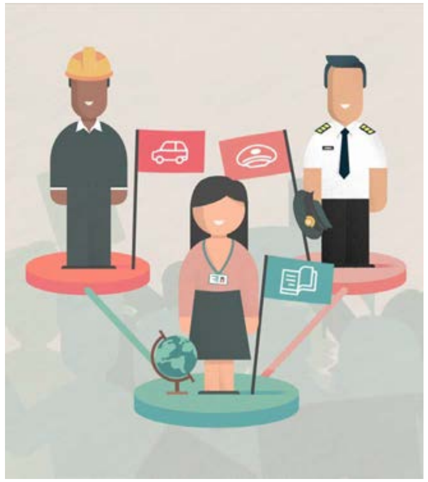
However, as most employees are 'high interest, low power' stakeholders, they will have limited scope to negotiate the terms in their favour. For the last century or so, employees have dealt with this drawback by forming trade unions to promote their interests.

Collective Bargaining

As we've established, low power stakeholders can gain power in numbers. The process of 'collective bargaining,' in which unions negotiate terms on behalf of their members, can change the balance of power in the relationship. The outcome of this negotiation is a 'collective agreement' which may expand to cover all employees of the organisation.



However, in order to engage in collective bargaining, the union must be recognised by the company. For this reason unions are strongest in companies with large, specialised workforces; pilots, teachers and car manufacturers all have powerful unions to protect their interests.



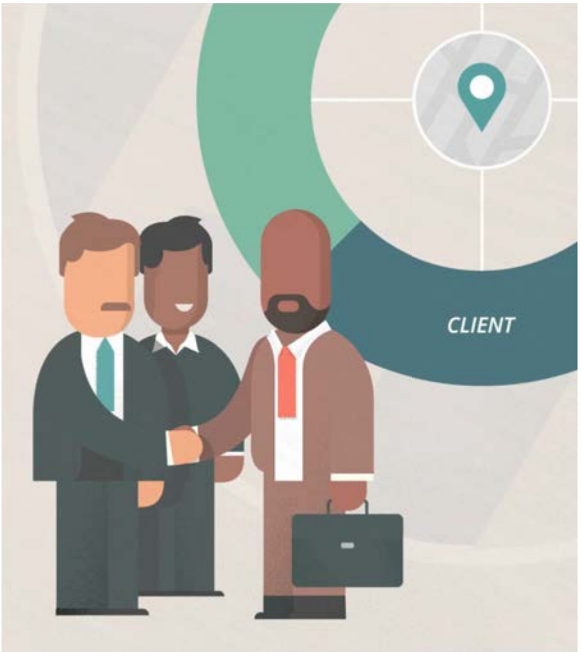
Contractors

Not all people who work for organisations are considered employees. The others include self-employed people who ‘contract’ to work with a company - otherwise known as ‘contractors.’ These are external stakeholders, who bring needed expertise to the company for a limited period of time.

Contractors sign what are known as ‘work for hire’ agreements. Like employee contracts, these cover payment terms and working conditions. However, because these stakeholders take part in individual projects rather than ongoing work, their contracts put more emphasis on timescales and the deliverables the company expects them to produce.

Service-level Agreements

Another common external stakeholder is the client - this is a person or company that uses the organisation's professional services. For example, an advertising agency will serve clients that want to promote products to a specific audience.



A company's client relationships are governed by the 'service-level agreement' or SLA. This is a kind of reverse 'work for hire' contract, because it's the organisation who is acting to supply services to the stakeholder, rather than the other way around.

Service-level Agreements (cont.)

SLAs define the level of service expected from the company, and any penalties or remedies if it falls below expectations. So if the ad agency delivers its artwork late, it may be penalised with lower payment for its work.

However, for this to work smoothly every aspect of the service must be carefully defined. If the contract requires a '24 hour turnaround time' for example, the SLA should spell out whether this includes weekends. Otherwise both parties may feel aggrieved and mutual suspicion may damage the relationship.

In fact, this is true of contracts in general: they are most useful when they clearly set out their terms. If they fail to do so, and there is a dispute, the parties may end up in court - an expensive way to resolve a stakeholder issue.

Challenges of Stakeholder Management

By now you probably sense how complex the management of stakeholders can be. While seeking to derive the greatest benefits from these relationships, organisations are also likely to encounter many challenges.

Some of these may be foreseen and avoided by the careful use of contracts, as we have already seen. This is the case with disputes over deadlines, for instance, as these terms are relatively simple to clarify in writing.

Conflict of Interest

But not all challenges can be anticipated or mitigated with a contract. Many of the obstacles to a good stakeholder relationship start with the goals of the stakeholders themselves.

A common challenge relates to the differing ‘needs and expectations’ of stakeholders, and the organisation’s wish to satisfy all of them. This may result in a conflict of interest.

Managing Stakeholder Interests

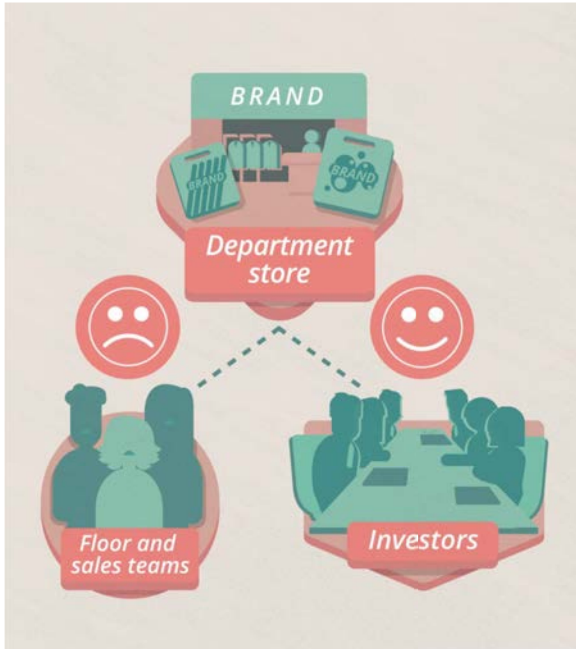
For example, imagine a department store which has lost profit for the third consecutive year. Its floor and sales teams are living with uncertainty, and have not received an annual pay rise or bonuses for Christmas.

Its investors are also becoming anxious, meeting often to discuss the future of the business. The store's senior management know that employee morale is low and they're eager to reward them for their hard work. They don't want to lose talent in case sales turn around next year. But giving their workers more money now may trigger investors to sell their shares, which will hit the company's finances and may eventually lead it to close.

Managing Stakeholder Interests (cont.)

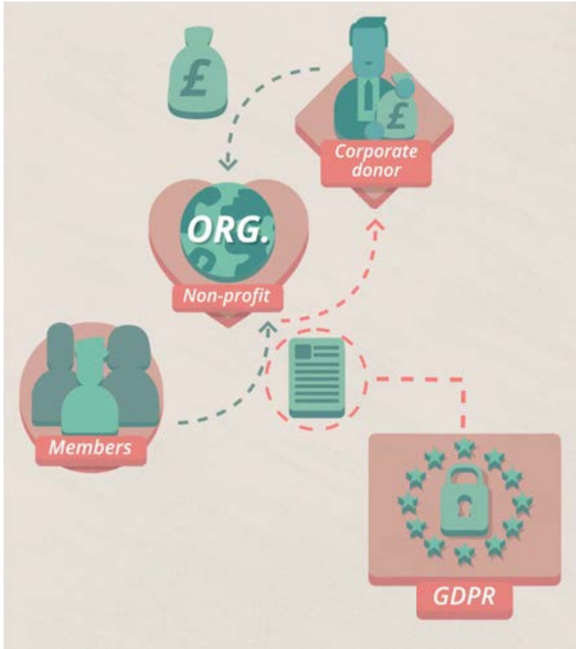
Managing the interests of both these stakeholder groups presents a conflict of interest for the company: the retailer can keep shareholders happy, but only at the expense of their employees - or vice versa.

Balancing the interests of different stakeholders is a particular challenge when one of them has more power and influence than another.



Managing Stakeholder Interests - Example

For example, a small non-profit which receives sponsorship from a corporate donor may be asked to share data on its members with the donor's marketing team. This would likely contravene the terms of the General Data Protection Regulation, or GDPR, and harm the group's relationship with its membership.



Both the donor and the members are primary stakeholders, and are equally important to the non-profit's long term strategy. But the donor has high power in this relationship; the nonprofit will want to avoid alienating them. Navigating such choices without damaging stakeholder relations is a major challenge for organisations - especially small ones, and those with modest funding.

Power Imbalances

Management theorist Richard Pettinger argues that the stakeholder with the highest level of financial investment in a company is likely to have their needs and interests prioritised.

He adds that this is the case ‘whether or not this is the correct course of action for the particular organisation.’ Maintaining a productive relationship when there is an imbalance of power between stakeholder and organisation is especially difficult.

Values and Culture

Finally, there are challenges which arise from differences between the values and culture of the organisation and its stakeholders.

'Culture' in this context could refer to the attitudes, customs and practices of a particular country. So, for example, when a multinational firm expands overseas they may encounter different employee habits than those expected in their own work culture.

Company Culture

However, culture can manifest itself on a much smaller scale - after all, every company has its own expectations for how work will get done.

These expectations reflect the 'values' of its senior management, and are reinforced through recruitment of people with similar values. This means that even when two organisations in the same city partner together, they may find that their expectations for the relationship don't match up.

Company Culture - Example

For example, a coffee manufacturer might feel that the company which sources their coffee beans isn't collaborative, and doesn't do enough planning to keep ingredients in stock. The supplier in turn may believe that the coffee company is overly demanding; they find the constant meetings and written updates they're expected to send a drain on their resources.

In extreme cases, the misalignment may cross over from day-to-day work and affect the public image of the organisation. If the coffee manufacturer takes pride in its sustainable practices, but a media investigation reveals that the supplier wastes resources, the relationship will become a liability for the manufacturer. In this case, a lack of transparency by the supplier has hidden a serious divergence of values, which will ultimately hurt both companies' brands.

Recap

In this lesson, you have learned about:

- Identifying different types of stakeholders
- The importance of building stakeholder relationships for organisations
- Stakeholder influence
- Challengers of working with stakeholders