Objectives of the Research Platform on Performance & Risk Management

- Bring together researchers from different management domains (strategic management, accounting and finance, human resources, operations management, marketing,...) who share a common interest in performance and risk management
- Through cross-fertilization of ideas build an integrated perspective on performance and risk management and create synergies in knowledge development
- Build national and international collaborations with the academic and business community in the field of performance and risk management
- Serve as a vehicle to attract research funding
- Contribute to the school’s teaching innovation efforts
Key research themes of the Research Platform

- The role of strategic focus, engaged workforce, collaborative structure, and information infrastructure in creating high-performing organizations

- Integrating risk management into enterprise governance and in the various business processes (supply chain, ICT,...) with the objective of improving the organization’s operational performance

Vlerick Book “Managing for Performance Excellence”
Regine Slagmulder, Kurt Verweire & Koen Dewettinck
Some history...

- 2001-04

- Strategy implementation model
  (IPMS – Electrabel)

- Contributions from many Vlerick authors

The new book!
Performance management defined

The book defines performance management as a **strategic and integrated approach to delivering sustained organizational performance**.

The overall purpose is to **create a high-performance climate** in which individuals and teams take responsibility for the continuous improvement of business activities and results.

Vlerick Performance Management Model
Book: Table of contents

- Ch 1: Introduction
  Regine Slagmulder, Kurt Verweire & Koen Dewettinck
- Ch 2: The Performance Management Process
  Regine Slagmulder
- Ch 3: Rewarding for Performance
  Xavier Baeten & Bart Verwaeren
- Ch 4: A Winning and Living Business Strategy
  Kurt Verweire
- Ch 5: Creating an Engaging Climate
  Koen Dewettinck
- Ch 6: Collaborative Structure: Organizational Design for High Performance Organizations
  Ralf Wetzel & Koen Dewettinck
- Ch 7: Intelligence in Action
  Luc Lutin & Stijn Viaene
- Ch 8: Putting Performance Management into Practice
  Kurt Verweire & Geert Letens
- Ch 9: Performance Management at the Corporate Level: Beyond Financial Performance
  Nigel Roome & Céline Louche
- Ch 10: Strategic Performance Management at Corporate Level
  Philippe Haspeslagh

Performance management from a management control perspective
Regine Slagmulder
Performance management ensures that the organization takes the right actions to execute its strategy and create value

A performance management system has 3 main objectives

**Evaluation**
- To highlight areas of opportunity through identification of trends and performance gaps
- To inform forward planning and support performance reporting
- To ensure rewards and consequences are made based on objective criteria

**Communication**
- To set direction for the whole business, driving strategy-aligned performance at all levels of the organization
- To communicate expectations and set clear performance objectives
- To generate ownership of performance at each level

**Improvement & Learning**
- To enable management to drive performance improvement in the right strategic areas
- To ensure that improvement actions address both short-term performance and long-term health
An effective PM system contains three elements that reinforce each other

1. Measuring performance
   - Identify metrics and KPIs
   - Cascade goals and metrics
   - Select target setting approach
   - Define employee responsibilities and accountabilities

2. Generating insights
   - Establish processes and systems to analyze linkages between performance data
   - Provide mechanisms for performance gap identification and resolution

3. Reporting for managerial action
   - Define consistent approach to review and communicate performance information across the business
   - Provide linkages between performance gap identification and strategic project management

PM system is only effective with all three parts working together

Potential problems with the traditional controlling approach to performance management

- Strategic planning process is resource intensive yet strategy is insufficiently integrated in the day-to-day activities of the organization
- Lack of strategic alignment, no sense of shared strategic purpose
- Budgeting process induces a conservative approach to strategy execution and performance improvement
- Inflexibility of traditional PM systems in the face of uncertainty
- Organizational silos as opposed to integrated process approach to performance management
- Difficulty to leverage information & IS for performance management
- Overemphasis on the formal scorecards & systems and not enough on the mindsets and behaviors
Achieving high performance requires an integrated approach to PM

PM system (measurement infrastructure) + PM culture (organizational context) = High-performing organization

PM-related research themes in the management accounting & control area @ Vlerick

- Strategic cost and profit management across the value chain
  - Target costing, integrated cost management
  - Inventory costing and performance management across the extended supply chain
  - Cases on performance measurement in the supply chain and on customer profitability analysis
- Value-Based Management
- Balanced scorecard
- Integration between performance and risk management and link with enterprise governance
Performance management from a strategic perspective

Kurt Verweire

Vlerick Performance Management Model
Clear strategic focus

- Do we have a winning strategy?
- Do we take the right actions in line with our operating model?
- Do we have the right organization to implement all this?

Working paper:

Research reports:

Case studies:
- Thibeault A, Verweire K. 2012. ING Direct USA: Asset or liability for ING Group?
- Verweire K, De Grande J, Letens G, Slagmulder R. 2011. Bringing German Cooperative Bank Berlin back on track: Can a rural bank thrive in the city? (A) + (B) + (C) + (D)

PhD project Judith Escalier Revollo
Performance management from an HR angle

Koen Dewettinck
Performance management from an HR angle

- Performance management?
- Research projects
  - HR perspective
  - Employee perspective
  - Line management perspective
  - Team perspective

Performance management?

Employee energy

Org. objectives
Research projects

- Study 1: HR perspective (2006)
  - PM-practices in Belgian organisations
  - N = 319

- Study 2: Employee perspective (2008)
  - Experience with PM-practices and quality of leadership
  - N = 5778 (96 % white-collars)

- Study 3: Line management perspective (2010)
  - PM-activities, support from company and HR
  - N = 721 (80 % male, >10 people mngt. Experience)
Publications


Research projects

- PM in times of crisis
  - Impact of crisis on people management behaviour
  - Comparison between employee expectations and supervisor behaviour within 1 company
  - 178 employee-supervisor dyads
- High performance climate (ARF project)
  - 228 employees from 43 teams
  - Employee perceptions of climate dimensions linked to supervisor rated team performance
Engaging climate

- Empowering jobs
  - meaning
  - competence
  - autonomy
  - impact
- Motivating leadership
  - setting the example
  - informing
  - coaching
  - participation
  - caring
- Constructive feedback
- Reward and recognition
Collaborative structure

- Functional / divisional / matrix organization
- Customer centred authority
- Personnel selection & incentive structures

- Managing informal arenas
- Reverse controlling
- Informal networks

- Cross-functional task forces
- Project based teams
- Integrators, coordinators, boundary spanners

- Communities of practice
- Signature relationship practices & socio-technical design
- ‘GIFT’ culture

Two early-stage research projects in performance & risk management @ Vlerick

Koen Weemaes
Maria Boicova
Overview

Problem Framing
- Crossroads of multiple Domains

Main Theoretical Frameworks
- Tournament Theory
- Principal – Agent Model
- Behavioral Models

Current Research
- Effect of CEO Stocks & Options (Holdings/Compensation) on M&A
- Effect of CEO Stocks & Options (Holdings/Compensation) on Risk Taking
- Varying CEO response to Compensation Design
- Effect of Compensation Design on Stakeholders
- Effect of CEO Compensation on Earnings Management

New Vlerick research project on Executive compensation design
Problem Framing

Crossroads of Different Fields

- Corporate Governance
- Psychology
- Sociology
- Organizational Science
- Accounting
- Corporate Finance
- Finance
- Strategy

Tournament Theory

- CEO
- Exec’s: CFO, COO, CIO
- Mgmt: GM1, GM2, GM3, GM4, GM5

**Theory:** When promoting, an employer will select from a pool of able candidates the one who is fractionally better. That employee enjoys the fruits of the promotion.

**Advantages:** It is easier to merely rank workers than to quantify their efforts; it provides competition in the workplace, which may drive people to work harder; may also ensure that workers stay even if they are underpaid at the start; a high executive compensation serves as an incentive for all.
**Principal – Agent Model**

**Principal:** Investor

**Investments**

- High Risk Projects

**Agent:** CEO

**Projects:** Positive NPV

- High Current Salary
- Low Employment Risk

Maximize Return by:

- Each Investment High Risk
- Diversified Portfolio Low Risk

Low info on

- CEO Performance
- Firm Performance

Maximize Return by:

- High Current Salary
- Low Employment Risk

High info on

- CEO Performance
- Firm Performance

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**Prospect Theory Application: Behavioral Agency Model**

A Behavioral Agency Model of Managerial Risk Taking

- Performance history
- Problem framing
- Risk bearing
- Risk taking

Internal/external performance indicators

- Compensation mix
- Stock options design

Behavioral evaluation criteria

- Risk taking
- Direct supervision
- Target difficulty

- P 1
- P 2
- P 4b
- P 5a, 5b
- P 3a, 3b, 4a
- P 9
- P 7a, 7b
- P 6a, 6b

- P 1
Current Research:
Effect of CEO Stocks & Options on Acquisitions

- Datta, 2001: Finds that acquiring managers' equity-based compensation (EBC) improves stock price performance following acquisition announcements. High EBC managers pay lower acquisition premiums, acquire targets with higher growth opportunities, make acquisitions increasing firm risk

- Ueng, 2001: Finds positive returns to acquirers with high Incentive Ratios (% Stock Owned / Annual Comp). Focused acquisitions generate positive stock returns for acquirers. Low IR managers pursue diversified rather than focused acquisitions

- Sanders 2001: Finds that stock ownership decreases and stock option pay increases acquisitions. stock ownership decreases and stock option pay increases divestitures

Current Research:
Effect of CEO Stocks & Options on Risk & Performance

- Sanders, 2007: Finds that stock options prompt CEOs to make high-variance bets, not simply larger bets and lead to big gains and big losses (more losses than gains).

- Souder, 2010: Finds that high levels of exercisable stock options reduces the likelihood of LT investments. Un-exercisable stock options increase the likelihood of Long-Term investments

- Hodak, 2005: Finds that rewarding managers for profit growth produces higher stock price returns than rewards based on multiple measures or balanced scorecards. Adding long-term incentive plans does not improve long-term performance. Granting of equity based on the past year’s performance is better than in annual fixed amounts.
Current Research: Varying CEO response to Compensation Design

- Wowak, 2010: Finds that stock options improves the performance of talented executives but worsen the performance of low-ability executives
- Kukich 2011: Gender Disparity: Finds that Male overall compensation is higher and more performance sensitive
- Becker 2006: Finds that Rich CEOs are less Risk Averse
- Chakraborty, 2007: Finds that managers who face a high termination risk make less risky investments than managers who face a low termination risk

Current Research: Effect of Compensation Design on Stakeholders

- Arora, ‘05: Finds that LTIP Adoption leads to R&D Expense (Customers), Employment (Employees) and Growth (Shareholder)
- Benson, 2010: Finds that stakeholder management is positively related to firm value. However, firms do not compensate managers for having good relationships with stakeholders.
- Faleye, 2011: Labor-friendly firms also outperform otherwise similar firms (stock returns, operating results). Top management derives income from labor-friendly practices.
- DeFusco, 1990: Finds that the approval of a CEO stock option plan leads to a positive stock and a negative bond market reaction
- Cassell, 2011: Finds that Large CEO Inside Debt Holdings (Deferred Comp, Pension Benefits) lead to less Risk Taking (lower Leverage, less R&D Expense, more Diversification and Asset Liquidity)
Current Research: 
Effect of CEO Compensation on Earnings Management

- Grant 2009: Finds that Executive Stock Options Plans and income smoothing are positively related
- Erickson 2006: no consistent evidence that executive equity incentives are associated with fraud
- Johnson 2009: Fraud firms have significantly greater incentives from unrestricted stockholdings than control firms do, and unrestricted stockholdings are their largest incentive source
- Schnatterly, 2003: operational governance (clarity of policies, formal communication, and performance-based pay for the board and employees) significantly reduces the likelihood of a crime commission

New Vlerick research on CEO Compensation Design

**Research Gap**
- Interaction of the different Compensation Package Elements
- EU vs. US perspective: Diversified Shareholder vs. Blockholder

**Research Questions**
- Stakeholder-Optimal level of Firm Risk?
- Optimal Compensation Package Composition? Level?
### Research hypotheses and issues to resolve

#### Impact on Firm Risk & Performance
- CEO Variable Pay
- CEO Fixed Salary
- CEO Total Pay
- CEO Shareholdings
- CEO delayed Salary
- CEO Bond Holdings

#### Measurement Issues
- Direct Observation of Behavior
- Risk?
- Performance?
- Value Restricted Stock / Option to the Executive
- Filter out Environmental Factors

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### Risk oversight by the board of directors: antecedents and consequences

**PhD project of Maria Boicova**  
**Supervisor: Prof. Dr. ir. Regine Slagmulder**
Optimism is a lack of information

**HOW**

□ ... is the board informed on risk?
□ ... is the risk information used by the board?
Motivation for the study

WE AGREED THAT YOUR CONTRACT WAS TOO COMPLICATED SO WE REDEATED IT TO COVER YOUR NEW RESPONSIBILITIES...

GET ALL THE INFORMATION YOU CAN, WE’LL THINK OF A USE FOR IT LATER.

© Vlerick Leuven Gent Management School
RQ1: How is board risk oversight related to the involvement of the board in the strategy process of a company?

RQ2: How does board risk oversight impact board strategic decisions?

Determinants of risk reporting to board of directors

ARF project
Prof. Dr. ir. Regine Slagmulder, Maria Boicova, Prof. Dr. Gerrit Sarens (UCL)
RQ1: what are the characteristics of the (formal) content and flows of risk related information to the board of directors?

RQ2: to what extent is the approach used to risk reporting to the board of directors dependent on the board’s involvement in the strategy process of the company?

RQ1: checklist

<table>
<thead>
<tr>
<th>Scope</th>
<th>The report contains historical risk information</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>The report contains risk information related to possible future events (early-warning signals)</td>
</tr>
<tr>
<td></td>
<td>The report contains financial risk information and financial integration of non-financial risk information</td>
</tr>
<tr>
<td></td>
<td>The report contains non-financial information of a customer perspective, employee attitudes, competitive threats, complaints, statistics, etc.</td>
</tr>
<tr>
<td>Timeless</td>
<td>The information on risk is provided immediately upon request</td>
</tr>
<tr>
<td></td>
<td>The information on risk is supplemented automatically upon receipt of information and processing thereof</td>
</tr>
<tr>
<td></td>
<td>The report contains processed information and comments on the importance of risks</td>
</tr>
<tr>
<td></td>
<td>There is no delay between an event occurring and relevant information reporting</td>
</tr>
<tr>
<td></td>
<td>The information on risk is provided by different functional areas in the organization (silos)</td>
</tr>
<tr>
<td></td>
<td>The information on risk is provided on the effects of events on short-term, medium-term and medium-term strategic goals</td>
</tr>
<tr>
<td></td>
<td>The information on risk is provided on the effects of events on financial objectives</td>
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<tr>
<td></td>
<td>The risk report contains information which enables to conduct what-if analysis</td>
</tr>
<tr>
<td></td>
<td>The report contains information on the impact of potential decisions in context with risk throughout the company (interdependencies)</td>
</tr>
<tr>
<td></td>
<td>The report contains action plans</td>
</tr>
<tr>
<td></td>
<td>The report contains information on the impact that decision has on performance</td>
</tr>
<tr>
<td></td>
<td>The report contains information on the status of risk management in different departments</td>
</tr>
<tr>
<td></td>
<td>The report contains a summarized risk information by functional area and by time period</td>
</tr>
<tr>
<td></td>
<td>The risk report reaches the Board of Directors directly via an Audit Committee</td>
</tr>
<tr>
<td></td>
<td>The risk report reaches the Board of Directors indirectly via CEO, CFO or other C-level executives</td>
</tr>
</tbody>
</table>

Degree of standardization

- The risk reporting is based on a risk management methodology common across the organization
- The risk reporting is based on uniform templates and is common across the organization
- The risk reporting is based on guidelines

Degree of formalization

- The risk reporting is based on formal information streams
- The risk reporting is also based on informal information streams
- The risk reporting is a written process
- The risk reporting is not a written risk discussion
### RQ1: checklist

<table>
<thead>
<tr>
<th>Source</th>
<th>The report contains historical risk information</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>The report contains trend information related to past events (early warning signals)</td>
</tr>
<tr>
<td></td>
<td>The report contains information on broad factors external to the company</td>
</tr>
<tr>
<td></td>
<td>The information is provided in a consistent and clear form</td>
</tr>
<tr>
<td></td>
<td>The information is provided in a timely manner</td>
</tr>
<tr>
<td></td>
<td>The information is updated regularly</td>
</tr>
<tr>
<td></td>
<td>The information is in a structured and consistent format</td>
</tr>
<tr>
<td></td>
<td>The information is integrated across the organization</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>RQ2: Board involvement scale</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>PASSIVE</strong></td>
</tr>
<tr>
<td>Boards as &quot;rubber stamps&quot;</td>
</tr>
<tr>
<td>No impact on strategy</td>
</tr>
<tr>
<td>Van Den Berghe &amp; Levaux, 2007</td>
</tr>
<tr>
<td><strong>ACTIVE</strong></td>
</tr>
<tr>
<td>The role of the board as approving, monitoring and reviewing strategy</td>
</tr>
<tr>
<td>Ingleby &amp; Van Der Walt, 2001</td>
</tr>
<tr>
<td><strong>LEADERSHIP</strong></td>
</tr>
<tr>
<td>A leadership role of active involvement in establishing goals, values and setting direction</td>
</tr>
<tr>
<td>Ingleby &amp; Van Der Walt, 2001</td>
</tr>
</tbody>
</table>
RQ2: Board involvement concept and measurements

ability

engagement

How engaged is the Board of directors in:
1. Establishing long-term objectives
2. Definition of company mission and direction
3. Identification of new business areas
4. Analysis of company strengths and weaknesses
5. Identification of new strategic options
6. Selection of company strategy
7. Ratification of strategy
8. Monitoring the strategy implementation
9. Monitoring the financial performance
10. Monitoring and evaluating management


Case Studies

Belgium

Switzerland

Netherlands

Russia
Preliminary findings

- an ability of the board to be involved predicts the real board engagement with strategy
- the board involvement has an impact on the content and flow of the risk reporting, as well as on the underlying structures for risk reporting
  - “Leadership” boards will be associated with a more mature board risk oversight.
  - “Passive” boards will be associated with a less mature board risk oversight.
  - “Active” boards will be associated with more mature board risk oversight than “passive” boards

Preliminary findings

- the use of information (Simons, 1995):
  - “Leadership” boards will use the risk reporting information interactively
  - “Active” boards will use the risk reporting more interactively rather than diagnostically
  - “Passive” boards will use the risk information diagnostically