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— Robb Willer

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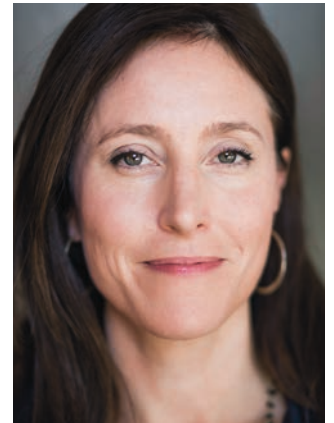
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Stanford Business

INSIGHTS AND IDEAS FROM STANFORD GRADUATE SCHOOL OF BUSINESS

AUTUMN 2015
VOLUME 83, NUMBER 3



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Cover illustration by Shout

INTRODUCTION

IMPACT

We all strive to bring meaning to our personal and professional lives. But what does it mean to be impactful? In this issue we explore that question from many angles and disciplines, showing how actions can produce change in life and work as well as in our neighborhoods and global community. ▶ Ilya A. Strebulaev's work discusses the impact of venture capital funding on the U.S. economy, and a study by Shai Bernstein looks at whether companies are more profitable when their investors step away from Skype and visit in person more often. The question of whether companies can make money while doing social good is answered with a resounding "yes" by a former basketball player who uses his star power and business acumen to do just that, while law scholar Paul Brest outlines the benefits of social impact investing. And what makes us altruistic? Sociologist Robb Willer tackles that question. ▶ An alumnus who leads Habitat for Humanity explains why he builds,



Construction by Jacob Lawrence in casein tempera over graphite on paperboard from the Cantor Arts Center collection

while Larissa Tiedens discusses how female leaders can make a difference in the boardroom. And, from Jeffrey Pfeffer, something we can all use: tips to leverage our own power to bring about change. Sometimes — as Pedro M. Gardete demonstrates — what influences us emanates from an unexpected source, such as a stranger on a flight. ► As always, we love to hear from you at StanfordBusiness@stanford.edu or [@Stanfordbiz](https://twitter.com/Stanfordbiz) on Twitter. You can find more stories, videos, and visual storytelling online at *Insights* by Stanford Business at www.gsb.stanford.edu/insights. — THE EDITORIAL TEAM

STANFORD BUSINESS

ONLINE



Jack Ma

YOUTUBE

“Spending money is more difficult than making money, especially for philanthropy.”

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WEB

Do Real Men Buy Bath Products?

New research shows that when a man's masculinity is called into question, he counterbalances by avoiding stereotypically “female” activities and products.

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Lives



“Negotiation is about

finding a solution

to your counterpart’s problem
that makes you better off
than you would have been had
you not negotiated.”

—Margaret Neale PAGE 11

STRATEGY

How Should Women Lead?

Research pinpoints management techniques that dampen backlash.

BY BILL SNYDER

How can women be strong leaders at work without being labeled as “bossy” or viewed as less likable than their male peers? Research by Larissa Tiedens, a Stanford GSB professor, suggests that women can exert control by engaging in more subtle or “implicit” methods of dominance.

A shift in facial expression, an expansive posture, or a different negotiating strategy can be just as effective as a direct command, a wagging finger, or other aggressive behavior, she says. When women use these methods, the backlash is weakened or even disappears, according to the research by Tiedens and Melissa Williams of Emory University’s Goizueta Business School.

Based on a review of hundreds of earlier studies, their work suggests a winning strategy for women in business: “While the obstacles to women’s achievement in leadership roles are real, there also is reason to hope that women may be able to work around them by relying more heavily on implicit methods of interpersonal influence,” write the researchers.

Larissa Tiedens is the Jonathan B. Lovelace Professor of Organizational Behavior at Stanford GSB and the senior associate dean for academic affairs.

Photograph by Boris Zharkov

LARISSA TIEDENS
Dominant women
face difficulties
in business.



“Requiring that women express dominance only in specific, relatively narrow ways is not a path to gender equity.”

Their upcoming paper, “The Subtle Suspension of Backlash: A Meta-Analysis of Penalties for Women’s Implicit and Explicit Dominance Behavior,” draws on research into animal behavior as well as Tiedens’ earlier work on hierarchy and dominance in business. The research will appear in *Psychological Bulletin*.

When threatened, many animals puff up their fur or take a very deep breath and expand their bodies because it makes them look larger. Similarly, “when people expand themselves and take up a lot of space, they are perceived as dominant, whereas when they constrict themselves and take up little space, they are perceived as submissive,” Tiedens wrote in an earlier paper on nonverbal behavior.

Standing tall and using a loud voice during a meeting can express authority, but it’s subtle enough not to be resented, she says. Sitting with an arm draped over a chair, and an ankle resting on a knee, makes a person look larger and more dominant — but not threatening.

Attitudes and preconceptions about gender roles are deeply rooted, so it’s not surprising that dominant women face difficulties in business. People believe that men should be dominant and that women should be warm, writes Tiedens. Women who violate those stereotypes aren’t seen as warm, and if they occupy leadership roles in business or politics, they may be viewed as a threat to men’s status as earners, the researchers say.

The contradiction between needing to act as a strong leader and needing to be seen as warm and nonthreatening is a catch-22 for women. In order to get ahead, an executive must be seen as strong and competent, yet if a woman makes a point of seeming competent, she won’t be seen as warm and could face a backlash and not get promoted.

Women internalize at least some of those stereotypes. In one experiment, cited by Tiedens, women were asked to write graduate school admissions essays on their own behalf and for another person. The essays about themselves were markedly poorer. Commenting on that research, Tiedens says, “this reduced success was explained by the women’s fear of being negatively evaluated by others for advocating strongly on their own behalf.”

In 2010, a group of researchers mentioned by Tiedens in her research found that women who ask for resources for themselves — a raise, for example — are liked less than men who make the same request. But if they ask for something for someone else, a higher salary for a subordinate, for example, there’s no penalty.

“Fighting back against budget cuts to the department or business unit that one leads may be an ideal opportunity for both male and female leaders to deploy their strongest persuasive weapons without fear of social costs. Indeed, leaders may be penalized for not advocating on behalf of others for whom they are responsible,” write Tiedens and Williams.

Although those strategies may be helpful, they are imperfect, says Tiedens. Women should not need to engage in corporate jujitsu in order to succeed as strong leaders.

“At some point in their careers, women leaders will need to make explicit, rather than implicit, demands of others, and requiring that women express dominance only in specific, relatively narrow ways is not a path to gender equity.” ▲



SHAKE ON IT Former Soviet Premier Mikhail Gorbachev and former U.S. President Ronald Reagan in Geneva, Switzerland, in 1985

LEVERAGE

Five Steps to Better Negotiating

How to get what you want

BY ELIZABETH MACBRIDE

The modern framework for negotiation is broken: Most of the prevailing theories see negotiations as battles in which the players act rationally in their own best interests. If you are lucky, this is a battle you might win.

But what if you reframed the whole idea to think of a negotiation not as a fight but as a problem-solving exercise? And one in which emotions can play a systematic and powerful role?

In a book published earlier this year, *Getting (More of) What You Want*, Margaret Neale, a Stanford GSB professor and co-author Thomas Lys challenge long-standing conventional wisdom on negotiating. They say that when people cease to see negotiation as a fight, they open themselves up to more creative solutions and are able see more situations as opportunities to negotiate.

Margaret Neale is the Adams Distinguished Professor of Management at Stanford GSB and the codirector of the Executive Program for Women Leaders.

To write the book, the duo drew on economics and behavioral economics to systematically analyze how emotions tend to affect negotiations. Perhaps the most important effect is that when people are drawn into the battle, they will sometimes give up too much — even against their own interest — just for the sake of coming to a resolution.

“Agreements for the sake of agreeing are not so great, unless of course agreement is all you care about,” says Neale. “But then, if that were the case, you wouldn’t need to negotiate. You’d just accept your counterpart’s first offer.”

There are other powerful psychological processes that can affect negotiations, too. For instance, merely expecting an outcome, or creating an expectation in your counterpart, can affect what happens at the table. And *Getting (More of) What You Want* leverages decades of research to help answer questions like who should make the first offer and how to create a packaged offer.

A “negotiation is about finding a solution to your counterpart’s problem that makes you better off than you would have been had you not negotiated,” Neale says.

In the business world, the “wins” are almost always defined by dollars. In Lys and Neale’s view, what you value in the deal — what you want — can range from the traditional view of dollars to control of your time, a better relationship with your counterpart, or achieving a particular outcome in a meeting.

The authors offer a five-step road map to negotiating:

ASSESS

Look at the situation and decide if this is a place where you can negotiate: “Can I change the outcome in a way that makes me better off?” One of the questions is whether you have the information you need to help you construct viable offers and creative packages in the negotiation.

If the answer to your assessment is yes, then move on to stage two.

PREPARE

This is where most people fall down, Neale says.

“Packaging is especially valuable when you are the party with less power.”

“We are struck by how many smart people act as if negotiation is simply improvisational theater rather than an interdependent process that requires planning and preparation, making strategic choices, and maintaining discipline,” write the authors.

The key is to figure out as much as you can about where you stand and where your counterpart stands prior to negotiating. “People may have positions, but those positions may have very little to do with what is driving the issue or dispute,” they write.

For instance, when Neale was asked by an associate dean at a previous post to take on a program directorship, she discovered that he’d been instructed to do so by his boss — and that one of the things driving him was that the program was important to the overall institution. She was able to factor in how to show loyalty to the school as she negotiated her compensation.

ASK

Conventional negotiating wisdom holds that “whoever makes the first offer loses the negotiation.”

But that old-school line of thinking ignores “anchoring.” When you make the first offer — informed by everything you’ve learned in your preparation about what you need and what your counterpart wants — you are anchoring the negotiation closer to where you want it.

There are ways to make that first offer more appealing: The more objective your first offer appears, the more value you’re likely to get. And, precise offers (and counteroffers) are better than “round numbers.” For instance, research shows that homes with precise listing prices sell for more, on average, than those with a more rounded listing — even when that rounded figure was higher.

PACKAGE

To avoid the battle mentality, prepare a proposal that is an entire package. You can then say, “How can we talk about crafting an outcome to make it work for us?”

Among other things, that gets the counterpart committed to the deal.

Packaging is an especially valuable tactic when you are the party with less power in a negotiation. If you can work hard enough to find creative sources of value — for instance, identifying your counterpart’s emotional need to save face or to look like a hero in the eyes of his boss — you can design a package that is more likely to be accepted — and is a better value for you.

ADOPT A POWERFUL MINDSET

Try power poses when negotiating. Research has demonstrated that sitting or standing in an expansive pose can influence your levels of cortisol and testosterone as well as your willingness to take risks.

Expectations are incredibly influential, including your expectations of yourself. Neale suggests that adopting a powerful mindset at the negotiation table is easier and more formulaic than you think.

Here are some tips to remember when you are sitting down to begin:

- **Recall a time when you had power over another person.** Focus on what happened, how you felt, and what that experience was like.
- **Think about a time when you felt physically attractive.** “Although it may surprise you,” the authors write, “research shows that recalling a time when you felt physically attractive influences your ability to claim value in the negotiation.”
- **Try power poses.** In a series of studies, researchers have demonstrated that sitting or standing in an expansive pose, versus a constricted one, can influence your levels of cortisol (the stress hormone) and testosterone (the power hormone) as well as your willingness to take risks. ▲

CHALLENGE

Three Entrepreneurs Discuss Ways to Create Change

BY ERIKA BROWN EKIEL

“Success Is The Product of Constant Reiteration.”

Emrecan Dogan is founder and CEO of ScoreBeyond, an app that helps students prepare for standardized tests. While many software-based learning tools aim to automate the process, ScoreBeyond also helps connect students to live tutors. The company is venture backed and has 15 full-time employees. ScoreBeyond serves one-third of the 3 million students who currently take the SAT and ACT in the United States each year. In time, Dogan, who received his MBA from Stanford Graduate School of Business in 2010, plans to expand beyond these two tests. He talks with *Stanford Business* about living in the modern-day Renaissance, getting new ideas from art museums, and appreciating the gift of freedom inherent in entrepreneurship.

In 10 words or fewer, what is the big idea behind your business? Democratizing one-to-one learning and making it 10 times better via mobile.

What is the best advice you've ever received? A professor of organizational behavior at Stanford said, “You don't change the world by taking a nap.” Even with a strong sense of purpose, a lot of people do not execute because they are waiting for the right time or a grand plan.

It's a very powerful idea. It encourages you to get up and start.

What was the most difficult lesson you have learned on the job? Focus is hard to master but helps you achieve so much more in a shorter timeframe. It goes for relationship building as well as day-to-day business. When I was fundraising, a fourth investor verbally agreed to invest. It would have given us the final amount we set out to raise. All I needed to do was send him the final documents and wire details for the bank. Instead, I was feeling good about the interest we were getting and decided to raise my target and reach out to five new investors. A week went by and the fourth investor emailed me to say he found something else and he was bailing out.

What advice would you give other entrepreneurs on how to build a great business? Every success story seems very straightforward, as if it was an overnight result. But most success stories are the product of constant reiteration and change and reflection on the part of the founders. I have so many ups and downs every day. I try to teach myself to overwhelmingly overplay the positive things and underplay the negative things. We need to rewire our brains to do this.

If there was one thing that has enabled you to be successful as an entrepreneur, what was it? Resilience and willpower. I am from a small town in Syria. I had several health weaknesses. I was not able to

run because I had some breathing issues. Within the first few weeks of being away at college, I had my first visit to urgent care. My family was very far away, and I needed to deal with it alone. It turned out not to be as big a deal as I thought. Those types of situations help you build confidence.

What inspires you? How do you come up with your best ideas? A few years ago I went through a period when I could not produce any ideas. My wife suggested I get out and go to the Museum of Modern Art in San Francisco. The art space was so stimulating, and I had a rush of ideas. I ended up sitting in the cafe for the rest of the day and wrote pages and pages of designs. I go there whenever I have a challenge.

What is your greatest achievement? My wife and I are living halfway around the world from our hometown in an area that I believe people in the future will reference like Florence during the Renaissance. I am blessed with the opportunity to build my company from scratch in a country where we are not citizens. I don't have a huge bank account, and my company is not worth billions of dollars, but I have many friends and the freedom to pursue what I want. It seems like a dream.

What impact would you like to have on the world? Education is the key to social mobility — even better than giving people money. If we do our job right, we can provide the highest quality education to anyone in the world in the cheapest way possible.



Emrecan Dogan

Why are you an entrepreneur? I love the stress and the infinite freedom in decision making.

What was your first paying job? When I was in the fifth grade, all the girls I knew collected paper napkins with designs on them. I had two aunts living in Germany, and I paid them \$2 for each pack of 100 napkins with German stamps on them that I would sell to the girls in my class.

What is the best business book you have read? Richard Branson's *Losing My Virginity*.

What businessperson do you most admire? Richard Branson. He seems to have so much fun with the ups and downs of business.

What is the most valuable thing you took away from your time at Stanford? The 10 close friends my wife and I made there, as well as the other 800 we don't see every year but feel we can reach out to at any time if we ever needed them.

What do you think is the greatest innovation in the past decade? Tesla's battery technology.

"I Never Wanted to Be an Entrepreneur."

Ai Chloe Chien is the cofounder and COO of Homemade Cooking, a community-based cooking school that teaches people how to prepare healthy meals. Homemade is profitable and has several locations in Palo Alto and Menlo Park, Calif. Chien launched the business in 2013, shortly after

"I want to cure type 2 diabetes in my lifetime."

she graduated from Stanford School of Medicine and Stanford Graduate School of Business with an MD and an MBA.

In 10 words or fewer, what is the big idea behind your business? Teach busy people to nourish mind and body by cooking real food.

Before going to Stanford Graduate School of Business, I was planning to do medicine and work on population change or become a practicing physician. When I was training at the county hospital, I saw a lot of amputations on diabetic patients who had foot infections that grew out of control. They kept coming back because their diabetes was not in check. I saw that it was painful not only for them but also for their families. I then tried primary care, but it became a pattern of managing medication and nagging people to change. Nothing was working. After I took the *Startup Garage* course at Stanford, I started to think about diabetes as a real-world problem I could solve. We teach people how to buy, cook, and eat healthy food, and support each other to create strong habits over time.

What is the best advice you've ever received? My cofounder Anna Rakoczy, whom I met in the course, advised me to meditate. It has made a big difference to my wellness, sleep, energy, and overall effectiveness.

What was the most difficult lesson you have learned on the job? When you are a cofounder of a startup, self-care is really important. You are working hard and not sleeping well, and exercise tends to be the first thing to go. You lose effectiveness at work, as a person, and at home. A little while back, I completely burned out. I found myself crying from exhaustion. I had to take an emergency vacation to recover. I went off the grid for a week. All I did was stay home, but afterward I felt renewed. That's when I knew we have to take care of ourselves in order for the company to survive. All our hearts and souls are in this.

What inspires you? Our mission. Cooking and eating real food should be joyful and inspiring.

What is your greatest achievement? Doing a startup in Silicon Valley that is non-tech with an all-female team.

What values are important to you in business? Service — to my employees, business partners, and customers.



Ai Chloe Chien

This may have carried over from my training in medicine.

What impact would you like to have on the world? I want to cure type 2 diabetes in my lifetime. After that I'd like to tackle other lifestyle diseases, such as heart disease.

Why are you an entrepreneur? I never wanted to be an entrepreneur. It was just the most logical, sensible way to have an impact on lifestyle diseases, such as diabetes.

What was your first paying job? This is it.

What is the best business book you have read? *The Power of Now* by Eckhart Tolle. Also *Value Proposition Design*. It helps you get to product/market fit.

What businessperson do you most admire? Anna. She is my mentor, best friend, and sister. We are very different personalities, yet we have very complementary approaches and perspectives.

What is the most valuable thing you took away from your time at Stanford? The "check-in" concept from *Startup Garage*. We do a personal check-in, as well as a business check-in, before each meeting starts.

What do you think is the greatest innovation in the past decade? Any innovation that is made accessible and scalable.

“Approach Error With Compassion.”

Edward Fenster is cofounder and chairman of Sunrun, which provides solar energy to homeowners. In August this year, Sunrun began trading on Nasdaq under the symbol RUN. The company operates in 15 states and has installed \$1.8 billion worth of solar energy systems.

Fenster studied computer science before switching into finance and working in private equity at Blackstone and corporate development at Asurion. He earned his MBA from Stanford Graduate School of Business in 2007.

In 10 words or fewer, what is the big idea behind your business? Homeowners will buy solar power if it's cheaper and easy.

What are the biggest challenges unique to your business? How multidisciplinary it is. There are a lot of things you have to do right: market, sell, install, finance, service, hire. The many companies that have failed in our industry usually miss one or two, but not always the same one or two.

We also face real regulatory challenges. For a long time, utilities didn't think we could be cost-competitive without unreasonable subsidies. Then they realized we were a serious competitive threat. Then their trade group launched a national campaign against rooftop solar two years ago. But voters supported rooftop solar because it's freedom from state-sponsored monopolies, and that support was powerful. Now some utilities are finally thinking about how to profit from rooftop solar rather than just how to stop it.

You started a company in an industry with rich, powerful competitors and high regulatory hurdles. How do you, as an entrepreneur, upend the balance of power when you begin with little money and no power? If you win the support of the

public and the media, you can beat wealthy adversaries with asymmetric warfare. Two things create regulation: one, products the government feels it needs to regulate because they are viewed as human necessities, like electricity, health care, or air-travel safety. The other type of regulation is rampant and not as well understood. It comes from existing companies creating moats around their franchises. Regulation often starts with good intentions, but there are many industries that have entrenched themselves behind unnecessary regulation, too.

The most effective way to neutralize that power and influence is twofold: You need to be careful to maintain the moral high ground and be viewed as the underdog, and you need public support.

We enjoy a few of these: People perceive solar to be magical. We also represent freedom from state-sponsored monopolies. It's a great David and Goliath story, which makes for good media.

What is the best advice you've ever received? My CFO told me that when he graduated from Harvard Business School, his professor told him about two-thirds of his class would end up divorced. Clay Christensen, a Harvard Business School professor, studied this effect. When you are driven by accomplishment, you end up staying at the office late each night, because it's easy to measure the resulting accomplishment and the damage to your relationships is very minor. But if you repeat that for years in a row, the compound effects on relationships are real.

What was the most difficult lesson you have learned on the job? The greatest Achilles heel I have had to overcome is how I react when people — myself included — make a forced or careless error: a failure of effort and common sense. I am trying to learn to approach those situations with compassion.

What advice would you give other entrepreneurs on how to build a great business? What scares me right now is that entrepreneurship is in vogue the way finance was in the 1980s and 1990s. But it's really hard. Once, I put on 20 pounds. I got divorced. Entrepreneurs are held up on pedestals today, but it's not a good fit for everyone. I thought all I had to do was work hard and have the right answer. I wasn't prepared for the emotional roller coaster.

If there was one thing that has enabled you to be successful as an entrepreneur, what was it? I try to bring humor to everything.

How do you come up with your best ideas? They show up in the back of my mind when I'm doing something unrelated: spending time in the mountains or listening to music. Even at Burning Man.

What is your greatest achievement? I figured out five years ago the reason I love business is that I approach it like a serious game. I want the company to succeed, but my personal self-worth isn't related to my professional success.

What do you consider your biggest failure? Not spending more time with my family, particularly my sister's family and my mother.

What was your first paying job? I wrote for the newswire at Bloomberg one summer. My desk was 30 feet from Michael Bloomberg.

What are you trying to balance, and how is that working? To stay engaged and happy. I need to operate slightly outside my comfort zone. If I get too far, I become incompetent and things can fall apart. If I stay too safely within my comfort zone, I get bored.

What do you think is the greatest innovation in the past decade? Advances in medicine and biotechnology, like in our understanding of the human immune system. Gadgets and apps are great, but in the end it's health that matters. ▲



Edward Fenster

For the full versions of these interviews and more on entrepreneurs, visit gsb.stanford.edu/insights/entrepreneurship

ALTRUISM

What Makes People Do Good?

How external factors pressure people to cooperate

BY LILY B. CLAUSEN

There's a tendency to think that generosity and cooperation are produced by internal factors like someone's inherent altruism or empathy. However, less often discussed is how external factors actually pressure someone to be prosocial.

For example, says Robb Willer, a Stanford GSB professor, when a manager praises coworkers for pitching in to finish a big project on time, the team leader is setting up cooperation as the norm and rewarding the most generous team members. Regardless of whether these employees are intrinsically cooperative, the manager is shaping the group culture to be more prosocial. In a similar way, studies show people tend to be more generous to charities that publicly praise their donors, he says. Someone might give just enough to receive a "gold level" donation status, which suggests that the desire to achieve these titles is motivating their generous behavior.

In this way, social mechanisms can help create productive and amicable groups of people who work well together.

New research by Willer and University of South Carolina professor Brent Simpson outlines three social factors or mechanisms that promote good deeds: rules, reputations, and relations. Their paper also notes that each of these factors has a potential downside, too, Willer says. "People may come to feel that the cooperativeness and generosity that they are giving and receiving is purely a product of these external factors."

As a result, the mechanisms can create ambiguity for the person performing the act and those benefiting from it. In the simplest of examples, an employee might be left wondering whether his colleague gave him a Secret Santa gift because of a company directive or because she actually wanted him to have the gift.

But even as they obscure others' motivations and their character, on balance these mechanisms produce social benefits, Willer says. After all, even if donors are giving to reach that "gold level" status, in the end they are still funding an important cause.

PLAYING BY THE RULES

Rules that spell out norms and sanctions play a key role in promoting cooperation in groups. In one study, households provided information about the average electricity usage of their neighborhood reduced their usage to fall in line with the neighborhood norm from the preceding weeks.

However, when rules are removed, studies find that people's trust in others can be lower than it would have been had the rule never existed. People can become accustomed to the assurances provided by norms, and when they are taken away, some research shows that previously benevolent people become less cooperative and less trusting of strangers.

AVOIDING A BAD REP

Online marketplaces like eBay, Airbnb, and Yelp are driven in large part by users' desires to maintain good reputations. Positive reputations indicate a history of cooperative interactions and provide useful information about the person's trustworthiness.

And, research shows that those with prosocial reputations are trusted more, they are cooperated with more, and they have more influence. They are picked as partners and group leaders more often. When prosocial reputations are rewarded, cooperative behavior increases.

The downside, however, is that people may become accustomed to having user

reviews as a metric for reputation. They're used to having an information system telling them whom to trust.

CONNECTING THE DOTS

Social networks also shape prosocial behavior. Cooperative people are the ones who are more often centrally located in a social network, extensively connected with other people. They demonstrate higher levels of commitment to the group.

Therefore, making outlying employees more central in workplace networks could encourage the social connections that lead to cooperative behavior. A manager could help develop more prosocial behavior in an employee by seating her with more networked employees or establishing mentorship with a more senior employee. Encouraging denser relationships at work means bringing workers out of isolation and into the social network so they feel that their behavior has meaningful social stakes.

However, such dense social networks can also be detrimental to organizational trust. Group members wonder whether another's cooperation should be attributed to the system, rather than intrinsic good will.

BEING AUTHENTIC

"The more that any of these social mechanisms can be deployed in authentic, organic ways, the less likely people are to say, 'Jane is only cooperating with me because she's trying to get ahead in the organization,' or because she's networking, or because we're in a very artificial team-building exercise," Willer says.

For example, workplace social functions are less effective if initiated by the manager. What's better are worker-established engagements set at times and places that are convenient for the team.

"People are smart and will notice if it's just being done strategically or if it's something you really believe in. They'll figure out if it's this is just a rule of my work place and this isn't a value that's sincerely endorsed by my coworkers and manager." ▲

Robb Willer is a professor of organizational behavior, by courtesy, at Stanford GSB, and a professor of sociology in the School of Humanities and Sciences at Stanford University.



INFLUENCE

Fellow Passengers Have Sway Over What You Buy

Seeing someone make a purchase makes you more likely to do the same.

BY EILENE ZIMMERMAN

If the passenger sitting next to you on a flight buys a snack or a movie, does that make it more likely that you, too, will buy something?

Yes, says, Pedro M. Gardete, a Stanford GSB professor. He examined what's known as social effect — when our behavior is influenced by the behavior of others — by studying one market, items for sale on an airplane during a flight.

Our friends and peers, Gardete says, have plenty of sway over what we buy and when we buy it, but there is still much that marketers and advertisers don't know about the magnitude of that influence. His new research found that when we see someone near us make a purchase, we're 30% more likely to buy something ourselves, and the relevance of that goes far beyond the confines of a plane's cabin, to marketing strategies in a wide array of industries.

Gardete chose the in-flight setting because it is a confined environment, with a variety of items for sale and an abundance of recorded transaction information. In-flight sales fall under the "ancillary revenue" category for airlines, which has seen major growth worldwide. From 1995 to 2013, ancillary revenue — sources such as food, beverages, and in-flight entertainment — grew about 26.5% per year for U.S. airlines, more than five times the airlines' total revenue growth over the same period. Gardete examined the purchase data of 2,000 flights from a major U.S.

Pedro M. Gardete is an assistant professor of marketing at Stanford GSB. "Understanding Social Effects in the In-Flight Marketplace: Characterization and Managerial Implications" was published in the *Journal of Marketing Research*.



“This could be because they share the same tastes or because they are influencing each other.”

airline during January and February 2012. That sample included about 257,000 people who together performed 65,525 purchases, an average of 33 per flight. Because the transactions were made with credit cards, Gardete had precise information about the transactions, including the buyers' flight numbers, seat numbers, what they bought, and what time they bought it.

In order to measure the social effects of purchases by one passenger on other passengers, Gardete set up a quasi-experiment. He looked at consumers in pairs, with each person sitting in the same kind of seat — aisle, window, or middle — and one right in front of the other. He assumed paired passengers were fairly similar because they were seated near each other, in the same type of seat and flying economy on the same flight. One passenger in the pair was in the treatment group, meaning the person observed a purchase by the passenger seated next to him or her. The other person in the pair, the control, was seated in the same kind of seat one row ahead but did not observe a purchase.

Gardete found that passengers were a lot more apt to buy something if someone next to them made a purchase first; in fact, they were 30% more likely to buy after exposure to a purchase than they were before exposure. That did not hold true if they saw a purchase by someone sitting behind them or diagonally in front of them, says Gardete. “It’s only the person next to them that affected them,” he says.

If two strangers could have this much influence over each other, Gardete wondered what would happen with two friends. Those friends, he reasoned, likely share the same tastes because of homophily, which is the tendency people have of associating and bonding with those like them. To test that, he analyzed the purchasing behavior of people traveling together under the same reservation number, assuming they knew each other. He found the likelihood that they will buy doubles if the person who is next to them making a purchase is someone they know. “This could be because they share the same tastes or because they are influencing each other,” Gardete says.

These findings show not only that people pay attention to what their friends buy but also, and perhaps just as important, that someone who has already bought a particular item — before seeing anyone else buy it — is even more sensitive to social influence than someone who hasn’t yet made a purchase. “Even though they’ve already bought something to eat or watched the movie, they remain extremely open to social influence, more so than someone who has bought only from social influence in the first place,” Gardete says. “When people buy a product, they aren’t just signaling they like the product or the experience, but they are telling you they are also more sensitive to promotions and very sensitive to social influence. That’s something that hadn’t been found before.”

Gardete’s findings have important implications for marketers, who are looking for information that tells them how consumers are influenced by their friends and the particular products and services their friends promote. It builds on a shift already taking place in digital advertising toward a reliance on social graphs, where businesses use consumers’ social network

connections to market to them. “This is the bread and butter of marketing companies right now, as they try to find the best way to approach consumers,” Gardete says.

And the best way may be through a consumer’s peer group. If a company sells bicycles, for instance, and you’ve bought an expensive bike, the company knows you’re interested in biking and it’s likely that some of your friends are, too. That’s where the effectiveness of social targeting comes in, says Gardete. As his in-flight research shows, our peers can have a significant influence over whether and what we buy.

The next step, says Gardete, is to look at ways companies can take advantage of social effects. “We know now people are prone to social influence. I’ve documented the features that are necessary for value to exist for companies, but how do they take advantage of that?” he asks. Airlines, for instance, might want to reward their passengers who have made in-flight purchases by sending them vouchers before their next flight or even right after they make a purchase, in real time, says Gardete. “Implementation is a whole side of this that we don’t know much about yet. But it will be an interesting problem to tackle.” ▲

Organizations



“Too often,
a nonprofit’s mission is
too broad and/or
unachievable, like

**‘ending world
hunger’**

or ‘breaking the cycle of poverty.’”

—William F. Meehan III PAGE 34

SKILLS

How to “Lean In” to Power

**Tips for bringing about change in
your career and life**

BY JEFFREY PFEFFER

It's not just women or Asian Americans who sometimes have trouble doing things such as advocating for themselves and their accomplishments, negotiating for salary and job responsibilities rather than just accepting what employers offer, networking, and not obsessively worrying about being liked — all things that bring increased power. Many people are uncomfortable with power and the behaviors required to obtain it. That's a big problem, because research shows that power skills and behaviors matter for career success.

Florida State professor Gerald Ferris and colleagues have carefully developed and validated a political skills inventory (available at www.jeffreypfeffer.com with Ferris' permission) that people can use to assess themselves (or better yet, have others assess them) on a set of political skills that include networking ability, social astuteness, apparent sincerity, and interpersonal influence. More importantly, Ferris and others have conducted numerous studies over the years that demonstrate the important relationship between political skill and career success and also political skill and group performance.

Jeffrey Pfeffer is the Thomas D. Dee II Professor of Organizational Behavior at Stanford GSB and the Hank McKinnell-Pfizer Inc. Faculty Fellow for 2015-2016. His new book, *Leadership BS: Fixing Workplaces and Careers One Truth at a Time*, was published this year by Harper Business.

Photograph by Jonathan Sprague

JEFFREY PFEFFER
Power skills
and behaviors
matter for career
success.



Contrary to what you may think, good job performance is not going to be enough to rocket your career ahead. After all, the numerous studies that show salary and promotions are affected by things such as race and gender, educational credentials, and years of experience — none of which are dimensions of job performance — make the point that the world is not always a just and fair place, and it takes more than doing a good job to be successful.

In my *Paths to Power* class and my book *Power: Why Some People Have It — and Others Don't*, I encourage people to take actions that are likely to increase their power and, as a consequence, their careers:

NETWORK

Spend more time building social relationships. Figure out who in your company, industry, and in even more distant and diverse environments might be helpful in your career. Make a list of those people and prioritize it. Then figure out a way to meet those people, ranging from “cold” emails to facilitated introductions to finding common organizations (including nonprofits) where you might connect.

“People often believe that political skill is something one has as part of one’s personality.”

Take on small but important tasks that can put you at the center of communication networks. Ascertain which people or groups might benefit from being connected — and connect them. (The technical term for this is filling structural holes, and Ronald Burt at the University of Chicago makes available network diagnostic tools.) And most important, recognize that weak ties are more valuable for job performance and careers than stronger relationships. That’s because weak ties provide you nonredundant information, while the people to whom you are most strongly tied, close friends and colleagues, probably know approximately the same things and the same people as you do. Therefore, they do not add as much additional value.

BUILD PERSONAL QUALITIES

Energy, the ability to tolerate conflict, the capacity to see others’ points of view and interests, resilience, and ambition, among others, are qualities that produce power. To accomplish this journey of personal development and growth, find a coach, a peer, or create a small “personal board of directors” of three to five individuals who are not likely to be competitive with you to provide advice and counsel — and hold you accountable — on your self-assessment of strengths and weaknesses and your plans to build the qualities that you need more of.

LEARN HOW TO ACT AND SPEAK WITH POWER

Body language is important, because we form impressions of others quickly and then subsequently assimilate information based on these first impressions. Use emotion-producing, vivid language and stories to convey your message. Use forceful, powerful gestures. Speak loudly and don’t raise your voice at the end of statements, implying a question rather than an assertion. To build your skills, get an acting, voice, or language coach if you need help, and find situations where you can practice.

CHALLENGE CONVENTION

Understand and then act on the insight that particularly if you are an underdog, breaking the rules — which are, after all, mostly set by those in power — is essential to winning. This idea was explored in Malcolm Gladwell’s wonderful *New Yorker* article, “How David Beats Goliath.” Moreover, since the powerful have the discretion to not conform to social conventions, breaking the rules can signal — and thereby create — power.

People often seem to believe that political skill is something one has as part of one’s personality — like the master politician, the late President Lyndon B. Johnson, so beautifully described in the set of biographical books by Robert Caro — or not. But that is not true. Without for a moment denying the existence of individual differences, political skill, like virtually all skills, can be improved through practice and coaching. So don’t accept your current set of strengths and weaknesses or, for that matter, your current tastes and preferences, as fixed and enduring.

Building power and influence skills is not about changing who you are or becoming someone else. It is about adding a set of activities and skills to your repertoire to become more effective and successful. So stop making excuses and get on with it. ▲



MAKING HOME Over 500 volunteers from around the world worked on 36 houses near Chitwan, Nepal.

GIVING

A Nonprofit Amplifies Its Impact

Jonathan Reckford has pushed Habitat for Humanity into advocacy, disaster relief, and sustainability.

BY IAN CHIPMAN

Jonathan Reckford's career road map has been a circuitous one. It includes a stint on Wall Street, executive and managerial positions in the corporate sector, coaching the Korean Olympic rowing team, and time as an executive pastor.

But when he was asked in 2005 to consider becoming the next leader of Habitat for Humanity, everything snapped into place. "I remember the shot of adrenaline going down my spine when I got that call," Reckford says. "Habitat for Humanity integrated my faith and my work in a very complete way."

In the 10 years since Reckford took the reins as CEO of Habitat for Humanity, he has led a steady amplification of the organization's impact. He helped widen the scope of Habitat's mission to include holistic neighborhood revitalization, in response to the housing crisis of 2008, and formal disaster relief efforts, following the Indian

Jonathan Reckford is the CEO of Habitat for Humanity. He received his MBA from Stanford GSB in 1998.

Ocean tsunami of 2004 and Hurricane Katrina in 2005. He has overseen new microfinance and advocacy initiatives to help the neediest populations secure loans and access to land. Under his leadership, the nonprofit's housing-product recycling enterprise Habitat for Humanity ReStores kept more than 128,000 tons of materials out of landfills and generated \$110 million in profits, used to build more homes.

All the while, Habitat's core model of helping family after family build one life-changing home at a time has flourished. He has seen the number of families that partner with the organization grow more than tenfold over the past decade, from

25,000 per year to more than 300,000 in fiscal year 2014.

"I have met so many families all across the world and seen how the process of earning their home and helping build it has really changed their self-identity," Reckford says. "There's a mindset shift. Rather than being a victim, now someone has a whole different identity. Habitat families are now property owners and taxpayers, adding economic value to the community. I love seeing that transformation."

Here, Reckford, a 1998 MBA graduate, shares three stories in his words that speak to that elemental power of a home to transform lives and communities across the world.

CAMBODIA

The tangible aspects of being in a safe home are better health, better educational outcomes, better livelihood prospects. But there are also intangible aspects, like being able to feel safe. We tend to take it for granted that you can lock the door.

Last year, with my daughter and a group in Cambodia, Habitat built a home in partnership with a woman named Soy Lorn and her family. Her husband had HIV/AIDS and eventually died from it. The family lived in a one-room shack with no electricity, no water, no sanitation, next to a garbage dump over a sewage pool.



BREAKING GROUND A group of Habitat for Humanity volunteers frame a home in Fort Worth, Texas.

And ultimately they couldn't even afford to live there, so they were literally squatting on the street under a tarp.

We were in Phnom Penh. It rains really hard in Cambodia. Soy Lornng told me that the night before we finished their house, it had just poured rain. She actually spent the night standing up — trying to hold the tarp from ripping apart and trying to keep her two kids and her mom dry along with all their belongings.

We dedicated their house, and just as we cut the ribbon, a big storm blew in. It started pelting down rain. She invited us into her new room, and we were all sitting on the floor that had just been finished. I watched



Sam Dean

as she and her daughter were looking around the walls and the ceiling to see if the water was going to come in. Great smiles broke out on their faces when they realized they were going to be safe from the elements. For the first time, instead of thinking, “Can I survive?” those children can begin to think about having a future. That’s why we build.

BOLIVIA

Primarily, single-family homeownership has been the heart of Habitat. But recently, we’ve gone into advocacy in a bigger way. The fact that we build in all these places gives us the credibility to influence the policy environment, so we’ve become very active in trying to impact housing policy, specifically.

We worked for about five years with Habitat Bolivia to impact the ability for women to own property. In Bolivia, women did not have the right to own their houses or their land. You can think about all the issues that come with that in terms of economic empowerment — or disempowerment.

We trained a cadre of mostly women and some men on how to work the legal process to try to get title. That group not only got title, they got the laws changed, which means that 1.8 million people were impacted. We’ve since trained more than 400 people in the legal pathways and processes to secure land and property rights. While we’ve still got to help them move from being enabled to actually getting title, that creates the environment where Habitat and other groups can help these families get the right to their property. So we’re doing a lot of work particularly around access to land for housing and property rights protection for the poor and vulnerable around the world.

NORTH CAROLINA

In the town of Winston-Salem, N.C., a couple hours from my hometown, there is a neighborhood called the Cherry Street community. This was a historically African-American community, architecturally important, in a great location near downtown. But for decades it had been going downhill — and then when the recession hit, things got worse yet.

The local Habitat affiliate interviewed the families there and found that what they really wanted was, first, for the community to be a place where young families would move back in again — instead of escaping the first chance they got. And, second, they wanted to do something about the extremely high crime rate and issues with drugs.

Habitat built a coalition with the community organization and made a commitment to tear down and rebuild 16 homes to change the visual look at the entrance to the community. Because of that commitment, private developers bought up other houses and rehabbed them as rental housing. Another nonprofit rehabbed some old, architecturally important rental housing into new, green rental housing. Then we got a commitment for a new charter school. The city agreed to increase the police presence in the community. And finally a wealth of faith organizations, the university, and others came out and participated.

I visited two years into the project, and I remember a policeman named Billy who walked me around. He stopped me and said, “You know, if you’d come here two years ago, I’d be here to protect you.” Then, with a big sweep of his arm, he said, “Now look what we’ve done.”

The before-and-after pictures are fairly breathtaking. Crime was already down 70% in the community. The charter school was doing really well and had a dynamic principal. Vacancies were down. Families were starting to move back in.

Now progress has continued, and the revitalization effort has expanded from a 4-block area to 120 blocks. The city manager told me — and I love this — he said, “You know, sometimes I get depressed. When I get depressed, I drive through Cherry Street just to be reminded of what’s possible.”

What fires me up, and I’m very blessed, is interacting with the families. That’s when it becomes personal. We can get overwhelmed by the statistics. Thinking about hundreds of thousands of families that we’re helping this year, you can’t really relate to that. But when it becomes personal and you actually work alongside and talk to a family, this is what motivates me.

A very good friend of my goddaughter house-sat for us while my wife and I went to a wedding. When she found out what I did, she told me, “You know, I grew up in a Habitat house.”

Now she’s pursuing her PhD in psychology and wants to help disabled children, particularly. When she was younger, she and her family got bounced all around. When she was 13, her mom was able to partner with Habitat and purchase a home. And she said that it fundamentally changed the trajectory of their life.

It’s those important little moments that can keep me doing this forever. ▲

PERSONALITY

In IPO Road Shows, the Messenger Is the Message

A CEO's presentation style can influence the valuation of a company.

BY LEE SIMMONS

When a firm is ready to go public, top executives head out on a “road show,” along with the company’s underwriters, to promote the stock offering. The information presented is little different from what’s in the prospectus (the lawyers make sure of that). Yet hotel conference rooms are packed with analysts and fund managers jostling for the best seats.

The lure of a free breakfast? No, they come to watch the CEO in action. Bill Whelan, head of the securities practice at law firm Cravath, Swaine & Moore, says institutional investors want to look the company’s leader in the eye and see how they handle an audience. “The most important takeaway” from the road show, he says, “is the impression they get from management.”

But do those subjective impressions actually affect stock price? Or, with all the hard information available in an IPO filing, do investors factor out personalities and focus on the financials? It’s a question that business scholars have long debated, and it’s exceptionally difficult to test. After all, you can’t run regressions on investors’ thoughts.

But Stanford Graduate School of Business professor Elizabeth Blankespoor and her coauthors, Greg Miller of the University of Michigan and Brad Hendricks of the University of North Carolina, have come up with an elegant solution, drawing on recent work in psychology. Their findings, reported in a paper, are unambiguous: The more favorably the CEO is perceived, the higher

the firm’s valuation — and that holds true at every stage of the IPO process.

The results underscore just how important the road show is to investors as a source of information. And for companies planning a road show, the message is clear: It’s not just what you say that matters, it’s also who says it and how well.

READING **INVESTORS' MINDS**

Managerial ability is often cited as a major concern of investors. In the case of firms that are already publicly traded, opinions about the CEO are formed and revised over time as new information trickles out. That makes it especially hard to isolate the effect of those opinions on stock price — it’s never clear who thinks or knows what, when.

In that respect, Blankespoor says, IPOs are an ideal laboratory: “For most investors, the road show is the first time they’ll see the CEO. And they all watch the same presentation within a roughly two-week span,” after the setting of an initial proposed price and before the revision to a final offer price. “That makes for a tight link between perceptions and valuation,” she says.

Still, investors aren’t about to share their conclusions publicly. So Blankespoor and her colleagues drew on insights from psychology to devise a clever proxy: By narrowing their focus to basic personality traits, as revealed through body language and other nonverbal cues, they were able to substitute ratings gathered from disinterested individuals after viewing short videos.

“The idea is we all form judgments of others rapidly and almost unconsciously,” Blankespoor says. It’s that intuitive cognition journalist Malcolm Gladwell wrote about in *Blink*; psychologist Daniel Kahneman calls it System 1 thinking. It might not be a good way to assess a CEO’s strategic vision, but these quick takes are surprisingly accurate at sizing up strangers in social situations. And because it’s a universal capability, the judgment of any random person should be similar to that of an investor.

Following this hunch, the researchers assembled 30-second video clips from 224 actual road show presentations

Elizabeth Blankespoor is an assistant professor of accounting at Stanford GSB and the R. Michael & Mary Shanahan Faculty Scholar for 2015-2016.



ELON MUSK, TESLA;
RANDY GARUTTI,
SHAKE SHACK;
NICK WOODMAN, GOPRO;
MARK ZUCKERBERG,
FACEBOOK

between 2011 and 2013. To zero in on expressive behavior, they filtered the audio to render the words unintelligible while retaining vocal pitch and rhythm. “It’s like the teacher in *Peanuts* cartoons,” Blankespoor laughs, “where they go, ‘Wah-wah-wah-wah.’”

The team then hired people on Mechanical Turk, a crowdsourcing task website, to rate the speakers for competence, attractiveness, and trustworthiness — attributes that previous work had shown are valued in a leader. At least 40 people viewed each video, and their scores were averaged. Finally, the three attribute scores were combined to yield a single composite index of perception for each CEO.

PERSONALITY MATTERS

To be sure, that number captures only some of what you’d look for in a CEO, but it doesn’t need to be complete. Think of it as the informational equivalent of the fluorescent dyes used as markers in biological tests: If even this partial, proxy variable has a measurable effect on shares, it proves that investors do fold subjective assessments of management into their valuations.

“Investors are gleaning information about the CEO from their nonverbal behavior.”

And that’s just what the analysis shows: After controlling for other factors that could affect stock price — including data about the CEO such as age, experience, and education — firms with CEOs who rate higher in these seemingly superficial personal assessments receive a larger price bump from the road show. For example, raising the perception score of an average CEO by just 5% yields an 11% boost in final market price.

Not only that, those firms attract more prestigious underwriters to start with, and they begin the road show with a higher proposed offer price, indicating that the underwriters make similar assessments. Likewise, at the end of the IPO process, those firms have a higher price after the first day of public trading — a final shout of “amen” from the broader market.

“This is the first study to examine how information learned during the road show influences IPO pricing,” Blankespoor says. “Institutional investors often say how valuable it is to get a feel for the management team in person, and now we have empirical evidence to quantify that.”

Interestingly, the researchers also ran separate regressions on each of the three attributes rated. While they found that the CEO’s perceived competence and attractiveness had a significant impact on firm valuation, trustworthiness on its own had no effect. “Maybe investors are relying on the SEC and auditors to cover that one,” she muses.

FIRST IMPRESSIONS ARE EVERYTHING

On the surface, these are rather astonishing results. After all, snap judgments of an executive’s podium manner would seem to be a very loose indicator of future profitability and growth.

But Blankespoor points out that much of a CEO’s job is communicating with stakeholders such as employees, customers, and suppliers. “A leader has to be able to command attention, persuade, and motivate people,” she says. “So personal presence, even just the ability to make a strong initial impression, is important. In a way, they’re constantly making first impressions.”

And studies in other fields have shown that our quick, intuitive judgments of people often predict future outcomes — for instance, in debt repayment, political elections, and medical malpractice. “The linkage between CEO behavior and firm performance isn’t as direct,” Blankespoor says, “but this literature demonstrates just how information-rich that thin slice of behavior is.”

So are investors right to incorporate subjective assessments of CEOs? If not, any resulting price premiums would dissipate over time. To check for this, the researchers also looked at stock prices up to a year after the IPO. They found no correction, suggesting that those assessments were not only accurate but also predictive of the company’s near-term success.

“It means investors are gleaning real additional information about the CEO from their nonverbal behavior,” Blankespoor says, “and, further, that perceptions of management are signals for firm value.”

KEEP IT REAL

But can’t a CEO fake it? After all, road show presentations are rehearsed and vetted like presidential stump speeches, and executives are coached on their speaking skills. “That’s true,” Blankespoor says, “but most of our expressive behavior is unconsciously generated. That’s why it’s a good signal — it can’t easily be manipulated.”

Still, she adds, if you’re a CEO preparing for a road show, training may be helpful. It won’t fool investors into seeing you as something you’re not, and that should never be the goal. But it may bolster your confidence and help you relax, so your own true qualities shine through.

Indeed, if the road show is in some ways a performance, executives might take a cue from theater: Good actors don’t “put on” a character; they find it in themselves. So when you get up in front of that audience, know yourself, be yourself, and show them who’s boss. That’s what they’ve come to see. ▲

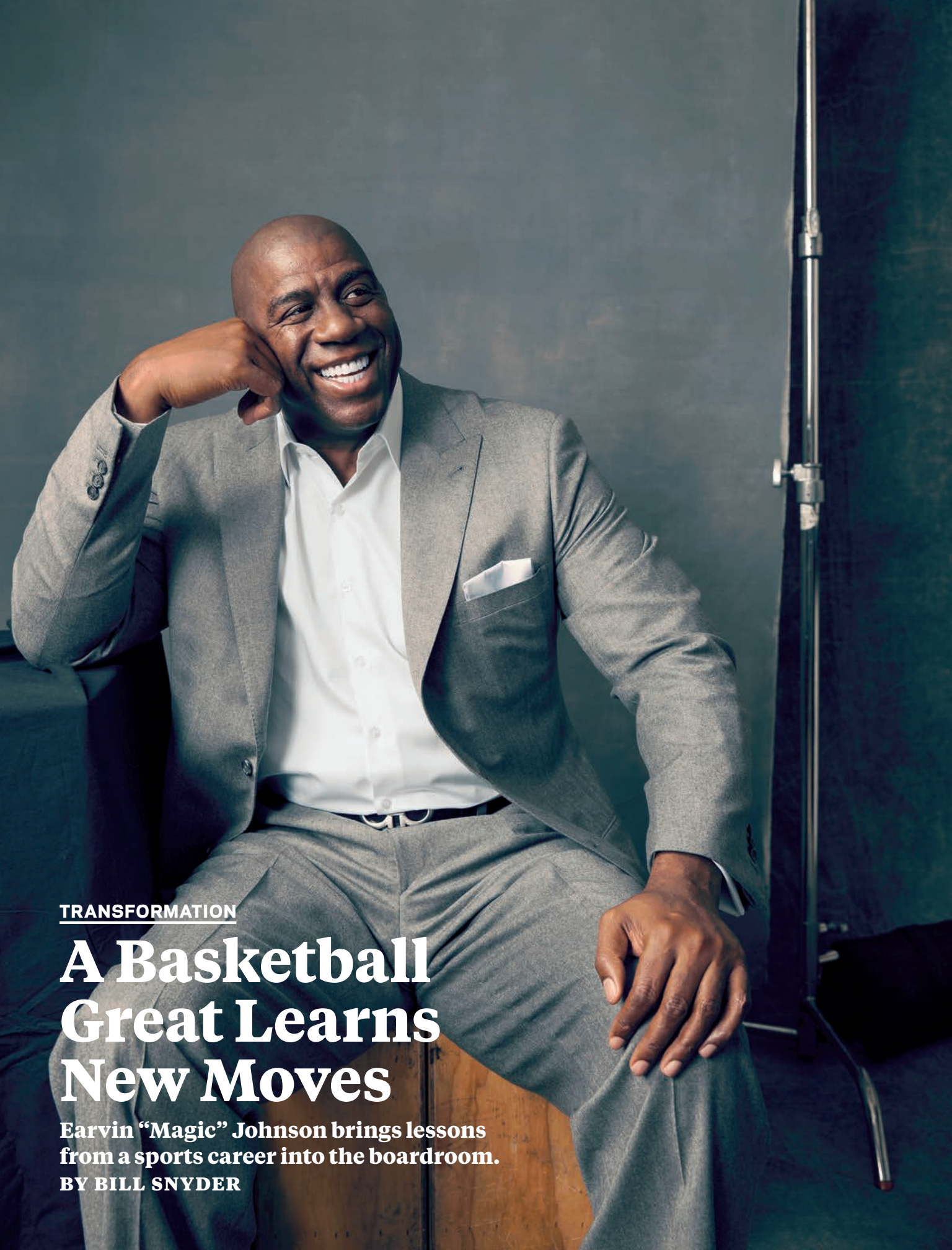
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TRANSFORMATION

A Basketball Great Learns New Moves

**Earvin "Magic" Johnson brings lessons
from a sports career into the boardroom.**

BY BILL SNYDER

The competitive drive that made Earvin “Magic” Johnson a 12-time NBA All-Star is powering his success in the business world. Nearly 20 years after hanging up his sneakers, Johnson’s net worth is a reported \$500 million, he owns parts of the Los Angeles Lakers and the Los Angeles Dodgers, and he’s the CEO of Magic Johnson Enterprises, a billion-dollar conglomerate, according to *Fortune* magazine.

His focus, though, goes well beyond making money. He wants to have an impact in the minority community. Johnson’s businesses have employed thousands of minorities and illustrated how profitable it can be to bring movie theaters, coffee shops, and other services to underserved urban areas. The Magic Johnson Foundation, founded in 1991, has provided free HIV/AIDS testing to more than 38,000 people, awarded over \$3 million in hardware and software grants, and provided educational services to over 250,000 young people. “Always remember that you can only change things when you’re successful,” he told a group of Stanford Graduate School of Business students recently.

Johnson’s pivot from basketball to business was, of course, made easier by his superstar status, but once he became an entrepreneur it was his ideas, he says, not his fame that investors and potential partners judged. His time on the basketball court taught him valuable lessons about focus, strategy, and discipline, he says.

Here are five lessons on becoming a business leader that he shared during a View From the Top talk in October.

GET IN THE ROOM WITH THE RIGHT PEOPLE

Johnson knew that he wanted to become an entrepreneur when he retired from basketball, but he realized that “what made me a great basketball player wouldn’t make me a great CEO.” His first step was to take his ego out of the game and acknowledge that he needed instruction. Johnson made lunch dates with 20 successful people and proceeded to pick their brains. “I got in the right room with the right people, and made sure I got experts in business to be my mentors and then made sure that I applied what I learned from them,” he says.

EXPECT TO BE TURNED DOWN

CalPERS said no to Johnson four times when he asked the pension fund for capital to invest in minority communities. On the fifth visit, CalPERS relented and invested \$50 million. “You’re going to get turned down. Somebody’s not going to like your business plan,” says Johnson. “But if you’ve done your homework and your research, and you find that you have a good chance to be successful with your business, keep going.”

“Always remember that you can only change things when you’re successful.”

BE READY TO CHANGE COURSE

Shortly after Johnson’s real estate fund constructed condos, the market crashed and it was impossible for prospective buyers to secure loans. Rather than wait out the recession, Johnson shifted the business model and began renting the units. “Make sure you’re quick and nimble enough to say, ‘You know what? I can adapt and adjust to what’s going on in the marketplace today. I can change my business or tweak my business to make it still work.’”

FIND A NEED

Because retail options were scarce in minority communities, people would often drive for 45 minutes or an hour to shop or go to the movies. So Johnson decided to start opening movie theaters. Adding services to those neighborhoods helped the community — and made Johnson’s businesses succeed because “I was able to understand what we [the minority community] wanted,” he says.

UNDERSTAND YOUR CUSTOMER BASE

Johnson has owned restaurants and coffee shops in minority neighborhoods, including 125 Starbucks cafes. They succeeded because prices were reasonable and they appealed to the tastes of those communities. “I had to take the scones out of my Starbucks and put in sweet potato pie, pound cake, sock-it-to-me cake, peach cobbler.” His TGI Fridays franchise in Los Angeles served Dom Pérignon, Cristal, and other high-end liquor, the first Fridays location to do so. “It succeeded because that’s what my customer base wanted,” he says. ▲

Earvin “Magic” Johnson was inducted into the Naismith Memorial Basketball Hall of Fame in 2002. He visited Stanford GSB in October to deliver a View From the Top address.

STEWARDSHIP

How to Be a Better Nonprofit Board Member

Apply the fundamentals of sound governance to charitable work.

**BY WILLIAM F. MEEHAN III AND
KIM STARKEY JONKER**

The importance of the nonprofit sector has never been greater. In the United States, there are several hundred thousand 501(c)(3)s that provide much of our health care, education, performing arts, and social services. In this environment, nonprofits face pressure to grow, and have few new proven business models to help.

There, too, is an ever larger demand on nonprofit executives and board leaders to do more fundraising.

Meanwhile, volunteer nonprofit board leaders, who are often unsure how to leverage their skills and contribute their leadership, often struggle with how they and their board colleagues can be most effective.

An old Sicilian proverb says, “Fish rot from the head.” Many nonprofits are rotting from a lack of leadership at their heads: their boards of directors.

Basic roles and responsibilities for board members that can seem like common sense — evaluating staff and impact, becoming deeply familiar with the operations of the nonprofit, and fundraising — are not widely practiced.

Previous research I’ve done with Stanford GSB Professor David F. Larcker, lecturer Nicholas Donatiello, and researcher Brian Tayan confirmed that many nonprofit boards have serious challenges. A survey of 924 nonprofit directors, conducted by the Rock Center for Corporate Governance and Stanford GSB in collaboration with GuideStar USA and BoardSource, found that:

- 27% of board members don’t think their colleagues have a strong understanding of the mission and strategy.
- 65% don’t think their board is very experienced, and about half don’t think their colleagues are very engaged in their work.
- 46% have little or no confidence that the performance data they review accurately measures the success of their organizations.

At their best, boards of directors help organizations head down the right strategic

path — to make good choices about program areas and geographic locations, and recruit skilled executive directors and get rid of bad ones. Weak board governance, on the other hand, keeps nonprofits from reaching their full potential and ultimately may even cause a nonprofit to struggle and die.

Good directors must do a few things to help a nonprofit organization excel — but they have to do them bravely, rigorously, and consistently.

Here are some suggestions:

ENSURE THE MISSION IS FOCUSED AND WELL UNDERSTOOD

Too often, a nonprofit’s mission is too broad and/or unachievable, like “ending world hunger” or “breaking the cycle of poverty.” Narrow your mission’s focus to fit the skills and resources you have or conceivably build on your existing ones.

The mission also must be understood and embraced by the board, management, and other key stakeholders. We invariably find an underperforming nonprofit has a mission that is not well understood or understandable — including and especially by the board.

William F. Meehan III is the Lafayette Partners Lecturer in Management at Stanford GSB. He and Kim Starkey Jonker, executive director of the Henry R. Kravis Prize in Nonprofit Leadership, are authors of *Fundamentals, Not Fads: A Roadmap for Transforming the Nonprofit Sector for Executives, Board Leaders and Philanthropists* published by Stanford University Press.



“Goal-setting efforts should be tied to compensation and performance evaluation.”

ASK STUPID QUESTIONS UNTIL YOU FIGURE OUT THE SMART ONES

It’s shocking how difficult this one is for many of us, because it goes against human nature. We don’t like to look stupid in front of our peers and, for many people, serving on nonprofit boards is a way of networking with their social or business peers.

If board members don’t engage directly and deeply in the substantive work of an organization, then board meetings degenerate into staff-driven, pre-baked exercises: “Finance Committee report; Development Committee report; blah, blah, blah.” Most board members, of course, are bright people with a wealth of experience. But they often lack specific expertise in the day-to-day work of their board’s organization and are unconfident that experience is relevant. Just get started asking questions and find out.

MAKE FIELD VISITS

To be truly effective, members of a nonprofit board must engage directly and deeply, and this often includes traveling to the field. Take Helen Keller International, recipient of the 2014 Kravis Prize, which honors leadership in the nonprofit sector. “HKI is somewhat unusual in that we required our board members to visit our programs in Africa and Asia at least once every three years,” Kathy Spahn, CEO, explains. “They learn that dispensing a vitamin A capsule is not as simple as it sounds!”

INSIST ON IMPACT EVALUATIONS

There is a sector-wide virus of too little evaluation, and boards are largely to blame because they allow and enable nonprofits to operate without impact evaluations. Boards must insist on impact evaluations (and funders, by the way, must be more willing to pay for them). If a nonprofit can’t demonstrate that programs work, why should anyone provide funding? Complaints by executive directors about an excessive focus on evaluation are largely a smoke screen and board members should recognize them as such.

This should also include an evaluation of the leader of the nonprofit. Many boards of directors neglect this most basic responsibility, especially when a powerful, passionate founder is serving as executive director. We suggest a fairly simple evaluation process. At the end of the year, the board chair plus one or two others should agree with the executive director on the goals for the organization over the next year. Then at the end of the following year, there should be a discussion with the chairman and the executive director about which goals have been achieved. These goal-setting efforts should be tied to compensation and performance evaluation.

DEVELOP A SUCCESSION PLAN

Part of your job as board member is also to ensure a succession plan. Start early; even 10 years or more is not too long when it comes to a founder’s leadership transition. At Landesa, a nonprofit focused on land rights for the world’s rural poor, leaders identified Tim Hanstad as the future replacement for founder and chief executive Roy Prosterman in 1992 — but Hanstad didn’t officially become president and CEO until 2005. During the intervening 13 years, Hanstad served as executive director.

CREATE A STRONG BOARD COMPOSITION

Many wonder what the right size for a board is — and there is no specific answer. This is the *sine qua non*: Every nonprofit board needs a small group of highly committed and cohesive leaders. If there is a board of 12 to 15 people, then the organization needs two to three seriously engaged, talented members spending most of their time and generosity focused on the organization. These people get the lion’s share of the work done. A larger board of 35 or even 75 likely needs a dozen or so highly engaged board members to be effective.

As for the overall size of the board, there’s no particular number that is perfect. Look for at least one, and maybe two or three, of the three W’s — the ability to contribute work (time, energy, advice), special knowledge or skills that translate to wisdom, or wealth — in each member. Also, be rigorous in not renewing those board members who not contributing. Even effective nonprofit boards will have 10% to 15% members who aren’t contributing. Having more than that risks a board culture that reinforces low commitment as the standard, acceptable behavior.

While generosity and fundraising outreach are essential for every nonprofit board overall, not everyone on the board must be a person of financial means. Nonprofits need to represent the diverse aspects of society and respect other important leadership contributions. That said, there is no good reason that 100% of all board members can’t contribute financially at some level.

If you have asked or volunteered to serve on a nonprofit board, chances are good that you know the fundamentals of governance from work elsewhere. Bring them into your work as a board member; they will lay the foundation for the kinds of innovation and scaling up that can solve your community’s — perhaps even the world’s — problems. But innovation and growth demand the fundamentals of good governance. ▲



RESEARCH DRIVERS VC-backed companies like Genentech are among the world's most innovative.

ECONOMY

Study Measures the Impact of Venture Capital

Most VC-backed companies fail; others change the world.

BY ILYA A. STREBULAEV AND WILL GORNALL

Over the past 30 years, venture capital has become a dominant force in the financing of innovative American companies. From Google to Intel to FedEx, companies supported by venture capital have profoundly changed the U.S. economy. Despite the young age of the venture capital industry, a fifth of current public U.S. companies received venture capital financing.

Venture capital (VC) is a high-touch form of financing that is used primarily by young, innovative, and highly risky companies. Venture capitalists provide not only financing but also mentorship, strategic guidance, network access, and other support. These investments are

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highly speculative — most of the companies that receive VC funding will fail, even as some become runaway successes. Three out of the five largest companies in the world received most of their early external financing from VC.

Clearly, Apple, Google, and Microsoft are among the most innovative and most important companies in a generation. But how important are these and other VC-backed companies to the U.S. economy? How do they compare with industrial behemoths such as General Motors or massive financial institutions such as Bank of America in terms of job creation and overall economic impact? We set out to quantify the long-term impact of VC on the U.S. economy. We started by classifying companies as either VC-backed or non-VC-backed, considering only public companies that are traded on major U.S. stock exchanges. While most successful VC investments end with the company being acquired, reliable information is currently available only on those companies that become publicly listed. Thus, our results likely underestimate the impact of VC on the economy.

We labeled a company as VC-backed if it was financed in its early stage by a VC fund. Our starting point is the classification used in Thomson One data. We cross-

checked that with IPO data constructed by University of Florida professor Jay Ritter. We then manually checked more than 200 companies that together represent more than 80% of the market capitalization of the VC-backed companies.

As of December 2013, our sample of public companies had 4,063 firms with total market capitalization of \$21.3 trillion. Of those, 710, or 18%, of the companies are VC-backed. Their total market capitalization is \$4.3 trillion (20%). These companies tend to be young and fast growing, which explains why their revenue is a relatively smaller fraction of the revenue of the total sample (10%), but their research and development is 42% of the total. That is more than a quarter of the total government, academic, and private U.S. R&D spending of \$454 billion. They also employ 4 million people.

This exercise both understates and overstates the importance of VC. We overstate the importance of VC funding to the extent that successful VC-backed companies may well have been successful even without VC financing. Of course, the fact that so many successful entrepreneurs choose VC financing suggests that this financing plays an important role in the entrepreneurial ecosystem.

On the other hand, we understate the importance of VC financing because we ignore the positive spillovers these firms create. From Windows to FedEx, the technologies developed by VC-backed firms have changed the world beyond.

Another major way our previous analysis understated the importance of VC for today's young companies is because so many public companies were founded before the VC industry even existed. For example, Ford and General Electric were founded more

than 100 years ago. While a number of well-known companies were funded by the first generation of the venture capitalists starting in the 1950s, the U.S. VC industry came into its own only after a regulatory change in 1979 that allowed pension funds to invest in VC. That rule change, known as the Prudent Man Rule, led to a greater than tenfold increase in the money entrusted to VC funds: VC funds raised \$4.5 billion annually from 1982 to 1987, up from just \$0.1 billion 10 years earlier.

To level the playing field, we redid our analysis using only those companies founded during or after 1979. The idea here is to see what portion of the companies that could have received VC financing chose to use VC financing. This exercise excluded the likes of Ford and General Electric, and focused on companies founded since the regulatory changes.

This analysis changed the results dramatically. Of the currently public U.S. companies we have founding dates for, approximately 1,330 were founded between 1979 and 2013. Of those, 574, or 43%, are VC-backed. These companies comprise 57% of the market capitalization and 38% of the employees of all such “new” public companies. Moreover, their R&D expenditure constitutes an overwhelming 82% of the total R&D of new public companies. Given that the VC industry has been in large part spurred by the relaxation of the Prudent Man Rule, these results also provide an illustration of the impact that changes in government regulation can have on the overall economy.

Our results also suggest that the VC industry has leveraged a small amount of capital — when compared with the private equity industry — into investments that resulted in a large number of important companies.

Over the past 50 years, the U.S. VC industry has raised \$0.6 trillion and made its investments from that pool. Over that same period, the private equity industry raised \$2.4 trillion — four times as much. In 2014, the private equity industry raised \$218 billion, almost 10 times the \$31 billion raised by the VC industry. In fact, VC funds invest in only 0.19% of new U.S. businesses.

VC-backed companies include some of the most innovative companies in the world. To get an idea of the importance of these companies, it is instructive to look at research and development. In 2013, VC-backed U.S. public companies spent \$115 billion on research and development, up from essentially zero in 1979. These VC-backed companies now account for 42% of the R&D spending by U.S. public companies. That R&D spending produces value for not just those companies, but also the entire world through positive spillovers.

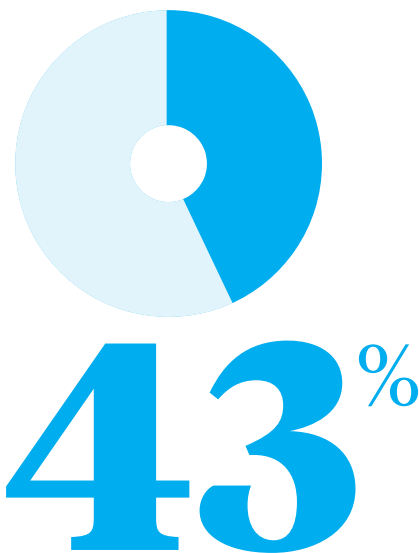
VC-backed companies make up a consistently high fraction of those companies undergoing initial public offerings. Between 1979 and 2013, over 2,600 VC-backed companies had their initial public offerings. They made up 28% of the total number of U.S. IPOs during that period. The percentage of initial public offerings that were VC-backed varies by year. That percentage reached a high of 59% during the dot-com boom, but has been greater than 18% in each of the last 20 years.

The VC industry specializes in investing in innovative companies with a huge potential for growth. Because these investments are risky and most of these companies fail, VC funds seek to invest

“In 2013, VC-backed U.S. public companies spent \$115 billion on research and development, up essentially from zero in 1979.”

in companies where small investments can generate huge returns. That naturally leads to a focus on certain industries. The industries most impacted by investment have been technology (for example, Apple, Google, or Cisco), retail trade (Amazon, Starbucks, or Costco), and biotechnology (Amgen, Celgene, or Genentech). Industries with higher capital needs, such as finance and primary industries, have seen relatively few VC successes. The small, targeted investments VC funds make are a poor vehicle to finance capital-intensive projects, such as real estate development or mining. While the technologies that VC-backed companies developed have transformed many of those industries as well, our current analysis does not allow us to study that indirect impact.

VC-backed companies play an increasingly important role in the U.S. economy. Over the past 20 years, these companies have been a prime driver of both economic growth and private sector employment. VC-style financing is not the sole reason these companies succeeded; in fact, VC was not even the sole source of financing for many of these companies. However, large and growing fractions of entrepreneurs are choosing VC financing. These entrepreneurs think VC financing is the best way to grow their companies. That makes it clear that VC is an important part of the innovation ecosystem and has helped some of the world’s most successful companies to grow. ▲



Percentage of public U.S. companies founded since 1979 that are funded by venture capital



SOCIAL ENTERPRISES A Massachusetts nonprofit provides employment training for high-risk young men in the juvenile justice system.

INVESTMENT

Making Money While Doing Good

Social impact investing is changing the way philanthropy is done.

BY THERESA JOHNSTON

Social impact investing takes many forms these days. Investors can bring capital to worthy causes that otherwise wouldn't be funded by investing in privately held businesses or engage with other shareholders to put pressure on less socially motivated companies. They, too, can make so-called "sacrificial" investments in innovative social enterprises by accepting below-market, risk-adjusted returns as the price for doing public good.

But vetting both the philanthropic causes and the potential financial returns takes work, says Paul Brest, emeritus dean and professor at Stanford Law School, who discussed impact investing with *Stanford Business* following a May symposium sponsored by the Center for Entrepreneurial Studies at Stanford Graduate School of Business.

DON'T IGNORE GOVERNMENT PROJECTS

Brest is particularly intrigued by a relatively new type of social impact investing in which investors put up the initial capital for innovative government pilot programs. Such pay-for-success contracts, also known as social impact bonds, started about a decade ago. They are allowing governments to experiment with new ways of dealing with chronic social problems.

One such project, the Massachusetts Juvenile Justice Pay-for-Success Initiative, was launched in summer 2012 by then-Governor Deval Patrick. At the time, two-thirds of the young males caught up in the commonwealth's juvenile justice system were landing back in jail within five years. So Massachusetts hired a nonprofit subcontractor named Roca to provide intensive life skills coaching and employment training for nearly 1,000 high-risk young men, ages 17-23, on probation or exiting the juvenile justice system.

The seven-year project received its initial funding from social impact investors and philanthropists rounded out by Third Sector Capital Partners. If an independent third-party evaluator eventually declares that Roca has met its target outcomes — reductions in days of incarceration, increases in job readiness, and increases in employment — the investors will be repaid, plus interest, by the Commonwealth of Massachusetts and the U.S. Department of Labor.

DO YOUR HOMEWORK

Like anyone funding a venture, social impact investors who seek to generate financial returns while leaving a positive mark on the world need to do their homework, says Brest. Sometimes, the research that impact investors face can be more daunting than that for traditional investors, adds Brest, who also teaches courses on philanthropy and social investing at Stanford GSB. "If you're doing pure philanthropy," he says, "you do due diligence to see whether it's a good nonprofit organization, and if you're doing pure investment, you do due diligence to see if it's solid and it's going to bring a financial return." Impact investing requires doing research in both these areas.

The high analysis requirements may diminish the charitable impulse for some. "But if you're going to be a savvy philanthropist or a savvy impact investor, you just have to push through that," he says.

SEEK OUT A FUND MANAGER

The best impact investing fund managers "have the same knowledge of social enterprises that John Doerr at Kleiner Perkins has of high-tech social media investments: great knowledge of a particular market," he says. The best ones see opportunities where others do not, he says. "And that's where the trick is."

"The best impact investors have the same knowledge of social enterprises that John Doerr at Kleiner Perkins has of high-tech social media investments."

BRINGING ACCOUNTABILITY TO NONPROFITS

Brest says one of the most promising things about pay-for-success projects is that they emphasize measurable outcomes. "That in itself is fairly unusual in government contracts," he says. It can help nongovernmental organizations too. "It's a terrific way for nonprofit organizations, which are often pretty sloppy about outcomes, to become more disciplined," he says.

ATTRACTING INVESTORS CAN BE CHALLENGING

Negotiating specific outcomes with multiple stakeholders and rounding up investors willing to pay for such experimental social programs may prove too cumbersome for some. "If you think about the plumbing system involved in putting this all together, it's pretty complicated," Brest says. There may not be enough investors willing to accept below-market risk-adjusted returns, or they may decide they could do just as well simply by making grants.

Yet Brest estimates that about 30 or 40 such projects have been launched or are being negotiated in the United States. In Silicon Valley, Santa Clara County has put out two requests for proposals: one dealing with acute mental health problems and the other with homelessness, he says. "If this works, you're going to find new ways of financing social enterprises and allowing them to scale in a way that philanthropy alone can't do." ▲

Paul Brest is professor emeritus of political economy at Stanford GSB and a dean and professor emeritus at Stanford Law School.



ENGAGEMENT

Does Face Time with Investors Make a Startup More Successful?

Where funding sources are located can impact the growth of a business.

BY EILENE ZIMMERMAN

TAKING FLIGHT
The proximity of airports impacts investing.

Want your startup to have an IPO? Start spending more time with your VCs.

Professor Shai Bernstein shows in his research that the more time venture capital investors spend with their portfolio companies, the more likely those startups are to produce innovation and have an exit, either an IPO or an acquisition. “This is compelling evidence that the active involvement of venture capitalists is very important for their portfolio companies,” says Bernstein.

The mystique surrounding venture capitalists, especially those at well-known firms like Kleiner Perkins or Andreessen Horowitz, is that their involvement with a startup is a golden ticket, making success much more likely. Yet even though about 40% of all companies that have an IPO in the United States are backed by venture

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“Cities might consider subsidizing direct flights to Silicon Valley.”

capitalists, it has been almost impossible to know if that is the result of an investor’s involvement with a company or simply that VCs know how to pick winners. “We had no way to know if their involvement with a startup was what made it a winner,” says Bernstein.

That’s because it is difficult to measure. But Bernstein and his colleagues Xavier Giroud at the MIT Sloan School of Management and Richard Townsend at Dartmouth’s Tuck School of Business found a way to do it.

They focused on transportation; specifically, how easy or difficult it was for VCs to visit one of their portfolio companies. About 40% of investors are located more than 600 miles from their portfolio companies. Bernstein says he and his colleagues turned their attention to the introduction of direct flights between cities where VCs were located and startups were based. “If you look at the flow of venture capital in the U.S., you find that it’s actually

strongly affected by the availability of direct flights,” says Bernstein. His guess was that direct flights increase the amount of time VCs spend with portfolio companies, and 80% of VCs surveyed by Bernstein and his colleagues said they did spend more time at portfolio companies that were reachable by a direct flight.

The researchers also compared pairs of companies located in the same industry and region, with one backed by a VC in a city connected to it by a direct flight and the other backed by a VC in a city that did not have a direct flight connection. They looked at 22,986 venture-backed companies that were active between 1977 and 2006. Collectively, the companies received funding from 3,158 VC firms.

To test whether or not that extra attention and interaction affects a company’s success, they looked at both the quality of the innovation produced by a startup and the likelihood of its IPO or acquisition.

Innovation was measured by the number of patent applications submitted by each startup (and the number of patents ultimately granted). But even more important was the number of citations — where patent applications submitted by other companies cited the startup’s technology. Citations show that an innovation or invention already exists and helps establish the scope of a new patent’s claim. “There aren’t that many patents that open up a new field of research, so citations mean that a company’s technology or invention is important in a way that generates a lot of new patents,” says Bernstein. “And that shows it’s innovative.” In fact, an extra citation per patent boosts a company’s market value by 3%.

The researchers also found that despite a variety of state and local initiatives to help create startup communities and generate VC investment, infrastructure — specifically, transportation access to the region — was crucial for a city to attract capital.

Bernstein says better airline connections between two cities actually foster more venture capital flow between them. He found that introducing a direct flight between two cities leads to a 4.6% increase in venture capital investments in those cities, and that VC firms tend to invest in places that are easier to access. That in itself, says Bernstein, shows investing isn’t just about the money. “It’s also about the time investment,” he says.

With that in mind, Bernstein’s recommendation for regions trying to foster entrepreneurial activity — and for startups considering where to locate — is to pay attention to access. Cities might consider subsidizing direct flights to Silicon Valley, says Bernstein, and company founders should think about where investors are located when they are trying to raise money. Bernstein says the research proved that face time — not just Skype meetings and conference calls — has a significant impact on a startup’s success. “Having investors you can easily interact with can really affect your ability to grow a business successfully,” he says. ▲

World



“When people talk about political risk,

they think it’s just something that’s present if you try to invest in Angola, or somewhere there might be a war.”

— Ken Shotts PAGE 50

Shout

FINANCE

Are Mutual Fund Managers Skilled or Just Lucky?

Research suggests managers have been unfairly castigated.

BY ELIZABETH MACBRIDE

In 1973, Princeton economist Burton Gordon Malkiel famously pointed out that a blindfolded money manager throwing darts at a newspaper's financial pages could select a portfolio that would do just as well as one carefully selected by experts.

He was translating into layman's terms research that suggested that most investors would do better investing in index funds than in actively managed funds. His conclusion was accurate, but new research from Stanford Graduate School of Business explains why no one — especially financial policymakers — should jump to the conclusion that active fund managers have no superior investment skills. Over time, people have used the truism about index funds to mistakenly conclude that mutual fund managers have no skill, and that it is impossible to ever beat the market.

In fact, research by Jonathan Berk of Stanford GSB and Jules H. van Binsbergen, formerly of Stanford and now at Wharton, suggests that the typical mutual fund manager is persistently skilled, and that top performers are especially good. It's just that the market is so hypercompetitive that most investors can't benefit from the skill — it is competed away too quickly as money pours into emerging managers' funds. The managers and their companies, rather than investors, capture the value of the total market earnings and fees charged to investors.

For policymakers, the research suggests that mutual fund managers have been unfairly castigated. If we confuse the questions of how skilled mutual fund managers are with how much individual investors can benefit from their skill, we risk making poor decisions about how to regulate and set policy in finance.

Jonathan Berk is the A.P. Giannini Professor of Finance at Stanford GSB. Jules H. van Binsbergen, formerly of Stanford GSB, is an associate professor of finance at the Wharton School, University of Pennsylvania.



MEASURING INVESTMENT SKILL

Though conventional wisdom holds that mutual fund managers are unskilled, they are some of the most highly compensated members of our society. The researchers began looking into how that could be.

The basic economic principle of rents holds that someone cannot earn a “rent” — a wage above costs, in this case — unless he or she possesses a desired skill in short supply. Though there can be distortions in the market, such as government incentives or penalties that might explain the high incomes, it seemed impossible that mutual fund managers would earn such high wages without possessing any skills at all.

“We then asked ourselves a basic but crucial question: Could we be measuring skill incorrectly?” Berk says.

Many people have used gross alpha — the industry term for returns above a benchmark of diversified stocks, such as the S&P 500, and before fees charged to investors are deducted — as a proxy for investment skill. The researchers offer the example of Peter Lynch to show why looking at skill this way could be a mistake.

In his first five years managing Fidelity’s Magellan Fund, Peter Lynch had a 2% monthly gross alpha on average assets of about \$40 million. In his last five years, his gross alpha was only 20 basis points per month, but on assets that ultimately grew to more than \$10 billion.

“Based on the lack of persistence in gross alpha, one could mistakenly conclude that most of Peter Lynch’s early performance was due to luck, rather than skill,” Berk and van Binsbergen write.

But the skill is still there, which you can see when you take into account how much money Lynch actually made from the funds he invested. The value he extracted from financial markets went from less than \$1 million per month in his first 5 years to over \$20 million per month in the last year.

If not gross alpha, then how ought skill be measured? Berk says it is important to first recognize how a manager makes money. First, she buys low and sells high, to make money for investors. She then charges fees to investors for the returns.

The money made by the manager — and the better representation of her skill — is the return she earns over her benchmark plus the fees that investors are willing to pay her, says Berk. As with the Lynch example, the measure needs to take into consideration the percentage fee charged and the size of the fund upon which the percentage is charged.

FUNDS ANALYZED

Berk and van Binsbergen looked at a universe of 5,974 mutual funds from 1969 to 2011 and compared their results to comparable Vanguard index funds, which are alternative products that investors can actually buy. When they divided the mutual funds into 10 groups based on the amount of money managers have made in the past, as described above, the researchers found that the funds that made the most in the past also made the most in the future. That is, the ability to make money is persistent. The researchers also calculate that the average fund manager added \$2 million in value each year.

“We then asked ourselves a basic but crucial question: Could we be measuring skill incorrectly?”

WHO BENEFITS?

If the higher earnings are persistent, why can’t individual investors benefit more from them?

The market responds very quickly when a new manager with skill emerges, rewarding her with more assets to invest. As the fund grows, it is harder for the manager to make money for a variety of reasons: For instance, placing trades in large enough quantities for all the investors becomes more difficult.

Over time, returns are lower on the larger funds. But the amount of money the skilled managers earn remains high, based on this analysis.

Does it matter that mutual fund managers are skilled if investors don’t benefit from the skill? Consider other professions. The Army, for instance, would not rate a doctor only on her rate of cures without regard to the difficulty of her cases, the number of people she is required to see every hour, and whether she is operating in a war zone. Conflating skill with results might lead to poor policy decisions. If mutual fund managers have no skill, then it follows that their high pay could be the result only of marketing — or worse, chicanery.

This research found the opposite story: Mutual fund managers walk an ever-narrower ledge in a highly competitive industry.

The research revealed another intriguing result: The mutual fund manager’s current compensation from aggregate fees and the value he or she added to the fund predicted the fund’s future returns even better than past value added. That suggests that investors pick up on tiny signals in the market to evaluate the potential for managers to outperform in the future. It’s possible that neither investors nor mutual fund managers have been as foolish as they have been portrayed. ▲



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POLICY

How to Mitigate Political Risk

Changes in government regulations can impact companies in all sorts of ways.

BY IAN CHIPMAN

Shortly after being elected president of Ecuador in 2006, Rafael Correa made good on a campaign promise. He announced plans to unilaterally change the contracts held by foreign oil companies and said he would tax away almost all of the profits for any company that refused to “renegotiate.” The subsequent negotiations resulted in several foreign oil companies losing their assets in Ecuador. It was a major step in Correa’s populist, anti-capitalist crusade.

Foreign investment in Ecuador has since plummeted as a result of the effective expropriation of oil companies’ assets. However, after his 2013 reelection, Correa tried to court just the sort of foreign investment he had scared off, claiming that “the advantages of our country for foreign investment [include] political stability.”

It’s a salient reminder of two things, says Ken Shotts, professor of political economy at Stanford Graduate School of Business. First, political risk is inevitable in any arrangement between a company and a sovereign state. And second, expropriation isn’t simply a matter of greed. The situation in Ecuador and countless other examples offer a lesson in the complex political and fiscal calculus being performed by companies and governments alike. The question, then, is how does one unpack something as nebulous and difficult to predict as political risk.

In a paper, Shotts developed a model using game theory to describe this tug of war between companies and governments, profits and taxes, investment and deterrence, and political costs and benefits. In addition to deciphering what motivates a government to expropriate or not, the work also outlines a range of options available to a company to help mitigate political risk.

Here Shotts discusses the challenges of addressing political risk and the importance of integrating an understanding of political risk into a company’s core strategy.

Ken Shotts is the David S. and Ann M. Barlow Professor of Political Economy at Stanford GSB and a professor of political science, by courtesy, at the School of Humanities and Sciences at Stanford University.

Photograph by Amy Harrity

KEN SHOTTS
Risk is inevitable.



What made you want to study political risk? It grew out of teaching. I had a student in the Stanford MSx Program a few years ago whose family business — an ecotourism resort — was expropriated by Hugo Chavez. She did a project on her family's experience, and I thought, "You know, I should start teaching about political risk."

Now it's a core part of what I teach, especially in executive education programs. In fact, my Stanford GSB colleague Steve Callander and I are developing a new executive program called *Strategy Beyond Markets* that covers political risk along with other topics like self-regulation and crisis management.

How do you define this notion of political risk? People use the term to mean a lot of different things. To me, political risk is any time a government could change its policies in a way that will affect a firm's profitability. It's a very broad definition. A government taking over a factory is one example, although that's more rare nowadays than what's called "creeping expropriation," which is the government changing policies in such a way that the firm essentially loses all of its profits. That's not really any different from taking over the factory, right? You change tax policy or regulations so the firm makes no profits. From the firm's perspective, it's the same difference. The most subtle form is currency controls, essentially saying, "I will not let you repatriate profits." But for analytical clarity, let's just say it's the government coming in and taking stuff from you.

A lot of the time when people talk about political risk, they think it's just something that's present if you try to invest in Angola or somewhere there might be a war, like Ukraine. In my view, political risk is present

anywhere governments can change their policies. For instance, in the paper I talk about water policy in California and how almond growers are subject to political risk.

Do companies often misunderstand what they're facing with political risk? I think the biggest mistake that businesses make is to assume that politicians are crazy, that they're unpredictable. But it's really a matter of understanding where they're coming from, what they care about, and what they're going to do.

This goes back to the Hugo Chavez expropriation. I always thought Chavez was crazy. But when I was talking with a student — and this woman did not like Chavez, obviously, because he took over her family business — she said, "No, no, no. He was very savvy about this. He was thinking about his electoral support coalition, how to claim as much credit for it as possible. It's not like he came in and nationalized everything instantly." So it's important to think about how politicians have different objectives and activist groups have different objectives. Environmentalists who are trying to stop a mine in Newfoundland and Labrador have different objectives from companies. But companies ought to think, "Let me try to understand them."

What are those key factors that inform a government's decision to expropriate or not? In my research I focus on three factors.

The first one is how much taxes the government gets from the firm. If all of the benefits are going to the company's bottom line and none are going to the government or society as a whole, then the government is much more inclined to expropriate the firm.

The second factor is the government's ability to operate the firm's assets on its own. If the government doesn't know how to run a factory, then it won't benefit much from taking it. On the other hand, if the government has technical and managerial expertise — or even if it thinks it has such expertise — then it will be more inclined to expropriate.

The third, and most complicated factor, is what I call political costs and benefits. A politician can get all sorts of benefits from expropriation. For example, Correa proved to voters that he's a real populist, not a friend of companies. Politicians also can benefit by using a company's assets for patronage or corruption. But politicians face political costs. If a government gets a bad reputation, this can deter investment, both by its own citizens and by foreign companies. And a government that expropriates also might be sanctioned by its own citizens or by foreign governments. Exactly what these costs and benefits are varies a lot across countries — they might seem puzzling to business people who are new to dealing with this issue, but political scientists have a pretty good handle on these types of things.

What are some of the options a business has to mitigate political risk? There is this notion of "integrated strategy" that I talk about in the paper, which is an idea that was actually developed here by Dave Baron. It means integrating all components of your business or market strategy with your government relations or public relations strategy. A lot of the time companies say, "We're going to do our business strategy and then we'll go hire some people to handle the politics for us." But for political risk, you can't do that.

“It’s easy to cut corners on things that don’t yield clear, short-run returns.”

The problem is that what you do in the business affects how the government relations and public relations stuff is going to work. If you’re not hiring locals to work in your factory, then it’s going to be a lot harder to have good government and public relations. So an integrated strategy means that everything a firm does — whether it’s finance, operations, human resources, supply chain, or even pricing — should all be done with an eye to how it affects the political aspects of the firm’s business.

What are the best ways to accomplish that? One thing that companies can mess up is not laying the groundwork early on for getting a broad support base within an area. You need to plan ahead to share the benefits of the profits. That includes things like sourcing locally more than you need to, employing local labor, training those people up, building roads, hospitals, things like that. Being what people call a good corporate citizen.

Another thing that companies mess up is failing to realize that if they start making a lot of money, then they’re at risk of expropriation, and they need to show that they’re not just coming in and looting the

place. There are legitimate objections that people have to their countries being looted. It’s probably good to take seriously the fact that it’s not crazy for people to be mad about that. And to anticipate it and say, “Wow, looks like things are going really well. How are we going to spread the wealth around?”

I don’t think of this as being a pure win-win. Sometimes win-wins exist, and sometimes they don’t. There are real trade-offs between the interests of the company and the interests of the local citizens. Companies like to do things cheaply, and they might not mind polluting or not care how many local people they hire. But when a company pushes as hard as it can on all those things, it’s running other risks. So for strategic reasons, they should be thinking about this stuff very carefully.

So companies need to be thinking about strategies that build meaningful, mutually beneficial relationships with the government and local citizens so that everyone’s incentives are in line. Easier said than done, right?

Yes, it’s normal that firms would really struggle with these things. When it comes to anything benevolent, there is a tendency for companies not to be as rigorous as when they think about traditional “business” decisions. It’s easier just to have a “division of doing good stuff and claiming credit for it” than it is to formulate a serious integrated strategy, which means taking the things we normally think of as being strictly business decisions — like how cheaply you can pay your labor or where you’re sourcing — and realizing that those things matter for other reasons. They need to take those things they’re being hardnosed and quantitative about and add in this thing that is impossible to quantify. And the horrible thing is that it really is impossible to quantify. The killer

question I always get and can’t answer is how do you assess your return on these investments. Even for people who have a good understanding of how governments and politicians work, that’s tough to do.

If it’s so hard to quantify the return on investment in this type of integrated strategy, how reasonable is it to expect that companies will go for it? I think it’s hard, and it gets pushed out very naturally, especially when times are rough. It’s easy to cut corners on things that don’t yield clear, short-run returns. But it’s also very risky to ignore these issues. Doing it well requires building it into the company’s culture, because there are so many people who have to be involved.

Who stands to gain the most by understanding your work here? Some companies are already very savvy about it, especially ones that deal with this stuff all the time. To me it’s most important for companies that are moving into new international environments. I also hope it would resonate with rapidly growing companies, but that’s often challenging. With most people, the things on their mental agenda are the issues they’ve dealt with in the recent past. For rapidly growing companies, that’s things like how do we hire the right engineers. When it comes to their non-market strategy, they’re not paying attention, not paying attention, not paying attention, and then all of a sudden — bang! It’s huge to them. ▲

ENERGY

How to Keep Green Policies from Crashing the Electricity Grid

What trading games can tell us about “cap and trade”

BY EDMUND L. ANDREWS

Many Californians still remember the electricity crisis in 2000 and 2001, when a combination of tangled state and federal regulations and opportunistic behavior by market participants led to soaring wholesale prices and rolling blackouts.

Could something similar happen today, but this time as a result of trading tied to policies for reducing carbon emissions and mandating a higher share of electricity produced from renewable energy?

Research led by Stanford Graduate School of Business courtesy professor Frank A. Wolak and Mark C. Thurber, associate director for research at Stanford’s Program on Energy and Sustainable Development, is shedding light on that question through an advanced electricity-trading game that incorporates both California’s cap-and-trade system for reducing greenhouse gas emissions and its mandate to produce 20% of electricity from renewable fuels.

Wolak and his colleagues describe a wide array of unexpected results that emerged through a series of trading games played by teams of students from Stanford GSB.

In at least one simulation, for example, one team essentially cornered the market on Renewable Energy Certificates, the product retailers must purchase to comply with the renewable energy mandate. The team then charged sky-high prices to electricity retailers that still needed to buy certificates as the compliance deadline drew near.

PRICE PROBLEMS

The games also highlight what is perhaps the biggest long-term conundrum tied to regulatory mandates for solar and wind power: a pricing dynamic that sends spot-market electricity prices crashing to almost zero at times when sunlight and wind are abundant, which can make it hard for other electricity providers that are essential during periods of peak demand to recover their fixed costs.

Price crashes have already become a serious issue in Germany, where government-supported mechanisms have propelled renewables to the point that,

during a few hours of the year, renewables are the nation’s largest source of electricity. Germany has actually experienced negative spot prices on days in the summer when solar output is high and electricity demand is relatively low. Negative prices also occur in U.S. electricity markets with substantial renewable energy shares, such as California and Texas.

The problem is that conventional power plants need to be available during all hours of the year because solar and wind power plants are often unable to produce electricity. Renewables mandates have lowered average spot prices and increased their volatility, but higher spot prices at certain times of the day can provide much-needed revenue for owners of conventional generation.

“If you stuff a lot of zero-cost renewables into the system and they all produce at the same time, you kill the spot price and get an infrequent and unpredictable demand for energy from conventional units, even though you need those units to be around,” Wolak says.

Wolak argues that these problems can be addressed. One strategy, he says, is for retailers to purchase a bigger share of the electricity they sell to final consumers through fixed-price forward contracts rather than from the spot market. The guaranteed payments from forward contracts provide revenue certainty for the owner of a conventional generation unit.

LEARNING THROUGH THE GAME

To better understand the potential problems, Wolak, Thurber, and graduate student Trevor L. Davis developed their advanced electricity trading game that incorporates California’s green policies and electricity markets.

“If you put smart people in the game, you can see how things can go wrong that you might never have expected.”



“It’s an ideal way to study these issues because the world is so complex that sitting down and figuring out a mathematical model is far too difficult,” Wolak says. “But if you put smart people in the game, you can see how things can go wrong that you might never have expected.”

California is at the cutting edge of market-based requirements to reduce greenhouse gas emissions. In 2013, the state launched a cap-and-trade system for carbon emissions under AB 32, the 2006 law that mandates reductions in carbon dioxide emissions to 1990 levels by 2020. Companies receive allowances for a certain volume of carbon emissions, and those allowances are tradable.

A separate pillar of California’s green policy landscape, the Renewables Portfolio Standard, requires electricity retailers to procure at least 20% of their electricity from qualified renewable sources. By 2020, the renewables share requirement goes

up to 33%. The utilities can meet their requirements by buying Renewable Energy Certificates. One certificate is produced each time a qualified renewable facility produces 1 megawatt hour of electricity.

The Stanford researchers spent a year programming the electricity-trading game that incorporated all these elements. In their class at Stanford Graduate School of Business, they then organized a number of games that pitted teams representing generating companies against teams representing electricity retailers.

For teams in regions with abundant solar and wind power, both spot prices and the demand for fossil-fuel electricity swung wildly during the course of each day. Prices crashed in the middle of the day. And though they spiked up again at night, the power companies didn’t always have the market clout to drive peak-time prices high enough to make up the mid-day losses. In part, that was because

renewable energy comes from legions of different sources.

That wasn’t the only source of increased price volatility. Electricity retailers recognized that with a higher share of renewable energy in total demand, the large conventional generation units supplied a smaller fraction of total electricity and were therefore less able to raise spot prices through their bidding behavior. Fixed-price forward contracts are like insurance policies, and tend to stabilize energy market prices. But the retailers had little interest in buying that protection because they weren’t as worried about price spikes from the owners of large conventional generation units.

That might sound like good news for consumers. Over time, however, it can reduce the availability of “dispatchable” power plants that can meet peaks in demand and provide electricity when solar and wind aren’t available.

One lesson from running the game, says Wolak, is that the details of the design of the various markets can make a big difference in market outcomes. For example, the researchers found that allocating carbon allowances fairly evenly among market participants at the outset of the game improved the liquidity of the market for carbon allowances, which in turn improved the performance of the overall electricity market. The researchers also found a number of ways to increase the stability of market outcomes.

“Electricity is different from all other commodities because it’s vital to all life and you don’t want things going off the rails suddenly,” Wolak says. “We don’t have much experience with markets where all of these policies interact, so it’s better to stage them in gradually. Letting it rip all at once rewards the sophisticated and intelligent players, who accumulate all the wealth — perhaps at the expense of everyone else.” ▲

Frank A. Wolak is a professor of economics, by courtesy, at Stanford GSB. He is the Holbrook Working Professor of Commodity Price Studies in the Department of Economics at Stanford University. He is a senior fellow at the Freeman Spogli Institute for International Studies, the Precourt Institute for Energy, and the Stanford Institute for Economic Policy Research.

MARKETING

Do Mentions of God Persuade Consumers to Buy?

Scholars find where omnipotence and advertising meet.

BY MARINA KRAKOVSKY

What does God have to do with the risks people are willing to take? The answer, new research suggests, depends on the nature of the risk.

All risky acts, from starting a new business to driving above the speed limit, hold out the possibility of either a good outcome or a bad one — but some risks are more morally laden than others. Alcoholics Anonymous and other 12-step programs talk about a higher power to help addicts overcome their risky behaviors; this is consistent with some past research that shows that religious people are less prone to take moral risks, or the kinds of risks that might trigger God's disapproval.

Yet with risks that don't have such a moral element — skydiving or investing in a speculative stock, for example — the opposite is true, according to a series of studies by a team of Stanford GSB scholars, including professors Kristin Laurin and Jonathan Levav. “God is commonly viewed as a source of security,” and feeling secure can make potential negative outcomes seem both

Kristin Laurin is an assistant professor of organizational behavior at Stanford GSB and Jonathan Levav is an associate professor of marketing and the Citi Faculty Director for the Behavioral Lab at Stanford GSB.

Illustration by Michael Kirkham



TRY SKYDIVING!
1-800-SKYFLY



**The “God knows”
in these ads is
just a figure of speech,
yet it seems to
remind people of
God’s protection.**

less likely and less severe, the researchers write. If you believe that God will protect you from harm, then nonmoral risks will seem to have more upside than downside, thus making them more attractive.

It’s impossible to say in a general way whether that’s a good thing or not, says Laurin, an assistant professor of organizational behavior: The optimal level of risk-taking varies greatly from one situation to another, and it may not even be known in advance. But one thing is certain: “Most people wouldn’t say they would take a risk just because they happen to be thinking about God right now,” Laurin says. “That’s not a factor that people would want to go into their decision making.” Yet it did affect people’s choices in these experiments.

Remarkably, the research didn’t find the effect only among believers — they saw it even among people who said they don’t believe in God. In one experiment conducted on Facebook, the researchers presented users with two slightly different versions of an ad for a local adventure: both urging users to click the ad to “find skydiving near you” and “feel the thrill.” But one ad said, “You don’t know what you’re missing!” while the other said, “God knows what you’re missing!” People who saw the “God” version of the ad clicked more often. A pair of ads for an immoral risk — “Learn how to bribe with little risk of

being caught!” — revealed the opposite pattern, with the God version attracting fewer clicks. When the advertised activity carried no risk at all — an ad for video games — the mention of God had no effect one way or the other.

“A lot of people who say they don’t believe in God, if you get into it with them, there’s some uncertainty there,” Laurin explains. The fact that people are responding to these reminders of God shows that latent beliefs about God’s reputed powers are holding sway.

The “God knows” in these ads is just a figure of speech, yet it seems to remind people of God’s protection nonetheless. In another experiment, the research team, led by PhD student Daniella M. Kupor, found that when a risk that participants took in the lab didn’t pan out, the participants who had been primed with reminders of God showed more negative feelings toward God than participants who had not been primed to think of God. That’s evidence that participants had expected God to protect them from such bad outcomes.

Together, these studies add to the mounting evidence that factors outside one’s conscious awareness can affect decisions. This insight might prove helpful for those in a position to influence other people’s decisions, such as a manager wishing to encourage employees to pursue bold ideas, a financial advisor nudging clients toward a slightly less conservative portfolio, or a marketer introducing a new product. Use of the word “God” could be just one more tool in a marketer’s toolbox, Laurin says, and it doesn’t have to be heavy-handed.

“There are tons of colloquial expressions we use to refer to God,” she points out — think of phrases like “Oh my God,” for example. People don’t necessarily think about God in any conscious way when they see such expressions. “But if what we found is true, then those are the kinds of phrases you might use if you’re advertising a risky product like an outdoor adventure.” This kind of messaging could help overcome consumers’ hesitance to try unfamiliar products of any kind, adds co-author Levav. New products, particularly really new products, are inherently risky, he points out, because buyers aren’t certain about their quality and performance. “So as a way to get people to try them more readily, you might try to slip in some God mentions, and now, as a result, the product will feel safer than it otherwise would.”▲



SLEEK RIDE “Every detail is important, even down to the color of the parts,” says Corvette chief engineer Tadge Juechter.

ENGINEERING

Why You Won't See a Self-Driving Sports Car

Tadge Juechter offers a long-view perspective on the auto industry.

BY JONATHAN XAVIER

Joe Vaughn

Corvette chief engineer Tadge Juechter never intended to work for General Motors. A teenage summer job on the assembly line had soured him on auto manufacturing, and Juechter said he couldn't see himself at a big company where he was just another cog in the machine.

Yet when a college friend asked Juechter to accompany him to an interview there, he went along and interviewed himself, mostly on a lark. To his surprise, he got the job.

That was 37 years ago.

Since then, Juechter, who earned his MBA from Stanford GSB in 1986, has climbed his way up the ladder at GM, spending the past 20 years working on its flagship sports car, Corvette. In 2006, he became just the fifth chief engineer in the storied automobile's 62-year history. In that role, he has final authority on the direction of one of the world's most iconic car brands, and was the driving force behind 2014's lap-time-obliterating Stingray C7, for which he was named *Automobile Magazine's* Man of the Year.

Even with all the accolades, Juechter hasn't been able to entirely escape the manufacturing work he dreaded in his youth. Like all engineers at Corvette, he spends at least one day a year at the company's plant in Kentucky, working on the assembly line. With the benefit of experience, Juechter says he now finds it informative.

“When you're sitting in an engineering office, and you see this great black finish on a part, it's like, ‘Oh, let's make it all black — it will match!’” he says. “Well, you get down to the plant and the light's not that great and maybe you're pushing 60 and you need reading glasses, and now you're trying to find this black hole on a black part to put in a black fastener, and suddenly you realize you've made a mistake.

“Every detail is important, even down to the color of the parts.”

Juechter describes his tinkering passion, Detroit's hubris, and self-driving cars in this interview with *Stanford Business*, edited for length and clarity.

Were you into cars at a young age? I had a fascination with taking things apart. The first car I actually owned, technically, was my mother's '64 Cadillac DeVille sedan, but I never really drove it because she gave it to

Tadge Juechter earned his MBA from Stanford GSB in 1986.

me after she wrapped it around a tree, so it was not really roadworthy. They donated it to me to take apart. They let me disassemble that entire vehicle just off the driveway of our home. It made a horrible, horrible mess.

But I was tinkering with everything. From cars to bicycles to building go-karts. Anything mechanical, I loved to play with. In the '70s, I built a bicycle with full suspension, not thinking that one day that'd be something you'd be able to buy. It was like a precursor to the mountain bike. I used to go boinging around the neighborhood on this bicycle with like a foot of ride travel on the suspension. It was hilarious to see.

You've been with GM for nearly 37 years. What's the biggest change you've noticed over the years? I don't know if I can even say there was one single biggest change. The whole place is just completely different. When I first started in the 1970s, General Motors was at the height of its power. I tell people, and they don't believe me, but it was like the Apple Computer of its day. We had 50% market share in cars, and we were in everything else, too. We were in locomotives. People don't realize we invented the iron lung. Medical devices, refrigeration, appliances, everything. That was the peak of GM's influence, to the point that the government was considering breaking the company up.

That's the company I started at. That's the company that got the reputation for being very arrogant, and not very flexible. That's the company that ignored the rise of foreign cars until it was too late. There was a lot of hubris there. I watched the evolution of the company as it suddenly had to fight for survival for many years, until we finally failed at that and went bankrupt [in 2009].

“Corvette has had its moments. I don't want it to seem like we've had a free ride the whole way.”

And then I watched the rebirth in the relatively recent past.

The company has a completely different feel today than when I started. For the better, I think. But you know, it's funny — my office is actually 50 feet from the office I had back then. So in 37 years, I've come 50 feet.

Given your unique perspective, what do you think of the recent “reinvention of Detroit” narrative? Has Detroit reinvented itself, and what does that look like on the ground? The major perception is that Detroit can't compete, and that's why we went bankrupt. But if you look at Corvette as an example, we compete exclusively with imported cars. Who produces sports cars? It's Porsche, BMW, Ferrari, Mercedes, Audi. Ford has the Mustang, but that's more of a Camaro competitor. If you look at two-seater sports cars, it's the elite, the who's-who of the auto world. And they're typically the flagships of their respective companies. You know, the Porsche 911. That's their flagship, and that's our competition.

And we not only compete, we dominate. Last figures I checked, in our segment we have something like 45% market share in North America. Nobody has 45% market share, in any segment. It's unheard of. We've been quite dominant for a long time.

Why do you think Corvette has been able to stay around for so long when the rest of the domestic auto industry has struggled? It's staying true to the mission of the car. Corvette has had its moments where it almost died. I don't want it to seem like we've had a free ride the whole way.

But if you look at other vehicles that are successful long term, they tend to stay true to their mission. They don't try to wander off and be something they're not. There are plenty of examples where cars tried to get bigger, or go from four passengers to two, or tried to migrate upmarket. They get cocky and think, “Wow, we could sell these things at a much higher price — let's do an upscale version.” That doesn't work. You have to stay true to what you are.

Is that harder to do in today's auto industry? It seems like there's a conversion going on. Years ago you wouldn't buy a luxury car because you were going to take it to the track, but now you have the Tesla Model S, which is a luxury sedan that goes from zero to 60 in three seconds. People want to have

their cake and eat it too. But that's our job, to figure out how to use technology to give them their cake and let them eat it too.

I think it's true of every market segment; people expect more of everything these days. I mean, economy cars these days are quite zippy, for example. They've got these little turbo engines, and they're faster than Corvettes used to be a couple decades ago.

Regardless of where we compete, we're all looking for the same things around technology. And people ask me, ‘why is GM even doing Corvettes anymore?’ Shouldn't you be focusing on things like fuel efficiency? But what they don't realize is that Corvette is the tip of the technology spear. What we do helps the whole portfolio because things that are great for making a sports car are also great for making an efficient car. We need very efficient engines to get high horsepower. We need great aerodynamics to get a high top speed, the exact same thing you need to have low drag in an efficient vehicle. A lot of the same technologies we push the envelope on apply to every market segment. We have a big poster here full of things where Corvette was first in the industry, and now they're commonplace. We were the first composite body car, for example. Way ahead of the curve. Now most companies use them.

Does that mean we'll see a self-driving Corvette some day? That's one technology where I expect we'll be last to the party. The whole purpose of our car is to enjoy the experience. It's not to text while driving. It's to be fully participating in a great ride. We want you to be the computer behind the wheel.

But there might be ways that we could use the same technology in a way that might be fun for us. For example, you could have the car be an on-track driving coach. You could use autonomous driving to show you the capabilities of a car on the track. I mean, this has already been proven — an autonomous car can drive the track the same way a racecar driver could. You have the car give drivers feedback when they're deviating from optimal driving. You might even use that technology to scale up the level of assist you're getting so you're effectively coached by the car on how to drive quickly and safely on a racetrack. Even for what looks like a foreign technology to a sports car, we might be able to use it to create a unique driving experience. ▲



PUBLIC SERVICE Young workers don't know of opportunities available in public management.

SERVICE

How to Make Change Through the Public Sector

Vetor Brasil persuades young people to consider careers in government.

BY LILY B. CLAUSEN

With one of the world's largest economies and a population of more than 200 million people, Brazil is Latin America's giant. The country's government is large and provides essential services to its people, but Brazil struggles to strengthen and consolidate its public institutions.

THE PROBLEM

"If we really want to have impact on people's lives, we can't do it working only with the private sector," says Joice Toyota. "If we want to have scale, we have to change the government."

However, changing the government is a Herculean task, and it's difficult to attract skilled government

Joice Toyota received her MBA from Stanford GSB in 2015. She is a 2015 Social Innovation Fellow. The fellowship provides up to \$180,000 in funding, advising, and support to graduating Stanford GSB students who want to start a nonprofit venture to address a pressing social or environmental need after graduation.

employees who are up to the job. People often steer clear of government work because of pervasive stereotypes that Brazil and its unbridled bureaucracy are corrupt. “That’s something that people don’t want to deal with,” says Toyota, who earned her MBA from Stanford GSB in 2015.

THE SOLUTION

Toyota’s nonprofit Vetor Brasil aims to develop leaders who can change Brazil’s public sector and how services are provided to the public. Think of it as Teach for America for government work. “We believe that there are thousands of high-potential university graduates who want to have social impact and give back to their country,” Toyota says.

What’s keeping them from rolling up their sleeves? These young workers don’t know of the opportunities available in public management, Toyota says. Vetor Brasil selects workers and places them in temporary government jobs. “The idea is to change the system by changing the people,” she says.

Toyota put out her first call for applicants last summer. She received 1,700 applicants and placed

12 trainees in state and local governments in four different states in Brazil.

Vetor Brasil will provide resources and counseling after their service to help them acquire jobs in the public sector or other types of public service organizations. Toyota’s goal is to staff a total of 800 people in the public sector within the next five years.

THE INNOVATOR

Toyota grew up in the countryside in São Paulo, Brazil. Initially she studied at private school but when her family could no longer afford the school, she switched to public school. “People shouldn’t have such different services because they don’t have the resources,” she says. “This was something I always wanted to work on, but I wasn’t sure how to start.”

As a recent college graduate, Toyota dreamed of working for a social cause. She soon became frustrated by the structure of nonprofits in Brazil and how difficult it was to make a major impact within such organizations. Discouraged, she left her dream for a more traditional career in international consulting. Then, her work with Bain & Co. brought her to Manaus in the Amazon to work on a project with the Amazonas State Department of Education. She was the only consultant within the firm who wanted to take the position, underlining the talent gap for this kind of work.

“I realized that I could break the vicious cycle that plagues Brazil’s public sector by founding an organization that would grow the network of high-potential leaders in the government,” Toyota says. ▲

12

Number of trainees Vetor Brasil placed in state and local governments in four different states in Brazil

EXCHANGE

SOME FINAL THOUGHTS ON IMPACT
EDITED BY NATALIE WHITE

“It’s not just about creating a product,
it’s about creating

impact.”

—**DeRemi Atanda**, SEED participant,
in an interview for *Stanford Business*
<http://stanford.io/1AGdtmd>

“Go into new decisions optimistically.

Expectations

can impact outcomes.”

—**Joel Peterson**, the Robert L. Joss Consulting
Professor of Finance at Stanford GSB;
chairman, JetBlue Airways, in his LinkedIn post
<http://stanford.io/1ImWpza>

“The way to have impact and
effect change

is through metrics and goals,
strategies and tactics.”

—**Laurene Powell Jobs**, a 1991 graduate of
Stanford GSB, during her
DFJ Entrepreneurial Thought Leaders Series talk
<http://stanford.io/1Gn1fBA>

“How conscious

are you of the emotions that
impact your decisions?”

—**Jerónimo Uribe**, a 2014 graduate
of Stanford GSB, in his *LOWkeynotes* talk
<http://stanford.io/1yvKFXS>

“The

bike

is a great example of
how a simple tool can have a profound
impact on our world.”

—**Mike McClure**, a 2015 graduate
of Stanford GSB,
during his *LOWkeynotes* talk
<http://stanford.io/1F1QTjh>

“We believe it is

critical

to tie the interests of the impact investing
movement to climate finance.”

—**Alicia Seiger**, Stanford GSB alumna,
in *Stanford Social Innovation Review*
<http://stanford.io/1NkCrKh>

“Be happy,

be impactful. Mindful decisions
have massive impact.”

—**Donna Ivry**, a 2014 graduate of
Stanford GSB, in her *LOWkeynotes* talk
<http://stanford.io/1roh5Of>

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The Takeaway

THE ESSENTIALS

**FIVE LESSONS FROM
OUR STORIES ON IMPACT**
EDITED BY
DEBORAH PETERSEN

Location, Location, Location

The availability of direct flights between venture capital investors and the companies they fund affects the success of those startups.

— **Shai Bernstein**



Why Personality Matters

For CEOs promoting their company's IPO, personal presence and the ability to make a strong initial impression can sway the stock's pricing.

— **Elizabeth Blankespoor**



Put Down the Gloves

When people stop seeing negotiations as a fight, they open themselves to more creative solutions.

— **Margaret Neale**

Prepare for Risk

Political risk is inevitable in any arrangement between a company and a sovereign state.

— **Ken Shotts**



Should Women Lead Differently?

Female leaders often face a backlash when they exert dominance; they could benefit from using more implicit methods.

— **Larissa Tiedens**

Pedro M. Gardete

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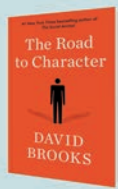
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THE RECOMMENDED LIST

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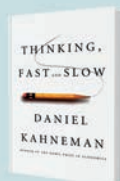
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