

Institute of Corporate Directors

Podcast Topic: **Be It Resolved: Disruption Doesn't Erode Trust, It Rewards It.**

Rahul Bhardwaj (0:06 - 1:07): Welcome to Be It Resolved, Season 2, where bold ideas meet courageous leadership. I'm Rahul Bhardwaj, President and CEO of the Institute of Corporate Directors in Canada. Each episode explores the issues that influence directors, governance, and decision-making in the boardroom.

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My guest today is José Hernández. He's an accountant, CPA, and a CFA. He's also the CEO of Orda Strategies AG, a global crisis management firm.

Jose has advised boards and governments on fraud, corruption, and misconduct across five continents, supporting organizations through complex regulatory and enforcement action. He's also an author of a book called Broken Business, and he's a frequent guest lecturer. Since 2016, he's also served on the Government of Canada's Advisory Committee on Money Laundering and Terrorist Financing.

Welcome Jose.

José Hernández (1:07 - 1:08): Thank you, Rahul.

Rahul Bhardwaj (1:08 - 2:03): Today, we've got a really interesting resolution. Be It Resolved: Disruption Doesn't Erode Trust, it Rewards it. Well, to the listeners, which way will you vote?

Jose, you're going to get to vote on this a little bit later. The question on the table in many ways is, is trust an asset or a liability in disrupted times? We're going to focus on trust and what it means for boards in a time of disruption.

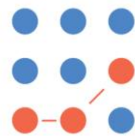
As geopolitical tensions, technological competition, economic pressures, as they reshape the global environment, companies are facing some very difficult choices about how to compete while maintaining integrity and credibility. Is it an asset or a liability? Let's get started.

When we're talking about trust, it's a very broad topic, but what's the meaning of trust for boards today?

José Hernández (2:03 - 3:54): Thank you, Rahul. It's really a pleasure to be here. I think I've spent about 25 years in Europe and in working with high trust nations, Sweden, Switzerland, Netherlands, and yet I was dealing with a very uncomfortable subject, meaning corruption.

When I came across about a decade ago to Canada to deal with a similar case, I faced that same challenge. And I think high trust nations like Canada take trust for granted. So we trust each other in terms of a board sitting at the top of, you can look at scandals like the major corruption scandal that have occurred and look at it and say, I should trust nobody.





But in fact, trust is what makes us special. I think one of the points is we need to get back to basics. To build trust, to have trust, to instill trust in our customers, we need to have good sound leadership and good cultures and organizations.

We need to have the right controls, the right governance to make sure that things don't go too far off the mean. And we need to have a sound strategy. The basics have not changed, but the context today is totally different than it was in 2018 when I first published this book, which I'm now updating because now we're dealing with technological disruption.

And what does that change? Well, if you look at just geopolitics, we can no longer assume that, for example, our partner in the South is going to have a fair, we don't even know what fair play is anymore. We have this hyper competitive environment.

If we go to auto shows in China, we see that all of a sudden within a decade or two, customers are more attracted to these new Chinese electric vehicles with incredible ranges as opposed to Western equipment. That's happened in a very, very short period of time. One of the big points is that with disruption, the speed has changed.

But however, as Canadians and as companies, we need to be thinking of where do we play? And I think technology is an opportunity.

Rahul Bhardwaj (3:55 - 4:24): Nobody's going to dispute the notion that we need more trust. Nobody's going to dispute the notion that we're in a real trust deficit environment. We've been talking about it for years.

If I'm serving on a board, of course we need trust and it's the lifeblood of governance, but is there a hierarchy of trust? Do we need to be thinking about that as directors? I mean, is the trust of regulators more important than shareholders, which is more important than employees or customers?

How does a director start to think about trust?

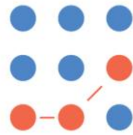
José Hernández (4:25 - 5:50): My experience is usually when the trust bond is totally broken. There's a criminal investigation, stock price is down 20%. What do we do next?

All stakeholders are important. Some are more important than others. If you're with a criminal investigation on top, clearly your job is to undertake an investigation and make sure that there's no further misconduct happening.

But my bank, I used to be a partner at PwC and then I set up a company almost 20 years ago. And we set it up at a Zurich and our bank was Credit Suisse. And I think we talked about it last time.

It's a 170-year-old institution. And really when you talked about Switzerland, you talked and referred to Credit Suisse, what brought Credit Suisse down? It was trust with two parties.





It was trust with their anchor investors. You know, a famous Saudi investor made a certain statement that started a bit of a panic. Two was your customers starting to pull money.

Those two are key. But the third was the regulators moved in very, very quickly. In terms of hierarchy, some customers can bring you down to their knees.

So, in terms of a package, you need to be thinking of them all, but thinking of those that can really, really set the tone for what happens next, and that is just how we need to think about it. And in terms of the board, just having good, solid links and relationships with all the stakeholders, particularly regulators these days is of critical importance.

Rahul Bhardwaj (5:50 - 6:25): We're going to talk a little bit more about what boards should do differently and even questions they can ask management. Let's talk a little bit more about how trust is an asset now. We're living in a time where competition is just accelerating for so many different reasons.

Talked about technological, geopolitical, considering where we are right now. And somebody's settled on the way that, you know, focus too much on this. It's like trying to bring a knife to a gunfight.

And if everybody else is lowering the bar, does trust become a liability? And I hope not. We'd like to think it's an asset but help us think through that.

José Hernández (6:25 - 7:58): It's a great subject. Trust is asymmetric. If you go to places like China, like Russia, Brazil, and some different geographies and doesn't have to be challenging geographies, especially as a Canadian entity, you're expected to bring trust to the table.

That's what they're buying. If you decide to assume local customs, local ways of operating, you're just competing with the rest. In fact, we're doing ourselves a disservice.

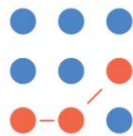
You know, I had a case about 10, 15 years ago where Chinese technology was really booming. And you may argue it wasn't booming because they copied technology, because the state was investing billions in the back door, whatever the reason. This one technology company decided we need to stay abreast and meet our short-term targets.

What they ended up doing is just adopting the local customs, paying bribes on the side, getting in colluding with competitors, and at the end, you end up with the cost of that, the cost of shortcuts, which is a criminal investigation that almost brought this company down. I think we need to just say that in some instances you have to step back and say, can we compete in this market in this way, is it worthwhile? Because there's a cost to shortcuts.

And I think that sometimes it helps to put it on the table, analyze it, and we could be wrong and then we can reassess. But I think that's how I approach it. And we constantly need to be checking assumptions.

Just because we're honest, good people doesn't mean that once we're far away from headquarters, that integrity is going to remain the same, especially when we are under so much pressure.





Rahul Bhardwaj (7:59 - 8:27): That's really intriguing when we think about we're somewhat in the age of diversification. We're hearing it everywhere. We were all in with all our trading partners and now we have to diversify.

Ironically, to reduce that risk of concentration, we're actually taking on another risk, which is the risk inherent in diversification. And would I be right if I say that there are some places that maybe Canadian companies should just not be trying to compete in?

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José Hernández (8:27 - 9:21): Yeah, I think that's right. There are some places where we just simply don't belong because there are some countries, geographies, industries where you need to go in with a partner. And you become as good as your partner.

And if your partner is questionable and they basically put your brand at risk. And then there are some sectors, like for example, in the last 20 years, I've had multiple engineering construction companies, global, whether in European and Canadian, investing in Brazil. There are some sectors, particularly 10 years ago in Brazil that were uninvestable as a global company, because you knew what was expected.

And we've seen it with the Petrobras scandal and all that transpired. But just basically be able to say the cost of doing business in this geography is too high because the risk is high. So, you need to put the infrastructure.

And even if you did put the infrastructure in place, chances are you're going to make a slip up that really is going to cost your brand too much in terms of what it brings.

Rahul Bhardwaj (9:21 - 9:24): Is that a short-term or a long-term conversation?

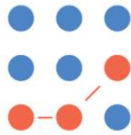
José Hernández (9:24 - 10:48): Both. The short-term pressure that I'm not ring your boss and say, boss, that deal that we've been working the last three years is not coming in. Why not?

Because there were payments made on the side that we've heard of. Somebody is going to have to explain to the markets that the growth in this particular geography is not meeting expectations. So that's a very short-term pressing risk.

The long-term implication is once you've entered with these sorts of sloppy agreements, chances are like in some of the corruption investigations that we looked at, people took the shortcut, the three, 5% commission through a channel. And when you start to tally it up, how much did we actually make on some of these deals, and this is excluding fines and penalties, we ended up with loss making contracts, but again, you know, we love the fame of winning a 3 billion, 30 billion contract in a geography because it's booming, you know, they're doing coast to coast projects. But then there's the reality that this is, is this really what we are going to do?

And that's where trust really comes in. You got to trust your people. When they're telling you, we can't do it.





You just say, you need to try harder and harder, even though what you know, what you're asking is push the border and potentially cross the line, right? So again, it's just something that we need to, we're humans. And at the end, humans under pressure, we make mistakes and we cross lines.

And a lot of the people that I've worked with, just, they felt like a useful idiot along the way because their bosses were pushing and they felt like they had no choice and then they rationalized it.

Rahul Bhardwaj (10:49 - 10:57): Given all that, what would you say about what do Canadian companies have to do differently if they want to remain competitive while maintaining trust?

José Hernández (10:58 - 11:48): I think we need to put our best assets forward, which is our people, our talent. I mean, we are deficient is our capital. We don't deploy enough capital.

We don't innovate enough and keep the innovation in Canada. If you're producing an electric vehicle, if you're producing some key strategic parts, how are you going to be better than Koreans, Chinese and American? What's your niche?

And it's really a question of choose your market, choose your niche where you can compete because people want more of Canada around the world. They want somebody they can trust and will be there for the long-term. And yes, some people will want the quick replacement for the time being, but eventually you want long-term partners that will be there for you.

I think picking our niche, whether it's in our talent, our innovation, our people, and be careful with shortcuts. There is no shortcut to having a sustainable market.

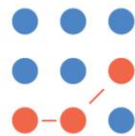
Rahul Bhardwaj (11:48 - 12:15): If trust is the lifeblood of both good governance and by the sound of a good corporate performance in this environment, sounds like complacency is really the risk here that if boards aren't attuned to this notion of trust, it's a big problem. Let's talk a little bit more about what signals should boards be really looking at to try to anticipate kind of misconduct risks or emerging governance problems around this idea of trust.

José Hernández (12:16 - 13:23): Yeah, I think there's an MO, a way of that these things start happening. So usually when there's misconduct in an organization, it doesn't occur overnight. These things have been brewing over time and signals have been given over time.

I think the boards need to be active listeners, speak to people, have direct lines with the folks in compliance and risks to know what the engine is doing and who's going away. I mean, like the other part is what gets real global companies in trouble at the end is superstar managers. They divert too far off the mean.

There's topics that we consider taboo, whether it's doing business in a certain market or in a certain way, and we call them fancy names. We cannot tell you about these because this would be in a, you know, it's a national security contract. We have natural ways of hiding things.





Look for dark corners, look for taboo areas, be careful with your superstar managers, and just sometimes be stupid on the board and says, I really don't understand what was just said, and maybe I need a half an hour afterwards. Somebody can explain it to me because sometimes things that are too good to be true or too complex to understand, that can be an indicator of problems.

Rahul Bhardwaj (13:23 - 13:25): It's a people thing, isn't it?

José Hernández (13:25 - 13:25): Totally.

Rahul Bhardwaj (13:26 - 13:44): Intuition, judgment, which is so much, you know, relying on experience. Yeah. But I'm seeing you, your body language says, you know, people trust your instincts here.

And in some cases, I guess I'm also hearing that your biggest asset could also be your biggest liability if you don't look at it really carefully.

José Hernández (13:45 - 15:00): Yeah. And you're seeing it with this Jeffrey Epstein scandal, you know, whether involving politics or business, you're seeing it with CEOs of major brands that were promoted in times of crisis and then blow themselves up because of sexual misconduct, you know, you're as good as your people, vet them properly. And vetting, it's not just getting in a boardroom and saying, are they a good guy?

Are they a good person? No. Vetting them means, tell me what has been the smoke through these person's career.

Check, you know, how they've made their targets in the past. The basics don't change, but somehow, we seem to not do it, or we're just not courageous enough to face the fact that we may have made a bad decision in the past, but we're just going to make an equally problematic one next. So, and again, then maybe some part of it is the 10 years, 10 years of CEOs, shorter and shorter directors as well.

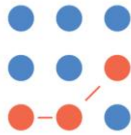
There's a lot of factors. I don't know exactly what is the cost, but sometimes these blind spots is what kills us and we should just do our homework on people, on their actions, and then make educated decisions, not just tummy decisions, because that's just, again, our instincts are great, but we easily misled, especially by people that we like or look like us.

Rahul Bhardwaj (15:00 - 15:37): Another classic example of culture eats strategy for breakfast. Got to get that piece right. Let's get even a little bit more specific here.

What can boards ask of their management teams to start to ferret this out? I mean, you started, I think, to open the conversation by saying, you know, ask those quote unquote dumb questions. They're not obviously, but they may be simplistic in the context.

But how would one go about exploring this further with management? Now you don't want to put management off either, right? There's got to be some sort of basis of working together and management wants to feel trusted by the board, but the board has to hold by account as well.





José Hernández (15:38 - 16:39): Correct.

I think sometimes asking for a deep dive into a particular set of market, a particular partner that's getting into trouble, a particular area, I think that's usually good. I think one of the best board members, particularly on the risk side, they have one-on-ones with the head of internal audit, head of compliance with the CFO. And there's a bit of a trusting relationship there.

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Again, as a board member, you cannot be micromanaging. And if you have doubts about management, you've got a very, very large problem in it. So, you, there should be an open, trusting conversation and there should be obviously some deference to the CEO.

But at the other side, we should be really guarding to ensure that the right information getting to us on the table and making sure that we are taking well thought through risk-based decisions. So again, it's just doing the basics and using the lines that we have as a board with the company. You know, talking to people, talking to stakeholders.

And then again, if there are warning signs, put them on the table and then stuck it around there, let's just address it.

Rahul Bhardwaj (16:39 - 17:09): We've often talked about values driving companies, and that's embedded in a lot of conversation today that we're having. But many of these values are really kind of taken for granted until they're really tested. In your opinion, what sort of values should boards really focus on protecting most carefully in today's really disruptive environment?

I mean, when we talk about values, it's really broad. You had to narrow it down to a couple, just to give a little bit of direction. Where would you start?

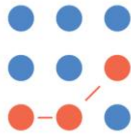
José Hernández (17:09 - 17:16): Well, so I just read that, for example, the Deutsche Bank, their annual report is over 800 pages long.

Rahul Bhardwaj (17:16 - 17:16): Wow.

José Hernández (17:17 - 18:45): And some of the European companies are putting out financial statements that are 50 pages long and sustainability reports that are three times longer. So, if that is a way of signaling what our values are, I think one observation is we're getting very confused. We're trying to do too many things, please too many stakeholders, and the system's gotten very complex.

If there's one thing to bear in mind is our brand and our integrity, because that's what makes us, gives us that competitive advantage, our brand, our integrity, but just, we cannot rest on our past laurels, that needs to be coupled with our innovation. What new are we producing that our competitors are not necessarily there yet? And sometimes it's data security, for example, because they know that our data potentially may not be as misused as other sources of data, and it could be reliability of access to resources, whatever it is, but I think it's looking





at our brand, our integrity, and our competitive advantage, but not be going back to your word complacent, I think a lot of these corporate brands just get lazy, just because we were great yesterday, we have a right to be great tomorrow and not anymore with the current wave of technology, geopolitics.

And also as we tackle climate change, whether that is being, regardless of our Southern partner decides, you know, the most of the world is subscribing to, we need to do something, and that is a risk and an opportunity, but it goes together with what's the value proposition and the integrity and innovation that we bring forward to our clients.

Rahul Bhardwaj (18:46 - 19:24): What an interesting conversation, and we're going to come back to trust again and again, I have a feeling. Jose, it is definitely an asset, and it's one that I think companies would agree. They want to deal with organizations that they trust and people they trust too.

And it's tough though, in this environment where, you know, the bar keeps getting lowered for short-term gains, so be very, very careful in what you do. I'd ask right now, let's have a look at our resolution, which is Be it Resolved: Disruption Doesn't Erode Trust, it Rewards it.

Ask our listeners to think about that. What's your take on, which way would you vote on that?

José Hernández (19:25 - 20:15): I vote that I agree, fully agree with this, but there's a short-term and a medium-term. In the short-term, when you see everything that's happening with geopolitics, with signals from our greatest competitors or greatest partners, you're bound to say, well, we're in a race to the bottom, but when you actually look at the world and our customers and whether they're government customers or retail customers, you know, people still want to buy a brand they trust and the product that's good. So that can become even more important in the future. But in the short run, of course, it's easy to say, it's all going down south.

Look at the corruption indicators, you know, all is lost, let's just follow that. And you can do that, but I think, especially for a nation like Canada, one of these middle powers, that's not our secret sauce, I would say. And then we become just like everyone else, which means eventually we're going to become obsolete.

Rahul Bhardwaj (20:15 - 20:41): What a great place to end the conversation today, Jose. I know we're going to come back to this another time, but to our listeners, I hope you enjoyed today's episode. I'd be at resolved that you deepen your boardroom insights to stay ahead of these types of emerging trends.

If you found today's discussion thought-provoking, we encourage you to subscribe and leave a review on your preferred podcast platform. From the Institute of Corporate Directors in Canada, I'm Rahul Bhardwaj. Until next time.

