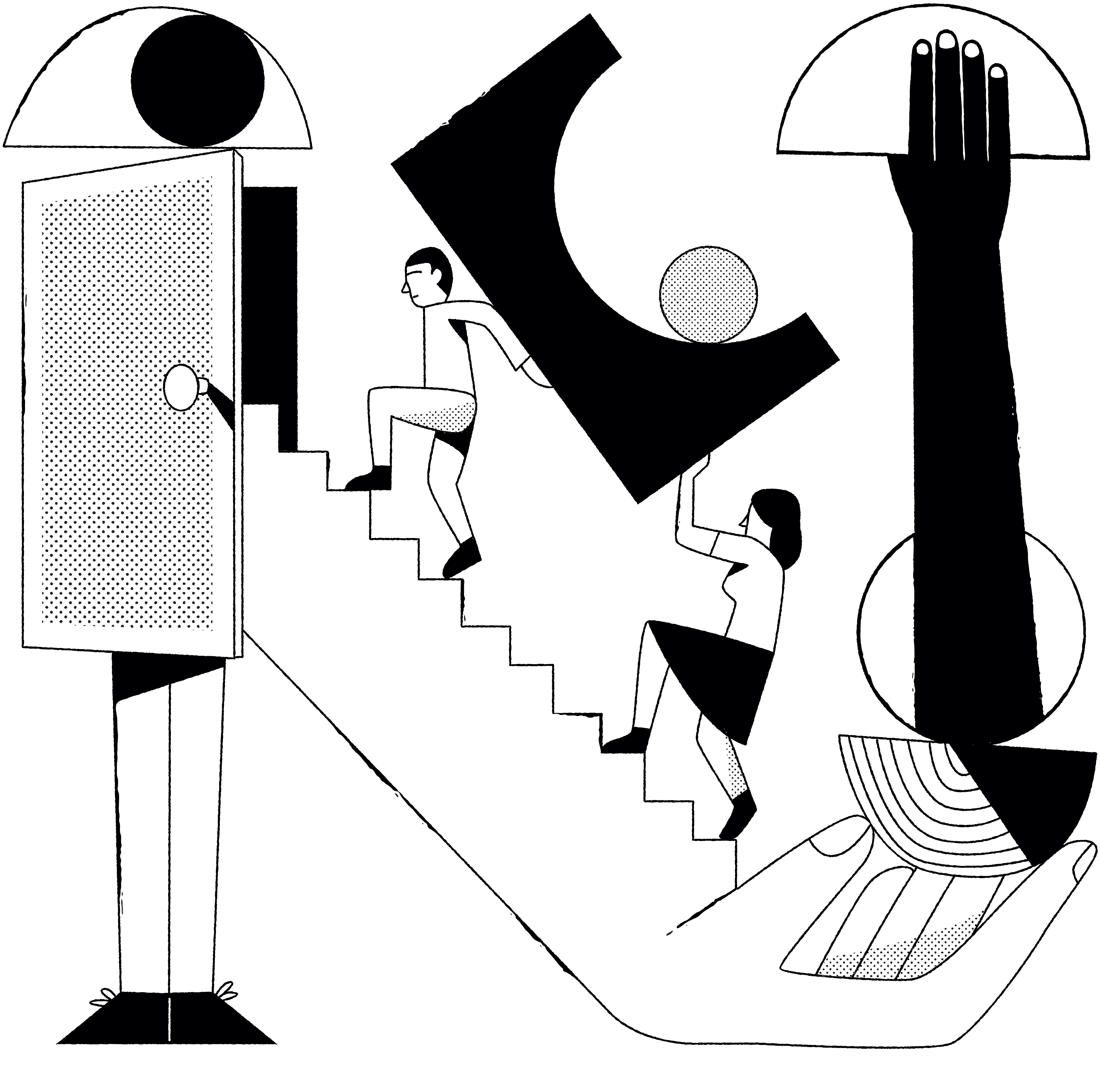
Stanford Business

SUMMER 2016



EQUITY

A LETTER FROM
DEAN GARTH SALONER

Looking at the Path Ahead

As I prepare to transition from the deanship to my faculty position at Stanford GSB, I have been reflecting on the research and teaching questions that interested me before I became dean. They have been influenced by the seven years I have been in this leadership position.

As my academic mental gears slowly start turning again (they are greatly in need of oil!), I have been thinking a lot about what is known as "path dependence" and its role in organizational strategy.

Path dependence is just a fancy academic way of saying that what you have done in the past strongly informs and influences what you can do in the future. This is true for individuals, and it is also true for organizations.

This is no less true for Stanford GSB. Over the past year I visited Japan, China, Chile, India, Kenya, and South Korea as well as much of the U.S. My primary purpose was to connect with alumni, but I also had the pleasure of meeting with young men and women who are considering a graduate business education. I heard time and time again that their dream is to come to the GSB. And, as our application statistics show year over year, we have clearly become the destination of choice for many of them. As I reflect on why this is the case, path dependence features prominently in my thinking.

Of course, we have benefited enormously from the ascendancy of Stanford University over the past 16 years under the leadership of outgoing President John Hennessy and Provost John Etchemendy, as well as from our symbiotic relationship with a flourishing Silicon Valley.

At the same time, we have blazed a path through our own deliberate efforts — not just over the past decade, but over many decades. We are in a position to do things now because of decisions that were made and directions that were taken years ago by our previous deans. Ernie Arbuckle led us on the path of combining rigor with relevance by embracing the social sciences. Arjay Miller added public management to our mission, a thrust that has enabled our current initiatives in social innovation. Mike Spence launched the Center for Entrepreneurial Studies, which I am so pleased to announce will soon be named for Professors Chuck Holloway and Irv Grousbeck. Bob Joss began and drove the campaign for the development of the Knight Management Center and the new curriculum that is now taught there. Our current experiential-based approach to teaching leadership has its roots in decades of teaching "touchy feely" interpersonal skills.

The culmination of these and so many other past decisions and actions makes us unique and demonstrates that Stanford GSB represents much more than "business school as usual." For prospective students, it holds the promise of a transformational opportunity that will allow them to pivot to a lifetime of meaning and impact — one that enables them to change lives, organizations, and the world.

The path upon which our 10th Stanford GSB dean, Jon Levin, will lead us will be influenced, as mine was, by our predecessors. I have known Jon for many years — first as a brilliant scholar in my own field of industrial organization, as described on page four in this magazine — and later as an equally brilliant administrator, whom I worked with when he was the head of the Department of Economics at Stanford University. When the dramatic increase in the status of such a department is the subject of articles in the international press, you know you are looking at the mark of great leadership.

One of the most important threads of our DNA is our alumni community. Thank you for all you have done for the school and for the support that I know Jon can count on in the future. For my part, I am excited about my return to teaching and look forward to staying in touch with all of you in the years ahead. It has been a privilege to serve as the ninth dean of a school that I love and that means so much to me and my family. Thank you.


Toni Bird
Garth Saloner

Garth Saloner is the Philip H. Knight Professor and outgoing Dean of Stanford Graduate School of Business.

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"People should be aware that there are constructive ways to ascend **the status hierarchy.**"

—**Nir Halevy**

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Stanford Business

INSIGHTS AND IDEAS FROM STANFORD GRADUATE SCHOOL OF BUSINESS

SUMMER 2016
VOLUME 84, NUMBER 2

EXODUS How should America confront a growing web of global crises, such as the millions of refugees fleeing countries besieged by war? PAGE 56

WORLD

Cover illustration by Christopher DeLorenzo

Top: Jerome Sessini/Magnum Photos; bottom: David Elliott

Jonathan Levin will begin serving as the new dean on September 1.

AN INTERVIEW WITH
NEW DEAN
JONATHAN LEVIN

An Economist Becomes the 10th Stanford GSB Dean

BY DEBORAH PETERSEN AND SHANA LYNCH

After Jonathan Levin was awarded the prestigious John Bates Clark Medal in 2011, a journal noted one of the many things that made the economist stand out from his peers: His exposure to economics started not in the classroom "but at the dinner table."

The newly appointed dean of Stanford GSB is the son of Richard Levin, an economist and former president of Yale University, and Jane Levin, PhD in English literature. The younger Levin had a seat at the table during recruiting dinners at his New Haven home. This included one attended by Barry Nalebuff, says the 2012 article in *Journal of Economic Perspectives*. Not only would Nalebuff (an author, game theory guru, and the cofounder of Honest Tea) become a professor of management at Yale, but he also soon recruited Levin as a research assistant. The paper they wrote about vote-counting schemes became Levin's first academic paper.

"I grew up in a family with two academics, and my father was an economist, so it was not a radical stretch," Levin, 43, says of his decision to become an economist.

"Then I went to Oxford, and I think I fell in love with economics reading GSB Professor David Kreps' textbook," he says. "It's this extraordinarily lucid explanation of microeconomics. It got me really excited about the field."

As an industrial economist who studies auction theory, Levin has worked on U.S. patent reform and informed a solution to a quintessential Silicon Valley challenge: accommodating the explosion in broadband demand. Taking advantage of the increasing availability of data that is making research easier, especially for economists, he studies U.S. health care costs and has brought new perspective to practical issues for firms about how to design their policies around compensation and incentives.

"My ideas can come from anywhere, from students or colleagues or newspapers," he says of what inspires his research. "I've always loved the way the great mathematical statistician David Blackwell explained what motivated him. He said he just wanted to understand things."

Toni Bird

> **"Teaching is a combination of persistence and innovation. You just have to keep iterating to get things to work."**

And, in the case of research, if you want to understand things, "sometimes you have to figure it out yourself because no one else has figured it out already."

As chairman of the economics department at Stanford from 2011 to 2014, Levin is no stranger to the campus nor to working with faculty and students. He was honored with teaching awards in 2004 and 2005 at Stanford.

"Teaching is a combination of persistence and innovation," he says. Sometimes, it goes great, and other times it does not. "You just have to keep iterating to get things to work," he says. "And then you have to switch up what you're doing before you get tired of it."

In some cases, he has even worked with professors before they came to Stanford GSB, including Susan Athey, who was teaching at MIT when Levin was a doctoral student there.

His passion for the design of auctions and marketplaces — the topic of his master's thesis at Oxford University — led him to collaborate with a team of economists to help design the Federal Communications Commission Broadcast Incentive Auction with the goal of trying to repurpose the broadcast television spectrum for wireless broadband.

"Technology has changed so that the most efficient use of radio spectrum is for people to use mobile devices and wireless broadband, rather than broadcast television, which was traditionally a large user of prime radio spectrum," he says.

"It's one of the most interesting auction problems I've encountered." The auction provides incentives to persuade more traditional licensees such as television stations to give up spectrum to wireless demands.

Technology, he says, also creates the opportunity to open up access to the educational experience in places like Stanford GSB. "In principle, online teaching is a transformative change in education," he says. "The question is how to educate in an effective way, how to create an economic model for it, and how to make sure the experience of the students is really fantastic."

Students at Stanford GSB not only have access to exceptional faculty and peers, he says, "they have opportunities all around the campus and across Silicon Valley to take advantage of all of the excitement and innovation in this area."

It creates an amazing educational experience for the students from the MBA and PhD programs to its MSx and executive education offerings, he says.

"Programs like Seed, the Ignite program, the online LEAD program are opportunities for Stanford GSB to reach a much broader audience and to bring that audience the sort of special mix of entrepreneurship, innovation, and scholarship that students here get."

When Levin was an undergraduate at Stanford, his favorite class was freshman math. "It was where I learned that there were so many people who were much, much smarter than I," he says.

"In the time that I've been at Stanford, I've had the chance to see what a great experience people have here at the GSB," he says. "It's such a phenomenal institution, with such a great faculty and exciting students, a cohesive and tight-knit community." That strong bond continues after students graduate. The alumni demonstrate a remarkable allegiance to the school and to each other, says Levin, who will start his new role in September. "Who wouldn't want to have the opportunity to be part of this community?"

Watch a video interview with Jonathan Levin: *http://stanford.io/1UOmC2c*

AT A GLANCE

Jonathan Levin

Education: BA in English, BS in Math, Stanford University; MPhil in Economics, Oxford; PhD in Economics, MIT

Awards: John Bates Clark Medal; Fellow of the American Academy of Arts and Sciences; World Economic Forum Young Global Leader

Family: Wife, Amy, a physician; three children

Book on your nightstand: *Big Science: Ernest Lawrence and the Invention That Launched the Military-Industrial Complex* by Michael Hiltzik

Favorite author: Norman Maclean

Best spot on Stanford campus: Stanford Dish

Hobbies: Tennis, hiking, reading

One thing you couldn't live without: My iPhone

Secret power: "I remain optimistic, even in faculty meetings."

Beach or mountains: Mountains

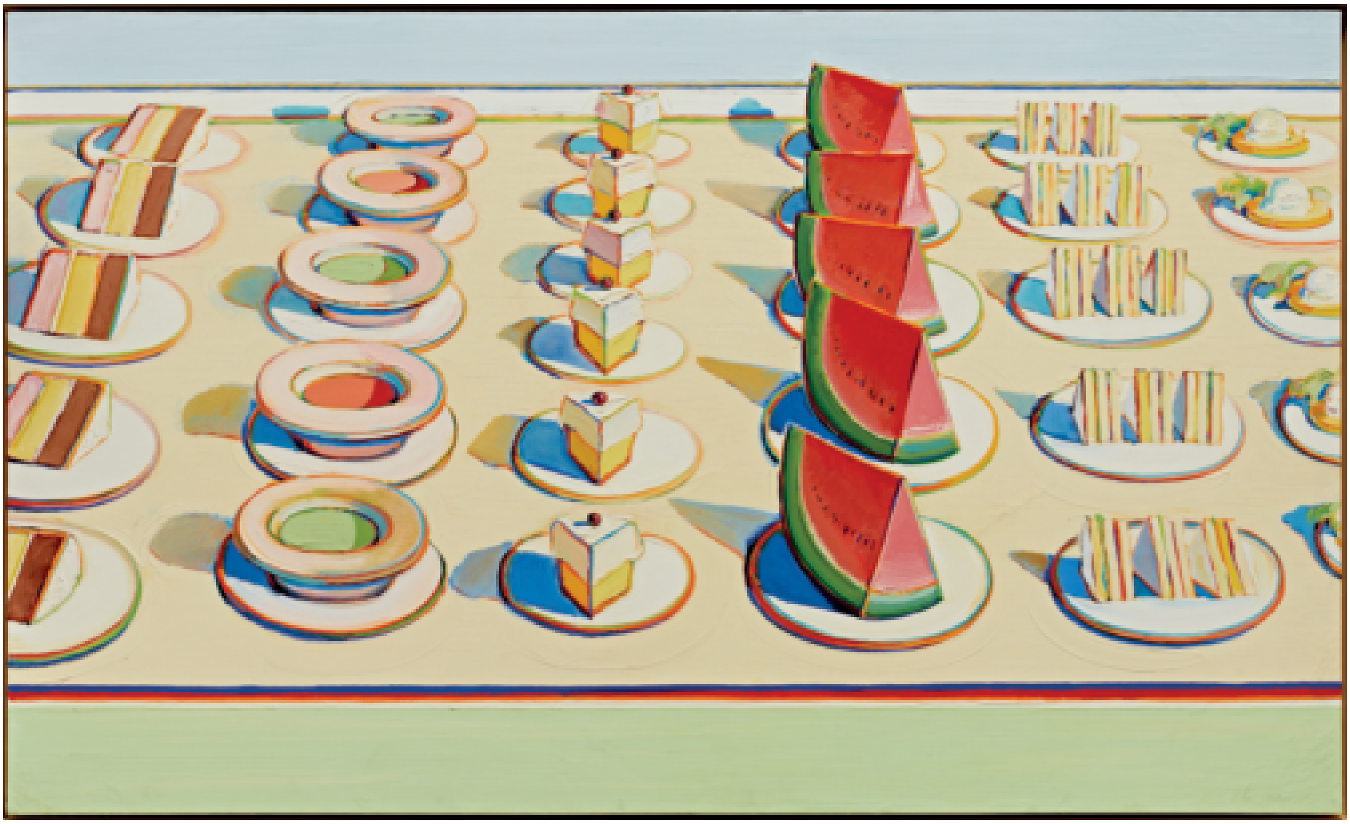
— SHANA LYNCH

INTRODUCTION

ENGAGE

Earlier this year, while making a presentation about *Stanford Business* magazine at a higher education conference for magazine editors, I asked what I thought was a simple question. ▶ *Who is your audience?* ▶ Many in the room looked up at me with blank stares. ▶ Perhaps I should have expected their response. The truth is that, as editors, we know *where* we send our magazines, but we often find it difficult to know *who* is actually reading our pages and, most important, what they think of our work. ▶ That is why we are starting a new section for you to do just that: Tell us who you are and what you think. ▶ In each issue we will prompt you with a specific question, but we also welcome you to send us commentary about any topic raised in the stories throughout the publication. We will edit the comments for space and clarity, of course, and select some to appear in the next issue. Our goal is to get to know you better and to help you learn more about each other as well.

— DEBORAH PETERSEN, EDITORIAL DIRECTOR



"Lunch Table" by Wayne Thiebaud

ENGAGE

Share Your Commentary With Us

Email *stanfordbusiness@stanford.edu* or send a note to *Deborah Petersen, Stanford Graduate School of Business, Knight Management Center, 655 Knight Way, Stanford, CA 94305.*

To Get You Started
Share a time when an equity question arose in your professional or personal life. How did you resolve it?

For me, the story is a personal one about pay equity. As the first in my family to graduate from a university, I suppose I was naive when I accepted my first job as a journalist in Connecticut. I happily accepted the pay, vacation, and health benefits package that was offered. A few years later, when the company conducted a pay equity study, I was told that, yes, I was underpaid compared with some of my peers.

It was only several years later, when I attended an all-day workshop on negotiation conducted by Margaret Neale, a Stanford GSB professor, that I learned how much my gender had played a role in my decision not to push for more pay — men are more likely to negotiate than women. Then, Neale shared some alarming math: An employee who negotiates just a $7,000 salary increase before starting a new job will, after 30 years, be making $100,000 more annually than she would have if she'd accepted the original offer.

After attending the workshop, I almost felt sorry for any hiring managers who sat across from me as I applied my new negotiating skills.

Almost.

Tell us *your* story.

—DEBORAH PETERSEN

STANFORD BUSINESS ONLINE

Arianna Huffington

Stacy Geiken

YOUTUBE

Sleep deprivation is the "cognitive equivalent of coming to work drunk."

Huffington Post founder Arianna Huffington promotes a better night's sleep as part of her View From the Top talk at Stanford GSB.

Watch More: *http://stanford.io/Sleep*

WEB

Solving the Pay Equity Problem

An economist shows how to close the salary gap.

Read More: *http://stanford.io/Family*

WEB

Finding the Next Billion-Dollar Company

Want to spot a unicorn? Look for the horse running against the herd.

Read More: *http://stanford.io/Unicorn*

WEB

Political Machinations

How candidates cater to — and shape — public opinion.

Read More: *http://stanford.io/Politics*

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Stanford Business magazine (ISSN 1094-5423) is published three times annually by Stanford Graduate School of Business.

Volume 84, Number 2. Printed in the United States.

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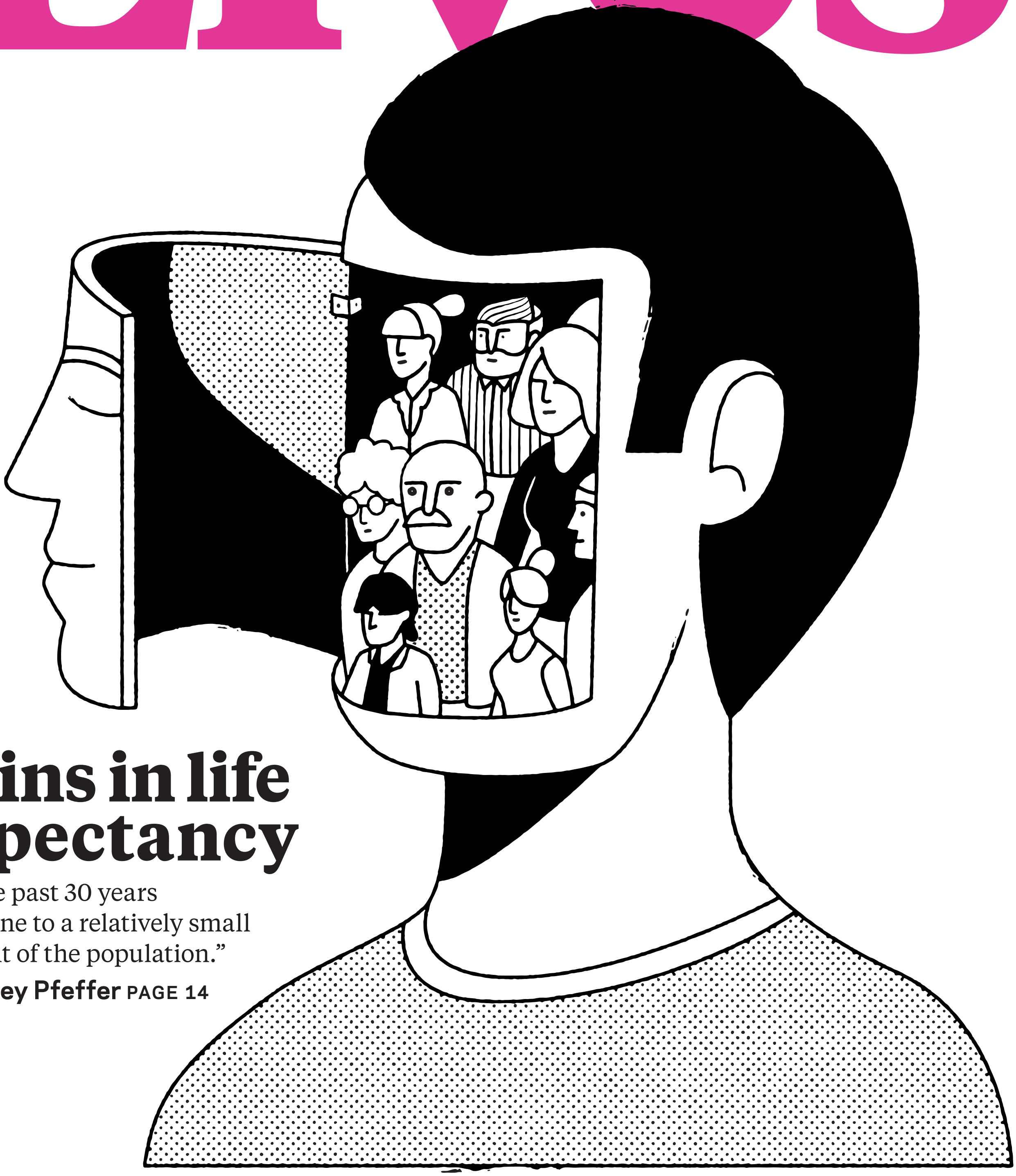


"Gains in life expectancy

over the past 30 years have gone to a relatively small segment of the population."

—**Jeffrey Pfeffer** PAGE 14

Christopher DeLorenzo

ENGAGEMENT

The 10-Minute Turnaround

With brief chats, canvassers can shift attitudes on divisive issues like transgender rights.

BY IAN CHIPMAN

For anyone who feels that healthy discourse is dead or at least increasingly out of reach in the current American political climate, a Stanford GSB professor says take heart. In a study published in *Science*, professor of political economy David Broockman found that a single 10-minute conversation with a stranger could reduce prejudice toward transgender people and increase support for nondiscrimination laws.

In 2015, Broockman and coauthor Joshua Kalla, a PhD student at the University of California, Berkeley, ran a field experiment to investigate the effects of a door-to-door canvassing operation conducted by the Los Angeles LGBT Center and SAVE (a South Florida LGBT organization) in Miami. The effort was organized after the Miami-Dade County Commission passed a law protecting transgender people from discrimination in housing, employment, and accommodations. To counter a potential public backlash and an increase in transphobia, the two LGBT advocacy organizations sent dozens of canvassers to knock on doors and talk with voters.

Both before and in several waves following those conversations, the researchers engaged a number of those voters in ostensibly unrelated online surveys to track their feelings toward transgender people. They found not only a dramatic decrease in transphobia and an increase in support for nondiscrimination laws after those conversations but also that the effects persisted for a period of at least three months following the encounters and were resistant to counterarguments.

These findings echo a now retracted paper by Michael LaCour and Donald Green about the effects of canvassing campaigns on support for gay marriage. Here, Broockman discusses what precipitated his research, what he found about changing people's attitudes, and how a greater understanding of interpersonal interactions might help advocates reduce prejudice.

David Broockman is an assistant professor of political economy at Stanford GSB.

Photograph by Aaron Wojack

DAVID BROOCKMAN
Personal interactions reduce prejudice.

Your study looks at how door-to-door canvassing can reduce prejudice toward transgender people. What made you want to investigate the effects of canvassing to begin with? I've long been interested in the effects of high-quality personal interaction from political campaigns. More than a decade of research has shown that these kinds of high-quality, face-to-face conversations are the best way to turn people out to vote. But there had been much less research on the role of such conversations in changing people's minds. And likewise, in the literature on prejudice, there had been very few studies that looked at whether there was some way to change somebody's attitudes about an out group along the basis of a personal conversation.

What motivated this study in particular, and how did you come to work with the Los Angeles LGBT Center? I wrote an article for *Vox* with Joshua Kalla in November 2014 about canvassing, citing this Michael LaCour and Donald Green study that I thought was so great, which then came out in *Science* in December of that year. It also really interested me in the work of the Los Angeles LGBT Center, which was what that study was ostensibly looking at.

I got to know Dave Fleischer, who is the head of the organization's Leadership LAB, and he asked me to study what they were working on with a Miami organization, SAVE. In planning the study to investigate canvassing's ability to reduce prejudice toward transgender people, we went back to look at LaCour's study. We examined the data and procedures much more carefully than one otherwise would because we wanted to follow that recipe. It's like the difference between eating a meal and hearing 15 seconds about how it was made — how most people were reading that study — versus actually trying to buy the ingredients and follow the recipe step-by-step.

> **"People have absorbed a lot of political messages that they believe on some surface level."**

That's when we realized a lot of things didn't add up. Ultimately, we brought some things in the data that we thought didn't look right to Green's attention. We realized that at least some of it was falsely described, and *Science* retracted it.

Everyone said, "Oh, well, now this hypothesis is disproven." No, it was just unproven. Despite the retraction, we knew we had to finish the Miami experiment, which had already been months in the planning.

How does your study differ? The big difference — because I don't want people to mistakenly think, "Oh, it was actually true all along" — is that with those findings it was all about the identity of the canvasser. It had to be a gay canvasser to change your mind. But we found that the canvasser's identity doesn't really seem to matter; both transgender and non-transgender canvassers were effective. What seems to matter most is that canvassers are experienced. And, of course, we weren't studying the same thing. These are attitudes toward transgender people, not toward gay people and marriage equality.

In your study, how much did people's minds change as a result of engaging in these conversations? We found a pretty large effect — and even more notably, a lasting effect. We saw a decrease in prejudice against transgender people as well as an increase in support for a nondiscrimination law that would protect transgender people from discrimination. The type of laws that, for example, the city of Charlotte passed and that the North Carolina legislature just got rid of. That's the kind of law that we find that people are more likely to support.

We used a feeling thermometer, which is a way to get a summary sense of how warmly or coolly someone feels toward a group, and saw a shift from those who had the conversation versus those who did not have it. It was similar to the shift you see in public opinion toward gay men and lesbians between 1998 and 2012.

So, when viewed in that way, it's about a decade and a half of change in 10 minutes.

Conventional wisdom holds that people's views are deeply ingrained and more or less impervious to persuasion. What do your results have to say about this stability of people's attitudes? I do want to caveat very heavily to say this is just one study. We also ran a similar study around the issue of abortion that found no effect. So it's not like this is some silver bullet, and I think we don't have the full story yet.

With that said, one hypothesis, which would be consistent with some public opinion research, would be that people have absorbed a lot of political messages that they believe on some surface level, but not on a deep level. Maybe the hardest-core partisans do, but a lot of people know what they're supposed to think, and they think that but not strongly. So when they have a rare moment that someone comes to their door and has a friendly conversation, all of a sudden they feel they've really made a decision about it in a lasting way.

How generalizable is that? Can it be generalized to climate change? To gun control? To racial prejudice? It could well be that this is an issue that is unique in some way. This is something that's animating a lot of politics, so even if this is just a way to reduce prejudice on this issue, I think that's great.

As evidenced by the recent law passed in North Carolina that you mentioned, and similar laws proposed elsewhere, transphobia seems pervasive even as homophobia seems on the decline. Why do you think that is? I think this is one of the next frontiers in the battle for LGBT rights. With the same-sex marriage issue largely off the political agenda in the U.S., both advocates and opponents of LGBT equality are turning to this issue more and more.

In some ways, we're seeing the same patterns that we saw with gay marriage, where 40 years ago in Miami — where this study took place — Anita Bryant had this infamous "Save Our Children" campaign that played on the same ideas about gay people that we're seeing about transgender people now: "You can't trust them around children. They are all sex offenders. They're unstable."

Those same stereotypes are being brought up again. And likewise, just as we saw with gay marriage over the last 10 or 20 years, opponents and supporters are going to use this issue to try to motivate people to vote.

What happened in these canvassing conversations that made them so effective in changing people's attitudes? There are two main theoretical paradigms at play here.

The first is the idea of perspective-taking, which is to think about what it's like to be somebody else in some way. The heart of the intervention is that canvassers build a rapport with people, where their goal is to try to get those people to tell stories of when they were discriminated against in their own life.

The second idea, called active processing, is just a fancy way of saying the difference between quick thinking and slow, effortful thinking. A recurring finding of laboratory studies is that a relatively short intervention can have a pretty lasting effect if people are engaged in this kind of effortful thinking.

Many theories suggest that prejudiced attitudes are resistant to change. Yet you found that this reduction in prejudice was remarkably resilient over time and even held strong against counterarguments. Does this fly in the face of what we thought we knew about attitude durability? I don't know if it flies in the face as much as it's a contrast to what we find when we study more impersonal tactics. The effects of mass media — mail and television ads, for example — typically decay within hours or days. One theory for what happens when people encounter arguments in mass media is that, again, they're not thinking them through. If you ask them about it the next day, they'll remember that they saw it. But they haven't actually taken the time to say, "I should really change how I think about this."

Our best guess of what's happening is that it's not just that someone shows up at your door and asks what you think. Instead, someone shows up at your door and asks you questions and gets you to have that kind of effortful thinking. Burning mental calories. That is what is leading people to remember this.

In contrast to the retracted study by LaCour and Green, which suggested that gay canvassers were able to change people's attitudes about gay marriage, your results show that the identity of the canvasser doesn't make much of a difference. Our best guess was that there was a small difference, but not much. Ultimately, the most important thing is what's happening in the mind of the person they're talking to. It's not likely about the message that the canvasser has, and it's not any aspect of them per se. It's about the work they get the voter to do. More experienced canvassers seem more effective, which points to the idea that knowing how to have these conversations is a skill that can be learned.

What else is particularly exciting about all this for you? Before, it was basically not feasible to study the effects of these interpersonal interactions on people's attitudes. We've taken a lot of best practices in experimental design and come up with a new method for studying canvassing, which we're releasing in a companion paper focused on the methodology itself and how to do it.

It opens the door for us to learn a lot more. More than anything, what I'm excited about is to do more work of this type, and to see others do more work of this type, and take advantage of this method.

Your work suggests there's some optimism for healthy discourse in an increasingly polarized public sphere. That's right. There have been two big shifts over the last 50 or 60 years in campaign practice. One is from personal contact to mass media contact. People who are politically ambitious, instead of staying in their communities and trying to build local organizations, now move to the coast and broadcast messages to the interior.

Second, the kinds of messages they're broadcasting are intended to take what people already believe and make them really angry or really excited about those things.

What we found suggests that campaigns might have more success than they expect trying to talk with people that have initially opposing views, even regarding controversial topics and across partisan lines.

So, for example, if you're a politician, I think our study underscores the following message from other research: It actually might be more effective to go meet voters one-on-one than to focus on raising money to send them mail. That is, it might be in politicians' and campaigners' own best interest to hear voters' concerns one-on-one. Therefore, regardless of the virtues of the causes that embrace this technique, I think our democracy as a whole will be better off as a result. ▲

CHANGE AGENT **Brief but thoughtful conversations reduce prejudice in lasting ways.**

HEALTH

Exploring the Inequities of Workplace Stress

Minorities are more likely to land jobs with "harmful work exposures."

BY MOLLIE BLOUDOFF-INDELICATO

Workplace stress can shave years off your life, according to a joint study by Stanford and Harvard researchers. But while these stressors, like job insecurity and high job demands, affect all American workers, they take the biggest toll on minorities and people with less education.

"The gains in life expectancy over the past 30 years have gone to a relatively small segment of the population, and there's another segment of the population — minorities — where it's gone in the other direction," says Jeffrey Pfeffer, an organizational behaviorist at Stanford Graduate School of Business.

Stressful jobs contribute to 120,000 deaths each year and cost U.S. businesses up to $190 billion in health care costs. These stressors particularly hurt minorities with low levels of education, who often work in unhealthy environments that can shorten lifespans. Researchers looked at 228 studies examining how 10 workplace stressors affect a person's health and used an algorithm to break down the results based on ethnicity.

Workplace stressors had the largest impact on non-Hispanic black men with less than 12 years of education, whose life expectancy decreased about 1.7 years. Non-Hispanic white women with more than 17 years of education were the least impacted, losing 0.3 years from their lives due to workplace stressors.

Pfeffer says he decided to study workplace stressors after skyrocketing health care costs kept showing up in the news. The U.S. government spends more on health care, per capita, than many other first-world countries. And while businesses were focused on coaxing individuals to practice healthier behaviors outside of the workplace, he adds, there was no research to show what kind of effect work had on an employee's health.

"We discovered that a significant fraction of the inequality in health outcomes can be attributed to the fact that the people with less education get sorted into jobs in which they are more likely to face harmful work exposures," Pfeffer says.

Workers with less education are more likely to take jobs with more workplace stress, such as those involving shift work, experiencing frequent layoffs, or demanding long hours. Occupations requiring more years of education also experience some of the same stressors, but those stressors are unlikely to have the same impact.

For example, an employee at a fast food chain has little job security and no job control. A banker, on the other hand, has a high level of control and more job stability. While both the fast food worker and the investment banker may have highly demanding jobs, says coauthor and operations researcher Stefanos Zenios, the banker is far more secure than the fast food employee.

"Pay attention to where you work if you have a choice," Zenios adds. "It does make a difference. It can cut your life expectancy."

Long term, however, there needs to be a shift in how companies treat employees, Pfeffer says. Instead of focusing on changing individual behaviors, like exercising more and smoking less, employers should take a hard look at the kinds of workplaces they're providing for employees. Because Americans spend so much time at work, a high-stress environment could push employees toward unhealthy habits, which increase health care costs for the company.

To prevent adverse health effects among employees, both Zenios and Pfeffer recommend putting time and effort into making the workplace less stressful. Creating a social support network, for example, can help employees better handle stress. Giving a manager more autonomy over tasks can also reduce stress.

Although the study is sound, the algorithm does have its limitations, says Joel Goh, an operations researcher at Harvard University. Because the data isn't perfect, the researchers used averages. Instead of differentiating between a fast food employee who was a fry cook and an employee at the same restaurant who was a manager, the health effects were averaged out, he adds. "We knew the limitation of this going into it," Goh says, "[but] having something imperfect is better than having nothing at all."

The next step is to use this information to advocate for workers, and minority workers in particular, Zenios says. Any improvements within the workplace will reduce mortality — and benefit the bottom line.

"If companies are serious about controlling their health care costs, they need to work on the problems caused by these [adverse] exposures," Pfeffer adds.

Jeffrey Pfeffer is the Thomas D. Dee II Professor of Organizational Behavior and the Hank McKinnell-Pfizer Inc. Faculty Fellow for 2015-16 at Stanford GSB. Stefanos Zenios is the Investment Group of Santa Barbara Professor of Entrepreneurship and professor of operations, information, and technology at Stanford GSB.

Illustration by Edel Rodriguez

HIERARCHY

The Peril of Power Without Status

Want to reduce conflict? Be careful with your org charts.

BY LOUISE LEE

Face it: Despite talk of flat, egalitarian workplaces where everyone is a "team member," some workers have more status or power than others. Some people have both status and power, some have neither, while others have some combination of the two. And, says Nir Halevy, a Stanford Graduate School of Business professor, those with little status but plenty of power can create corporate havoc not because they're unpleasant people, but because their unenviable positions make them prone to bad behavior.

Managers can reduce conflict, Halevy and his fellow researchers conclude, by avoiding placing workers in positions that sit low in a corporation's status hierarchy but that give them significant power over others.

In research published in the February issue of *Organization Science*, Halevy says that such high-power/low-status individuals are at risk of treating others in rude or demeaning ways. The paper, with lead author Eric M. Anicich of Columbia University, Adam D. Galinsky of Columbia, and Nathanael J. Fast of the University of Southern California, emphasizes the seldom-recognized distinction between status and power. By their definitions, people with status are respected and admired, while people with power control resources and influence outcomes.

Compare, for instance, the position of chief executive, which carries both power and status, with the position of professor emeritus, which bestows status but little power. Both the professor and the CEO benefit from the positive feelings that come with high status and thus are likely to treat others well, the researchers say.

On the flip side, people in low-status jobs often receive little respect and thus experience negative feelings about themselves and others. "People with a lot of control over resources but little of the respect that comes with high status may be prone to act based on the negative feelings that they have," says Halevy. "And they can have a negative impact because they control resources, so power without status is toxic."

In one of several experiments, the researchers recruited 226 adults and randomly assigned them into four organizational roles reflecting different combinations of status and power levels. Those with high power were told that "you need to lay off one of your employees," while those with little power were told that "your boss asked you to lay off one of the other employees." Each person then wrote a layoff memo. Next, a separate group of individuals, who remained uninformed about the power and status level of any of the writers, each read one layoff notice and reported the level of conflict they anticipated with the writer. The recipients also rated the extent to which the layoff memos were "demeaning," "humiliating," "degrading," and "uncomfortable." Those who received memos written by people in the low-status/high-power role were most likely to regard the messages as demeaning and to anticipate conflict with the writer.

Another experiment, in which the researchers polled 108 anonymous workers, determined that conflict initiated by a person in a low-status/high-power job is likely to continue and perhaps even escalate into a spiral of incivility. The target retaliates, causing the originator to feel even worse and to act again, leading to yet more retaliation by the target.

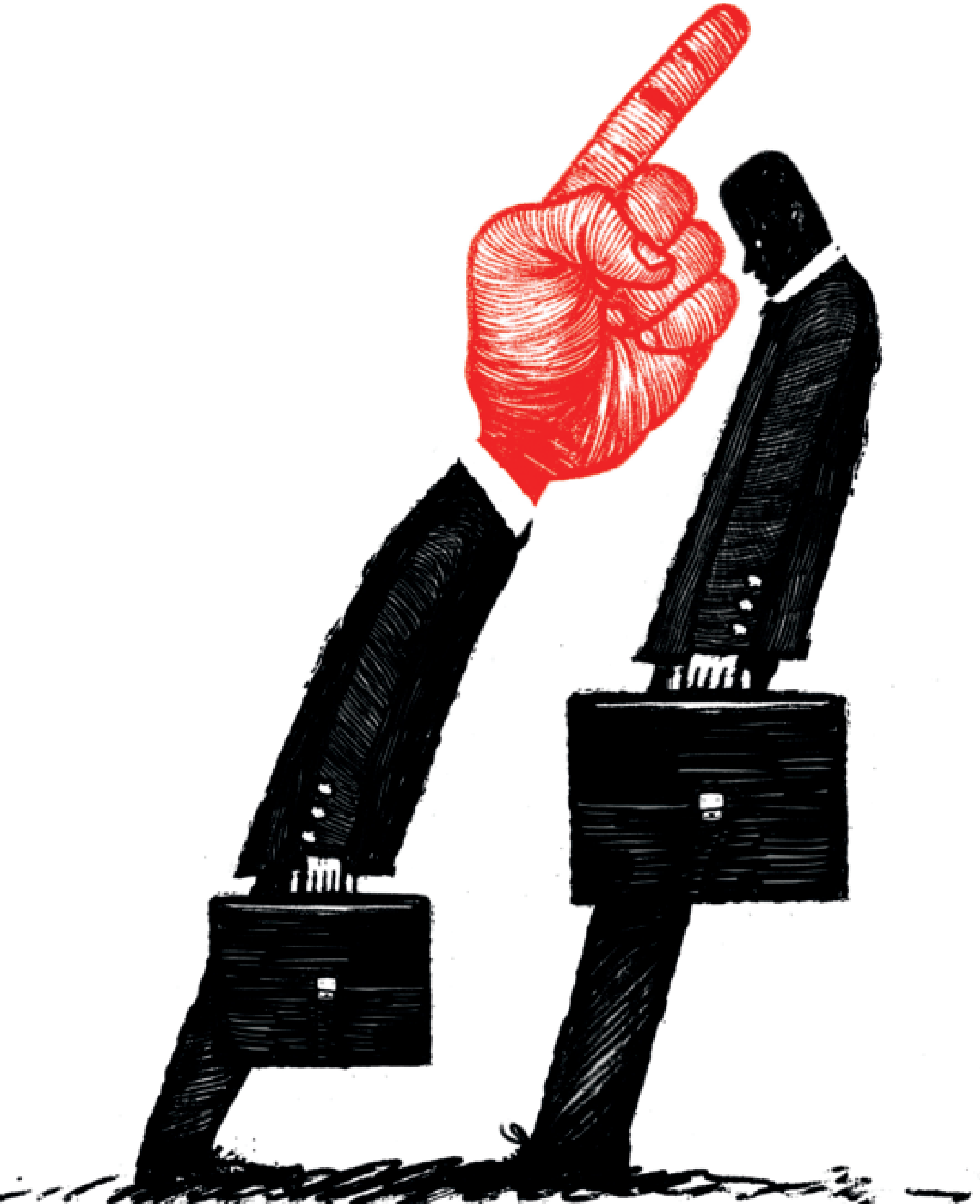
Managers trying to reduce workplace friction need to remember that distasteful temperaments aren't necessarily the root cause of conflict. "Don't single out people in those tough positions and say they have a difficult personality," says Halevy. "Rather, understand that sometimes the role is the source of the problem."

The researchers say that managers should examine positions of low status and high power and consider elevating role-holders' stature, perhaps by changing the job title or acknowledging the workers' contributions to the company's mission and success. And when an employee gains additional power, he or she should be given a commensurate boost in status as well.

And what if you yourself sense that you're acting out due to your own position of low status but high power? By mistreating others, you'll further reduce your status in the eyes of coworkers and feel even more disrespected, setting up a "vicious cycle" of conflict, the researchers say. You're better off using your energy to boost your status by, for instance, contributing more and demonstrating your competence. "People should be aware that there are constructive ways to ascend the status hierarchy," says Halevy.

Nir Halevy is an associate professor of organizational behavior at Stanford GSB. "When the Bases of Social Hierarchy Collide: Power Without Status Drives Interpersonal Conflict," written with lead author Eric M. Anicich of Columbia University, Adam D. Galinsky of Columbia, and Nathanael J. Fast of the University of Southern California, was published in *Organization Science* in February.

Illustration by David Foldvari



Joe Robbins/Getty Images

MARKETING

Real Men Wear Pink; the Rest Lie About Their Height

Make sure your male customers are secure in their masculinity before you pitch them skin cream.

BY EILENE ZIMMERMAN

The phrase "real man" usually brings to mind images of muscular athletes or military heroes, men who are physically strong, aggressive, and powerful. Those depictions of masculinity may seem outdated in a society where the notion of gender is ever-evolving, but in fact many men still want to project an image of physical strength and preferences that clearly set them apart from women, says Benoît Monin, a professor at Stanford Graduate School of Business.

When their masculinity is threatened, many men scramble to recover it, using strategies such as avoiding stereotypically feminine products and activities — think moisturizing lotions, day spas, or figure skating — and exaggerating their own stereotypical masculine characteristics such as their height or the number of women they've dated, Monin's research shows.

Although on the surface this may look like a lot of assertive chest-thumping, Monin says it's really about identity and people's sense of belonging to important groups. He and his colleagues have studied threats to identity before, as it relates to different ethnic groups. Looking at what it means to be a man is a novel direction, says Monin, but overall the logic is the same. "In the same way that we find that when Asian Americans' identity as Americans is questioned they reassert it by displaying local cultural knowledge and choosing typical American food, men whose masculinity is questioned react by exaggerating characteristics they associate with masculinity and downplaying feminine ones." Monin and three colleagues examined the strategies men use to compensate when their masculinity is threatened.

They conducted two studies. In the first study, men were asked to complete a computer-based "masculinity test" and were told it measured the level of their masculinity as compared with other men (in reality, men were randomly assigned scores). After the test, participants were asked about their interest in receiving a variety of products seen as either masculine, feminine, or gender neutral. The second study used a handgrip test to rank the physical strength of participants. The results purportedly showed how strong a man's grip was compared with the average grip strength for a woman (again, participants were randomly assigned a score). After seeing their score, the men answered questions about things like their height, number of previous relationships, handiness with tools, and certain masculine and feminine personality traits.

Men who were told they scored low on the masculinity tests were less interested in receiving products seen as feminine, like clothing and beauty products, compared with the other men, who were equally interested in all products. The men who believed they had scored low also significantly exaggerated their height, claimed having had a greater number of past relationship partners, and reported higher levels of aggressiveness and athleticism than men whose masculinity wasn't threatened.

Monin says these findings have implications for companies. If men who feel their masculinity is threatened are willing to exaggerate their height or the number of their previous relationships, those who feel that way at work because of negative feedback or evaluations may be equally willing to behave unethically (for example, stretching performance numbers) to reassert themselves.

Those men could also react by behaving in a hostile manner, as suggested by the higher reported aggressiveness among

MALE IMAGE How men view themselves should matter to marketers.

threatened participants. "It could explain why some men react to frustration on the job or to a threat to status at work by lashing out at employees or coworkers," says Monin. For managers, predicting what men might do when they feel threatened could help prevent the resulting negative consequences.

The findings also say something about male consumer behavior. The studies showed that one determinant of whether or not men will embrace products considered feminine is how secure those men are about their masculinity. This directly relates to the market for male beauty and grooming products, which is potentially huge, but getting men to embrace those products has proved challenging. "Marketers have to figure out how to alleviate concerns about masculinity as they try to convince men to buy products that could be perceived as feminine," such as skin care products, says Monin. "These companies need to design ads and marketing campaigns that make men feel very secure in their masculinity."

"These companies need to design ads that make men feel very secure in their masculinity."

Benoît Monin is a professor of organizational behavior at Stanford GSB and professor of psychology in the School of Humanities and Sciences at Stanford University.

OPPORTUNITY

Three Entrepreneurs Discuss Their Startup Journeys

BY ERIKA BROWN EKIEL

"We are looking for entrepreneurs in Africa."

Originally from Tanzania, **Mbwana Alliy** went on to earn degrees in England and America, all the while planning to eventually return home to East Africa.

Upon returning, he cofounded Savannah Fund, a seed capital investment firm located in Nairobi, Kenya, with links to Silicon Valley, where he first worked at a small accelerator fund, i/o ventures. He invests small sums of capital — between $25,000 and $500,000 — in ambitious early-stage mobile and internet startups in sub-Saharan Africa. To date, he has made 22 investments in six countries.

He graduated from the University of Bristol with a degree in electrical and communications engineering before working as an aerospace systems engineer at the UK's Defense Evaluation Research Agency (now known as QinetiQ). Later he became a product manager at Microsoft after earning his MBA from Stanford Graduate School of Business in 2007.

Alliy talked to *Stanford Business* about the negative impacts of Ebola, terrorism, and well-meaning charitable organizations on entrepreneurship in Africa.

In 10 words or fewer, what is the big idea behind your business? We want to be the leading venture capital firm in Africa.

Why now? Africa is about to peak: Smartphone connectivity, an emerging middle class, and opportunities for technology are unprecedented. People are starting to see Africa as a private-sector market, rather than just a recipient for aid. Africa is not just composed of poor people who need to be saved. People here want the same things people have in the U.S.

How do you describe your primary target audience? We are looking for entrepreneurs in Africa who are shut off from access to risk capital. There is too much "soft" capital; they do not only depend on grants. Some entrepreneurs want to raise risk capital to build large-scale, fast-growing businesses. They are bold and can navigate the local environment, versus foreign founders coming to Africa for opportunity. The Alibaba of Africa will be founded by an African.

What are your biggest challenges right now in building your business? Fundraising. Explaining to investors that there is an opportunity in tech VC in Africa. This is not yet a proven category. When there is a negative event, like Ebola or a terrorist incident, investment momentum gets set back and talent leaves. Operating in emerging markets can be harsh; entrepreneurs burn out quickly. Roads are badly congested, which leads to negative productivity. The ecosystem is still developing, so it can be harder to find competent lawyers, advisors, product managers, and others who are willing to work with startups for lower fees. One year of operating in Africa is like two or three years in the U.S.

What is the best advice you've ever received? I have climbed Mount Kilimanjaro three times. The guides have a saying: "Pole, pole. Slow, slow." They keep you from getting altitude sickness by ascending the mountain too quickly. You can easily burn out. You need to take three steps up because you slide two steps back. It is like entrepreneurship in Africa. You are pushing against corruption and unreliable roads. You will still get up to the top, but you can't think of these as normal steps.

What was the most difficult lesson you have learned on the job? Convincing entrepreneurs in Africa, particularly Kenya, that venture capital is the right way to go for their business, rather than accept free donor money. Venture capital is still largely a foreign concept. We want better reporting than they are used to. We ask for monthly updates on users and churn just like Valley-backed startups. We require proper governance and accountability.

What inspires you? How do you come up with your best ideas? Travel and photography. I get out, turn off everything, including the internet, and allow my mind to recharge.

What impact would you like to have on the world? I love helping a founder of a company that starts in obscurity in Africa without capital or a network to get a venture off the ground. It does not have to come from an incubator in Silicon Valley.

Mbwana Alliy

What was your first paying job? I was an aerospace test engineer. My mentor never went to college but took the apprenticeship route. When he first showed me all the parts of a new helicopter, it was like he was showing me the inside of his apartment. The way he learned was through experience, not through theory. That is how I work. I talk to people on the bus or when I am walking around in the market. I want to know what technology they use and why.

What businessperson do you most admire? Said Salim Awadh Bakhresa. He started out as a shoe polisher in Zanzibar and now his business is the biggest conglomerate in Tanzania.

What do you think is the greatest innovation in the past decade? The introduction of mobile money and payments in Africa. Basic technology and a little business model innovation have leapfrogged traditional banking infrastructure. People who have never had a bank account use mobile money to pay their rent and get paid.

"Men have always cared about the way they look."

Soon after **Nick Karnaze** returned from service in Afghanistan, the U.S. Marine Corps Special Operations combat veteran learned that one of his close friends had been killed in Afghanistan. Karnaze grew out his beard for the funeral. His search for solutions to the itching of the new growth inspired him to start stubble & 'stache, a company that makes beard care and skincare products for men.

Based in Arlington, Virginia, the company sells a wash and moisturizer for face and beard, as well as a styling beard balm. The CEO, who attended the Ignite program at Stanford Graduate School of Business in 2015, is also committed to donating a portion of his company's profits to benefit wounded veterans.

In 10 words or fewer, what is the big idea behind your business? Men want to look and feel good about themselves.

Why now? Men have always cared about the way they look, whether they admit it or not. It used to be considered not manly to pay attention to your appearance, but that is

Nick Karnaze

changing. Not long ago you had to get your hair or skin products from your girlfriend or wife. In 2014 the men's toiletry market surpassed the men's shaving market for the first time. It could be that more men are growing facial hair. Maybe they lost jobs in the recession and didn't need to shave every day, or they work at a startup where the culture is more relaxed.

How do you describe your primary target audience? Our primary target audience is men, 25 to 40 years old, who have facial hair and care about their appearance and personal health. Half of our buyers are women who are getting products for their husbands. We have a lot of traction in the military and veteran community. After they leave the service, a lot of men who shaved every single day will grow out their beards because they can.

Hipsters are another market for us. Having a beard has become a sort of refined masculinity. We are aiming for James Bond meets The Most Interesting Man in the World.

What are your biggest challenges right now in building your business? Brand awareness.

What is the best advice you've ever received? One of the first things they teach you in the Marine Corps is: no plan survives first contact with the enemy. You need to put together a good plan and understand what you are doing. But once the first shot is fired, your plan goes out the window. You have to keep thinking, "How can we move forward? How can we adjust?"

What was the most difficult lesson you have learned on the job? I didn't appreciate how lonely it would be to have a single-founder startup. It's like solitary confinement. It is very important to have a network of people you can reach out to who understand what you're going through. I needed help to get traction. My aunt used to work in PR and gave me a list of writers and bloggers to call. In one day we did more sales than the first two months combined.

What advice would you give other entrepreneurs? Life's a team sport. You can't do anything of value entirely on your own. Don't be afraid to ask for help.

What inspires you? I used to be shy. Now I just walk up to people with beards and talk to them. I'll see a guy with a beard and ask about his grooming routine. I also ask his partner: What do you think about his beard? I look for points of friction. Our beard balm came from those conversations.

What is your greatest achievement? On my last deployment to Afghanistan, we were doing a lot of traditional special operations: kinetic operations, or kill/capture missions. It wasn't achieving the desired effect. Instead of focusing on the enemy, we decided to focus our attention on the people in the community. I visited with the village elders and learned about an important road. It used to connect two villages and served as a trading hub before it became a violent area that people were unable to cross. Crops were dying and tourists stopped coming. I proposed a project to connect the two villages and provide micro-grants to local businessmen.

What impact would you like to have on the world? I want people to know they are not alone. I testified before the Senate Committee on Veterans Affairs in an effort to improve veterans' access to mental health care through the VA. It is easy as a veteran to feel you are alone. Civilians don't always "get" you. We will all have dark days. I want to do things that bring people together.

What was your first paying job? When I was 6, we lived on a golf course. We used to get a lot of stray balls in our yard. I sold them back to the players. When I was in high school, I was a waiter at a retirement community. I remember one couple I met there. After we talked a bit, they rolled up their sleeves and showed me their tattoos from Auschwitz where they met. They told me their story and then said, "Nothing is impossible."

What is the best business book you have read? *Good to Great* by Jim Collins.

What businessperson do you most admire? My mother. She raised two kids, worked full time, and pursued her master's degree. She became an executive with a network of hospitals. She maintained a balance of looking out for her family while also commanding respect from the people who worked for her. She defined for me the image of what I thought a strong business person would look like.

What do you think is the greatest innovation in the past decade? The rise of social media. Platforms like Twitter, Facebook, and Instagram that allow small businesses like mine to compete with billion-dollar companies and achieve market share. Those same platforms can be used to start movements and overthrow governments.

"The place where you live carries a lot of emotion."

As residents of the San Francisco Bay Area, **Alex Lofton** and **Jonathan Asmis** saw firsthand how rising costs of housing can make homeownership impossible for many who want to buy their first home. Seeking a solution, they founded Landed Inc. just weeks after earning their MBAs from Stanford Graduate School of Business in June 2015.

Lofton and Asmis are taking a new approach to equity. Landed raises capital from outside investors who want a piece of their local real estate market and uses those funds to help people buy their first home. Landed has raised more than $1 million for home-buying teachers in California so far. For those who already have a 10% down payment on a house, Landed will match those funds to give the homeowner a 20% total down payment.

After seven years, the homeowner pays back the invested capital, as well as up to 25% of any increase in value on the house if it appreciates.

The fledgling company is backed by angel investors from the Stanford community, as well as Y Combinator. Lofton talked with *Stanford Business* about his venture.

In 10 words or fewer, what is the big idea behind your business? "Smarter home ownership" is people helping people buy their first home.

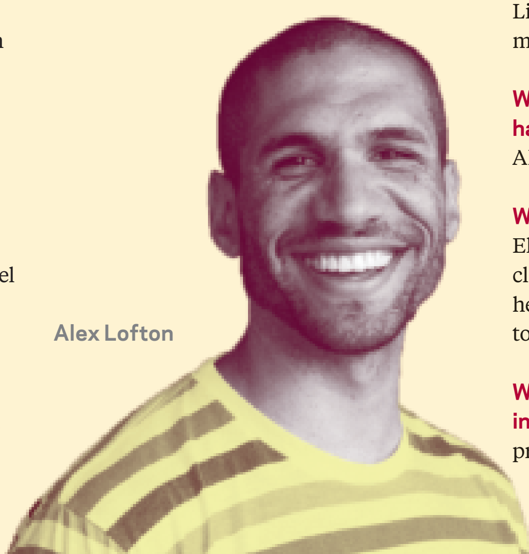
Why now? The place where you live carries a lot of emotion and is the biggest financial investment for most people. Having a roof over your head that you own is part of the American dream and can give you a sense of security, control, and togetherness. However, it is harder and harder to achieve in places like the Bay Area. Even people with high-paying jobs need help.

At the same time, investors are looking for more places to put their money. Residential homes are historically hard to invest in unless you do it at scale. Community investment is a smarter way for people to build wealth.

How would you describe your business model? We connect home buyers and people who want to invest in homes so that they can share the upside and the downside of home investment. Our role in that is to make sure both sides are holding up their end of the bargain and to provide a marketplace.

Personally, I have family members who lost everything in the real estate crisis of 2009. There is responsibility on every side. My relatives took on more risk than they should have and ended up losing their home. I feel personally passionate about playing a market maker role in this. There is a big problem that needs to be figured out.

How do you describe your primary target audience? Our buyers are first-time buyers, mostly millennials, in stable jobs making relatively good money but unable to buy a home without help. Right now they have only two choices: rent or take out a big mortgage. We think there should be more options. Perhaps larger family-and-friend networks want to invest in them. More than 50% of people already get help from their families to buy their first homes.



Alex Lofton

What are your biggest challenges right now in building your business? Continuing to deliver real value to the customers we have, as well as building a strong pipeline of new customers. It can be dangerous to blow a lot of money on a marketing campaign when you still need to put so much care into customer relationships and build a reputation.

What is the best advice you've ever received? A friend told me a few years ago to always start with self-care. There is a chance you will fail. All you have at the end is yourself. I find ways to laugh even when things are stressful. I love the dance floor and yoga.

What was the most difficult lesson you have learned on the job? When we first got started, we didn't know what we were doing. We had a great idea and started to engage with a buyer in Los Angeles. We tried to match him with an outside investor but were not able to come through for him. We ended up having to scramble to find an alternative way for him to purchase the house. It put into perspective how central buying a house is to people's lives. The design processes of iterating and failing fast are not always aligned with something as big as a home purchase.

What values are important to you in business? Being real with yourself and your business, both with the solutions you are creating as well as the problems you are exacerbating.

What impact would you like to have on the world? I would love to be an example for people of how to get more and more comfortable with stuff "outside the box." Life is not a rigid, controllable reality. It's much more fluid than that.

What is the best business book you have read? *Business Model Generation* by Alexander Osterwalder and Yves Pigneur.

What businessperson do you most admire? Elon Musk, CEO of Tesla and SpaceX. He is clear about the problems in the world that he wants to go after. He gives me permission to think and dream wild and act on stuff.

What do you think is the greatest innovation in the past decade? 3D printing. ▲

FINANCE

Homeowners Need a New Kind of Lifesaver

Banks and borrowers alike would benefit from automatic rate adjustments during recesssions.

BY EDMUND L. ANDREWS

The federal government spent countless billions during the Great Recession to help troubled homeowners avoid foreclosure, and the results were, at best, mixed. But what if mortgages themselves came with built-in protection, an "automatic stabilizer" that would reduce a borrower's interest rate during a recession? What if that protection cost little or nothing for banks or taxpayers to provide?

Two economists, Arvind Krishnamurthy at Stanford Graduate School of Business and Janice Eberly at Northwestern's Kellogg School of Management, outline exactly that kind of idea and argue it could be a win for all sides — banks, homeowners, and the economy as a whole.

Both economists have deep experience in the field. Krishnamurthy is a leading analyst of the Federal Reserve's rescue efforts, which included buying up trillions of dollars in mortgage-backed securities. Eberly, who served as assistant secretary of the Treasury for economic policy from 2011 to 2013, led efforts to retool the Obama administration's foreclosure-prevention programs.

In their research for the Brookings Papers on Economic Activity, the two develop a framework for analyzing alternative strategies for helping homeowners if a similar crisis arises in the future. One key idea: an automatic mortgage stabilizer that would become a standard feature of any home loan.

One raging debate during the mortgage meltdown was whether the government should reduce the principal amounts that homeowners owed on their mortgages. Advocates of debt reduction argued that it was crucial to prevent a wave of "strategic defaults" by underwater borrowers — those whose homes had fallen in value to less than their unpaid mortgage.

Krishnamurthy and Eberly disagree. Many troubled borrowers, even those who are underwater, will go to great lengths to avoid losing their homes. The bigger problem is that millions of people simply can't keep up with their payments during a recession. They also have to cut back on all other spending, which only adds to the economic downturn.

"What you want to do is create the maximum amount of relief upfront, during the crisis," Krishnamurthy says. "Reducing principal is helpful, but the benefits are spread over the life of the mortgage. It doesn't do much to boost consumption and reduce defaults during the crisis."

By driving interest rates down to almost record lows, the Federal Reserve did indeed help many homeowners reduce their monthly payments. But most distressed borrowers weren't able to refinance, at least not without government help, because their incomes and creditworthiness had fallen and banks had drastically tightened lending standards. Those whose loans were underwater could not get a new one for an equivalent amount because it would exceed the value of the home.

"The Fed's monetary policies couldn't target distressed households," Krishnamurthy says.

The proposed automatic stabilizer could be a standard feature of every new mortgage. In effect, it's a provision that would automatically let borrowers reset their mortgage at a lower interest rate during a recession.

The lower rate wouldn't have to be subsidized by either the bank or the government, because interest rates almost always decline in a recession anyway. Indeed, millions of homeowners whose finances were still solid enough to qualify for a new mortgage did in fact reduce their monthly payments by hundreds of dollars.

The new stabilizer would provide that same opportunity to distressed homeowners, even if they are underwater and unable to get a new mortgage at a lower rate. "It's essentially an automatic refinancing, and it's much cheaper and easier than going through the whole process of getting a new mortgage," Krishnamurthy says. It might seem that this kind of protection would add to the cost of a standard mortgage. After all, a lender loses revenue when it reduces the interest rate its borrowers have to pay.

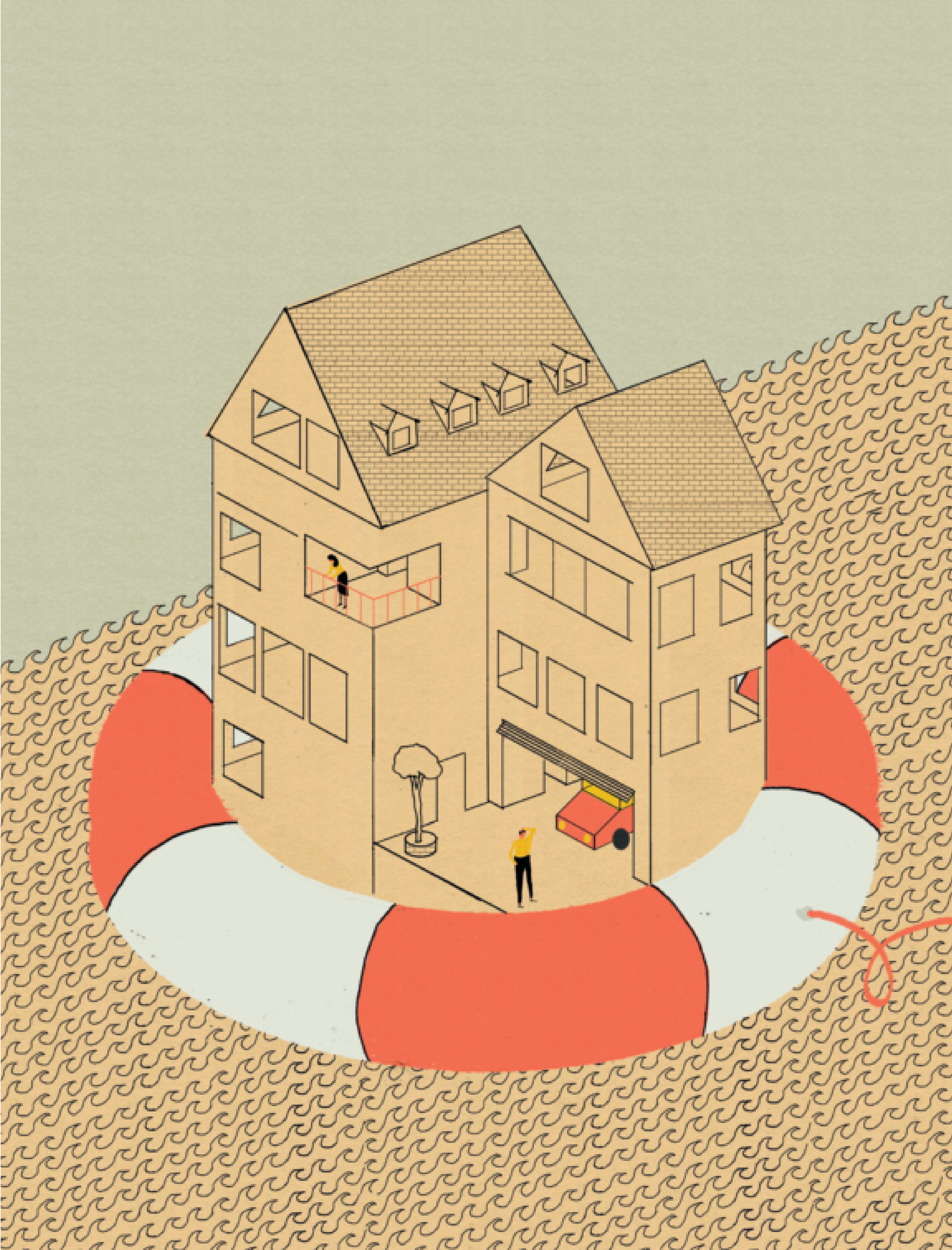
But Krishnamurthy says that doesn't have to be the case. In fact, he says, it is possible that the automatic stabilizer would actually reduce a bank's cost. The key reason is that investors in mortgages already price in the risk of lower rates. Banks and institutional investors know that many borrowers will refinance if interest rates drop significantly, so they already factor that potential cost into the price of a mortgage.

On top of that, Krishnamurthy says, the automatic stabilizer may actually reduce a bank's cost by reducing the risk of default during bad times. "It could be a win-win," he says. "The big advantage of this proposal is that it is very close to what banks are already doing. It wouldn't be a radical change."

Krishnamurthy and Eberly are not saying that an automatic stabilizer mortgage would resolve a crisis on its own. In a severe meltdown like the last one, the government may still have to prop up homeowners and the economy with taxpayer money. The main purpose of their paper is to identify the most effective way to deploy those scarce public resources when that kind of crisis arrives. Nevertheless, their proposal offers a creative new tool that could ease the next crisis before the government has to step in.

Arvind Krishnamurthy is a professor of finance at Stanford GSB. Janice Eberly is the James R. and Helen D. Russell Professor of Finance at the Kellogg School of Management at Northwestern University.

Illustration by Ryan Peltier



PERCEPTION

Why Privilege Is Hard to Accept

Faced with evidence of their racial advantage, white Americans exaggerate their hardships.

BY KERRY A. DOLAN

In the past few years, the killings of unarmed black men by police officers, as well as a mass shooting in a black church in South Carolina, have garnered enormous media attention. The shootings have become touch points in a larger discussion about race relations and racial bias in the United States. Amid the dialogue are references to the privileges that white Americans enjoy solely because of their race.

But Stanford researchers found that on an individual level, whites do not think that the privileges extend to them.

The research by L. Taylor Phillips, a PhD student at Stanford Graduate School of Business, and Brian Lowery, a professor at Stanford GSB, found that whites exposed to evidence of racial privilege responded by claiming their own personal hardships.

Brian Lowery is the Walter Kenneth Kilpatrick Professor of Organizational Behavior at Stanford GSB, where L. Taylor Phillips is a doctoral student of organizational behavior.

Illustration by Laurie Hastings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Those surveyed didn't deny the existence of racial privileges held by whites as a group, they just came up with other reasons — namely, personal obstacles — why they should be considered differently from that overall group.

How does Lowery explain this? He says, "You like to have nice things. But you don't want to think you got those things as a result of unearned advantages." People feel better about what they have if they believe they have earned those things as a result of hard work, not via birthright. So denying built-in advantages is essentially a form of self-protection.

Plenty of studies have documented that white Americans have numerous advantages: greater lifetime earnings, longer life expectancies, and better access to health care and quality education than blacks do. Phillips and Lowery say that despite the persistence of racial privilege in America, "policymakers and power brokers continue to debate whether racial privilege even exists and whether to address such inequity."

The study attempts to answer a hypothesis about why this is so: Perhaps those in power aren't moved to change the status quo because they are unwilling to acknowledge racial privilege even exists. "This acknowledgement … may be difficult given that whites are motivated to believe that meritocratic systems and personal virtues determine life outcomes," the authors write.

In their research, published in the *Journal of Experimental Social Psychology*, Phillips and Lowery conducted two principal experiments. In the first experiment, they surveyed 185 white people online, using Amazon's Mechanical Turk. The first group read a paragraph about white advantages in American society and then took two surveys, one on beliefs about inequality in America and the second about childhood memories, which contained questions about life hardships. The second group did not read about racial privilege before answering the same two surveys. "In both experiments, we found that whites exposed to evidence of white privilege claimed more hardships than those not exposed to evidence of privilege," the authors wrote in the study.

"Policymakers and power brokers continue to debate whether racial privilege even exists."

There is another possible explanation for these results, says Lowery: "If you go to a poor country, you wouldn't wear expensive jewelry. In certain situations, it's not smart to flaunt." Put in the context of racial privilege: Whites might not want to display their advantages to others.

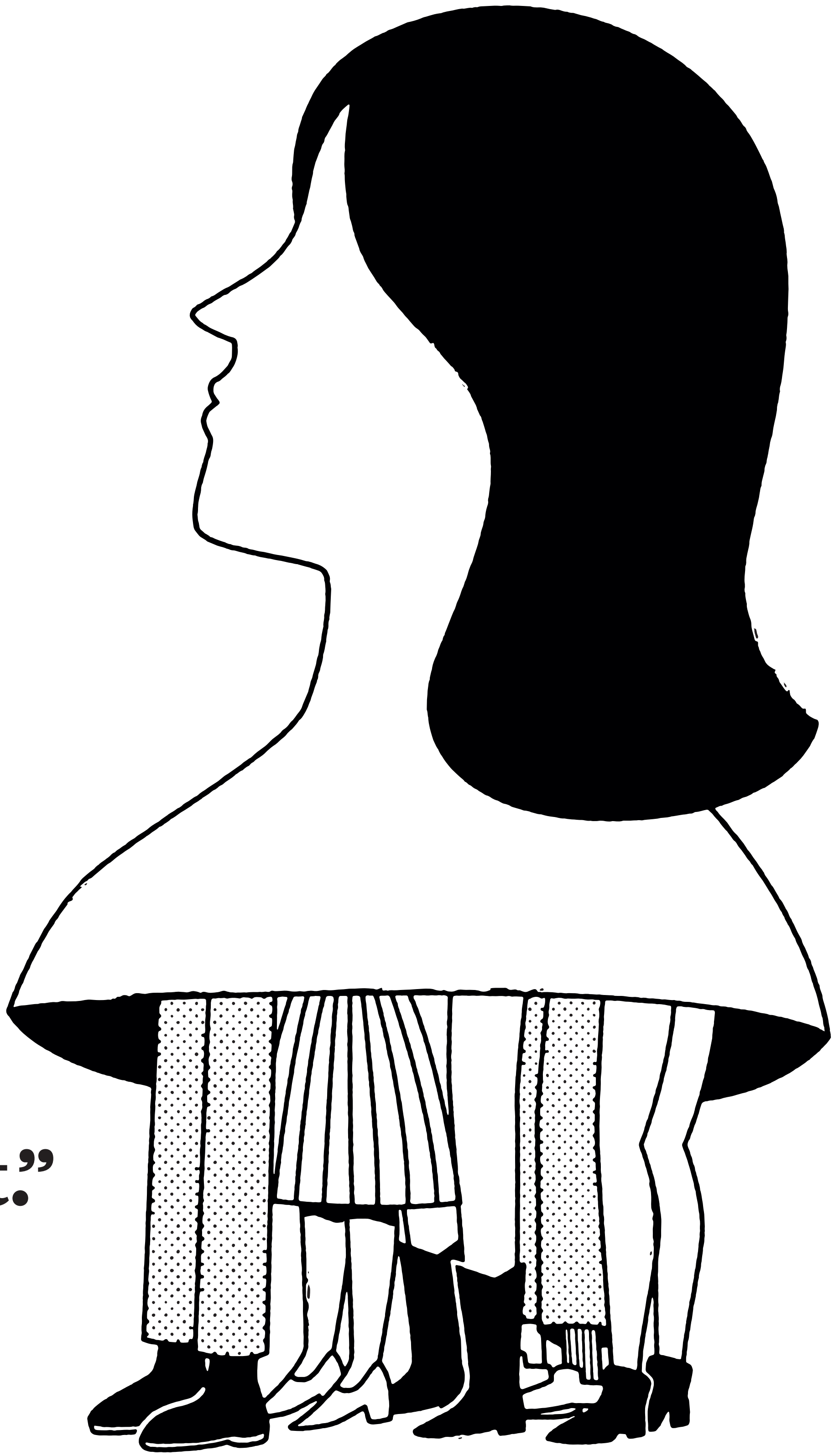
Still, a second experiment showed that whites can become more comfortable with their privileged status. The researchers found that when whites in the study were asked to complete a self-affirming exercise before taking a survey on American inequality, they would not claim to have undergone personal hardships to the degree that the first group had.

The 106 whites were asked to rank 12 values provided to them and explain what was important about their highest-ranked value. A second group of 128 people were not given this "affirmation" exercise. Participants from both groups were randomly assigned to take similar surveys given in the first experiment — about belief in inequality and about childhood memories; the latter group also was asked to answer questions about their experiences of hardship, their belief that they personally benefit from privilege, and their support for affirmative action.

Those who went through the affirmation exercise "expressed a significantly higher belief in personal privilege than did those who were not affirmed," the authors wrote. This same group also tended to be more supportive of affirmative action policies.

"We show you can turn off the 'denial' effect," Phillips says. "The self-affirmation task helps people reduce their feelings of defensiveness," which makes them more open to acknowledging their own privilege. ∆

Organizations



"One guy, who meant well, told us that women just **need to be patient.**"
—**Monica Leas** PAGE 30

Christopher DeLorenzo

GENDER

Silicon Valley Remains a Male Domain

A survey of women in high tech unearths pervasive gender imbalance — especially among VC firms.

BY LEE SIMMONS

Last year, many were transfixed by the spectacle of Ellen Pao's discrimination lawsuit against the VC firm Kleiner Perkins Caufield & Byers. While the jury rejected Pao's claims, Kleiner Perkins didn't come out unscathed: Testimony revealed a startling lack of diversity and pervasive sexism, not just in venture capital but throughout Silicon Valley. When women started talking, it turned out that many had faced similar problems, and their male colleagues were mostly unware of it.

So a group led by Trae Vassallo, a former partner at Kleiner Perkins, put together a survey to document the experiences of women in high tech, focusing on those who had been in the business for at least 10 years. Their searing report, "Elephant in the Valley," was released in January. Vassallo and coauthor Michele Madansky spoke at SXSW Interactive this year about their findings.

We sat down with the two women who launched the project — Julie Oberweis, a tech entrepreneur and investor, and Monica Leas, a digital media executive — while they were students in the MSx Program for experienced leaders at Stanford Graduate School of Business in 2015.

Julie Oberweis and Monica Leas graduated from the MSx Program for experienced leaders at Stanford GSB in 2015.

Photograph by Gabriela Hasbun

JULIE OBERWEIS AND
MONICA LEAS

How did the "Elephant in the Valley" project come about?

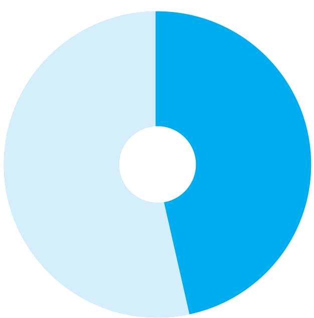
Leas: It started as an independent study that Julie and I concocted at Stanford. Our advisor, Stanford GSB professor Margaret Neale, is a renowned expert in negotiation, and we were going to look at how women in venture capital negotiate — whether it's different than for men. But when we started doing interviews with VCs, we realized there was a much bigger story about the position of women in this business.

Oberweis: Basically, there hardly are any. VC partners are like 95% men [a 2014 *Fortune* magazine study found that 96% of partner-level VCs were men]. It's ridiculous, even worse than Wall Street, and we wanted to understand why. So we were talking to these women, and they all had tales to tell. It wasn't always overt discrimination; often it was just a lot of little things, but it added up to a culture that was inhospitable to women.

Leas: In the middle of our project the whole Ellen Pao thing blew up. One of our meetings happened to be with Trae Vassallo [a 2000 graduate of Stanford GSB] who was testifying at the trial. She said, "You know, people don't believe this stuff happens in the tech industry. We should do a survey." So she pulled in some other people, and we launched this broader survey. Julie and I also published our findings from the VC interviews in a *TechCrunch* article .

The tech world prides itself on being a meritocracy. If women are underrepresented, some say it's because there aren't enough women who have the chops.

Leas: Yeah, we heard that a lot from male VCs: "It's just a pipeline issue. Sure, more women are entering STEM fields now, but it takes time for them to work their way up." One guy, who meant well, told us that women just need to be patient. Well, yes, there's a pipeline issue, but we found that there are also big issues with recruiting practices and retention. There's unconscious bias; there's blatant bias and harassment. If you're not looking at all these things, you're not going to solve the problem.



47%

The percentage of high-level women asked to do menial tasks

It sounds like, at least in venture capital, there wasn't even agreement that a problem exists.

Oberweis: The men we talked to would always say, "The way to become partner is to close deals." In their view, it was all measurable. But the women, almost across the board, said they'd had to push harder to get in and had to work harder and close more deals than their male counterparts to be recognized. Some also felt they'd lost deals because of their gender. They weren't whining. It was just, "yeah, that's the fact of the matter. But let's giddyap; we can do this!"

So they didn't want to get tangled up in fighting the situation?

Oberweis: Right, and I mean, it makes sense. These are women who've faced some steep hurdles and succeeded; they're not going to get bogged down in a victim mentality. And they knew that complaining would be a career-hindering move. That isn't going to change. Even with egregious things like harassment, women aren't going to start reporting it. It's a lose-lose situation.

Leas: Also, it would feed the story line that women aren't tough enough for this alpha-male business. So it was "let's just move on" — brush it aside and keep going. And that's what it takes! But it means the problems never get reported or addressed. That's why I think this survey is so important, to put some numbers on the experiences of women in Silicon Valley and start a conversation.

Was there anything in the results that especially surprised you?

Leas: I guess I was surprised by the pervasiveness of the problems throughout the tech industry, not just in venture capital. Remember, these are high-level women, and 47% said they'd been asked to do menial tasks like taking notes because of their gender; 60% had faced unwanted sexual advances; 33% reported having been afraid for their safety at some point. Two-thirds felt they'd been excluded from essential networking opportunities.

Did the findings match your own personal experiences?

Leas: I actually came up through the media industry, where there are a lot more women in positions of leadership, so frankly, a lot of this was new to me. I certainly never faced anything as blatant as what our study found. But then, too, I was in a large corporation with human resource systems in place to prevent these things. In tech startups or in private VC firms, there's not the same oversight.

Many in the Valley would say those HR structures create red tape that keep companies from moving fast.

Leas: Sure, when you're scrambling to bring a product to market so you can make payroll, hiring an HR department isn't at the top of your to-do list. But without those institutional checks and balances, you can get abuses of power. Maybe that's the flip side of being lean and nimble. Certainly without some procedures, it's easier for unconscious biases to act themselves out. It's just human nature to surround yourself with people who are like you.

In your article on venture capital, you said it often wasn't overt discrimination so much as all the subtle slights and disadvantages and embarrassments that discouraged women.

Oberweis: Right. Individually, none of them seem big enough to make a fuss over, but it's like death by a thousand cuts. And it's so often unintentional. I'll give you an example — I feel like I live this one every day. One VC partner said she wasn't invited to any meetings that started after 5 o'clock, because her colleagues assumed she wanted to be home with her kids. They were trying to be nice, but meanwhile, she was missing opportunities to get in on important deals.

Leas: Or we had one male VC who liked to throw a football at people when they came in the door. It was a harmless, playful gesture. But he found that he was throwing the ball to male colleagues and not to women, because it didn't seem right. It's a little thing, but that's one little bonding moment lost. Or men who greet each other with a fist bump: They're not going to do that to a woman. But how do you even raise that as an issue? There's nothing wrong with it, and it's not meant to be exclusionary.

Oberweis: But that's why I believe, in every bone in my body, that we have to talk about it. Because, by the way, it's probably true that more women than men want to get home to their kids for dinner. But I need the chance to say, "Hey, look, I want to be as much a part of this as anyone else. I'll take care of my family situation. Let me make those decisions." Right? We need to have these conversations as a society as we try to create an equal world.

Some of these awkward issues arise because tech has always been such a boys' club. Do we just need to increase the number of women in the room for the culture to change?

Leas: I do think there's a tipping point at which the similarity bias in hiring goes away and diversity becomes self-sustaining. So I think companies who are putting forth some kind of target numbers are on the right track, as controversial as that might be. Pinterest, Salesforce — a lot of these companies have now established hiring goals for women and minorities.

The dreaded "hiring quota"?

Leas: They're goals, not quotas. My perspective is that even if you don't hit the numbers on the timeline, you're making progress, and just setting a target forces managers to think through all the pieces that go into the equation.

> **"Pinterest, Salesforce — a lot of these companies have now <u>established hiring goals</u> for women and minorities."**

How have leaders in the industry received your report? Has it had an impact?

Oberweis: Women's voices are being heard now, loud and clear, and we've been very pleased with the reaction. I think it's caused a lot of companies to look at themselves and acknowledge that change is needed. We're still at the beginning of the conversation, but we're being asked over and over, "What's the answer?" Just the fact that they're asking is progress.

Some of the big tech companies have pledged millions of dollars to improve diversity. Are they taking the right steps? Is throwing money at the problem the right approach?

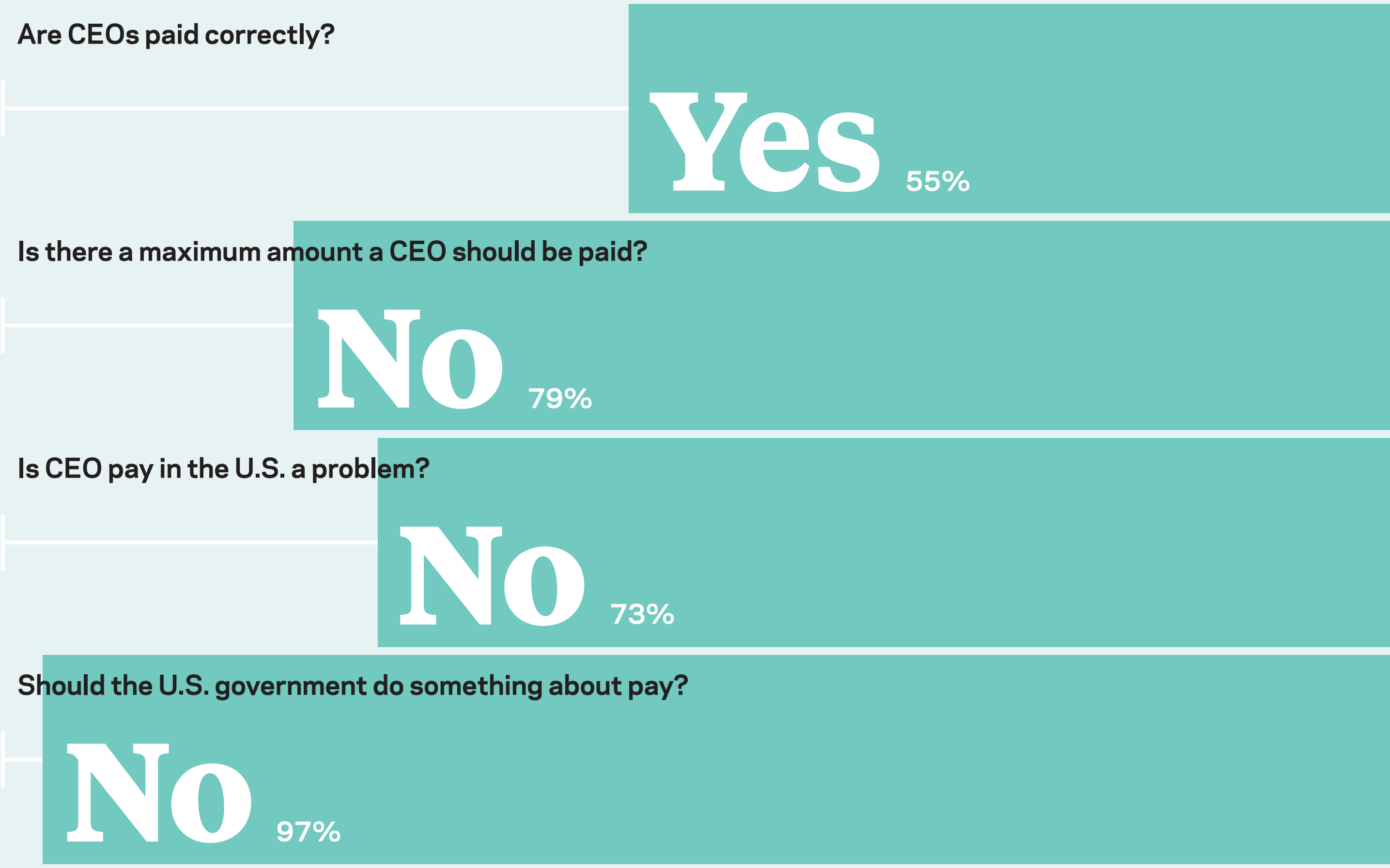
Oberweis: There's been a lot of chatter and criticism. But look, this is a hard problem, and even people who work on diversity disagree about how to pursue it. We should applaud and encourage companies that are trying, and then we'll see how they follow through. Do I think the money will make a difference? Absolutely. Thank God they're doing it. But do I think this problem is going away tomorrow? No.

Leas: One thing I'm sure of is we won't get there with lawsuits. The change has to come from people with power in the industry — and that means mainly men at first — who *want* it to be different. But hey, come on, this is Silicon Valley! These companies are changing the world and reinventing how we live. If they take that awesome creative energy and turn it inward, they can crack this. ∆

COMPENSATION

How much should the CEO make? It depends whom you ask.

Directors



If a company's value increases $100M in one year, how much should the CEO get?

DIRECTORS		PUBLIC	
Mean	Median	Mean	Median
$3.6 million	$1.5 million	$3.2 million	$0.5 million

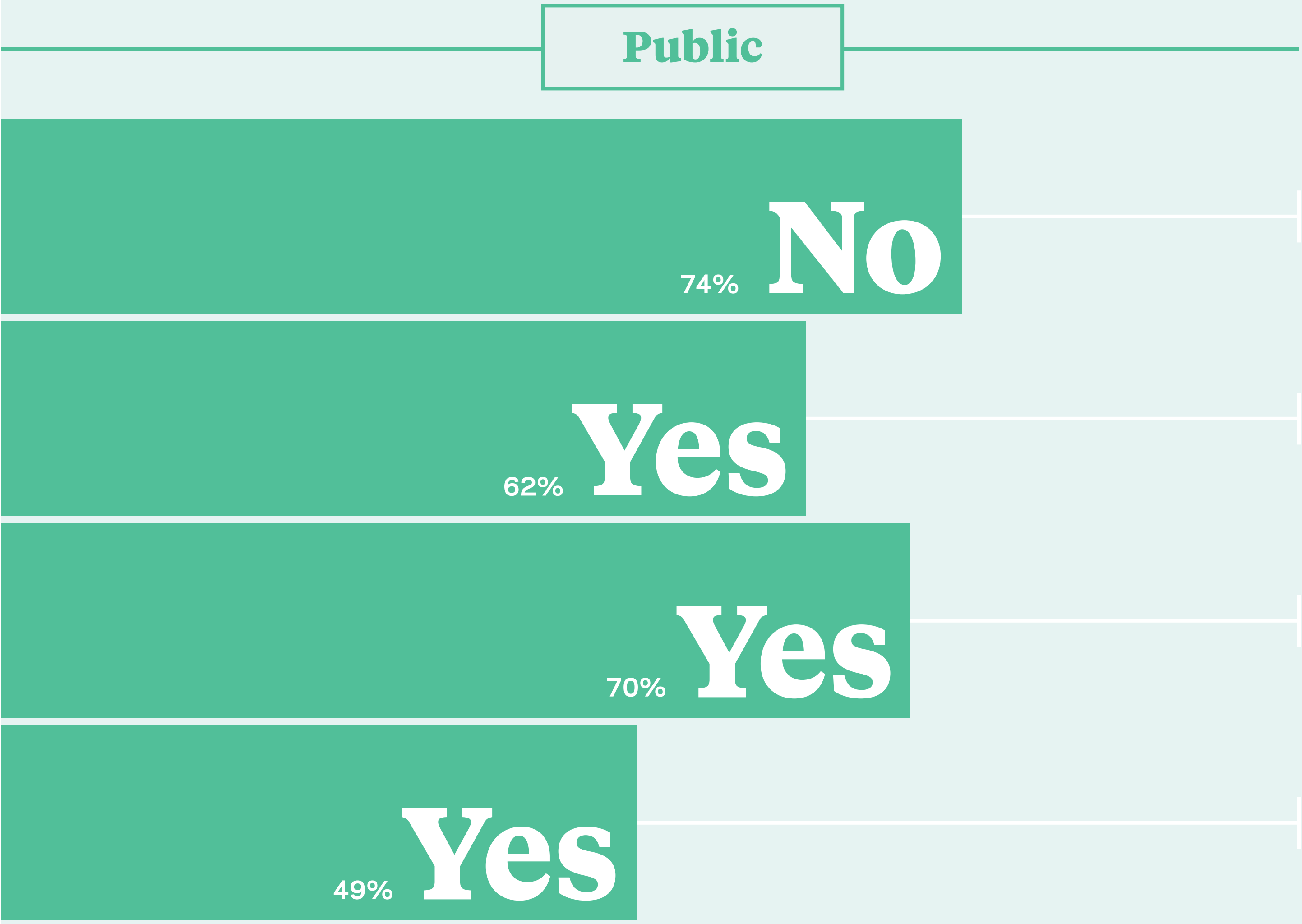
Based on the papers "Americans and CEO Pay: 2016 Public Perception Survey on CEO Compensation," and "CEO Pay, Performance, and Value Sharing," by David F. Larcker, Nicholas E. Donatiello, and Brian Tayan.

Infographics by Andrea A. Trabucco-Campos

In two new studies, scholars find that the public's perception of CEO pay varies wildly from company board members' perceptions.

BY SHANA LYNCH

David Larcker is the James Irvin Miller Professor of Accounting at Stanford GSB and a professor of law at Stanford Law School. Nicholas E. Donatiello is a lecturer in management at Stanford GSB and the CEO of Odyssey. Brian Tayan is a researcher at Stanford GSB's Corporate Governance Research Initiative.



What's the average CEO compensation?

PERCEPTION $1 million

REALITY $10 million

How much has CEO compensation increased?

997%

since 1978 when adjusted for inflation

In 2015, relative to workers, how much were CEOS paid?

300×

more than the average worker

ACQUISITIONS

Buying Businesses Is an “Extreme Sport”

Why taking over an existing company can be profitable

BY THERESA JOHNSTON

The way Coley Andrews sees it, there are two breeds of entrepreneurs. Some love the thrill of a startup; they’re passionate about nurturing ideas and products that no one has seen before. Others care less about the kind of product or service but instead love the idea of acquiring an existing small business and growing it to its full potential.

Andrews and his fellow investors like to put their money behind the second type. Their strategy, known as investing in small-cap leveraged buyouts via the search fund model, provides financial support and guidance to promising recent MBA graduates looking to buy and operate a single small business. Typically, the companies are B2B service businesses with enterprise value between $5 million to $30 million and owned by founders seeking retirement. Post-acquisition, the search fund entrepreneur becomes the new CEO. If the business grows under the recent MBA graduate’s new leadership, the investors will get their money back and then some after sharing a significant portion with the entrepreneur. The usual return is around 35%, according to Stanford Graduate School of Business Center for Entrepreneurial Studies.

“Take a sports analogy,” Andrews says of the model, which was developed in the mid-1980s by H. Irving Grousbeck, a professor of management at Stanford GSB. “You’ve got a horse, which is the company, that is running reasonably well around the track, and all we are doing is switching out the jockey. The founder/CEO is replaced by an inexperienced, but highly motivated and talented young person who is surrounded by active board members to help her succeed.” By matching healthy businesses with these talented recent graduates of top MBA programs, he says, “You create an environment where a lot of magical things can and do happen.”

Andrews cofounded his own Boston-based private equity firm, Pacific Lake Partners, shortly after graduating from Stanford GSB in 2009, to focus exclusively on investing in search fund entrepreneurs and the companies they acquire. He discussed entrepreneurship through acquisition, which he calls “the extreme sport of business,” at a symposium sponsored by the Center for Entrepreneurial Studies at Stanford GSB.

IT’S NOT FOR THE FAINTHEARTED

Although search fund entrepreneurs don’t face the same risks as startup founders, they’re still under a lot of pressure. “As a search fund entrepreneur, it’s your job to find, acquire, and then grow the business. You go out there and knock on doors, make thousands of phone calls, get ignored or rejected the majority of the time, all the while believing that you can find and convince one business owner to sell his or her company to you,” Andrews says. Search fund entrepreneurs also have to be comfortable with uncertainty, since the company they end up buying could be anything from a printing business to a wireless service provider. “It will likely be something that’s boring,” Andrews says, “but that’s not what search funding is about. It’s the opportunity to be the leader early in your career, to have significant financial upside, and to build a company.”

LISTENING IS PARAMOUNT

Acquisition entrepreneurs must be resourceful and fully committed to the enterprise. But the most important thing Andrews looks for in a new CEO is a willingness to listen. “The search fund model is predicated on taking somebody with high potential and surrounding her with experienced investors and former operators that can improve the odds of success,” he says. “If the entrepreneur is willing to listen, and take advice from those who have gone down this path before, she can avoid a lot of basic mistakes.”

IT TAKES TIME

Andrews advises his CEOs to settle in and avoid changing too much at their new companies in the first year. “Just listen and learn,” he says, and after 12 to 18 months, both the entrepreneur and the board will know a lot more about the business and the industry. At that point, the entrepreneur will have a much improved perspective on what changes to make and the direction to take the company. “The individuals who choose to do this, they want to build a company, and building a company takes time,” Andrews notes. “The average holding period is seven years from the time of acquisition, and the winners can go much, much longer.”

THE ODDS ARE IN YOUR FAVOR

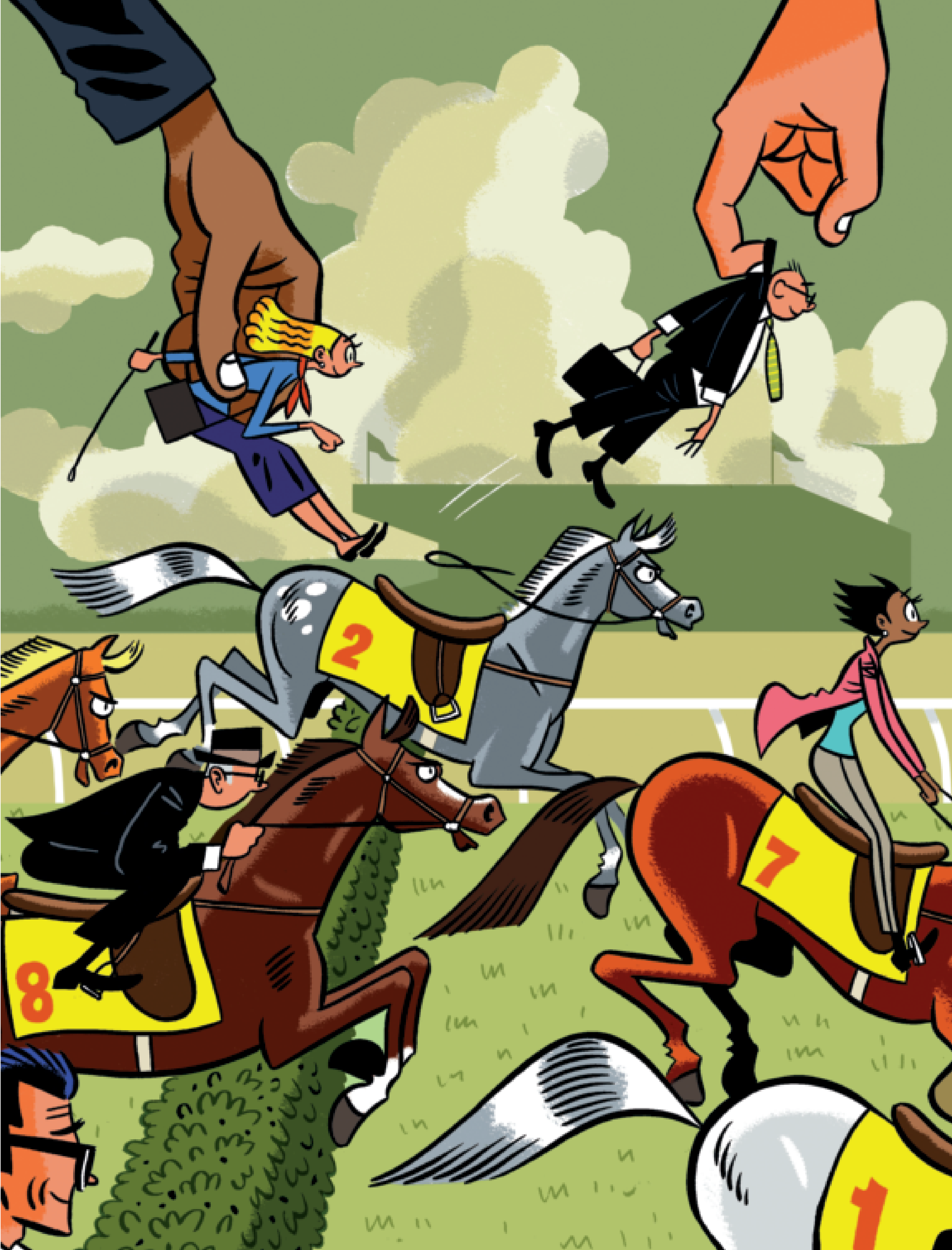
In Andrews’ experience, entrepreneurs who raise money to acquire a company have about a 75% chance of finding and buying a business within two years. After that they have about a 67% chance of being successful growing the company and making money for themselves and their investors. “So when you walk it all through, you have a greater than 50% chance of being successful as a young CEO. You get to build a company, have a meaningful financial outcome, and the life experience that you want,” he says. “That’s very different from startup risks, where it’s much more boom or bust.”

IT’S A FAST-GROWING TREND

Twenty years ago there were just two or three new search funds forming per year; today there are more than 50 active searches ongoing. It’s now a viable path for those who want to be their own boss but don’t want to face startup risk, Andrews says. While Stanford is still the intellectual center of the search fund model, he says, it has taken root far and wide. “I was just in Barcelona last week for an international search fund conference,” he notes. “Over 150 people were there interested in doing search funds in various countries around the world.” ▲

Coley Andrews is a 2009 graduate of Stanford GSB and the cofounder of Pacific Lake Partners in Boston.

Illustration by Jason Ford



JUSTICE

Want to Fix Overcrowded Jails? Set Prisoners Free

Sometimes releasing convicted felons is better than releasing inmates awaiting trial.

BY LEE SIMMONS

The United States locks up more of its citizens than any other country — more than Cuba, Russia, or Iran, as a percentage of population, and far more than European nations. Since the 1970s, incarceration rates have soared, and many of our prisons and jails are now dangerously overcrowded. There's a growing bipartisan consensus that change is needed; we simply have no place to put new prisoners. But what's the solution?

At the local level, one way to relieve the pressure on jails is pretrial release, leaving defendants free until they're convicted. It's an intuitively appealing answer, since more than 60% of jail inmates nationwide have not yet been convicted of any crime, and

Illustration by Adam McCauley

it costs taxpayers $17 billion a year to keep them behind bars. But there's always a risk they might use their liberty to commit more crimes or flee, escaping justice altogether.

Research from Stanford Graduate School of Business suggests a better way: split sentencing, an arrangement whereby low-level felony sentences are divided between jail time and community supervision. "It turns out that this gives you the best trade-off between jail population and public safety," says Lawrence Wein, a professor of management science. Compared with status quo policies, split sentencing not only alleviates jail congestion but also actually reduces recidivism.

OPERATIONS MANAGEMENT APPROACH

In 2011 the U.S. Supreme Court ruled that conditions in California's teeming prisons constituted cruel and unusual punishment and ordered the state to reduce its inmate population by 25%. So it did — in part by shuffling low-level felons (those convicted of nonviolent crimes) into county jails. Now the county jails are overwhelmed, and those inmates are deprived of the rehabilitation programs offered in prison. This maneuver, known as "realignment," met the state's legal obligation, but only by relocating the problem.

To find a real solution, Wein and Mericcan Usta , a recent Stanford PhD who is now a research scientist at GroupM in New York City, built a mathematical model of the Los Angeles County jail system — the country's largest and one of its most troubled. Borrowing a framework from operations management, the model simulates the flow of inmates through the judicial process, from arrest through sentencing, custody, and eventual discharge. Then, using data on recidivism and flight risk, the researchers were able to test alternative policies.

"There's always a trade-off," Wein says. "If the only objective was to minimize crime, you'd lock up every offender until they were no longer a threat. But the cost would be immense. So the real question is what policy gives you the best trade-off between the goals of protecting society and limiting inmate numbers."

The two main tools courts have to reduce overcrowding are pretrial release and split sentencing. Until recently, the latter was rarely used in Los Angeles (or anywhere else), and some judges have resisted it. It's easy to understand why: Split sentencing means putting convicted criminals on the street, while pretrial release frees defendants who, after all, may be found not guilty.

> **"You can't make a big dent in jail congestion with pretrial release alone, and certainly not at an acceptable level of risk."**

Wein and Usta examined different ways of implementing these policies: for instance, limiting pretrial release to misdemeanor cases or adopting split sentencing only for low-risk felons — those deemed unlikely to re-offend, using a risk-assessment tool commonly employed by correctional agencies. For every such permutation, they ran 1,000 simulations, each replicating a time span of more than five years.

A COUNTERINTUITIVE CONCLUSION

The results are surprising: Split sentencing can accomplish any targeted reduction in jail population with a smaller increase in crime than would result from a policy of pretrial release alone, even though it means freeing convicted felons. What's more, the optimal trade-off comes from extending split sentencing to all low-level felons, including those categorized as high risk.

"It's counterintuitive, but there are two things driving this," Wein says. "First, convicted felons now make up 45% of all the inmates in LA jails, and most of those are high-risk — which is mainly to say they're young, since that's the key determinant in risk assessments. So to really reduce crowding, you have to go where the numbers are."

The other factor is more subtle. Because of the pressure to turn over jail beds, the wheels of justice move faster for defendants in custody than for those on pretrial release. In Los Angeles, someone detained on a low-level felony charge will have the case decided in 53 days, on average, from the time of arraignment; for a defendant out on bail, it takes 191 days. Those in detention are also more likely to accept a plea deal.

That means pretrial release saves only 53 days of jail time per inmate while adding 191 days of recidivism risk. In other words, it exposes the public to 3.6 days of increased crime risk for every day of jail time saved. For split sentencing, the risk ratio is 1:1 — every day of increased crime risk is one day off the jail rolls — a much more favorable trade-off, in terms of both public safety and cost to taxpayers.

"We're not saying split sentencing should be used instead of pretrial release," Wein adds. "But it's the key lever. You can't make a big dent in jail congestion with pretrial release alone, and certainly not at an acceptable level of risk." Indeed, California's legislature endorsed split sentencing in January 2015, and its use has rapidly increased since then — with negligible increase in crime to date.

In fact, compared with the status quo policy in Los Angeles in 2014, the model simulations show that a full implementation of split sentencing would not only reduce jail population by 20%, it would actually cut recidivism by 7% — no trade-off required.

Wein stresses that this is all contingent on having strong systems in place for outside supervision and support, including drug treatment. "California has actually done a good job on this, and one benefit of realignment is that by handling it at the local level, you can keep a person under supervision in his or her home community, which really helps. That's probably why there hasn't been an uptick in crime."

While the study focuses on the Los Angeles jail system, the lessons are applicable anywhere. "Jails in other states might not have as many felons, so the magnitude of the benefits from split sentencing would differ," Wein says. "But the same forces are in play. This is something courts should definitely be looking at." ∆

Lawrence Wein is the Jeffrey S. Skoll Professor of Management Science at Stanford GSB. Merrican Usta is a research scientist at GroupM in New York City.

LEVERAGE

How Shareholder Pressure Feeds the Debt Spiral

Slanted tax incentives entice corporations to become addicted to dangerous levels of borrowing.

BY EDMUND L. ANDREWS

Three years ago, a team of financial scholars at Stanford Graduate School of Business and at Germany's Max Planck Institute provocatively argued that banks become "addicted" to steadily more dangerous levels of debt.

Disputing the standard models of finance, which hold that corporations carefully reckon the trade-offs of taking on higher debt, or "leverage," the researchers argued that banks develop an almost irresistible urge to increase borrowing once they start.

"Leverage begets leverage," they declared, identifying a "leverage ratchet effect" that keeps banks nudging their debt higher. The ratchet stems in part from a basic conflict of interest between shareholders and creditors and in part from government policies that encourage debt and risk-taking.

Anat R. Admati is the George G.C. Parker Professor of Finance and Economics at Stanford GSB, Peter M. DeMarzo is the Mizuho Financial Group Professor of Finance, and Paul Pfleiderer is the C.O.G. Miller Distinguished Professor of Finance and the senior associate dean for academic affairs.

Photograph by Drew Kelly

PAUL PFLEIDERER,
ANAT R. ADMATI, AND
PETER M. DEMARZO

LEVERAGE BEGETS LEVERAGE **Stanford GSB finance experts found that banks are not alone in becoming addicted to debt.**

Now, in a new paper, the researchers argue that banks are not alone. Other corporations become addicted to debt, even when it reduces the total value of the enterprise.

Once a company begins to take on debt, they say, the leverage becomes almost "irreversible." Shareholders will generally oppose measures that reduce debt and support moves to increase it whenever the opportunity arises.

"It's similar to eating potato chips,'' says Paul Pfleiderer, a professor of finance at Stanford, who coauthored the new research "You may be fine if you can commit to eating just a few chips. But if you can't stick with that commitment, you might be better off if you hadn't started eating them at all."

Pfleiderer teamed up with Anat R. Admati and Peter M. DeMarzo, also at Stanford GSB, and Martin F. Hellwig at the Max Planck Institute for Research on Collective Goods in Bonn, Germany.

The authors argue that since reducing debt entails a transfer of risk — and wealth — from shareholders to creditors, there is a clear disincentive for shareholders to cut back on borrowing.

If a company buys back its bonds, for example, bondholders will demand a premium above the current market price for those bonds. That's because bondholders will insist that the buyback price reflect the fact that the remaining debt will be at less risk of default. In other words, bondholders get all the benefits of debt reduction and shareholders have to foot the cost upfront.

Government tax policy makes companies even more biased toward higher debt, because it allows companies to deduct interest payments — but not dividend payments to shareholders — from their taxable incomes.

In theory, creditors can protect themselves by insisting on contracts or "covenants" that restrict a company's ability to increase its leverage in the future. Among other things, covenants can restrict a company from selling additional bonds or making big payouts to shareholders (which reduce the company's equity).

In practice, the authors argue, covenants are difficult to enforce. Most covenants give companies at least some discretion to take on more debt, because companies need flexibility in dealing with new opportunities and problems. On top of that, the creditors are often dispersed and unable to take a unified position.

"The difficulty is that you want to give flexibility to corporations to do things when the environment changes," Pfleiderer says. "If you know everything that's going to happen, you can write down rules for what to do in each situation. But you can't do that, because you can't anticipate everything."

The most obvious risk of high debt is the increased danger of falling into financial distress or even bankruptcy. But the authors argue that rising leverage can also make companies reluctant to invest in promising new projects. That's because part of the increase in value generated by an investment would flow not to shareholders but to creditors, because their bonds and loans would become more secure.

WHAT TO DO?

When it comes to banks and other financial institutions, the coauthors argue that tougher financial regulation must play a key role. Banks are especially prone to debt addiction, they say, because bank creditors (who include millions of depositors) are protected by a wide range of explicit and implicit government guarantees in the case of insolvency. These protections range from federal deposit insurance to the possibility of bailouts similar to those during the Wall Street collapse in 2008 and 2009.

The Federal Reserve and regulators in other nations have increased capital requirements, and the 2010 Dodd-Frank financial reform bill imposed restrictions on many bank activities. But the coauthors see remaining flaws in the regulations and room for additional work to address leverage addiction more generally.

One big step for corporations of all types would be to narrow or eliminate the special tax preference for debt over equity.

One big step for corporations of all types would be to narrow or eliminate the special tax preference for debt over equity. To be sure, eliminating the deductibility of interest payments would pose nearly insurmountable political obstacles.

But coauthor DeMarzo, a professor of finance at Stanford GSB, suggests that the United States could quite plausibly reduce the tax benefits of debt by lowering corporate tax rates. DeMarzo notes that the United States has much higher corporate rates than most other nations. Tax reformers in both political parties have proposed revenue-neutral reforms that would reduce corporate rates and make up the lost revenue by eliminating vast numbers of special breaks.

DeMarzo also suggests that corporate boards take a hard new look at how much they compensate management through stock options and other grants of equity in the company. The more money that managers earn from grants of stock and options, rather than from their salaries, the more they will align their self-interest with shareholders rather than creditors, he says.

The main purpose of their work, the authors say, is to shed light on why companies can become hooked on high debt. As they say about other forms of addiction, admitting you have a problem is the first step toward solving it.

POLITICS

Want to Lower the Curtain on Political Ads?

Eliminating the Electoral College would cut presidential election spending in half.

BY LEE SIMMONS

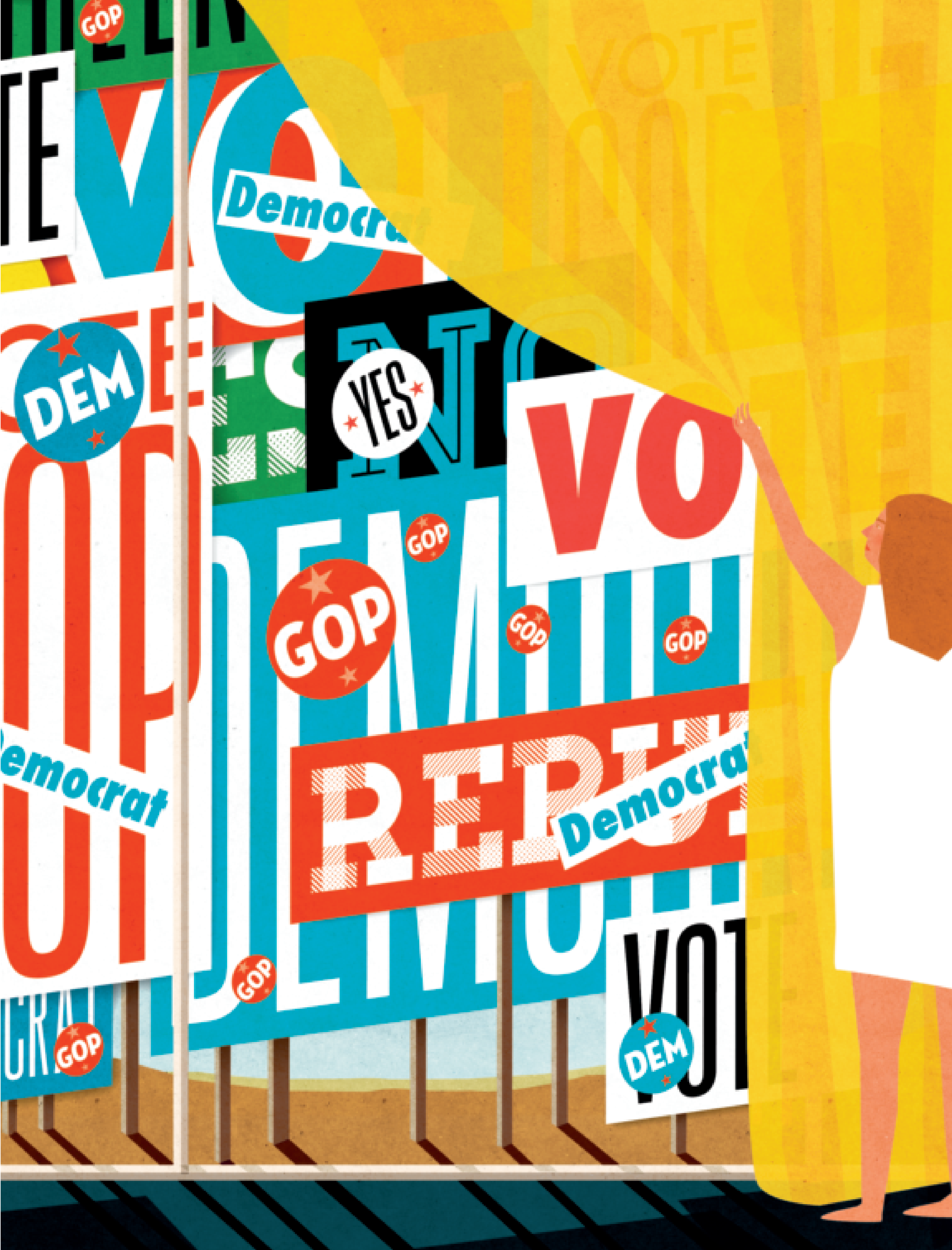
Ever since the "college of electors" was dreamt up at the Constitutional Convention of 1787 (at the last second, by a Committee on Postponed Matters), Americans have been debating its merits. Over the years, Congress has entertained more than 700 proposals to reform or abolish it. Opinion polls show that a majority of citizens dislike it. Yet this oddly undemocratic institution lives on.

The common criticism of the Electoral College is that it can potentially crown the "wrong" candidate — a president without a mandate. It's happened four times in our history, most recently in 2000, when George W. Bush lost the popular vote by a slim margin but won the electoral vote.

But a deeper issue is how it distorts the campaigns. Because all but two states assign all of their electors to a single candidate, both parties largely ignore states they're fairly sure of winning or losing. And nowadays that's about 80% of the country. Instead, all of the action happens in a handful of swing states like Iowa, Ohio, Nevada, Colorado, and Florida. It's no surprise, then, that nearly every candidate supports otherwise indefensible subsidies on corn ethanol — a litmus test for Iowans.

Wesley R. Hartmann is a professor of marketing at Stanford GSB. The paper "Advertising Competition in Presidential Elections," coauthored with Brett Gordon, an associate professor of marketing at Northwestern's Kellogg School of Management, appeared in the April 15, 2016, edition of *Quantitative Marketing and Economics*.

Illustration by Amy Martin


GOP
DEM
YES
GOP
GOP
GOP
GOP
GOP
GOP
DEM

Before you gripe about your vote not counting, however, consider what the swing states endure to earn that clout. Data from the Wesleyan Media Project shows that in the 2012 general election, 60% of all campaign ads were rained down upon just seven states, home to less than 15% of the U.S. population. Residents of Denver, for instance, were subjected to more than 40,000 ads, while San Franciscans saw fewer than 50.

So what would happen if we dumped the Electoral College? To find out, Stanford Graduate School of Business professor Wesley R. Hartmann and Brett Gordon of Northwestern's Kellogg School of Management simulated the elections of 2000 and 2004 to see how they would have played out under a direct vote. The researchers focused on ad spending, which offers a handy, quantifiable indicator of where campaigns are trying to compete.

Their findings may surprise you. As you'd expect, the concentration of advertising in swing states goes away, and ad spending rises everywhere else. What you might not have predicted is that, in a typical election, total advertising nationwide is much lower.

> **"A thousand votes in one state can swing the whole election. So candidates will spend huge sums on advertising to 'buy' those votes."**

AN ALTERNATE ELECTION

To rerun the 2000 and 2004 presidential elections under a direct vote, the researchers used what's called a structural econometrics model. "This works really well when you want to see what would happen in a scenario you can't observe," Hartmann says. "We used data from the real elections to find out what drives behavior — for instance, how much does advertising influence voters? — then we combined it with economic theory on incentives to extrapolate to this other world."

Under our current system, some votes count more than others. "Because of the winner-take-all rule, a thousand extra votes in a battleground state like Florida can swing the whole election — as we saw in 2000," Hartmann explains. "So candidates will spend huge sums on advertising to 'buy' those votes."

By contrast, a marginal vote in California is literally worth nothing to campaign strategists. "You might say, 'Great, I don't have to see any political ads.' But if they're focusing their ad dollars, it's a good bet they're also focusing their message. Your preferences, maybe as a more socially liberal Republican, aren't going to be represented."

Moving to a direct vote changes the math. For starters, the whole notion of battleground states vanishes. Every vote counts equally in the national tally, and that's reflected in the simulations: Ad spending declines in the former swing states and rises in the 40 or so others.

Since the competition gets spread across the entire country, you might expect an overall jump in advertising. But at least in the simulation for 2004, that's not what happens. Without the leverage of the Electoral College, no increment of votes in any one market has the power to tip the election, so those marginal votes aren't worth as much. The result: Ad spending falls by an astonishing 54%.

That's not *always* the case. In a really tight election like 2000, with a razor-thin margin separating victory from defeat, every last vote matters, and the model shows ad spending rising by 13% under direct voting. But that's an outlier, Hartmann says. The 2004 election was still very close by historical standards, so the large decline witnessed in that year would more likely be the norm.

A WHOLE NEW BALL GAME

Does that mean we'd all see the same number of ads? Actually, no. Although all votes carry equal weight in a direct election, the cost of acquiring them varies. "Affluent markets like New York are more attractive to corporate advertisers, so competition for airtime drives the price up — the cost per ad impression is higher," Hartmann explains. "But politically, those ad impressions are no more valuable than ones in Omaha."

As a result, the model shows that presidential campaigns will focus somewhat more on areas with lower incomes — which, as it happens, tend to lean further to the right. In other words, every vote is equal, but some are cheaper than others. We can abolish the Electoral College, but we can't revoke the laws of supply and demand.

That also points to one of the most interesting insights of the study: One can't just look at historic election results and assume that the winner under a direct vote would have been the candidate who won the popular vote in that year. Changing the election mechanism "changes candidates' strategic priorities and how they compete," Hartmann says. "It's a whole new ball game."

In Hartmann and Gordon's simulation, voter turnout in 2000 rises by 2 million. Gore would still win the popular vote — though by an even narrower, finger-biting margin — and would have become the 43rd president in place of Bush. With the entire country in play, however, it's not certain that the parties would even have advanced the same candidates.

What does seem likely is that under a system of direct voting for president, candidates would feel less compelled to tailor their appeal to the parochial interests of a small minority. And in most election years, there would actually be much less advertising.

Half as much rage and vitriol on the airwaves? Now that's a platform we can all get behind.

DISPARITY

Latino-Owned Businesses Lag Behind Their Counterparts

More Latinos are starting businesses than the general population, but they aren't making as much money.

BY ELIZABETH MACBRIDE

America's Latino population is one of the country's fastest-growing minority demographics: Latinos are expected to make up 29% of the country by 2050, an increase from 17% today. Nearly 20% of children under age 5 are Latino.

Yet, Latino-owned businesses are falling behind their non-Latino counterparts. Stanford Graduate School of Business research shows that while Latinos are starting businesses more frequently than the overall population, these businesses are smaller and making less money than their non-Latino counterparts. Latino businesses could have generated an additional $1.4 trillion in 2012 if they had been of equal average size to non-Latino businesses.

"The future economic health of the country depends on this part of the population carrying its share of the load," says Jerry Porras, a professor

Jerry Porras is the Lane Professor of Organizational Behavior and Change, Emeritus, at Stanford GSB and Douglas Rivers is a senior fellow at the Hoover Institution and professor of political science at Stanford University.

Illustration by Alvaro Dominguez

The average Latino business experienced flat sales from 1997 to 2012, while its non-Latino counterpart increased 34%.

emeritus, and one of the researchers on the study. "The Latino business community is not at the point where it can sustain that level of contribution."

Porras, with Douglas Rivers, a senior fellow at the Hoover Institution, surveyed 1,800 Latino-owned businesses on their size, revenues, financing, and other characteristics. The researchers, who are continuing their work, have compiled a dataset of 1.3 million Latino-owned businesses.

The research was done under the auspices of the Stanford Latino Entrepreneurship Initiative, a collaboration between Stanford GSB and the Latino Business Action Network, a nonprofit formed by Porras and a group of Stanford alumni to work on improving the lives of Latinos, lately by helping Latino-owned businesses scale up.

Porras and Rivers found that while the rate of Latinos starting businesses is growing faster than any other demographic, the average Latino business sales were flat from 1997 to 2012. In comparison, non-Latino business sales increased 34% over the same time frame.

Currently, less than 2% of Latino-owned businesses have revenues of more than $1 million per year, the survey says. That compares with 4.9% among all businesses.

While many minority communities are at an economic disadvantage in the United States, the extent of the disparity surprised researchers.

"We don't lack entrepreneurs," Porras says. "What we lack are entrepreneurs who scale." To that end, the Latino Entrepreneurship Initiative has developed a program to mentor entrepreneurs.

The full survey results were released at a Stanford State of U.S. Latino Entrepreneurship event late last year. The research draws the first portrait of Latino-owned businesses in the United States.

Some 91% of Latino businesses are family owned, compared with 85% of non-Latino businesses. About 12% of Latino-owned businesses were owned by a husband and wife.

The three biggest sources of financing for these companies were personal savings, credit cards, and friends. For non-Latino-owned businesses, the sources were personal savings, commercial loans, and personal bank loans. Less than 1% of the startups funded by venture capitalists were founded by a Latino, says Porras.

The average Latino-owned firm had 8.6 employees, compared with 12 at non-Latino-owned firms. The average Latino business has sales of $150,000 a year, compared with $573,000 at the average non-Latino-owned business.

Trying to tease out why the disparity exists, the researchers looked at the industries in which Latinos tend to start businesses — such as construction, health care, and retail — to examine whether conditions in those industries tend to force or favor smaller companies. The researchers also looked at whether Latino-owned businesses tend to serve only Latinos, which could limit their growth potential. They found evidence of neither, Porras says.

Now, the researchers are examining the role that outside money or ownership might play in Latino-owned businesses size and stagnant sales. Banks and other lending or equity partners could be less willing to work with Latinos, Porras says, or Latinos might be reluctant to give up ownership.

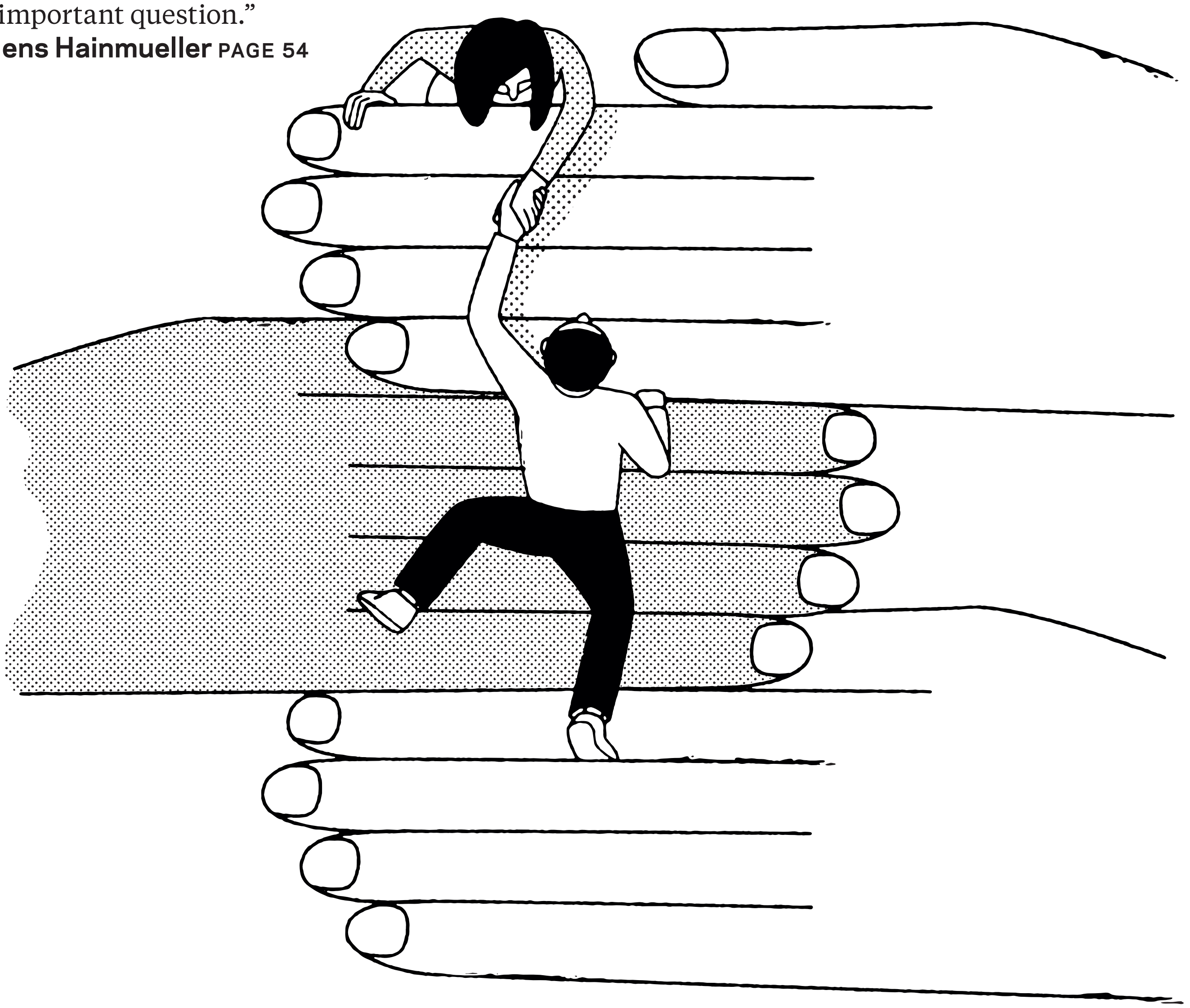
The researchers say they were motivated to do the survey and research by a sense that strengthening Latino businesses will help Latino communities and the nation's economy as a whole.

"There is wealth lacking in the Latino community. When you don't have wealth, you tend to have poor schools, crime, and poor housing," Porras says. "We really believe the economics is where this needs to be attacked. How can we help Latino-owned businesses grow?"

World

“Understanding the effect of naturalization

on long-term immigration is an important question.”
—**Jens Hainmueller** PAGE 54



Christopher DeLorenzo

POLICY

Corporate Tax Avoidance Is Growing

Companies are becoming more savvy at shifting income to lower-tax countries.

BY LEE SIMMONS

Globalization has generally been an excellent thing, but one downside is that it facilitates tax avoidance. Multinational firms, facing inconsistent tax rates and rules around the world, structure their operations in ways that channel earnings out of the typically high-tax countries where the value is created. Executives say that they're simply responding to the incentives that legislators put in place — as shareholders expect them to do — but the effect has been to siphon trillions of dollars out of public coffers.

How companies accomplish this can be dizzyingly complex. But fundamentally, income shifting centers on the use of foreign subsidiaries. By setting up transactions between related companies and calibrating prices just right, savvy firms can make profit margins vanish in one place and reappear in friendlier jurisdictions.

Lisa De Simone, a professor at Stanford Graduate School of Business, has devoted her research to advancing our understanding of this issue: how income shifting works, what causes it, how prevalent it is — and what, if anything, policymakers can do about it. She has a unique perspective. Before donning an academic gown, De Simone devised tax-mitigation strategies as a consultant for Ernst & Young.

In a pair of new studies, she argues that income shifting is more pervasive than we think — and companies are only getting better at it. *Stanford Business* sat down with her to learn more.

Lisa De Simone is an accounting professor at Stanford GSB who focuses on multinational corporations and corporate taxation.

Photograph by David Elliott

LISA DE SIMONE
Can policymakers assure multinationals pay more taxes?

Tax rates are lower in Ireland. Now you have an incentive to report earnings there instead of in the U.S.

So you were once a practitioner of this rarefied art? Yes, I helped clients, mostly U.S. multinationals, work out the transfer pricing on intercompany transactions — which now, on this side of the desk, I call income shifting. I also helped put together some of these structures you hear about, like the “double Irish/Dutch sandwich.” That’s where, say, royalties for the use of intellectual property are paid by an Irish subsidiary to another subsidiary in the Netherlands, which then pays a second Irish unit, which is tax-resident in the Caribbean. It’s complicated.

That’s a structure the big tech firms favored. It’s been eliminated now, though, hasn’t it? They’re phasing it out. The EU pressured Ireland to get rid of the quirky residency rule that gave rise to it. Of course, Ireland doesn’t want to lose its advantage, so now it says it’s going to further reduce its already low tax rate. But the latest thing seems to be going through the Netherlands and Luxembourg; apparently some companies have gotten private deals with the governments, although those are also now under fire.

Could you explain what transfer pricing is and how firms use it to reduce their tax liability? Sure. Say you’re a U.S. multinational and you’re supplying parts to an Irish subsidiary. Ultimately it’s an internal transfer, but you need to stipulate a price. It would be the same between two subsidiaries; transfer prices are just prices paid by related companies. Since they’re not set by competitive negotiation or an open market like normal prices, you need to decide what they should be.

That sounds harmless enough. Companies *have* to set transfer prices. It irks me when I see it portrayed as this nefarious activity. But now bring in the fact that tax rates are much lower in Ireland: Now you have an incentive to report earnings there instead of in the U.S., and you can accomplish that by setting a low transfer price. It inflates your profits abroad and deflates them at home. So then transfer pricing becomes part of your tax strategy. Corporations respond to the incentives that governments create.

50%

The amount by which past studies may have underestimated income shifting

But firms can’t just set any price they want, can they? No, there’s an “arm’s length” standard, meaning the price should be the same *as if* the parties were unrelated. But it’s so hard to enforce. If you’re providing a unique technology or management services to an affiliate, there *is* no market price. So often what you do is find a “comparable” company in the same business, look at its profit rate, and set a price that yields the same margin. That counts as compliance. Of course you’re going to look at all the possible benchmark firms and cherry-pick the ones that give you the best prices.

So the key is what counts as “comparable,” right? You have a new study on that very issue. Right. It used to be that if you had, say, a Spanish affiliate, you had to use a Spanish company as a benchmark, because accounting standards varied from country to country. You couldn’t compare book profits across borders; it was all apples and oranges. But there’s been a big push to harmonize financial reporting, especially in Europe — which is great! It certainly facilitates international investment. But it also expands the set of comparables for transfer pricing.

By quite a bit if you’re moving from Spain to the entire EU. Exactly. Instead of a dozen candidates, maybe you now have 200, and that gives you a wider range of prices to choose from. My hunch, based on my own experience, was that it would lead to more income shifting. So in this new paper, we looked at what happened in European countries that adopted the International Financial Reporting Standards for subsidiaries and, sure enough, it increased by 11%. That translates to a lot of money. It illustrates the kind of subtle interactions you can get between accounting and tax systems. There can really be unintended consequences.

You argue that researchers have underestimated the amount of income shifting that goes on. These studies typically assume it's all driven by statutory tax rates, but there's more to it. For example, I have another new paper that looks at what happens when firms have an unprofitable affiliate. Even if it's in a high-tax country, it effectively has a zero marginal tax rate, and you can take advantage of that by adjusting your transfer prices — reducing the amount of income shifted out of that company or even shifting income into it. We call that a shift-to-loss strategy.

Even better than a tax haven. And it doesn't look as bad. Anyway, that's one piece of the puzzle that's been left out. So not only do those studies miss that shift in an unexpected direction, the shift they do measure, from high-tax to low-tax countries, seems smaller because it's really a net effect. When we included unprofitable affiliates in our analysis, we found that the amount of income shifted in response to a change in tax incentive — what we call the tax elasticity — nearly doubled.

Wow. Yeah. It means prior studies may have understated income shifting by as much as 50%. In our European sample, instead of $54 billion being moved, we find that it's more like $99 billion. At the very least, the estimates in prior studies should be considered a lower bound. Also, the elasticity is important for policy, because it tells us that a change in the tax code could have a bigger effect on the tax base than previously thought. Say, for example, a country raises its tax rate, hoping to generate more revenue; you could get enough outward income shifting that tax revenue actually goes down. In a global economy, the corporate tax base is a very leaky vessel.

Reuters/Jonathan Ernst

FISCAL OSMOSIS "In a global economy, the corporate tax base is a very leaky vessel."

Is there anything we can do to plug the leaks? We can't stop income shifting. Until we have some broad tax reform in the U.S. and change the incentives, it'll continue. And it's distorting business decisions. All that cash is sitting idle overseas, and companies can't bring it home to reinvest or pay dividends unless they pay the taxes they already tried to avoid. Some are clearly banking on the hope that the government will give in and declare a tax repatriation holiday. But then it would start all over again.

How has your perspective changed since you left industry? Is there anything you've learned in your research that's surprised you? I worked for some of the largest multinationals, so I knew all the tricks, but I wasn't sure how much of this was going on in the broader economy. At the time there were plenty of midsize firms that didn't even know what transfer pricing was, and we helped some just to become compliant. But companies were learning by watching, and more and more of them began using their foreign subsidiaries as part of proactive tax planning strategies. So I've been trying to find out, is this how the average business operates now? And the answer, for better or worse, appears to be yes. ∆

INTEGRATION

Granting Citizenship to Immigrants Builds a Sense of Belonging

A Swiss study finds that naturalized citizens are more socially and politically engaged.

BY BETHANY AUGLIERE

Heated debate surrounds the topic of immigrants and their access to citizenship. But naturalization actually acts as a catalyst that builds greater social and political integration for these immigrants and their new countries, Stanford research shows.

A study by Stanford political scientist Jens Hainmueller in *Proceedings of the National Academy of Sciences* shows how citizenship can strengthen social and political bonds. His research focused on Switzerland, which currently has a very high number of immigrants relative to population size, with many of them marginalized socially and politically.

As Hainmueller noted, one in four residents in Switzerland is a foreigner, and a considerable anti-immigration sentiment exists in the country.

"Understanding the effect of naturalization on long-term integration of immigrants is an important question in light of these problems," says Hainmueller, co-director of the Immigration and Integration Policy Lab and faculty affiliate of the Europe Center.

IMPACT OF CITIZENSHIP

To conduct this study, Hainmueller and his collaborators, Dominik Hangartner and Giuseppe Pietrantuono from the Migration Policy Lab at the University of Zurich, used a natural experiment in Switzerland that allowed them to uniquely isolate the effect of naturalization. Between 1970 and 2003, Swiss residents decided on individual naturalization requests based on secret ballot referendums, a practice shown to be highly discriminatory and no longer used. Applicants had to win at least 50% of "yes" votes to receive citizenship.

Hainmueller compared applicants who barely got accepted with those who were barely rejected. All applicants had similar characteristics, including educational background, financial stability, and language skills. The difference between them were just a few votes, he says.

"It was luck if they got it or not," Hainmueller says, "similar to random assignment in a randomized experiment."

Nearly 15 years later, researchers tracked down the immigrants who faced these votes. It took almost two years to conduct more than 750 personal interviews — they got a 45% response rate. According to the results, those who became citizens were integrated much better socially and politically.

To determine political integration, Hainmueller asked the study participants questions regarding information on the current president and if they voted. Immigrants who gained citizenship voted at the same rate as rooted Swiss natives. They also had the same political knowledge as rooted natives, if not more.

Hainmueller and his team also asked the immigrants a series of social questions. Compared with immigrants who did not earn citizenship, those who were naturalized were more likely to read the Swiss newspaper and not a foreign newspaper. Naturalized immigrants were also more likely to express the desire to stay in Switzerland long term.

Results from the study indicate that more socially marginalized groups, such as immigrants from Turkey and the former Yugoslavia, or those with less education, benefited the most from naturalization.

"This is what you would hope," says Duncan Lawrence, executive director of the Immigration and Integration Policy Lab. "Those groups that are more negatively affected benefit the most from naturalization."

Although this study did not examine why naturalization increased political integration, Hainmueller suggests it is related to becoming a more active participant in the democratic process.

He and his colleagues plan to expand this work to measure the impact of naturalization in other European countries and the United States.

IMMIGRANTS IN AMERICA

In recent decades, immigration has increased across Western countries. In 2013, 41.3 million immigrants lived in the United States. In September, the Obama administration announced the Stand Stronger Citizenship Awareness Campaign, which is a new campaign that encourages the 8.8 million eligible immigrants to take steps toward citizenship.

"But nobody really knows what the impact of naturalization is in the United States because immigrants self-select into becoming citizens. If you simply compare naturalized and non-naturalized immigrants as most studies do, it is like comparing apples and oranges," Hainmueller says.

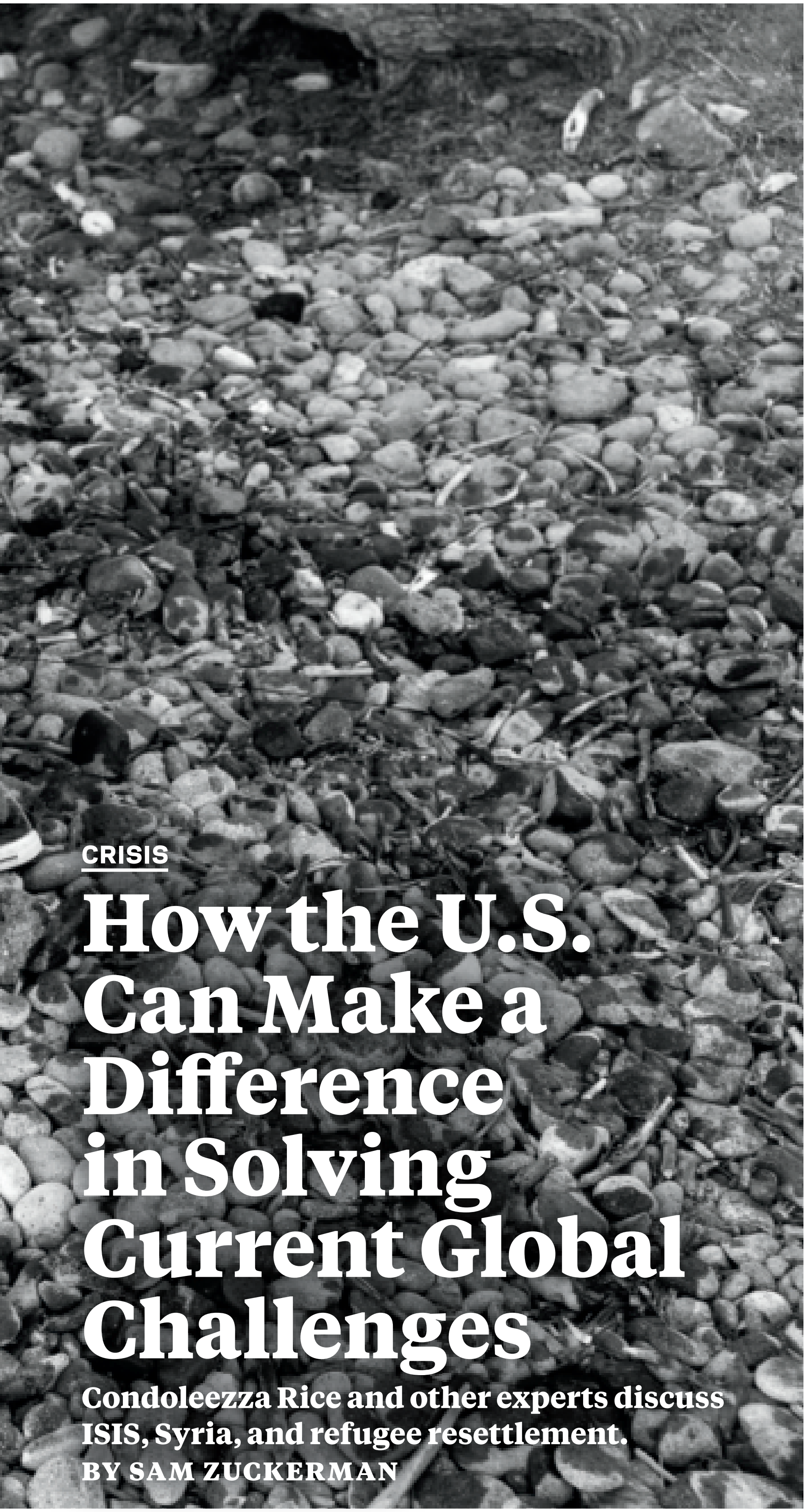
To answer these questions, Hainmueller and his team have designed a study to evaluate the impact of naturalization on immigrants in the United States. He plans to set up a lottery in which people can win a fee voucher to cover the cost of application fees ($680), which provides a financial encouragement to apply. Then he can make comparisons between those who won the lottery and became naturalized with those who did not.

The Immigration Lab is looking at a whole array of policies and programs that affect various types of immigrants, including refugees, undocumented immigrants, and long-term residents. "The next step is systematically analyzing the economic impact of naturalization," Hainmueller says. He hopes this work can provide evidence to inform policymakers, practitioners, and advocates leading to more evidence-based policymaking.

This research was supported by Stanford's Immigration and Integration Policy Lab, which is part of the Institute for Research in the Social Sciences, and was funded by a grant from the Swiss National Science Foundation. ▲

Jens Hainmueller is a professor of political economy, by courtesy, at Stanford GSB and an associate professor of political science at Stanford's School of Humanities and Sciences.

Illustration by Ping Zhu



Paolo Pellegrin/Magnum Photos

REFUGE A woman seeking asylum comforts a child after traveling by raft from Turkey to Greece.

CRISIS

How the U.S. Can Make a Difference in Solving Current Global Challenges

Condoleezza Rice and other experts discuss ISIS, Syria, and refugee resettlement.

BY SAM ZUCKERMAN

America won World War II and the Cold War. But, a generation after the fall of the Berlin Wall, it faces a witch's brew of challenges that demonstrate the limits of American power. From Syria to Afghanistan, from the grotesque violence of the Islamic State group to the aggressive expansionism of Russia and China, from the breakdown of civil society in much of the Middle East to a refugee calamity, the landscape is littered with seemingly insoluble crises and threats to security.

That was the theme of "When the World Is Aflame," a campus forum featuring three Stanford political scientists who worked in the top ranks of the U.S. foreign policy establishment: former Secretary of State Condoleezza Rice, former ambassador to Russia Michael McFaul, and former deputy ambassador to the United Nations Jeremy Weinstein.

Former Secretary of State Condoleezza Rice is the Denning Professor in Global Business and the Economy at Stanford GSB and the Thomas and Barbara Stephenson Senior Fellow on Public Policy at the Hoover Institution. Former ambassador to Russia Michael McFaul and former deputy ambassador to the United Nations Jeremy Weinstein are senior fellows at the Freeman Spogli Institute for International Studies and professors of political science at Stanford University.

> **"Growing the resources to support refugee resettlement in the U.S. means getting support from Congress."**

The forum portrayed a world in which America no longer faces the existential perils of the Cold War but must instead navigate a fragmented, sectarian, and explosive geopolitical environment. "We watch the Middle East in free fall, borders disappearing, state authority collapsing, massive [death] tolls, an overwhelming refugee crisis, humanitarian disasters," noted moderator Janine Zacharia, former Middle East correspondent for the *Washington Post* and the Carlos Kelly McClatchy Visiting Lecturer at Stanford University's Department of Communication.

Policies regarding the Syrian civil war, relations with Russia, and the fight against terrorism offer no good solutions, just tradeoffs among unpleasant alternatives, the panelists stressed. Yet, while American power may be limited, the panelists agreed, it is still formidable. The United States can make a difference when it uses its military power and diplomatic influence in wise and measured ways. And, no matter how grim the news at any given moment, people everywhere want dignity and self-determination. That's a fundamental truth U.S. policy can build on.

REFUGEES

The exodus of 4.8 million Syrians displaced by civil war has overwhelmed the developed world's humanitarian relief infrastructure. In the United States, as elsewhere, the breakdown reflects a mix of political and logistical factors. American support for refugee resettlement has run headlong into anti-immigrant fervor and fears of terrorism. At the same time, the unique American system of using combined public and private resources to find homes for refugees in communities across the country can't handle a crisis of this magnitude. "Even though I'm a very firm believer that the United States has a moral obligation to take people, let's remember that we have to have a way to take them that is actually going to work within our system," Rice said.

President Barack Obama's plan to accept 10,000 Syrians — a small number by international standards — has met stiff congressional opposition. To make progress, the United States must scale up its refugee programs and persuade Americans that it's in our interest to do so. "We have a humanitarian architecture that simply isn't up to the task," Weinstein said. "Growing ... the resources that we use to support refugee resettlement in the U.S. means getting support from Congress."

RUSSIA

Russia under Vladimir Putin has emerged as a major destabilizing force on the world stage, as its previous support for Syrian dictator Bashar Assad and its annexation of Ukrainian territory demonstrate, the panelists said. Meanwhile, Putin exploits virulent anti-Americanism to win backing at home for his brand of power politics. Managing the relationship with Russia is a challenge of the first order, the panelists agreed. Cooperation may be possible in limited areas, such as the Iran nuclear agreement. But, overall, Russia can't be turned into a reliable partner for peace. "We're not going to have a kind of fundamental new relationship with Russia until Putin changes his policy," McFaul said.

Means of influencing Russia are limited, but international pressure and economic weapons have some effect. In the long run though, America's most effective tool is exactly the thing Putin fears most — moral and political support for the democratic elements in Russian society.

SYRIA

In Syria, all the policy options were bad, the panelists said. When thousands of people rose against the Assad dictatorship in 2011, the United States considered a large-scale program to supply arms to the rebels. But some of that weaponry would have fallen into the hands of anti-democratic groups linked to terrorism, so arms aid was kept limited. Russia had less compunction and offered military aid and political support to keep Assad in power. That has left the United States with little advantage.

"They [the Russians] have succeeded in many ways in strengthening the hands of the Assad regime," said Weinstein. "And that gives them leverage at the diplomatic table."

America learned a hard lesson a decade ago in Iraq when it intervened to oust a brutal dictator. In Syria, panelists agreed, the United States has learned a hard lesson about what can happen when it stays its hand.

The panelists were more optimistic about the fight against the Islamic State group known as ISIS. They noted that a combination of American air power, limited special forces deployment, and training of Iraqis holds the promise of reversing the jihadist group's gains. Ultimately, the Islamic State can be defeated only by conventional military forces, but therein lies a problem. Any army dominated by Kurds or Shiites could alienate the Sunni population, thereby deepening regional divisions and fueling continued insurgency.

"There's broad agreement that we need a ground force," Weinstein said. "The challenge is who's in that ground force." ∆

POWERLESS 80 million homes in India lack electricity.

Ajay Verma/Reuters

ENERGY

Entrepreneurs Face Barriers to Ending Energy Poverty in India

Can solar-driven mini-grids alleviate a deficit that leaves millions in the dark?

BY IAN CHIPMAN

An estimated 360 million to 460 million people in India have little or no access to electricity. That's roughly a third of the people in one of the world's most populous countries, and more than the United States and Canada's populations combined. In terms of these raw numbers, India suffers from the most extreme energy poverty in the world.

As a basic lack of power is a major impediment to economic growth, the Indian government has articulated ambitious electrification goals to extend access to those people, many of whom live in rural areas currently beyond the reach of the central grid. These goals come at a time when the public utilities are under financial distress, however, so the hope is that private enterprise might help fill the gap. And yet, says Stefan J. Reichelstein, a professor at Stanford Graduate School of Business, "those electrification goals are not being met left or right."

Research by Reichelstein and Stephen D. Comello, associate director of the Stanford GSB Sustainable Energy Initiative, identifies a key regulatory barrier that the researchers believe is freezing the government's hopes that entrepreneurs will step in to accelerate the effort to power upward of 80 million homes that now lack electricity. The research was funded partially by the Stanford Institute for Innovation in Developing Economies and coauthored by Anshuman Sahoo, a research fellow at Stanford's Steyer-Taylor Center for Energy Policy and Finance, and Tobias Schmidt, an assistant professor of energy politics at ETH Zurich.

CENTRAL-GRID WOES

One of the main complicating factors in India's energy puzzle is the poor financial health of the state-run distribution companies, or discoms. These companies are required by law to deliver electricity to residential and agricultural users at highly

Stefan J. Reichelstein is the William R. Timkin Professor of Accounting at Stanford GSB and Stephen D. Comello is the associate director of the Stanford GSB Sustainable Energy Initiative.

subsidized rates that do not come close to covering their full cost. The resulting losses are exacerbated when discoms extend the central grid to unpowered villages. In other words, Comello says, "if you don't have electricity, don't look to the central grid to give it to you because they can't afford to bring it."

Given the mismatch between the government's lofty goals and the public utilities' inability to provide the infrastructure, Reichelstein says, the government is left with a natural question: "Could entrepreneurs or other entities fill this role at a more distributed form and smaller scale?"

The answer, as it stands, is mixed. While private capital has flowed to some very small-scale projects such as solar lanterns or solar home systems, it has been virtually absent from the types of systems with the greatest economic potential. After analyzing the economics at play and interviewing dozens of players in the field, the researchers believe they have identified the sticking point.

THE MINI-GRID SOLUTION

The researchers first calculated the costs of the various alternatives to central-grid electricity and identified which would be the most attractive for private developers. These options can vary both in generation source (the most common being kerosene, diesel, and renewables) and size, from micro-scale systems capable of charging small devices to pooled generators shared by individual homes to mini-grids capable of powering entire villages.

The researchers' cost analysis suggests that solar-powered mini-grid systems with storage should be an attractive option for private investment. For one, the cost per kilowatt-hour of mini-grid electrification for consumers is cheaper than other common services like kerosene-based lighting and diesel power generation, and consumers' willingness to pay for energy services would likely exceed the costs associated with building mini-grid systems. Mini-grids can also provide a foundation for economic development because, like the central grid, they can provide for productive capacity to power machinery or communications towers, for example. Mini-grids powered by solar photovoltaics and storage can also easily scale up as demand rises, thereby providing a flexible and carbon emission-free source of electricity.

India has abundant sunshine — on par with Arizona and California on average — and the government has made solar power a centerpiece of its energy goals. The Ministry of New and Renewable Energy recently set a target of installing 100 gigawatts of solar power capacity by 2022 through its National Solar Mission. "To put that into perspective," Comello says, "right now they have approximately 5 gigawatts. So they need to grow at an incredible rate."

India has abundant sunshine and the government has made solar power a centerpiece of energy goals.

THE HOLDUP PROBLEM

But the researchers noted that, despite the entrepreneurial catnip of this massive untapped market, private enterprises weren't rushing to meet India's energy demand. To get to the bottom of this, the researchers spoke to dozens of entrepreneurs, policymakers, and analysts in India.

What surfaced from these discussions was something outside the range of typical technological or financial challenges. "What kept coming up was the barrier that an entrepreneur can do nothing about — the threat of central-grid extension," Comello says. In other words, even though the central grid is unlikely to reach unpowered rural areas as a general rule, the simple threat that it could puts private development at an impasse. Entrepreneurs can't compete with discoms' highly subsidized rates, and in fact there have been multiple instances where the central grid extended to a mini-grid and forced the operator out.

What's more, Indian laws expressly written to spur these private developments have in fact made the problem more intractable, says Reichelstein. "In the case of a mini-grid, you don't need a license from anybody to distribute electricity, whereas in most other countries in the world, you do. So if entrepreneurs want to go in and set up electricity off-grid, they're free to do so." But that is a double-edged sword, one government official told the researchers. Private developers have no legal standing as an entity entitled to distribute electricity, and thus no way to protect their assets should the central grid extend to a village they had tried to electrify with a mini-grid.

"You potentially have a huge gorilla walking into the room at any time that you can't control," Reichelstein says.

As a result, the promise for deploying electricity to those experiencing energy poverty in India remains vastly unfulfilled.

THE SWEET SPOT OF REGULATION

The good news is that a fix isn't all that difficult or costly, Reichelstein says: "Because it is really a set of regulations that needs to be written, you don't have to deploy billions of dollars."

India has seen some movement. The state of Uttar Pradesh has passed the first formal policy that explicitly considers mini-grids a good, but imperfect, first step, the researchers say. And the Forum of Regulators, a key advisory body of state and central electricity regulators, has proposed a policy that would begin to untangle this impasse and encourage private development.

In their research paper, Reichelstein and Comello endorse the proposal, while suggesting some modifications on how electricity rates would be calculated and collected, and the terms under which discoms would purchase private developers' assets.

Putting these new regulations in place, Reichelstein says, should mitigate the risks of private development and offer a solution should the central grid come to a village that has been covered by a mini-grid. "Our proposal is, in case the grid comes to this area, the solar entrepreneur can say, 'I can't compete with your highly subsidized electricity rates, so I am selling you my mini-grid infrastructure assets at a rate that has been set in advance by the regulators.' " That price would protect the entrepreneur's investment, as if the grid extension hadn't occurred.

"Given the renewed commitment that India has made not only to electrification but also to sustainable energy, and given that solar is such an attractive resource, this is a very natural angle," Reichelstein says. "It's low-hanging fruit." ▲

HOME

Will the U.S. Become a More Family-Friendly Nation?

Other countries outpace America when it comes to parental leave.

BY LILY B. CLAUSEN

Illustration by Monica Ramos

The United States is the only country among 37 developed nations that doesn't mandate paid maternity leave. Estonia, for example, offers almost two years of paid leave for mothers.

But U.S. parents and caregivers have started pushing corporate and political leaders for paid family leave. Response has been mixed. Companies like Facebook and Google now offer generous packages like baby cash bonuses and several months' leave for both moms and dads, but those policies are the exceptions. Today, only 12% of private sector workers have access to paid family leave through their employers, according to the U.S. Department of Labor.

In the public sector, San Francisco in May voted to become the first city in the nation to offer six weeks of full paid leave for new parents. New York City has also taken recent steps to expand its parental leave policy.

These are big moves toward gender equality in the workplace, according to labor economist Myra Strober, professor emerita at Stanford. Paid maternity and paternity leave are vital steps in keeping women in the workforce, developing workplace acceptance for involved dads, and closing the gender pay gap. However, as Strober explains in this conversation with *Stanford Business*, we have a long road ahead.

You say paid parental leave is key to leveling the playing field. Why is that? We are the only industrialized country that doesn't have paid maternity leave. This is a big deal. We know that many women can't afford to leave their jobs and not have any income coming in. And we know that many women are concerned that if they take the time they need, their jobs may not be there when they are ready to come back.

One of the reasons why women earn less than men is because they take time out — much more than six months — to care for a young child. And then they may have a second child and take out still more time. The data show that throughout their work lives women are penalized in terms of salary for having left the labor force when their children were young. If we had paid maternity leave with a guarantee of their job being held for them, many more women would come back after six months and continue to accrue job experience.

But this can't just be a women's issue. We must also have paid paternity leave. We know from the literature that men who take paternity leave to care for newborns develop a different kind of bond with those children, a very close bond. And when men begin to have a closer relationship with their children, that's good for gender equity in the whole society.

"In Scandinavia, not only can you get paid maternity leave and paternity leave but you can also get part-time work very easily."

European models — particularly in Scandinavia — offer families more time off to care for babies. Do you think these are good examples for the United States? Or do you have a different model in mind? Well, the Scandinavian models have another problem. In Scandinavia, not only can you get paid maternity leave and paternity leave but you can also get part-time work very easily. Although that looks like a blessing, it turns out to be detrimental to women's movement up the ladder. We don't have employers now who see part-time workers as really committed and warranting promotion. So if you take part-time work, it often winds up being mommy track work — poorly paid on a per-hour basis and not leading to mainline jobs. Also, part-time workers often find that they in fact work many more hours than they get paid for.

You'll see that women in the U.S. do better than Scandinavian women in terms of reaching the tops of their professions. I'd like to have the paid maternity and paternity leave without the part-time work, at least as extensive as it is in Scandinavia. Part-time work for a short time could be a terrific opportunity. So let's say you take a maternity leave for six months and then you take part-time work for six months, but you wouldn't go part time for the next 10 or 15 years.

The other problem is that in many European countries, paid maternity leaves are so long that they interfere with women coming back. Women get used to being out of the workforce. So you don't want a maternity leave paid for three years, especially if you then take a second one maybe for another three years. Now you're out of the workforce for six years, and that plays havoc with your career. What is the ideal paid maternity leave? I'm not sure. But six months seems good, with the opportunity to work part time for another six months.

What's the business case for paid maternity leave? The business case is that it costs a tremendous amount of money to recruit good employees. And if you've got good employees, you can keep them by offering them a paid maternity leave for six months and then they come back.

Should companies be more competitive by offering maternity leave, child care, and part-time work? Or do you think it should be instituted at a national level through policy, like what San Francisco just did? Both. I think the responsibility is societal. I don't think corporations should be asked to bear a societal responsibility, but corporations or in many cases nonprofits do provide paid parental leave and child care because they see that there's a business case to be made for them.

We almost had a national child care system in 1971, but President Nixon vetoed the legislation because he thought it would weaken the family. I think he was wrong. I think it's just the opposite: Good child care strengthens the family by allowing families to have two earners so that the family is economically self-sufficient. If it's a single-parent family, then it's really important because most single parents are moms. Having affordable, accessible, quality child care, so that single moms can come back to work, makes a huge difference in the economic well-being of those families. ∆

Myra Strober is a professor emerita at Stanford Graduate School of Education and a professor emerita of economics, by courtesy, at Stanford GSB. Her most recent book, *Sharing the Work: What My Family and Career Taught Me About Breaking Through (and Holding the Door Open for Others)*, was published by The MIT Press.

EXCHANGE

SOME FINAL THOUGHTS ON EQUITY

EDITED BY NATALIE WHITE

"A classic mistake by founders
is raising too much money early on.
You should have a very

selfish

view toward equity."
— **Doug Leone**, a partner at Sequoia Capital,
during his takeover of
the *@StanfordBiz* Twitter account
http://stanford.io/1O6Fx97

"The first time someone has to be

fired,

the culture of equality may be shattered."
— **Lindred Greer**, a Stanford GSB professor,
for *Insights*
http://stanford.io/25zqOYC

"In spite of the progress,
it is estimated that

41%

of LGBT employees in the United States
remain in the closet at work."
— **John Browne**, former CEO of BP
and a 1981 Sloan Fellow,
excerpted from his book *The Glass Closet*
http://stanford.io/1sqdN5E

"Developing countries have to make
investments in their people. The most important ones
start when a woman becomes

pregnant."

— **Jim Yong Kim**, president of the World Bank,
in a speech at Stanford GSB
http://stanford.io/1ZQBOwf

"Don't allocate all the shares amongst the founding
team. ... Hold 15% for later for what we call

course correction."

— **Peter Ziebelman**, cofounder of
Palo Alto Venture Partners
and a Stanford GSB lecturer, for *Insights*
http://stanford.io/1MVNXsp

"If people

at the bottom

of an organization are informed, they can
make decisions on their own."
— **Nicholas Bloom**, a Stanford GSB professor,
for *Insights*
http://stanford.io/1m43e3H

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THE ESSENTIALS

FIVE LESSONS FROM OUR STORIES ON EQUITY

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Even brief personal conversations with door-to-door canvassers can change attitudes and reduce prejudice.
— David Broockman

The Tax Haven Problem Is Big and Getting Bigger

Multinational companies are becoming increasingly skilled at shifting income from high-tax countries to low-tax ones.
— Lisa De Simone

Tired of Campaign Ads?

Picking the U.S. president through a popular vote, rather than the Electoral College, would not only eliminate “swing states” but also reduce overall campaign spending.
— Wesley R. Hartmann

Helping Homeowners Stay Afloat

Automatically resetting mortgage interest rates during a recession could protect borrowers and even save banks money.
— Arvind Krishnamurthy

Why White People Deny the Advantages of Race

Exposed to evidence of racial privilege, Caucasians are inclined to exaggerate their personal hardships.
— Brian Lowery

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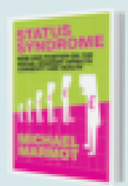

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