What Do Financial Executives Say about Corporate Culture and Strategy?

Executive Summary
Thinking quantitatively about culture and continuously investing in it can drive success, increase a firm's value, and help employees thrive. While strategy lays down the rules, culture fuels a firm's spirit. By analyzing the views of financial executives about when, how, and why strategy and culture influence performance, we derive novel insights for scholars who seek to improve their theories and practitioners who want to build better businesses. We show that financial executives believe that culture can be quantified and optimized. They also consider a firm's characteristics to be central to determining how culture and strategy will interact. We conclude by sharing ideas for building an effective culture.

John R. Graham
Duke University

Jillian Grennan
University of California, Berkeley

Campbell R. Harvey
Duke University

Shivaram Rajgopal
Columbia University

John Graham, Jillian Grennan, Campbell Harvey, and Shivaram Rajgopal describe how financial executives understand when, how, and why strategy and culture influence a firm's performance.

Leading management and business intellectuals make a range of assertions about strategy and culture. McKinsey's framework for organizational effectiveness describes strategy as a hard element and culture as a soft element.[1] Others state that the impact of strategy on growth and profit can be measured, while the impact of culture cannot. Still, others say that changing strategy is quick, but changing culture takes a very long time. All of these assertions, which have been repeated many times, reflect an outmoded way of thinking about the drivers of modern business.

©shutterstock.com/PopTika

The role of strategic plans has changed dramatically in recent decades, as has the ability of leaders to rely solely on manipulating tangible capital inputs to achieve superior organizational performance. Today, companies that routinely outperform their competitors are led by managers adept at maximizing intangible value. They know how to design and propagate culture, human relationships, and community. Yet while most company leaders claim to prioritize speed and innovation, many pursue growth and service by sticking to the time-worn, hierarchical, budget-driven, check-the-box approaches that leave workers feeling alienated and unmotivated.

We interviewed chief financial officers (CFOs) to discover their perspectives about culture and strategy. We found that those who think about culture quantitatively and continually invest in culture tend to increase their firms' success and value while helping employees to thrive. Because quantifying culture is challenging, managers will have to embrace the views of those who are not traditionally responsible for culture work or human resources. Accounting and finance professionals have traditionally been responsible for developing reliable, quantitative models, so their views are of particular value. CFOs understand creating value, so they are well equipped to understand the evolving impact of culture and strategy. Although they are best known for their financial acumen, they are also skilled at cultivating close relationships.

By analyzing the views of today's leading CFOs, we show that these financial executives believe the impact of culture on profit and long-term value can be thought of in a rigorous, quantitative manner. By formulating the links among culture, strategy, and performance, from a quantitative perspective, our research provides a base on which leaders can quickly implement new insights as a means to change their own firm's culture trajectory. For example, the quantitative conceptualization of culture makes it clear that making the necessary culture changes to improve firm value can be engineered in months, not years, and certainly within the typical leader's tenure.

Interviewing CFOs

We collected the data for our analysis as part of a multi-pronged study on corporate culture.[2,3] We conducted individual interviews with select CFOs and completed a comprehensive, large-sample survey. This work, presented here for the first time, confirmed our belief about the importance of the interactions between culture and strategy. The 1,348 corporate executives in North America who responded to our survey indicated that culture is the most important driver of a firm's long-term value and that strategy is the second biggest. Operations were ranked third, marketing fifth, and engineering sixth. Trailing well behind were compensation (8), regulation (9), human resources (10), and governance (11).

The respondents also described *how* culture and strategy influence value creation. We began each interview by asking, "What, in your view, is corporate culture?" and let the conversation progress organically from there. The wording of our questions about the relationship between culture and strategy varied, but roughly followed this example: "A popular business quote attributable to Peter Drucker is 'Culture eats strategy for breakfast.' Do you agree with this statement? You may want to consider whether maintaining or building a corporate culture is part of your strategic plan, or is culture part of the execution of the strategic plan? In strategy meetings is culture ever mentioned either explicitly or implicitly? What is your sense of the relative importance of strategy and culture?" In many interviews, we asked clarifying questions to determine precisely how the interviewee understood strategy and culture to interact.

We learned a great deal about when, how, and why strategy and culture influence workers' performance, drawing novel insights that will help scholars to improve their theories of strategy and culture and practitioners to build better businesses. We found, for example, that because culture is dynamic, CFOs have found that small, continuous investments in culture are less expensive and more effective in creating long-term value than big, one-time investments. These ongoing investments help leaders to align the culture with their firm's most important performance drivers.

> "Culture will trump strategy every time because people would do what culture supports and leads them to do, and so a great strategy that is not in sync with culture will never get implemented in the same way."

Key Insights about Strategy and Culture from CFOs

Strategy should be rooted in a firm's cultural strengths

Financial executives reported that culture can offset mistakes in a way that other executive actions, financial policies, and corporate assets cannot. Whether it embodies a firm's stated values or needs a massive overhaul, culture influences people's actions, which means that investments in culture amplify the returns on other types of investments. One executive said, "Culture will trump strategy every time because people would do what culture supports and leads them to do, and so a great strategy that is not in sync with culture will never get implemented in the same way."

This view exemplifies a broader shift in thinking over the last few decades. Where most executives once considered formulating a good strategy to be the key to making a firm perform, they now tend to believe that both good strategy and efficient execution are essential. To execute strategy to greatest advantage, leaders must focus on culture, which necessarily determines their success. As another executive told us, "Strategy lays down the rules for playing the game, and culture fuels the spirit for how the game will be played."

Many executives believe that the best way to develop a strategy is to root it in the firm's cultural strengths. As one respondent put it, "Culture is never a part of the strategic plan, but the culture tells you what the strategic plan should be." Another said, "You can write up a brilliant strategy, but the execution is made by the company. Poor culture can certainly be an impediment to effective execution, but a strong culture does not guarantee a strong execution." A better approach, then, is to develop a strategy rooted in the right cultural values, which makes the most of the norms that employees follow.

> The right cultural values are those that are foundational for strategy.

But what exactly are the ideal cultural values? The right cultural values are those that are foundational for strategy. One executive emphasized the importance of incorporating the firm's aspirational cultural values into any strategic plan. When the day-to-day actions of employees are informed by these values, they will increase the firm's returns. As the interviewee said, "We have a vision document that outlines who we are as a company, and what our overarching principles are. Everyone can tell you about the principles. On top of that, last year we articulated five strategies to drive the business. I'm not sure that everyone in this company could tell you about those strategies. But the culture actually will tell you the five strategic items make perfect sense. The culture will drive the business."

The optimal culture depends on the firm's characteristics

CFOs said that culture can be purposefully engineered. One even suggested that it might be possible to optimize culture much as we optimize financial policy. An optimal culture, then, is one which allows executives to maximize the return on their culture investment.

To determine how to improve culture from a quantitative perspective, CFOs carefully consider the characteristics of their specific firm. The reason for considering firm-specific characteristics is the belief that no universally optimal culture exists. As one executive said, "There is no set of cultural values that is always effective within the same industry at the same time or even within the same firm." Instead, CFOs suggested that leaders should invest in cultural changes that balance cultural elements against their costs. Some of the company characteristics that CFOs believe play a meaningful role in determining whether a certain cultural element would be beneficial or costly include asset tangibility, financial position, competitive position, and lifecycle stage.

> With regard to tangibility of assets, one executive explained: At one firm I was at, the strategy was more important, but at another firm the culture was more important because baseline execution was more important. At the firm where execution mattered most, the nature of the business, the nature of the customer, the nature of the asset, the nature of the competitive field [makes culture more important]. The importance of culture relative to strategy depends on the business.…Strategy becomes more important when there are no hard assets anchoring anybody. You have to be pretty smart about how you're using your brand, what markets you're attacking, what is your customer acquisition strategy in order to grow because everything is so wide open.

In the last two decades, the largest public firms by equity market valuation transitioned from holding mostly tangible assets, like ExxonMobil, Coca-Cola, and Walmart, to holding mostly intangible assets, like Apple, Google, and Microsoft. These modern leaders of the S&P 500 Index have seven to ten times as many intangible as tangible assets. It is therefore essential for executives to understand that intangible assets require specific cultural values and a greater reliance on strategy. This idea suggests the possibility that brick-and-mortar businesses are being destroyed not only by digital sales, but also by their leaders' failure to select and invest in the right cultural elements.

One executive told us that the impact of corporate culture on the value of a firm with mostly intangible assets could be as high as 40 percent. They said, "We have a couple of business [units] where the culture is very valuable to their executing their strategy. So much so that if key people [and intangible capital they possessed] walked away, you would short the business immediately. The reason the stock price goes down when key people leave is that people are worried about culture and continuity. You take a lot of disruption if you lose people and have to reform the culture and figure out how to execute."

The financial health of the company can also help executives select the right cultural values and norms. As one respondent explained, "In an environment of scarcity you are going to end up with a particular type of culture that would have emphasis on control. It would have a lot of emphasis on competition in the sense of finding the very best way to apply the limited resources and I think there will be a lot of focus on not making mistakes. And in an environment of plenty, you got a culture that is much more focused on facilitating creativity and exploiting successes as opposed to avoiding failures." While most executives understand the direct costs of financial distress, they may be less familiar with the indirect costs of cultural distress. As firms move through business cycles, it is essential that their leaders take advantage of the resulting cultural mindset and select the appropriate cultural values to encourage.

> "Just relying on what worked before is probably the biggest thing that can cause you to fail because you need to develop how you need to execute given the facts and circumstances of that time."

Executives should also consider their firm's industrial competitiveness when deciding how best to invest in culture. As one respondent explained, "As things started to heat up with competition, the cultures had to adapt and evolve to the environment, both internally and externally, and that slowness in adaptation is what kills businesses. The problem we were having is we weren't adapting fast enough." Another agreed, "If the external environment becomes more competitive and more unpredictable, it requires a different culture and comprehension of what was going on than what was going on before and you have to change. Just relying on what worked before is probably the biggest thing that can cause you to fail because you need to develop how you need to execute given the facts and circumstances of that time."

The firm's lifecycle stage is also essential to culture. Although there is not a fixed set of cultural elements that is ideal for all firms at the start of their lifecycle, or for all mature firms, lifecycle stage should influence how leaders invest in changing and optimizing their company's culture. One CFO explained, "The reality is that cultures change over time due to the lifecycle of the company.... [Our CEO] would put a disparate, new group together to lead a huge bet.... That group's innovative new methods would seep out into the rest of the organization. As [our CEO] knew, you have to try to shake things up to continue improving the culture."

Align culture and strategy to create sustainable long-term value

Business scholars have long said: Strategy is a plan. Strategy is short term. Strategy changes. Culture is a pattern of behavior. Culture is a longer-term relative of strategy. The CFOs we interviewed agreed that strategy changes faster than culture. One stated that "culture is always longer-term because that is the code and behavior of the company. Until there is a deliberate effort to change it, that persists. But your strategy can change from year to year. Strategy is easier to change than culture."

Yet our interviewees also pointed out that focusing on the tension between the short term and the long term misses the point. They view culture and strategy as the number one and two drivers of long-term firm value. The dual importance of emphasizing both strategy and culture to long-term value is perhaps the most powerful insight we gained from these CFOs, though it may also be the simplest. Although culture is long term and strategy is short term, their *alignment* can produce sustainable long-term value. As one respondent said, "When culture and strategy align, execution is repeatable. Repeated execution allows for growth and scale, which becomes a source of sustained value."

Building an Effective Corporate Culture

So how can leaders build a culture that creates value for their company? Two essential ideas that emerged from our discussions with CFOs are the importance of continuous investment and ongoing conversations about culture.

Cultivate cultural momentum

Executives and business gurus have pointed out that companies need to walk the talk, living up to the cultural aspirations touted by management. While our respondents generally agreed, some held that a company's culture often needs an overhaul, even when employees act in keeping with its stated cultural values.

> If a company's leaders want to create a culture that builds long-term value and is aligned with their strategy, they must generate not just agreement with cultural values, but also cultural momentum.

If a company's leaders want to create a culture that builds long-term value and is aligned with their strategy, they must generate not just agreement with cultural values, but also cultural momentum. To understand cultural momentum, envision culture as a round rock on top of a hill. The rock has potential energy and influence. Now imagine if you could make the rock bigger, increasing its potential influence. More employees now embody the company's values. But, although the rock's potential has grown, its power will only be realized if something sets it in motion. The rock's path down the hill is equivalent to cultural momentum, affecting everything along the way. Just remember, the heavier the rock, the harder it is to change its course.

The rock analogy demonstrates that culture is not a fixed asset; it is dynamic and needs continuous management and investment. Even a purposefully engineered, uniformly accepted culture could change quickly from an asset to a liability if it has lost momentum or stalled in an evolving business environment. It is essential that leaders be always ready to keep their rock moving or to steer it in a new direction. As one CFO pointed out, "There's also the downside to a very strong culture, and it can become a set of handcuffs, limiting freedom of thought, limiting the ability for outside talent to hit the ground running and become part of the team. So, that's the balancing act, it's a blessing and a curse."

> "One thing I've realized as I've reached the most senior management is how much work it is and how conscious you have to be to sustain and adapt that culture."

Selecting the right cultural values at the outset and persuading workers to agree with the intended culture are certainly essential steps toward optimizing culture, but focusing on them can cause leaders to overlook the need to continuously invest in that culture. As one CFO said, "One thing I've realized as I've reached the most senior management is how much work it is and how conscious you have to be to sustain and adapt that culture. I think most employees take culture for granted. It takes continuous refinement and reinvestment to keep the culture alive." Like the rock rolling down the mountain, culture will continue to move along its initial trajectory unless leaders alter its course through continuous tactical investments. To keep the rock moving in the desired direction as circumstances change, leaders must invest in changing the topography that guides it, generating positive financial returns. Without this continuous investment, it is too easy for culture, hurtling unchecked along its original course, to become a liability.

So, what holds leaders back from setting out to change culture? They may feel daunted by the sheer size of the task, instead accepting the inertia of the existing culture and hoping it will one day improve on its own. These leaders are likely to end up watching their rock roll off in the wrong direction. One executive explained, "Part of the culture, frankly, is carried forward by momentum. Why? The memorable leaders substantially define the culture. Even years after they ceased to be an active force in the organization, their legacy is still alive." And changing the rock's path after it picks up speed takes a big investment, while turning culture around is both difficult and risky.

By contrast, the ongoing investments needed to keep a firm's culture moving in the right direction are considerably smaller. Leaders could appoint a culture ambassador to guide, encourage, or celebrate the culture throughout the organization, not just by describing its history when bringing new workers onboard, but by routinely spotlighting and rewarding employees who embody it. They could also invest in culture by debriefing after both successful and unsuccessful product launches as well as quarterly earnings surprises, interpreting what happened both strategically and culturally. Promoting managers who build culture and relationships by promoting their direct reports is also an investment in culture. Even simply listening to employees is a small, ongoing investment in culture. They are likely to be the first to notice when the company's culture has gone astray and might have the best suggestions for how to put it back on track. All of these little investments fuel the cultural momentum essential to success.

Retail CFOs we interviewed described other small investments. One firm's leaders made a point of having regular conversations with the managers of daily operations in its retail stores, noticeably strengthening its inventory and supply chain management.

Another firm's leaders found that, after an initial period of rapid growth, it lost its focus on the customer, and that, although the firm prided itself on teamwork, new employees did not really trust more experienced ones. The situation had deteriorated to the point that the CFO admitted that the firm's executives often did not have information they needed to make critical decisions. In an effort to change this damaging cultural, the CFO explained, "We now do phone calls with [the managers] twice a week where they can get on the phone and tell us about their stores and their experiences, and are we getting them inventory on time, and did our software work correctly for billing and logistics.

Versus before, that would filter up to the manager of preferred retail who would then talk to the head of retail who would talk to the head of the next level. It would take six layers to get there." This small investment of time assured retailers that their concerns were being heard and alerted managers to barriers preventing the company from succeeding.

If you are trying to decide what small cultural investments would be best for your own company, we encourage you to write down three catalysts for cultural change—people, systems, and events—and then think of one small investment in each category that would move the company toward your intended culture. As you consider these small investments, you will discover that many of the cultural benefits will power more than one of the catalysts.

Imagine you lead a firm whose committee meetings are neither efficient nor productive. Committees meet at various levels of the organization, but at all levels only a quarter of the attendees are prepared, employees show too much deference to senior managers, and the meetings are only marginally beneficial. One thing you could do to change this pattern of behavior, and also the cultural dynamics that make it acceptable, would be to make a small investment in a technology systems catalyst.

You could move some of the committee meetings to a technology platform designed for crowdsourcing, that will alert more employees to whom the committee's task is important, inviting them to participate and volunteer their thoughts. You may find that only a few employees respond, but they're likely to be the ones who really care about the meeting's topic and who will thus be more likely to share their ideas. Their active participation will probably reassure others that the meeting is a safe space in which to share their ideas, encouraging ever broader participation. As the crowdsourcing technology is adopted throughout the organization, it will start to move the culture in the right direction. This small systems investment will also bring the firm's people benefits by empowering workers and encouraging them to contribute.

The leaders of firms at any stage in their lifecycle can profitably make small investments in culture. Startups often claim to have too few resources and too little time to invest in cultural development. Investing in culture often seems like a luxury to the leaders of a startup so small that it does not yet have a human resources leader. Yet CFOs with experience in young firms told us that the returns from investing in culture may be even higher at young firms. Imagine, for example, the outsized impact of one seemingly talented, yet toxic, employee on a small firm.

Consider the following observation from an executive with years of experience in Silicon Valley: "At another startup founded by a bunch of previously successful guys, I never had a feel for a culture there. I don't know that they thought about a culture. There was a lot of energy there, there was a lot of activity, but there wasn't anything that I would have defined as a cohesive culture. That company ended up going bust after about three months. Whereas at other ultimately successful companies, the founders really set the tone for the company from day one." Young founders should recognize the importance of continuously investing just a little time and money in culture, and of starting very early on.

Commit to bold debates as part of your culture

Aligning culture with strategy creates sustainable value in the long term, but achieving this alignment can be difficult due to the sheer number of potential paths a firm could pursue, each requiring a unique set of investments. When executives assess investment decisions in isolation, finance dictates that they should only select investments or acquisitions whose projected revenues will be greater than their costs. But when leaders make a series of investments, sometimes in sequence, the realized value may be lower than initially expected.

To successfully refine the list of investment options and embrace a strategy and culture that are well-aligned and capable of effectively executing a series of value-generating investments, it is important to engage many experts in the decision. Most executives know that maximizing cognitive diversity creates an environment conducive to generating bold, valuable ideas. However, the key to properly aligning culture with strategy lies in the firm's leaders ensuring that managers and employees fully commit to the bold choice they have made, even if it was subject to debate.

This concept can be likened to the final moments of a basketball game, where multiple players may desire the opportunity to take the game-winning shot, but only one can be selected. While the coach and the team may debate on the sidelines about who is the best choice, once the decision is made, all players must commit to it if they want to win the game.

Still, it can be difficult to ensure that employees commit to the decision once it is made. One executive described a "firm where a lot of people protect each other and won't bring up something that is derogatory to their colleague's project or program. They are even less willing to say something to a superior. As one of my colleagues said, 'They are terrified of me, so they will not challenge me when I say something and I am going to drive us off a cliff, if they don't.'"

Indeed, for a firm to repeatedly generate value, its leaders must ensure that its employees are willing to share unpopular ideas, which requires that they feel safe and confident in doing so. Firms whose employees feel a sense of belonging and ownership are thus far more likely to generate long-term, sustainable value consistent with a well-aligned culture and strategy.

Conclusion

Our interviews with financial executives were designed to improve our understanding of culture and strategy by drawing upon their quantitative perspectives. In this regard, the interviews are not an empirical exercise meant to establish trends or causality. By asking questions like "how do culture and strategy interact?" we found that financial executives interpret the interaction between culture and strategy in distinctive ways that sometimes contradict previously accepted wisdom. We hope that modern researchers and corporate leaders can use this diversity of perspectives to develop stronger theories and approaches, allowing executives to manage culture and strategy ever more effectively in the future.

Author Bios

John R. Graham is D. Richard Mead Jr. Family Professor of Finance at the Fuqua School of Business and a Research Associate of the National Bureau of Economic Research. A Phi Beta Kappa winner and former president of the American Finance Association, Graham has written many award-winning research papers and is director of Duke's CFO Survey, which polls hundreds of CFOs worldwide. Graham earned a BA from William and Mary and a PhD from Duke.

Jillian Grennan is an Associate Adjunct Professor of Finance and Sustainability at the Haas School of Business. Grennan has earned numerous awards for her research on corporate culture and sustainable investment. Grennan earned a BA from Wellesley College and a PhD from the Wharton School of Business.

Campbell R. Harvey is a Professor of Finance at the Fuqua School of Business, Duke University and a Research Associate of the National Bureau of Economic Research. A former president of the American Finance Association, Harvey has won numerous awards and published over 150 articles on investments, emerging markets, corporate finance, behavioral finance, financial econometrics, and decentralized finance. Harvey earned a BA from the University of Toronto and a PhD from the University of Chicago.

Shivaram Rajgopal is the Kester and Byrnes Professor of Accounting and Auditing at Columbia Business School. Professor Rajgopal's research interests span financial reporting, earnings quality, fraud, executive compensation, and corporate culture. His findings are frequently cited in the popular press. He has made many notable contributions to the accounting literature. Rajgopal earned a BCom from the University of Bombay and a PhD from the University of Iowa.

Endnotes

1. Ankur Agrawal, Christian Grube, and Meagan Hill, "Mastering Change: The New CFO Mandate," *McKinsey.com Strategy & Corporate Finance Practice* October (2021): 1-10.
2. John R. Graham, Jillian A. Grennan, Campbell R. Harvey, and Shivaram Rajgopal, "Corporate Culture: Evidence from the Field," *Journal of Financial Economics* 146, no. 2 (2022): 552-593.
3. John R. Graham, Jillian A. Grennan, Campbell R. Harvey, and Shivaram Rajgopal, "Corporate Culture: The Interview Evidence," *Journal of Applied Corporate Finance* 34, no. 4 (2022): 22-41.