How Global Upheaval Influences Board Decision-Making

By Michael Montelongo

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100

What is the effect of Cold War II on corporate governance?

What should boards and companies do or not do when confronting the impact of geopolitical crises? It may be helpful to consider the broader context giving rise to these issues, namely why we’re in the situation, the lessons we’re learning about geopolitical risk in real time and the key insights that may be helpful in preparing for future geopolitical crises. These questions are timely because they address very important, urgent and serious matters that deserve thoughtful and prudent consideration.

History Did Not End After the First Cold War

After winning the Cold War, the West embraced the hopeful but mistaken notion that we could dismiss traditional forms of great-power competition and balance-of-power diplomacy. But hope is not a strategy; that misguided consensus was based on two faulty assumptions:

- America’s victory in the Cold War was absolute and America’s economic, military and diplomatic power ensured our indisputable supremacy for decades.
- The international “rules-based” world order we were building would be popular abroad and uncontroversial at home.

That new world order also ushered in an era of globalization complete with increasing economic and trade dependencies. The result created a tailwind for many of today's top executives while serious geopolitical issues were relegated to the stuff of history books.

Today, with simultaneous geopolitical crises in Europe, the Middle East and East Asia, we are at a new and critical inflection point in geopolitics and the political economy. We face the most hostile international outlook since the dimmest days of the first Cold War.

Still, there is good news: Russia has made NATO matter again, reaffirming the transatlantic military alliance's modern-day relevance, value and solidarity.

But actions by authoritarian regimes are transforming the existing order, reshuffling global alliances, redrawing the geopolitical landscape with unclear economic and political implications, and rewiring global power flows that threaten to erect new barriers. Some say we are on the cusp of Cold War II, if not a hot one.

And even as we focus on deterring China and imposing costs on Russia, we cannot ignore threats from other states, such as Iran and North Korea.

The Blurring Line Between the Private and Public Sectors

Corporate activism is on the rise. Corporations are engaging in the public square, a domain once considered the exclusive province of policymakers, regulators, nongovernmental organizations and others. This is part of a recent trend that has seen more companies willing to take public stands on causes that are important to their constituents or can't be resolved by policymakers. Contributing to this is a breakdown in trust in other institutions. The 2021 Edelman Trust Barometer, which gauges trust in institutions, found that business was more trusted worldwide than government or the media.

Russia's invasion of Ukraine demonstrates that taking a stand now extends beyond domestic policy and includes foreign policy and statecraft. Indeed, withdrawing or suspending operations in an entire nation — particularly one as large as Russia — signals a dramatic expansion of the corporate role in society, with potentially significant consequences for a company's performance and prospects.

Proactive Risk Management Matters

Some commentators suggest geopolitical risks have suddenly and unexpectedly reappeared. In fact, these risks have always been present — we just ignored them. The relative peace of the post-Cold War era and the unprecedented expansion in global trade during that period masked the growing geopolitical tensions that are now more apparent and, most assuredly, will continue.

Russia's Ukraine invasion places business leaders right back in crisis-management mode, as they update business continuity plans and crisis manuals to deal with unanticipated geopolitical scenarios, the unintended consequences from an unprecedented regime of sanctions and an increased level of cybersecurity risk exposure. At minimum, companies need to carefully evaluate the risks of their global activities.

This crisis highlights the major repercussions that geopolitical events may have on a company's ability to execute its business strategy, and it underscores the imperative to address such issues proactively. Most companies have been in reactive mode; unfortunately, many boards and management teams feel ill-equipped to assess and manage these issues, perhaps because they grew up in an era of increasing globalization or don't have this expertise. Research shows that only a small fraction of the director population in the United States has geopolitical experience, with just 13.1% of S&P 500 directors in 2021 having such qualifications. For Russell 3000 board members, the number drops to 6.8%.

This emerging world order underscores the growing importance of scenario-based planning — or war-gaming — as a complement to strategic planning and the benefit of having direct access to geopolitical risk expertise in the boardroom. Even those companies that lack multinational operations may want to consider seeking geopolitical advice. Companies should weigh the risks of being caught in the crossfire of geopolitical tensions and the risk of operating in countries where weak rule of law, human rights abuses and autocratic governments impose a de facto financial and reputational tax on doing business.

Michael Montelongo is a director of Civeo Corporation and Conduent Inc., president and CEO of GRC Advisory Services LLC, and former assistant secretary of the U.S. Air Force. The views expressed in this article are those of Mr. Montelongo in his personal capacity.