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The Pursuit of Meaning and Impact, Tied to a Passion for What We Do

I hope all of our readers are enjoying a wonderful 2014 filled with happiness and joy!

But what is the source of happiness? In this issue of the magazine devoted to “pursuits,” it is worth noting that research by GSB faculty member Jennifer Aaker suggests that an important source of happiness for many of us is finding meaning in our pursuits, both professional and personal. Indeed, one of the things that I talk to prospective and current students about is living lives of impact and meaning. We want to educate future generations of leaders who will make a real, positive difference in the world. Steve Jobs famously said, “The only way to do great work is to love what you do.” I believe that finding meaning in your work is the surest way to love what you do.

In a recent town hall meeting, one of our students noted that we ask our students to aim high, be aspirational, and dream big. But what, he asked, do we believe lives well lived will look like for our students? What are our aspirations for them? And how should they go about achieving that? I was so pleased with the questions because they showed what I see every day in our student body: young men and women who want to live the GSB’s mantra to change lives, change organizations, and change the world. Find a passion, I told him, and you will find meaning and happiness in what you do. The rest will follow. Those who pursue fame or fortune for their own sakes are seldom fulfilled.

I am fortunate to be part of a community filled with people who seek meaning through work. Conducting research in a place like the GSB is one of the loneliest kinds of work activities. In the life sciences, researchers at least work in labs. A typical social scientist, on the other hand, works alone or with a coauthor or two. They work, for months at a time, in solitude on a single paper. They do so in the pursuit of knowledge, not for rewards or riches, but for its own sake. It requires deep immersion in a problem often of the researchers’ own making, and to the exclusion of the world around them. My daughters tease me to this day that they would sometimes find me propped up against a wall in a hallway, deep in thought, having forgotten where I was going and oblivious to their playing at my feet!

You will see this kind of immersion too if you visit the Stanford Venture Studio at the GSB, where more than 40 student teams are working on start-up ideas. Last year 18 percent of our graduates started their own companies straight out of school. A startup can also be a lonely and challenging pursuit. It, too, requires the fuel of intrinsic motivation.

We create meaning as well in all of the ways in which the entire GSB is pulling together to pursue current priorities, such as the use of educational technology to reach more people and deepen the educational experience of our own students; the establishment of regional innovation centers in Africa through SEED; and the education of entrepreneurs around the world through Stanford Ignite.

I feel honored to be part of an institution that attracts the very best young men and women from around the world, helps them to live lives of meaning and impact, and integrates them into a community where all of us can find such joy in what we do every day. And I feel proud to be a part of a community that recognizes changing the world through knowledge creation and education is in itself such a meaningful and rewarding pursuit.
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“Repotting, that’s how you get new bloom... you should have a plan of accomplishment and when that is achieved you should be willing to start off again.” —Ernie Arbuckle on career paths PAGE 24

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FROM THE ARCHIVES
“It Starts With You.”

VOICES FROM THE TOWN SQUARE
What do you pursue?

Cover illustration by Richard Mia
Flipbook illustration by Nicholas Blechman
Some 140 years ago, Leland Stanford became intrigued by what seemed like a straightforward question but was a matter of real debate among horseracing enthusiasts: Does a running horse at some point in its gait maintain all four feet off the ground? To find out, Stanford invited the photographer Eadweard Muybridge to conduct a series of experiments. On what’s now part of Stanford University campus, he set up a series of cameras triggered by trip wires to snap a quick series of shots as Stanford’s Kentucky-bred mare Sallie Gardner galloped around a track. Their finding, to the surprise of both the art and science communities, was that the answer was yes. Stanford’s efforts to find the answer to this question is illustrative of something found deep in the DNA of the university he founded soon after: a thirst for knowledge and understanding, and for innovative approaches to problem solving. *Stanford Business* celebrates these values.
As we began rethinking this magazine 18 months ago, we asked ourselves two questions: What is special about Stanford GSB, and what do we hope to achieve with this publication? Our answers reflect the school’s commitment to the joys of inquiry and innovation, and the delight of discovery. They serve as guideposts in our editorial decision making and push us to try new things. In the pages that follow, you will find stories that echo these ideals. In their spirit, and inspired in part by the ingenuity of the racehorse experiment, we also invited illustrator and art designer Nicholas Blechman to try something a bit different. Flip through the pages and see what we mean — and let us know what you think at StanfordBusiness@Stanford.edu

— MICHAEL FREEDMAN, EDITORIAL DIRECTOR
IN THE MAGAZINE

Loren Mooney is a longtime magazine editor and writer who has covered a variety of subjects — from human behavior to the business of NASCAR to day spas — in her time on staff at Sports Illustrated, Reader’s Digest, Bicycling (where she was editor in chief), and Sunset. A contributing editor at Stanford Business, she wrote several stories for this issue, including interviews with James March, Huggy Rao, and Bob Sutton. Follow her on Twitter @loremooney

Steve Fyffe interviewed Steve Jurvetson for our story on satellites and space that begins on page 56. The senior producer of video and multimedia at Stanford GSB, he was a reporter at one of Australia’s best-selling daily newspapers before moving to the Bay Area 14 years ago. You can watch his videos on business and management on our YouTube channel, YouTube.com/StanfordBusiness

Brian Eule is a journalist and the author of the book Match Day: One Day and One Dramatic Year in the Lives of Three New Doctors (St. Martin’s Press). He interviewed John-Paul Ferguson and Sharique Hasan about their research on whether professionals should specialize or branch out as they pursue their careers. The story, which begins on page 19, is Brian’s first for Stanford Business. You can follow him on Twitter @brianeule

Eilene Zimmerman is a journalist based in San Diego who for six years wrote the monthly “Career Couch” column in the New York Times, and now writes a weekly blog/column on startups and technology for NYTtimes.com. You can read her story on faith and leadership on page 36 and follow her on Twitter @EileneZ

ON THE WEB

Film producer J. Todd Harris discusses the quest to discover Hollywood’s next blockbuster. Find this video and many others at YouTube.com/StanfordBusiness

“Providing a supportive, positive environment for employees fosters creativity & innovation.” Follow us @StanfordBiz
“Many people have no problem starting a goal, but they often find themselves losing motivation in the middle of the journey.”

—Szu-chi Huang, PAGE 12
PAUL OYER
Bringing game theory to his personal life
When I set up my dating profile, I was upfront about my teenage children and my sweet but impish golden retriever, but I left out the YouTube videos my children introduced me to under “Things I Find Entertaining,” and in the section of OkCupid.com where they ask some very personal questions, I checked a few boxes that were not technically accurate.

I admit it. I left out details — and lied. What led me to be honest on some parts of my profile and not others?

We can find the answer in a branch of game theory known as cheap talk. A cheap talk framework considers the potential conflict between my preferences and those of the women I am trying to attract and lets us analyze, in a given situation, when and if it is sensible to hide information or lie outright. Since what was true and what I thought would appeal to people were often the same, I could quickly fill in most answers. But sometimes there was a conflict between an honest answer and what I thought would make me attractive. Game theory would say it all came down to utility: the degree to which I was forthcoming depended on what I thought the people were looking for, as well as the probable cost to me of lying about myself.

As much as we would all love to be loved for the people we are, things are more complicated. A woman and I can find each other attractive, but at the same time, she finds my favorite internet video extremely

Paul Oyer is the Fred H. Merrill Professor of Economics at Stanford GSB, where Maureen McNichols is the Marriner S. Eccles Professor of Public and Private Management, and A. Michael Spence is the Philip H. Knight Professor and Dean, Emeritus. Oyer discusses the book at http://stnfd.biz/tjHXO

Photograph by Amy Harrity
unfunny, or feels she could never go out with anyone who checked a certain box regarding politics. If I revealed my video and views, that woman would never agree to meet me in the first place.

So I, like many others, hide these minutiae. I rationalize that even if a woman eventually finds these things out, she’ll accept these small negative traits as part of the whole package. And I justify my minor deception by arguing that I’m doing myself and the woman a favor. It’s cooperative game theory. Our interests are aligned, and I’ve simply removed some minor hurdles.

Research shows that minor lying is prevalent on dating sites, with a typical person claiming to be an inch taller, about 5 pounds lighter, and a year or two younger. OkCupid’s blog found that the average heights claimed by men on their profiles are suspiciously greater than that of American men, with an inexplicable number claiming to be exactly 6 feet tall. Similarly, they report that there are four times as many people making $100,000 per year as there should be. Finally, they found that people often posted dated pictures that likely made them look more attractive than they really were, reaching the very scientific finding that “hotter photos were much more likely to be outdated than normal ones.”

Unfortunately, profile inflators have a major impact on those of us who would like to tell the truth. Their lies lead all of us to discount claims as cheap talk. If everybody knows that many people who claim to be “Athletic and Toned” on Match.com are closer to the “A Few Extra Pounds” category, then to claim “A Few Extra Pounds” would mean one is actually significantly overweight. If you insist on always telling the truth, “profile inflation” will make everyone assume you are fatter, poorer and uglier than you are.

But I prominently displayed two features on my profile — my teenage children and the big, friendly dog that is not so familiar with the concepts of personal space and hygiene — that would be big turnoffs to many people. When it comes to children and dogs, my interests need to be perfectly aligned with those of potential partners. This is key to cheap talk models: The cooperative side suggests that the more genuinely aligned the interests of the provider and consumer of information, the more accurate the information will be. Lying — the noncooperative part of game theory — occurs far more often with baseline data we all share, like looks, income, and age, where everyone wants to seem as attractive as possible. But not everybody has teenagers or a hairy canine sidekick, which are non-negotiable.

**COMPANIES’ TALK IS CHEAP, TOO**

The logic that drives our online profiles also leads companies and their top managers to stretch the truth. One example was documented by Dartmouth economists Jonathan Zinman and Eric Zitzewitz, who found that ski resorts exaggerate their snowfall, especially during periods (generally weekends) when they have more to gain by doing so.

But just as internet daters will exaggerate less if they think they will get caught, ski resorts tell the truth more when skiers can catch their lies. The proliferation of smartphones has made it possible to question snow reports in real time. One SkiReport.com user post in 2009, for example, read, “Jackson Hole/ Teton Village DID NOT get 15 inches today. More like 0.” This immediate feedback had an effect: Zinman and Zitzewitz show that snow exaggeration shrank noticeably at a typical resort as iPhone reception reached that resort.

Corporate cheap talk is so common it extends all the way to top executives. Over the last couple of decades, there has been a rapid increase in firms’ use of stock and stock options to pay CEOs, justified by the need to align the interests of CEOs and their shareholders. But sophisticated shareholders are a lot like skeptical Internet daters. When the CEO makes a pronouncement about the prospects of the company, the stockholders know she might well be engaging in cheap talk and, as a result, they’re likely to discount the CEO’s statements. The CEO, knowing the market will discount what she says, really has no choice but to inflate expectations. Harvard economist Jeremy Stein analyzed the cheap talk of CEOs and how markets react, concluding that careful analysis “clearly exposes the fallacy inherent in a statement such as ‘since managers can’t systematically fool the market, they won’t bother trying.’”

Similarly, stock analysts have also been widely identified as potential providers of cheap talk. When a company goes public, analysts at investment banks evaluate the company’s prospects and make recommendations about the stock. By convention and SEC rules, the people who do these analyses are supposed to be isolated from people at the bank who handle the stock offering. However, the bank can gain overall when analysts inflate their estimates, because this makes the value of the bank’s other services (especially underwriting securities) greater.

Hsiou-wei Lin and Maureen McNichols studied in detail the recommendations of investment bank analysts at the time of new stock offerings. They compared the recommendations made by analysts at banks that underwrite a firm’s securities relative to recommendations made by analysts at independent banks. Lin and McNichols showed that independent analysts were considerably less generous with their forecasts than analysts whose bank had a relationship with a company. As we would expect, however, the market assumes this exaggeration. As a result, the stock market is less responsive to the recommendations made by an analyst whose bank has an underwriting relationship with the company he analyzes relative to those made by a truly independent analyst.

In addition to hanging on the words of analysts and CEOs, the stock market waits breathlessly for statements by one person in particular — the chairman
of the Federal Reserve. Remember how Alan Greenspan could move the market seemingly with the mere raise of an eyebrow and how, during the financial crisis, Ben Bernanke’s every word was parsed for meaning? Statements by the Fed chairman have the potential to be cheap talk. The Fed can always say he or she plans to take certain actions regarding interest rates just to try to calm the markets, or that things look better than they do. But the Fed is often somewhat cagier about its intentions, providing ranges — rather than exact numbers — for certain financial targets. Jeremy Stein (who has subsequently become a Federal Reserve member himself) analyzed the Fed’s incentives to reveal information. He found that if the Fed announced a precise target, such as that the inflation rate should be 2 percent, there might be situations in which it made this announcement when its true goal was 4 percent inflation. But then markets would back out the Fed’s true intentions and undermine its goals.

There is less scope for manipulation when announcing a target range, such as 1 percent to 3 percent inflation. So cheap talk is more believable when a range is provided than when someone pins himself down with an exact figure. Perhaps, then, I should update my online profile to say that I am between 45 and 55 years old and between 5 feet 8 inches and 6 feet 2 inches tall.

**SIGNALING YOU REALLY MEAN IT**

So, how can you overcome cheap talk? An online dating site in Korea tried to find out. The site, essentially the Korean equivalent of Match.com, ran a special event: Over a five-day proposal period, participants browsed online profiles as in standard online dating, but could show only up to 10 people that they were interested in a date. In addition, some participants could offer a virtual rose along with two of their date requests. The rose, in effect, told the recipient that he or she was one of the person’s top choices. Next, there was a four-day period during which people responded (essentially yes or no) to the proposals they received. The company then matched up the mutually interested pairs. Participants paid the equivalent of about $50 to take part, which is a little less than the one-month fee for this particular dating site.

Why did the site add the element of the virtual rose, and did it affect the outcomes of the dating arrangements? The answers are that a couple of economists talked them into it, and, yes, it had large effects. The idea of signaling something to someone you are trying to impress was modeled by Michael Spence in the early 1970s (and won a Nobel Prize in 2001), and these economists wanted to try it out.

In the promotion, some daters received two “I really mean it” signals that were completely credible. But note that what makes the signal work in this case is that it costs something. Participants who use the virtual rose have to give up something very important — the ability to show special interest in others. That’s what elevates talk from cheap to credible. Signals become meaningful only if they are costly.

When Michael Spence originally explained signaling, online dating had not yet been invented and he had to think of another venue for his idea. He imagined a world where colleges exist only so that prospective employers can figure out whom they want to hire. In the model, there are exactly two types of people — those who are talented and those who are innately unskilled. Talented individuals cannot simply tell people “I’m talented” because such cheap talk proves nothing.

But suppose that only the talented people will be able to graduate from college. They may learn nothing useful, but they show employers that they are talented and, as a result, they are eligible for higher-level jobs. In this model, education has solved our cheap talk problem. A potential employee puts his money where his mouth is by spending a lot of time and money on his education to prove (rather than just say) that he is talented.

As the Korean dating site results showed, the signaling idea applies quite nicely to the virtual rose. If a man or woman sent a standard proposal, the recipient accepted about 15 percent of the time. But about 18 percent of proposals that came with a virtual rose were accepted, which means sending a rose increased the chances of acceptance by about one-fifth.

Looking at who accepted which proposals provides more evidence for the credibility of virtual rose proposals. Tracking height, earnings, education, and other characteristics, the company that runs the dating site can determine which participants will be viewed as more or less desirable. The virtual roses do not matter that much for the most desirable people. That’s no great surprise — those people already expect to be among the most sought after.

But the effect of a virtual rose is largest on the middle desirability group. They are almost twice as likely to accept a proposal with a rose than one without. To them, being told in a credible manner that they really are particularly attractive is very meaningful. They have heard a lot of cheap talk in their lives, and they value someone backing it up. Or, put another way, the rose is a meaningful investment in the person because the sender had to give up other opportunities in order to send it.

The basic principles behind the Korean dating site’s virtual roses apply to other situations, too, such as early admission college applications and companies’ underpricing shares at an IPO to signal quality and make it easier to raise more cash in the future. These are effective ways to signal that you really mean what you say.

*Adapted from Everything I Ever Needed to Know About Economics I Learned From Online Dating (Harvard Business Review Press). Copyright 2014 Paul Oyer. All rights reserved.*
DECISIONS

Why Too Many Choices Can Make It Hard to Finish the Job

Research shows that what motivates people to achieve a goal changes along the journey.

BY LOUISE LEE

Have you ever been oh-so-close to reaching a goal but then fallen short or even thrown in the towel, only to become frustrated and discouraged? Perhaps the reason wasn’t a lack of willpower. Maybe you simply faced too many options for making that final push to the end.

When people are close to achieving something, whether it’s as challenging as losing weight or as simple as earning enough points to get a free cup of coffee, having more than one possible path leading to success can actually derail it, says Szu-chi Huang, an assistant professor of marketing at Stanford GSB. Yet when those same people are just starting out on a pursuit, having a number of ways to make progress is motivating and encourages them to keep going, Huang says. Her study, “All Roads Lead to Rome: The Impact of Multiple Attainment Means on Motivation,” was published in 2013 in the Journal of Personality and Social Psychology.

Huang, who joined Stanford GSB in 2013 after receiving her PhD from the University of Texas at Austin, researches consumer motivation, producing findings relevant to businesses and other organizations that persuade people to buy, donate, or otherwise participate. Much of her research examines how individuals attain goals. The big takeaway: What motivates people to achieve a goal is dynamic, changing over the course of the journey, and organizations should adjust the options they offer individuals to help them maintain their drive.

Early in any initiative, people wonder, “Can I achieve this goal at all?” and they seek reassurance that they can, says Huang, who coauthored the study with Ying Zhang of Peking University and the University of Texas at Austin, and teaches a class at Stanford GSB in consumer behavior. Offering people several paths to follow when they are taking their first steps makes the goal seem easier, encouraging them to go for it. But when people are close to the end of the pursuit, they ask, “How do I speed to the end?” Offering choices undermines people’s motivation at this stage because it makes answering that question harder, she says. “By providing multiple ways to attain the goal, we’re actually forcing people to stop and think and make a choice instead of giving them a straightforward path to rush to the end,” says Huang. “If you tell them, ‘Here are five things and you can do them all and you have to choose,’ we’re interrupting their momentum with choices. They now have to think and make a choice. Therefore, options are demotivating when people have reached the advanced stage of the pursuit.”

Huang’s latest findings follow her previous research showing similarly counterintuitive findings on the effect of flexibility on people’s likelihood of achieving goals. In another study, published in 2013 in the Journal of Consumer Research, Huang learned that customers who were required to make purchases in a strict order of six flavors in a yogurt shop’s loyalty program were more likely to complete the purchases of these flavors to earn a reward than those who were given the flexibility to choose their own order of purchases of the same six flavors of yogurt. “People fail to realize that relatively rigid structures can often simplify goal pursuit by removing the need to make choices, especially when people are already well into the process” she says.

In field research for her latest study, Huang gave coffee-shop customers different versions of invitations to join the café’s loyalty program. Some invitations gave customers a head start by providing them with six of the 12 stamps needed to earn a free coffee. Half of those in this advanced stage of purchases were told they could earn more stamps in several ways: buying coffee, tea, or any other drink. The rest of the advanced-stage customers were offered only one route to more stamps: by buying a drink.

Another set of invitations gave customers no stamps at all, placing them in an “initial” stage. Again, half the customers were given multiple ways to earn more stamps, and the rest a single method.

Among the customers starting with six stamps, those instructed only to buy...
a drink joined the program at a 40% rate, compared with 26.5% for those who were given multiple options. The results flipped among the early-stage customers. Those who were offered several options were more likely to sign up (37.5%) than those who were instructed only to buy a drink (21.6%). The findings suggest that people with significant progress under their belt were more motivated to join if given just the narrow path of “buying a drink.” And for those starting out with a blank slate, having more options gave them the motivation to sign up.

Many types of organizations typically give customers and donors multiple choices without adjusting them as their clients approach their goals, Huang notes. Companies running loyalty programs give members sitting on thousands of points many ways to keep earning more. The risk is not that they will never turn in their points, but that they will stop purchasing from the company altogether because their motivation to earn more points in the program is weakened by the overwhelming options. Nonprofits let patrons donate in various ways, and even late in a fundraising campaign as the organization approaches its goal. Instead, Huang says, organizations should consider narrowing the options once a goal is within reach.

Some organizations are reluctant to actually take away options or design separate programs for advanced-stage customers. Instead, the company or group can simply tailor its pitch, Huang says. A gym, for example, can market just one type of fitness program to a population that’s already relatively fit. Then, when the New Year rolls around and people make their resolutions to lose weight, the fitness club can play up a range of programs to make their customers’ goals seem easier.

Analyzing customer data is another way for organizations to determine what to offer to whom and when, adds Huang. A customer with only a few points might wonder if she can ever collect enough to earn her reward, so telling her about a few more ways to earn points would give her a nudge. But a customer with many points is likely to respond to a pitch that highlights simply one way to get to the reward.

“When customers are in the advanced stage, you’re dealing with a completely different animal,” Huang says, “so we can’t be static in our communications or in our design of loyalty programs and promotions. It’s a dynamic process.”

Now, Huang, who has a longtime interest in consumer marketing and was formerly an account director at the advertising agency JWT, is studying people’s motivations when they’re in the middle of a pursuit. “Many people have no problem starting a goal, but they often find themselves losing motivation in the middle of the journey,” she says. She is trying to determine the effectiveness of encouraging those people with “social information,” such as messages about the progress of others.

“Your friends are working out or using a product or donating money,” she says. “Our prediction is that social information could provide that extra push when you’re in that middle stage.”
JENNIFER AAKER
Seeking to understand the building blocks of a meaningful life
The Search for Meaning

What do success and satisfaction look like in 2014?

BY EMILY ESFAHANI SMITH AND JENNIFER L. AAKER

For Viktor Frankl, the Holocaust survivor who wrote the best-selling book *Man’s Search for Meaning*, the call to answer life’s ultimate question came early. When he was a high school student, one of his science teachers declared to the class, “Life is nothing more than a combustion process, a process of oxidation.” But Frankl would have none of it. “Sir, if this is so,” he cried, jumping out of his chair, “then what can be the meaning of life?”

The teenage Frankl made this statement nearly a hundred years ago — but he had more in common with today’s young people than we might assume.

Today’s young adults born after 1980, known as Generation Y or the millennial generation, are the most educated generation in American history and, like the baby boomers, one of the largest. Yet since the Great Recession of 2008, they have been having a hard time. They are facing one of the worst job markets in decades. They are in debt. Many of them are unemployed. The income gap between old and young Americans is widening.

To give you a sense of their lot, when you search “are millennials” in Google, the search options that come up include: “are millennials selfish,” “are millennials lazy,” and “are millennials narcissistic.”

Do we have a lost generation on our hands? In our classes, among our peers, and through our research, we are seeing that millennials are not so much a lost generation as a generation in flux.

Chastened by these tough economic times, today’s young adults have been forced to rethink success so that it’s less about material prosperity and more about something else.

And what is that something else? Many researchers believe that millennials are focusing more on happiness than prior generations, and that the younger ones in that age cohort are doing so even more.

Emily Esfahani Smith is an editor at *The New Criterion* and *Defining Ideas*, a Hoover Institution journal. Jennifer L. Aaker is the General Atlantic Professor of Marketing at Stanford GSB. This piece was originally published in the *New York Times* and is reprinted with permission. She discusses related research with Stanford President John Hennessy and other scholars at http://stnfd.biz/tjHZz

Photograph by Gabriela Hasbun
People who lead meaningful lives feel connected to others, to work, to a life purpose, and to the world itself.”

than the older ones who did not take the brunt of the recession. Rather than chasing the money, they appear to want a career that makes them happy — a job that combines the perks of Google with the flexibility of a startup. But a closer look at the data paints a slightly different picture. Millennials appear to be more interested in living lives defined by meaning than by what some would call happiness. They report being less focused on financial success than they are on making a difference. A 2011 report commissioned by the Career Advisory Board and conducted by Harris Interactive found that the No. 1 factor that young adults ages 21 to 31 wanted in a successful career was a sense of meaning. Though their managers, according to the study, continue to think that millennials are primarily motivated by money, nearly three-quarters of the young adults surveyed said that “meaningful work was among the three most important factors defining career success.”

Meaning, of course, is a mercurial concept. But it’s one that social scientists have made real progress understanding and measuring in recent years. Social psychologists define meaning as a cognitive and emotional assessment of the degree to which we feel our lives have purpose, value and impact. In our joint research, we are looking closely at what the building blocks of a meaningful life are. Although meaning is subjective — signifying different things to different people — a defining feature is connection to something bigger than the self. People who lead meaningful lives feel connected to others, to work, to a life purpose, and to the world itself. There is no one meaning of life, but rather, many sources of meaning that we all experience day to day, moment to moment, in the form of these connections.

It’s also important to understand what meaning is not. Having a sense of meaning is not the same as feeling happy. In a new longitudinal study done by one of us, Jennifer L. Aaker, with Roy F. Baumeister, Kathleen D. Vohs and Emily N. Garbinsky, 397 Americans were followed over a monthlong period and asked the degree to which they considered their lives to be meaningful and happy, as well as beliefs and values they held, and what type of choices they had made in their lives.

It turns out that people can reliably assess the extent to which their lives have meaning, much in the same way that people can assess their degree of life satisfaction or happiness. Although a meaningful life and a happy life overlap in certain ways, they are ultimately quite different. Those who reported having a meaningful life saw themselves as more other-oriented — by being, more specifically, a “giver.” People who said that doing things for others was important to them reported having more meaning in their lives.

This was in stark contrast to those who reported having a happy life. Happiness was associated with being more self-oriented — by being a “taker.” People felt happy in a superficial sense, when they got what they wanted, and not necessarily when they put others first, which can be stressful and requires sacrificing what you want for what others want. Having children, for instance, is associated with high meaning but lower happiness.

When individuals adopt what we call a meaning mindset — that is, they seek connections, give to others, and orient themselves to a larger purpose — clear benefits can result, including improved psychological well-being, more creativity, and enhanced work performance. Workers who find their jobs meaningful are more engaged and less likely to leave their current positions.

Further, this mindset affects what types of careers millennials search for. Today’s young adults are hoping to go into careers that make an enduring impact on others. Last spring, when the National Society of High School Scholars, a global honor society for high school students, asked more than 9,000 top students and recent graduates what they wanted to do with their lives, they found that these recession-era millennials favored careers in health care and government. Of the top 25 companies they wanted to pursue out of a list of more than 200, eight were in health care or at hospitals while six were in government or the military. St. Jude Children’s Research Hospital came in as the No. 1 place these millennials wanted to work. “The focus on helping others is what millennials are responding to,” James W. Lewis, the chief executive of the honor society, told Forbes.

Some studies have suggested that millennials are narcissistic and flaky in their professional and personal lives, and are more selfish than prior generations. But new data suggests that these negative trends are starting to reverse. In a study published this summer in the journal Social Psychological and Personality Science, the researchers Heejung Park, Jean M. Twenge and Patricia M. Greenfield looked at surveys that have, each year since the 1970s, tracked the attitudes of hundreds of thousands of 12th graders. Although concern for others had been decreasing among high school seniors and certain markers of materialism — like valuing expensive products such as cars — had been increasing for nearly four decades, these trends began to reverse after 2008. Whereas older millennials showed a concern for meaning, the younger millennials who came of age during the Great Recession started reporting more concern for others and less interest in material goods.

This data reflects a broader pattern. Between 1976 and 2010, high school seniors expressed more concern for others during times of economic hardship, and less concern for others during times of economic prosperity. During times of hardship, young people more frequently look outward to others and the world at large.

Of course, nobody likes living through tough economic times — and the millennials have been dealt a tough hand. But at the same time, there are certain benefits to economic deprivation. Millennials have been forced to reconsider what a successful life constitutes. By focusing on making a positive difference in the lives of others, rather than on more materialistic markers of success, they are setting themselves up for the meaningful life they yearn to have — the very thing that Frankl realized makes life worth living.
Is Art a Good Investment?

A group of researchers say you should buy paintings if you like looking at them, not for high returns.

BY ARTHUR KORTEWEG, ROMAN KRÄUSSL, AND PATRICK VERWIJMeren

“INVESTORS ARE EAGER TO BUY” Andy Warhol’s Dollar Sign, painted in 1981

Art has been emerging as a new asset class for the well-diversified portfolio. The reported returns are enough to catch anyone’s eye: The index of fine art sales, used by art advisors to sell art funds, shows an average annual return of 10% over the past four decades.

Investors are eager to buy. Many so-called passion investments have been gaining in popularity, and a handful of funds, such as The Fine Art Fund Group, led by CEO Philip Hoffman, are making it easier for investors of all income levels to put their money into fine art.

In short, investors are embracing art-as-an-asset-class as if it were a newly discovered van Gogh. But is it?

Research we completed recently and presented in August 2013 at the European Finance Association conference shows investors would be wise to be wary. The returns of fine art have been significantly overestimated, and the risk underestimated. Our research, based on the most complete auction database, BASI (Blouin Art Sales Index) shows the true annual return of art as an asset class over 1972 to 2010 was closer to 6.5%, instead of the 10% that the index shows. Moreover,
holding an art fund in your portfolio does not increase the chances that the portfolio will outperform.

The underlying cause of the overestimation of returns (and an accompanying underestimation of risk) is what is known as selection bias. People have suspected this bias in the indices used to report returns of some alternative asset classes for years, but our analysis is the first, we believe, to find a way to account for it.

The selection bias arises when returns are based on indices built on repeat sales of fairly illiquid assets that are not sold at random. Many of the returns based on those kinds of indices — including the S&P/Case-Shiller Home Price Indices — may be biased upward.

Not only are the returns of art lower than investors think, but also the risk is higher. Our analysis, of 20,538 paintings repeatedly sold between 1972 and 2010, found the Sharpe Ratio for art is 0.04, rather than the 0.24 that has been previously found. The Sharpe Ratio on U.S. equities over the same time period is 0.30. (The Sharpe Ratio is the risk-free rate of return — such as that of the 10-year U.S. Treasury bond — subtracted from the average rate of return for a portfolio or asset class, divided by the standard deviation of the return on the portfolio or class. It is the best tool for comparing asset classes on a risk-adjusted basis, and is often used by researchers to develop ideas for the best portfolios.)

The selection bias in art occurs for several reasons. Among them: Paintings that happen to be in high demand tend to go to auction more frequently and sell at higher prices. People also tend to sell the paintings that have increased in value the most since the time of purchase. A similar selection bias is probably at work in real estate, when, for instance, people sell houses after they have appreciated a lot in value.

Here’s an illustration of the way this works in the art market:

Imagine two paintings were purchased at an art dealer in 1972, each for $10,000. The career of one of the artists, Roy, took off, and the painting by him is sold in 2010 for $20,000. The other artist, Tony, turned out to be a flash in the pan. That painting was never sold; but say, for the sake of argument, that it retained its $10,000 value. As the artist faded from public view, it remained on the living room wall.

The art index — one of those repeat sales indices we mentioned before — uses the price appreciation for Roy’s painting to assign a value to Tony’s painting. According to that calculation, each painting is worth $20,000. The index therefore would report the return on the investor’s original $20,000 at 100% — $40,000, although in reality she realized only a 50% return, as she owns paintings worth $30,000, not $40,000.

If Roy’s painting were an average painting, using it to assign a value to paintings like Tony’s wouldn’t be a bad way to estimate returns. Our research shows, however, that the paintings that sell are far from average: They are those that appreciate the most in value. To impute a more accurate value to the paintings that never sell or sell less frequently, our methodology uses what we know about how rapidly the paintings that sell have appreciated, and how often they are sold.

Our model allows us to look at five different styles of painting, including Post-War and Contemporary, Impressionist and Modern, Old Masters, American, and 19th-Century European. In addition, we considered the returns of paintings by top-selling artists.

As an aside, we turned up some interesting facts about the art market. More than 2% of sales occur within two years after the artist died, confirming a generally held view in the art world that death sells. The average hammer price in the full sample was $61,939, with a long right tail of extremely expensive paintings. About 22% of sales took place at Christie’s, and 25% at Sotheby’s. Among the styles, the Impressionist and Modern style accounted for one-third of sales, followed by European 19th-century paintings with about one-quarter. About 16% of sales were of Post-War and Contemporary paintings, 12% were American paintings, and 5% were Old Masters.

The conclusion about art as an investment is clear: When we compared the investment returns and risk of all the styles of art to a portfolio of pure stocks, we found that art investments would not substantially improve the risk/return profile of a portfolio diversified among traditional asset classes, such as stocks and bonds.

Our analysis applies to art purchased via a fund. What about art that you buy on a one-off basis? In other words, what if you are a smart and tasteful collector of art who enjoys art but also buys with an eye to reselling it to make a good return? This is the equivalent of investing in a single stock or a tiny handful of them: You might be one of the few people with the skill or luck to pick winners, but chances are you are not. And if you own a painting, you bear the physical risks and costs, including insurance, damage, and theft or forgery, among others.

In short, buy paintings if you like looking at them. You can hope that your children will sell one or more of them later for a gain — but paintings are primarily aesthetic investments, not financial ones.\(^\text{A}\)
It’s one of the first questions John-Paul Ferguson hears from the first-year students in the strategy course he teaches each year at Stanford GSB: Is it better to have a career as a specialist, or take the path less traveled and develop a broad skill set from a range of experiences and areas?

Ferguson and his colleague Sharique Hasan had their assumptions as to the answer, and it was easy to romanticize one notion over another. But the truth is, “It’s a very hard thing to know,” Ferguson says. “For most folks, we can’t tell.” There are far too many variables.

Then the professors got excited. If they looked at the officers in the Indian Administrative Service (IAS) — the bureaucratic service of the government of India and one of the most prestigious careers in the country — there was a

John-Paul Ferguson and Sharique Hasan are assistant professors of organizational behavior at Stanford GSB.
identify individuals with comparable high ability, assigns those individuals careers that vary in the diversity of the constituent experiences, and evaluates those individuals for a common set of rewards,” the authors write in their recent report for Administrative Science Quarterly. Ferguson and Hasan not only were interested in the question of specialization versus broad experience, but also they were interested in whether its importance varied at different stages of the officers’ careers. What they found was that specialization helps at all stages.

Early in the officers’ careers, the authors conclude, specialization signals general ability. Specialized officers get promoted more, but not necessarily to do jobs in their specialization. Later, those who have specialized are rewarded for the skills they have acquired. To some extent, specialization produced a self-fulfilling prophecy, “wherein people who specialize acquire skills and thus have incentives to continue specializing.”

Ferguson mentions that, if a person moves around from career to career, “you can’t tell if they’re good at everything or bad at everything. For most people, it makes sense to specialize.” A diverse work history, the study concludes, hurts one’s chances of promotion.

That said, Ferguson also wants to emphasize that one of the benefits of a student’s period in business school is the chance to experiment with different career options. “That’s the time when it doesn’t hurt them,” he says. “This is the chance they have to get a little bit of experience. You want to sample as many different kinds while you’re in business school.”

Given these findings, Ferguson and Hasan are now interested in taking the next step in their research. Whereas the IAS enabled them to explore a pool of employees changing jobs under one employer, the authors would next like to examine this question of specialization among candidates who change both jobs and employers.

If a person moves around from career to career, says Ferguson, “you can’t tell if they’re good at everything or bad at everything.”

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Chip Conley, a 1984 graduate of Stanford GSB, is the founder of Joie de Vivre Hotels, California’s largest boutique hotel collection, which includes more than 30 properties, and the author of four books, including Emotional Equations: Simple Truths for Creating Happiness and Success and The Rebel Rules: Daring to Be Yourself in Business. Leading up to our interview, Conley said he had just returned from a weeklong silent meditation retreat. “All my answers will be in haiku,” he says.

In 10 words or fewer, what is the big idea behind your business?

Pose as boutique hotelier instead create identity refreshments

What is the best advice you’ve ever received? Oscar Wilde said, “Be yourself, everyone else is taken.” Most businesses benchmark themselves versus others and don’t imagine how they could be transformative and disruptive. About 10 years ago during the dot-com bust, I chose to use Maslow’s Hierarchy of Needs as an evolved business model for how JDV would operate. There was no evidence that anyone else had ever done that before. It was well suited for my personality. The idea of applying a psychology theory to a fundamental business model was sort of weird but it helped us triple in size when many others went out of business.
What was the most difficult lesson you have learned on the job? The most difficult time in my career was in 2008 and 2009 when it became extremely apparent to me that what had been a calling was now merely a job. It came at a time when I had to work 100 hours a week and had to act as if it was a calling. To be the CEO of a company means if you have 3,500 employees, as we did then, you are under the microscope. Your emotional state of being is magnified. I felt embarrassed and guilty that my state of mind — and my state of heart — for the company was not there when it needed to be. That is one reason I decided to sell a majority interest in my company to an investor who didn’t mind me stepping out of the business.

The lesson was that vulnerability can be very powerful. We say we want leaders to be authentic, and we want them to be strong. But being vulnerable and confident at the same time is a powerful combination.

What advice would you give other entrepreneurs on how to build a great business? I’m a huge believer in Abraham Maslow’s Hierarchy of Needs. What brings a sense of meaning for your stakeholders? What creates a transformative, self-actualized experience for your customers? How do you create pride of ownership for your investors? Remember, we are all human. If you are a good reader of emotions you will be successful wherever you are.

What values are important to you in business? You can see who’s most powerful in a society based on who has the tallest buildings. Two hundred years ago it was cathedrals. Fifty years ago it was a government building. Today, in most urban areas, the power rests with business and skyscrapers. Business is the most powerful influence in the world today. Fifty-four of the 100 most powerful entities in the world today are companies, not countries. That means it is that much more important that businesses take a conscious capitalist perspective to make a difference in the world. I’m a big believer in that on a global level. Businesses are finally asking, what is our ecological footprint? I also believe businesses need to look at their emotional fist print on their employees.

Our work is the most predominant use of our time. We spend more hours in our working life than our family life. Yet for many people their working life leaves an emotional fist print as if they’re getting punched. It creates anxiety, anger, and a sense of being abused. That can have a contagious effect on their family, friends, and everybody around them. How do we measure that? Fifty years ago we had no idea we could measure our ecological footprint. How can we start measuring and managing what’s most important in life?

What is the best business book you have read? Man’s Search for Meaning, by Viktor Frankl. It influenced my perspective on how to create meaning for employees and how to create culture in my organization.

“Passion Is a Prerequisite”

Andy Dunn is the founding CEO of Bonobos, a clothing company that launched online in 2007 with the introduction of a line of pants that promise a more flattering fit for men. The company has since expanded, and it now sells a full line of menswear through its e-commerce “guideshop” stores and online. Dunn graduated from Stanford GSB in 2007.

What was the most difficult lesson you have learned on the job? One, “it’s all your fault,” and two, “nobody cares.” “It’s all your fault” came from Mark Leslie. “Nobody cares” is from Ben Horowitz. As CEO, when things go well, your job is to pass the credit on to someone else. But when things go wrong, it’s your fault.

Our site crashed on Cyber Monday of 2011 and stayed down for two weeks. It was a traumatic time for our company. We have a great customer experience, but that obviously doesn’t matter if you can’t shop on our site. Our customer-service ninjas are all energetic, empathetic people, and they were working day and night with phone calls and monitoring and responding to Facebook and Twitter. Our new head of engineering had just joined. He had the weight of the world on his shoulders four weeks into his new job.

How did it come to this? It was my fault. We had an engineering team when we started, but we dismantled it and outsourced our technology for two years. We should not have completely outsourced it. After that it took me too long to hire our head of engineering. If I could go back in time, I would have retained some of that initial team and been less extremist about the transitions to create more continuity.

It’s easy as a leader to point fingers and blame people because you have power and authority. The reality is, you can’t blame employees, because if they aren’t doing well, it is your responsibility to move them out. Not only can you take responsibility, but you have to take responsibility. Everything the company does is in your purview. As the CEO, you are responsible for everyone who is there, and as founding CEO, you can’t even blame it on your predecessor. You can make all the excuses you want about how the world changed, etc., but if you fail, no one cares why it didn’t work. It can feel psychologically daunting to think of things this way — it’s all your fault and nobody cares why it didn’t work if it doesn’t work — but it’s also empowering. If you recognize you have agency in creating problems, then you can solve them, too.

What advice would you give other entrepreneurs on how to build a great business? Passion is a prerequisite. So is an unfair advantage. This world is intensely competitive. It’s not so much a question of whether you are a high-potential entrepreneur or whether your idea is great, but are you a high-potential entrepreneur for that great idea?

Before Bonobos, I worked on an idea for a personalized content magazine, similar to Instapaper. There was no reason I was the right person to build that business, and therefore I didn’t. People say great companies are built by great teams. I think that’s true. But I look for more than just great teams and great ideas; I like ideas that are uniquely authentic for that particular team.

What inspires you? Creating something people love. We have around 350,000 Facebook fans. I think of all the people who clicked our “like” button because they think our brand is cool. I’m inspired by that. I love this world that makes it possible for people to imagine something should exist and then conspires to enable them to create it.
What is your greatest achievement?
The most proud I’ve ever felt was when Bonobos was named by Crain’s as one of the top 50 places to work in New York. Building a company that customers love already puts you in the top decile, but building a company that employees love is the most elegant challenge in business. That’s the top 1%. So many people don’t like their jobs or their bosses.

It is especially meaningful to me coming from 2007, when I felt like I had no idea what I was doing or how to build an organization where humans could be motivated and engaged. I once thought “company human values” were things people wrote on posters with pictures of an eagle soaring in the sunrise. I always thought that was a cliché.

I have learned there is actually something to it. What helped me was when we had about 30 employees, I took stock of the 10 best people I had ever hired and made a list of the five attributes that I believe unified them and all the great people we have hired since. Those are self-awareness, judgment, positive energy, intellectual honesty and empathy. I worked those five values into how we hire, fire, promote, have hired since. Those are self-awareness, judgment, positive energy, intellectual honesty and empathy. I worked those five values into how we hire, fire, promote, made a list of the five attributes that I believe unified them and all the great people we have hired since. Those are self-awareness, judgment, positive energy, intellectual honesty and empathy. I worked those five values into how we hire, fire, promote, and retain people; we have gotten pretty empirical about it. That process of being thoughtful about how to create and protect our culture has been more important than I would ever have imagined when we began.

What businessperson do you most admire? Joel Peterson, the chairman of JetBlue. He approaches business from a really weird place: love. He talks about treating people with profound grace and dignity, even when things are difficult. I think he’s got a unique view of how to meld caring into capitalism; it personally inspires me.

That process of being thoughtful about how to create and protect our culture has been more important than I ever would have imagined.

“Visualize Massive Success from Day 1”

Beth Cross is the founder and CEO of Ariat International. Based in Union City, California, the company makes footwear and apparel for riders and the equestrian lifestyle. Cross grew up on a horse farm in Pennsylvania, and moved to California to attend Stanford GSB, graduating in the class of 1988. She went on to work at Bain and Company, where she worked with a team that developed strategy for athletic shoe makers Reebok and Avia. She cofounded Ariat in 1990 with Pam Parker, a fellow student from Stanford GSB. Their first product was a boot made for both English and western-style riding, which used materials and construction techniques common in athletic shoe manufacturing. More than 20 years after its founding, Ariat continues to push the boundaries of style and technology.

What was the most difficult lesson you have learned on the job? There are no do-overs. There is so much on-the-job training when you build a business. Every day, there seems to be at least one decision or discussion, large or small, that in hindsight I would love the opportunity to rethink or redo. I’m reminded of a decision I pushed for to make an inventory purchase of a new product that I thought would be terrific — but our buying team was very skeptical. I thought it was a great opportunity and convinced everyone we should go for it. Well, of course the product was a flop, and we were stuck with the inventory. My team teased me about it for a long time, and I learned to not interfere with the collective wisdom of an experienced team. You have to own your bad decisions, and in doing so you reinforce a culture that celebrates success and learns from failure.

What advice would you give other entrepreneurs on how to build a great business? The most critical thing is to visualize the company as a fully formed entity. We started out with an idea to revolutionize the equestrian footwear industry with performance technology. Once we pressure-tested the idea with consumers, we started to architect the company on paper. We asked ourselves, what will the company look like at $1 million in sales? At $50 million in sales? Study the leading companies in your industry and learn everything you can about their structure and go-to-market strategy. Sketch it out by function so you know what you will be competing against, and also have a sense of what relevant organization structures look like as you’re building your team.

Visualizing massive success from Day 1 helps you design the many small elements of what will eventually form the structure, strategy, and business model of a much larger company. Often the excitement of the startup — of product development and fund raising — distracts people from taking the long view about the company and the culture. Perhaps it can be compared to the difference between a wedding and a marriage — the excitement and flurry of activity during the start-up phase is the wedding, and the hard work of building a sustainable company is more like a marriage.

See a video of Conley at http://stnfd.biz/tj11u For the full-length versions of these interviews, and for more insights and ideas from entrepreneurs, go to http://stnfd.biz/hpWK1
JOBS

Is It Time to “Repot” Your Career?

How changing your trajectory can lead to greater innovation, success, and meaning in your work.

BY LOREN MOONEY

Fifty years ago, in his book Self-Renewal, John Gardner, the late former Cabinet secretary, Stanford professor, and founder of advocacy group Common Cause, first described a career strategy he referred to as “repotting” as a way to stay engaged and innovative. The idea is that a career reboot not only helps prevent managers from staying in one position too long, being lulled into complacency or leadership fatigue, but that it also pushes leaders to keep learning, to see new challenges with a fresh perspective and ultimately find meaningful work that leaves a lasting legacy.

The concept took root. A few years later, as dean of Stanford GSB, Ernie Arbuckle told a reporter: “Repotting, that’s how you get new bloom … you should have a plan of accomplishment and when that is achieved you should be willing to start off again.”

Arbuckle mentored Stanford GSB students and colleagues in the repotting philosophy, including his successor as dean, Arjay Miller, who said “it’s time to repot” when he resigned, and Donald E. Petersen, who told the New York Times when he stepped down as head of Ford Motor in 1989 that he was “struck with the philosophy of Ernie Arbuckle,” who said one should change occupations every 10 years. “Well, 10 years are up,” he said, “and it’s time to repot myself.”

Among Arbuckle’s many other mentees is Peter Hero, who worked at a Madison Avenue ad agency during the Mad Men era, shortly after earning his MBA at Stanford GSB in 1966. “It was creative and fun, but after a time I began to think, ‘What difference does this make?’” he says. One day, sitting in a very smoky room with five other grown men in ties, heatedly debating whether Sugar Bear would say that Sugar Crisp cereal gave him energy or made him stronger, Hero hit his limit. “I stood up and said, ‘I have to get out of here.’” He never went back to advertising. Instead, he repotted.

He moved to San Francisco and managed Spice Islands, a spice company, to significant growth; completed a graduate degree in art history; ran the Oregon Arts Commission; was appointed president of the Maine College of Art; and then returned to the Bay Area as CEO of the Silicon Valley Community Foundation, where he’s credited with transforming philanthropy from old-world, end-of-life giving to an active engagement with newly wealthy tech entrepreneurs. “The real benefit of repotting is that you’re designing your life instead of having someone else or society define it for you,” Hero says.

Here is some advice he gleaned from Arbuckle, as well as from his own experience:
1. KNOW WHEN IT’S TIME TO CHANGE.
Arbuckle suggested that a decade is long enough to dig into a project and see your vision through to completion, but not so long that you experience leadership fatigue. Having a timeline sets a horizon, but individual experiences can vary greatly, says Hero, who himself repotted after periods from less than five years to nearly 20. The most important thing is to periodically check in with yourself. “If you think, ‘Wow, this is too cool to leave — I still can have more of an impact,’” then you’re probably in the right place for now, he says. But if you feel like you’re on autopilot or aren’t fully invested in the future trajectory of your organization, it’s probably time to move on.

2. SEEK SUPPORT AND COMMIT TO A NEW DIRECTION.
Hero is careful to note that one can’t repot in isolation. He shared ideas and received encouragement from trusted advisers like Arbuckle. “And having a supportive partner is probably the most important key to repotting,” he says, particularly for larger transformations that involve relocating or income fluctuation.

Sometimes people don’t even know what they want to do next. It’s OK to begin repotting without fully realizing what the next pot will look like. “When you start off in a new direction in anything, you never really know the ultimate destination,” says Hero. The important thing is to commit to a new direction that interests you.

3. EMBRACE UNCERTAINTY AND TUNE OUT NOISE.
A big repotting may mean going back to school or starting at a lower level in a different field. Hero remembers one particular time, in art history graduate school in Massachusetts, thinking it had been nine years since he earned his MBA, his furniture was in storage, he’d moved his wife and young twins across the country, and he’d given up a large salary. “My wife is trying to find a job to support us, and I’m tending bar on the side, thinking, maybe selling spices wasn’t so bad — maybe they’ll take me back,” says Hero. Periods of self-doubt are common, especially when coupled with comments from friends and family questioning why you’d leave something stable for the unknown. “This is when you have to just steel yourself and trust that where you end up will ultimately be better than where you were,” says Hero.

4. NETWORK BROADLY AND TAP THOSE NETWORKS.
When Hero meets fellow Stanford alumni at events and retreats, he’s impressed with their robust attitude toward making professional connections. “They network like crazy, but it’s usually on behalf of a very narrow vision that they have,” he says. Over time, though, it’s helpful to build and maintain a broad base of contacts. Those people help you learn about different possibilities and what fields you might be interested in next. But they also may be helpful in future endeavors. Hero notes that his contacts in the business, government, arts and education fields served him well once he began working in philanthropy.

5. SYNTHESIZE YOUR EXPERIENCE TO MAKE A DIFFERENCE.
Some may believe that a more wandering career trajectory reveals a lack of focus, or that being a generalist means one doesn’t have deep expertise in anything. Hero sees the opposite as true. Rather than climbing a single corporate ladder with blinders on, he says, people with a repotting mindset stay engaged with the world around them, “keeping the radar on,” and bring a wealth of experience to the next challenge that may allow them to design innovative solutions.

For Hero, he brought his perspectives from marketing, business, and academic leadership and fundraising to rebrand charitable giving in Silicon Valley. He engaged entrepreneurs like eBay co-founder Jeff Skoll and software developer Steve Kirsch to establish and grow in their own charitable funds. In the process, he led the growth of the Silicon Valley Community Foundation from $9 million to more than $1.2 billion in assets, giving away a million dollars per week to community development and other charitable organizations. “I realized later on that the whole time I was exploring new paths, I was moving toward a job that for me was far more than a way to earn money,” says Hero. “And deciding that the values, impact, and the measurable consequences of what I did for work were critically important to me.”

Peter Hero, Donald Petersen, and Jeff Skoll received their Stanford MBAs in 1966, 1949, and 1995. Ernie Arbuckle was dean from 1958 to 1968; Arjay Miller was dean from 1969 to 1979. John Gardner received multiple degrees and awards from Stanford and was the Miriam and Peter Haas Centennial Professor in Public Service.
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—Research by Kristin Laurin, PAGE 36
GROWTH

How Do You Build a Culture of Excellence?

INTERVIEW CONDUCTED BY LOREN MOONEY

Eight years ago, over dinner and a bottle of wine, Hayagreeva “Huggy” Rao and Robert Sutton realized they needed better answers for the students of a Stanford management education program, Customer-Focused Innovation, they were running. The business executives appreciated what the pair had to say about reducing bureaucracy in an organization and enabling creativity, but invariably asked, “How do we scale this?” So, the longtime collaborators set out to find the answer. For more than seven years, they interviewed business leaders, reviewed research, and studied and conducted case studies about the mindset and strategies companies can use to spread excellence within an organization.

The result is their book, Scaling Up Excellence: Getting to More Without Settling for Less. We sat down with them to discuss key ideas from the book. Excerpts follow:
COLLABORATION
Robert Sutton, left, and Hayagreeva Rao
You begin your book by saying that companies that want to spread excellence have the “problem of more.” What exactly do you mean by that?

Rao: To put it simply, the problem of “more” is that organizations have pockets of goodness, and what you want is more of the goodness. At the same time that you’re adding good — by adding pockets or expanding them — you want to make sure you get rid of the bad. So, the problem of “more” is the problem — the challenge — of proliferating goodness.

Sutton: And the word “problem” is important because when things get bigger or you spread them further, not everything that happens is good. There’s this notion of growth and progress in America, that everything gets better as it gets bigger. But it’s a messy process. There will be things that annoy you. And the more you want to scale, probably, the more you have to suffer personally, which is not something I think leaders want to hear.

So how do leaders actually get through that?

Rao: You can have the illusion of drawing up nice little organizational charts and figuring out what growth looks like, but they’re all things on paper. In reality you need both story and structure. What I mean by story is lofty, inspirational messaging about excellence. But you also need the structure — the plumbing, if you will — the unglamorous parts of scaling. If you don’t have both of those, you’re never going to get anywhere.

Sutton: There’s always this challenge, as you get bigger, about structure. If people are telling the same story, you can have less bureaucracy, less micromanagement. But you do need some authority. And people like Twitter’s Chris Fry and Steve Greene, who grew Salesforce from 40 to 600 people, and venture capitalist Ben Horowitz — all of them make this argument that you should have a little less structure than you think you need. Then, wait for things to break a little bit as a sign that you should add just a little bit more. Greene called this light structure “running a little bit hot.” If you’re a little bit too heavy, it feels like you’re walking in muck. And, if you’re way too light, things fall apart. So, the ideal condition for scaling is that little things should be breaking all the time, but not the big things.

You make the point that if you’re adding new processes or people, naturally you will need to find ways to subtract or stop doing other things. How do you do that?

Rao: That’s what we refer to as “cognitive load.” If the load is too great, there’s a coordination circus. If I’ve got to run an idea by a bunch of people in order to do some single thing, I’m going to give up because it’s too much effort. When Bob and I teach executives, sometimes we say, “Hey, how about having a rule that says ‘If you want to have a meeting, kill an existing meeting.’” Now, that sounds quite obvious, but they say, “Really?” They haven’t even questioned the idea that meetings are to be added, that calendars are to be monopolized. It’s no wonder in a large company you feel like a victim.

Sutton: Now, that’s not true of all companies. Take Apple and Wal-Mart — those are two companies where they have a culture of small teams, so they have fewer meetings and people actually are doing the work most of the time. A lot of this depends on leadership and focus. The question is: “Where is your focus?”

Is there any common thread among organizations that are successful at spreading excellence?

Rao: They tend to “connect and cascade,” as we call it. You connect people so that you cascade the right behaviors throughout the organization. The real problem of scaling excellence is ignorance. What is an excellent organization? One that doesn’t repeat the same mistakes. And when do you repeat mistakes? When the connections inside organizations are weak or atrophied. If people aren’t connecting, your ignorance multiplies.

Sutton: And I think the important part for senior leaders is to find a way that people can share information in reasonably efficient ways. We talk about many ways in the book, but I really like the example of Salesforce under Steve Greene and Chris Fry — they had a policy where engineers were free to change jobs within the company. So, every four months they’d have an internal job fair, like a bazaar with booths, where people would walk around and learn about what other teams were working on. The policy had many advantages, but one was a higher collective understanding of how the piece of code they’re working on fit into the overall whole.

What are the implications of the size of your organization on a scaling effort — going from, say, two to 20 people versus 2,000 to 10,000?

Rao: Going from two to 20, you’re probably all still sitting in the same room. It’s just a bigger room.

Sutton: Then there’s a next level, 150 to 200, where you can no longer recognize all the names and faces, and up from there. The thing that companies that were successful at scaling all have in common — regardless of size — is that they were thinking of scaling as spreading a mindset, not a footprint. One person who demonstrates this well is John Lilly, the former CEO of Mozilla, who grew the company from 12 to about 500 people. John told us, “When we were 40 or 50 people, I was always changing my mind, but as the company got bigger I had to stifle myself.” He had to be sure he said the same thing over and over so that people wouldn’t get conflicting messages.
So how do you build the right mix of people for positive growth?

Rao: This is a big, big thing. Scaling doesn’t just require stars. It requires sherpas as well — the people who get you to the summit each day. Now, in order to make sure that the sherpas are taken care of, you should hire managers who are prone to feeling guilty. This idea is based on actual research done by a PhD student and Frank Flynn, a colleague here at Stanford.

I think about the U.S. Army general in the Korean War that we talk about in the book, Matthew Ridgway. He says, “The hard decisions are not the ones you make in the heat of battle.” A lot of people can do that. The hard part is actually sitting in a meeting and speaking your mind about a bad idea that’s going to put thousands of lives in jeopardy — and convincing the decision makers that it’s a stupid idea. The kinds of people who are going to do that are people who put the interests of others above their own.

Sutton: It’s interesting, the people who are really good at getting things done, they’re not just optimists. In fact, research shows they have high positive and high negative affect, which means they’re really optimistic and confident things will turn out in the end, but they’re really, really worried about every little detail and how it’s going to screw things up.

The two things I would add are that you should make sure to have as many women as possible, because the more men you have in a group, the dumber it gets, controlling for their IQ. There’s actually very good evidence of that. And, that you want people with a sense of accountability, who feel like “I own the place, and the place owns me.” They will push themselves and each other, and feel obligated to teach and to learn.

You mention that some mistakes are part of any scaling effort. But what are the kinds of mistakes that can cause failure?

Sutton: When we looked at cases where scaling failed, they seemed to have the trifecta of illusion, incompetence, and impatience; this idea of “We’re going to do it all at once, we don’t have time to slow down and do it right. But we’re so great, we can do it.” You can see it, for example, in what the Obama administration did with their healthcare rollout. Apparently, the guy in charge was some career bureaucrat who didn’t really understand how to do it but was a good politician, so he was competent at the wrong thing. But that creates a scenario where you’re turning other people incompetent.

So, how do you start a successful scaling effort?

Rao: One thing to keep in mind is that scaling doesn’t mean “Waiting for Godot” — you know, wait for the new boss, wait for a new opportunity, wait for new technology. In reality, you better do something. One good way to develop a plan is to do a postmortem: Take a team of people, and get half of them to imagine the plan has been put in motion and failed terribly. Then write a story of why that happened. And get the other half to imagine that it succeeded, and write a story of how that happened. The advantage of this is you get more of the unsaid said. You can actually make sure those small details that bite you don’t get in the way. Often, scaling doesn’t work because the mistakes you make early on aren’t caught until it’s too late.

Sutton: We talked to a top executive who turned around the largest company in Australia, who had the top 100 or so folks write him a 2-page memo about what they should do to turn around the organization. And he said, “I just talked to each person for an hour, and took the best ideas.” That said, we also found a single person who wanted to spread an idea, and so began by redecorating her cubicle and starting small, informal training sessions for colleagues. The bottom line is: In every case of successful scaling, you start where you are with what you have.

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NO REAL NEED?
Customers in line for the new iPhone in 2013.
CONSUMERS

You Want Customers? You Might Have to Change Your Approach.

The authors of a new book explain how a shift in consumer decision-making habits affect marketing.

BY ITAMAR SIMONSON AND EMANUEL ROSEN
In 2007, 10,000 people around the globe were asked about portable digital devices. It was part of a study conducted by the global media company Universal McCann. One of the hottest topics at the time was the first iPhone, which was announced but hadn’t yet been released. Once researchers tallied the results, they reached an interesting conclusion: Products like the iPhone are desired by consumers in countries such as Mexico or India, but not in affluent countries. The study stated: “There is no real need for a convergent product in the U.S., Germany, and Japan,” places where, one researcher later theorized, users would not be motivated to replace their existing digital cameras, cellphones, and MP3 players with one device that did everything.

There’s a growing feeling that something is not working with market research, where billions are spent every year but results are mixed at best. Some of the problems relate to the basic challenge of using research to predict what consumers will want (especially with respect to products that are radically different). But marketers face one additional key problem: Study participants typically indicate preferences without first checking other information sources — yet this is very different from the way people shop for many products today.

In the Universal McCann study, for example, people were asked how much they agree with the statement, “I like the idea of having one portable device to fulfill all my needs.” Indeed, there was a significant difference between the percentage of people who completely agreed with this statement in Mexico (79 percent) and in the United States (31 percent). So, in theory, people in the United States were much less excited about a phone that’s also a camera and a music player.

But it was a different story when people got closer to making a decision. They heard about the iPhone in the media, where it was declared a revolutionary device, and read blogs and reviews from real users. As iPhones started rolling into the marketplace, the idea of “having one portable device to fulfill all my needs” was replaced by actual reports from users. It’s easy to blame the market research firm for this, but this is not our point. We are trying to explain the inherent difficulties in assessing consumers’ reaction in this new era. First, more decisions today are impacted by what we call O sources of information — “Other” information sources, such as user reviews, friend and expert opinions, price comparison tools, and emerging technologies or sources — whereas market research measures P sources — “Prior” preferences, beliefs and experiences. But let’s go beyond that: As we discussed, consumers have limited insight into their real preferences. This is especially true with respect to products that are radically different. Universal McCann correctly reported what it found. What market researchers often underestimate, though, is the degree to which consumers have difficulty imagining or anticipating a new and very different reality. What makes the task of a market research firm even trickier is that just as consumers’ expectations may be wrong (as was the case with the iPhone), there are many cases where industry expectations about what consumers will buy are wrong.

Not to mention that O-sourced information is often much more dynamic, so even if a researcher were trying to somehow account for the present effect of O, that may become largely irrelevant and out of date by the time actual purchase decisions are made. Also, beyond the unpredictability of O’s influence, decisions made under the influence of O are much “noisier” than hypothetical decisions made by an individual consumer on her own when completing a questionnaire. While a limited set of studied features might be reasonably representative of the factors that an individual consumer will consider, a larger set of reviewers and information sources introduces various unpredictable factors (for example, “coolness,” popularity, highlighting of seemingly insignificant features) that will be difficult to capture in traditional measurement.

The noise and hard-to-anticipate information sources similarly limit the usefulness of other common research techniques such as brand equity measures or pricing studies. While predicting individual decisions that are made in isolation is not a simple task, predicting the joint evaluations of many consumers and the influences of other information sources is likely to be an order of magnitude more difficult.

Indeed, trying to predict where things are going has become more challenging. While traditional consumer research can still tell a marketer if their next toothpaste...
will do better with purple or black stripes, it is not of great help for more radical, unfamiliar changes. There is no effective way to use market research to predict consumer reaction to major changes. When assessing new concepts, consumers tend to be locked into what they are used to and believe today, which makes them less receptive to very different concepts and more receptive to small improvements over the current state. Similarly, experts who try to predict the success or failure of radically new products are unlikely to be much more accurate than consumers. (Among other things, experts have famously made bad predictions regarding the success of the telephone, the internet, and television.) What marketers are often left with is trying to quickly figure out where things are going and what consumers and competitors appear to follow. And then try to offer a better solution. Instead of predicting vague consumer preferences (which may change anyway when it’s time to buy), these days one of the few things a marketer can do is follow O and play along to make the best of a situation they no longer control.

The current environment does not mean the end of market research, just a shift in focus with some silver linings. We expect that future market research will focus more on tracking and responding to consumers’ decisions as they occur, and less on long-term preference forecasting. Instead of measuring individual consumers’ preferences, expectations, satisfaction, and loyalty, marketers should systematically track the readily available public information on review sites, user forums, and other social media. △


Itamar Simonson is the Sebastian S. Kresge Professor of Marketing at Stanford GSB. Emanuel Rosen, the author of The Anatomy of Buzz, was previously vice president of marketing at Niles Software. They discuss the book at http://stnfd.biz/tjHW1

“Stanford University’s Economic Impact via Innovation and Entrepreneurship,” a 2012 study by Stanford professors Charles Eesley and William F. Miller
More than 90% of Americans say they believe in God, or some approximation thereof, and psychologist Kristin Laurin has been trying to understand how those beliefs influence our behavior. Over the last several years, Laurin, now an assistant professor of organizational behavior at Stanford GSB, and a handful of psychologists at universities in Canada and the U.S. have conducted studies in an effort to understand the connection between divine belief and earthly behavior. Does that belief affect how we behave, for example, at work or in school?

In several studies published in the *Journal of Personality and Social Psychology*, Laurin and her colleagues looked at whether awareness of God affects how we pursue our goals. In some cases, they
as God, can have as great an impact on behavior as the actual presence of a witness.

By decoupling active goal pursuit from temptation resistance in their experiments, the researchers hoped to tease apart why reminders of God might both help and hinder goal pursuit. They conducted six experiments that exposed college students to the idea of God and then assessed their performance on various measures of self-regulation.

In one experiment, 37 engineering students participated in what was called an “engineering skills” study. The students first completed a warm-up task that involved creating sentences using four words from a set of five. Some saw the word God or words related to the concept of God, such as divine, sacred, or prophet. Others saw words that were considered positive, such as sun, flowers, or puppy, or neutral words. After that, participants were asked to form as many words as they could from six specific letters and were told performance on the test was strongly linked to future success in engineering. Students who had been primed first with the God-related words formed only two-thirds as many words from the same letters as the students who were primed first with positive or neutral words. As Laurin and her colleagues predicted, the God-primed students didn’t appear to work as hard at achieving the goal.

To test whether reminding people of God could increase resistance to temptation, however, the researchers recruited 23 undergraduate students with self-professed healthy eating goals to participate in another study. The students first were asked to evaluate a student club website, where they read an excerpt from the website, where they read an excerpt from a speech either about the declassification of Pluto as a planet or a speech about God, with pronouncements showing omniscience such as: “God is the beginning and end of all things, all things else are from Him, and by Him, and in Him.”

The students were then given a bowl of 35 bite-sized cookies and asked to evaluate their taste by eating one or more. Left alone in a room for 10 minutes, individuals who had first read the speech about God ate, on average, fewer than three cookies while those who had read a speech about Pluto averaged nearly eight cookies each.

To Laurin, the results from the first study indicate that people who think of God as powerful and intervening in their lives might be less likely to proactively pursue their goals because “there’s no sense in expending valuable energy proactively pursuing a goal if you believe that God will decide what happens to you,” she says. But if, instead, you are thinking of God as omniscient and watchful, as opposed to all-powerful, your conception of God might help you resist temptations that derail your pursuit of a goal. “That would mean there’s always someone watching you, and we know when people are being watched they don’t like to do ‘bad things.’” In the case of a health improvement goal, “that bad thing could be binging on chips and ice cream,” she says.

All six studies examined how exposure to God influences behavior when it comes to pursuing goals. Although the results were largely as Laurin and her colleagues predicted, one aspect surprised them, she says. “We found it doesn’t even matter what someone believes, or even whether they are an atheist. Everyone knows what the idea of God means, so even just thinking of it, even if you don’t believe in it, that affects behavior.”

References to God appear to affect people regardless of their religiosity, because the concept of God is so culturally ingrained. As a result, references to God could have far-reaching societal consequences, Laurin says, especially since self-regulation underlies much of health, happiness, and human productivity.

Kristin Laurin is an assistant professor of organizational behavior at Stanford GSB. She received her PhD from the University of Waterloo in 2012.
"We live in a world that emphasizes realistic expectations and clear successes. Quixote had neither," narrates James March in his 2003 film, *Passion and Discipline: Don Quixote’s Lessons for Leadership*. “But through failure after failure, he persists in his vision and his commitment. He persists because he knows who he is.”

The film, inspired by March’s landmark *Organizational Leadership* course, which he taught at Stanford GSB from 1980 to 1994, weaves together examples from the 17th-century Spanish novel, interviews with Stanford alumni leaders, and vignettes from news broadcasts and movies to illustrate that pursuing a dream with all one’s convictions can be crazy, but can also lead to joy and even success. We recently asked March about what leaders can learn from *Don Quixote* and other literature.

**Of all the characters in literature, why did you select Don Quixote as the subject of your film about leadership?**

As I say in the film, Quixote is hardly a good model for leadership, but he provides a basis for thinking about what justifies great action. Why do we do what we do? Our standard answer is that we do what we do because we expect it to lead to good consequences. Quixote reminds us that there is another possible answer: We do what we do because it fulfills our identity, our sense of self. Identity-based actions protect us from the discouragement of disappointing feedback. Of course, the cost is that it also slows learning. Both types of actions are essential elements of human sensibility, but our usual conversations — particularly in business settings and schools — tend to forget the second.

James March is the Jack Steele Parker Professor of International Management, Emeritus, at Stanford GSB, where he has been on faculty since 1970.

**INTERVIEW CONDUCTED BY LOREN MOONEY**
There's a point made in the film that cynical. A decision-maker becomes discouraged when pursuing consequences is that great of expected consequences. A major problem with actions taken to maximize the utility the society associate virtue, or intelligence, with actions taken to maximize the utility of expected consequences. A major problem with pursuing consequences is that great expectations are rarely realized, and a decision-maker becomes discouraged and cynical.

In your writing, you have called our society "consequentialist." What do you mean by this, and what are the limitations of this kind of society? Different writers mean somewhat different things when they talk about consequentialism, but I mean simply an emphasis on expected consequences as a justification for action. When I say our society is consequentialist, I mean simply that the dominant norms in the society associate virtue, or intelligence, with actions taken to maximize the utility of expected consequences. A major problem with pursuing consequences is that great expectations are rarely realized, and a decision-maker becomes discouraged and cynical.

There's a point made in the film that most visions are misguided and are more likely to lead to spectacular failure than success. How does one recognize the rare vision with the potential for success? The two most important things to know about innovation are: (a) that most new ideas are bad ones, and (b) that separating the rare good ideas from the many bad ones among new ideas is ordinarily impossible. A good deal of effort has been expended in trying to develop some reasonable procedures for the early identification of good ideas. Most such procedures involve applying existing knowledge to identify errors, but what distinguishes truly innovative new ideas is precisely that they violate some aspects of existing knowledge, so are particularly vulnerable to early rejection. Although numerous people have proposed ways of dealing with this dilemma, I think it is fair to say that no one has demonstrated a procedure with any significant reliability.

As Marc Andreessen, one of the founders of Netscape, said, "Fundamental change comes out of left field. It has to be an idea that’s viewed as crazy at the time. If any idea looks like a good idea, there are lots of big companies out there like Microsoft that would already be doing it."

Is there an effective way to orchestrate innovation within an organization? Or does it depend on the arrival of a visionary making identity-based decisions? I'm not sure those are the only two alternatives. Not so long ago, I wrote a little book, The Ambiguities of Experience, that has a chapter on novelty and a section on "The Engineering of Novelty." The section is short, and the ideas are not particularly profound. One well-known strategy is to limit the "bet size" of investments in novelty by differentiating among wild ideas by small-scale experiments and then increasing investments in successful projects. Another strategy is to partition an organization into diverse subgroups. Parochialism among units encourages homogenization within them but diversity among them. The diversity is useful, however, only if the boundaries between groups are at least partially permeable, and it is difficult to specify the optimum balance of parochialism and cross-group contact. Identity-based visionaries are useful in stimulating new ideas and persistence in them, but they are not always as useful in encouraging cross-group contact. And, of course, visionaries are more likely to be crazies than geniuses.

You used to include in syllabi for leadership and literature courses caveats such as, "No claims of practicality or relevance are made or implied." What did you hope students would get out of your classes? The cliché is, of course, that I hoped the course would make them think, not answer questions but shape how they think about them. I suppose every teacher hopes for that, but most of the time we try to sneak thought-provoking ideas into some exercise that will strike the students as relevant in a practical way. My strategy, to some extent, was to challenge the instinct for relevance that gave students an illusion of practicality in their studies.

If a leader wants to be inspired through literature to think broadly about leadership, management, and power what in addition to Don Quixote would you put on the reading list, and why? I used to tell students that, properly approached, any work of great literature would do the job. I think that is true, but it is particularly true of the works of people such as Ibsen, Dostoyevsky and Henry James.

The point is not that there are role models, but that the novels and plays wrestle with fundamental questions relevant to leadership. For example, I have written about how Ibsen can be used to examine the way in which individuals reconcile the claims of their ideals with the reality of their lives, in particular the way in which high ideals suborn lies. The issue is particularly salient to The Wild Duck, but it appears in many of Ibsen's plays.

What are your interests currently? I am still trying to figure out the contradictory lessons of Quixote and occasionally giving lectures to Chinese executives in which I encourage them to look at classical Chinese literature, which, as I read it, urges a ruler to be deeply committed to the pursuit of a project and, at the same time, profoundly skeptical of the commitment and the project.

“Quixote is hardly a good model for leadership, but he provides a basis for thinking about what justifies great action.”
DON’T BE FOOLED BY THE WORD ANGEL.

These investors aren’t donating to charity. Most are disciplined investors; they are often successful entrepreneurs and high-tech professionals in their own right. But it’s important for entrepreneurs to understand an angel’s personal priorities. Angels may be willing to take slightly more risk with startups in a field of particular interest to them, or with those for which the angel can provide specialized expertise and guidance.

DEALS

How Do You Get Financing for Your Startup?

A finance professor gives seven basic insights to better understand angel investors.

BY ILYA STREBULAEV

It’s often assumed that the archetypal venture capital firms around Silicon Valley and Boston — the likes of Kleiner Perkins and Sequoia Capital — supply almost all the initial financing for high-growth startups.

If that was ever true, it’s becoming less so by the day. Largely unnoticed, angel investors have been muscling in on traditional venture firms. Thanks in part to the plunging cost of technology, angels have enjoyed a growing competitive advantage in funding very early stage companies. That’s because the capital required for a tech startup today is often a fraction of what it was 10 or 15 years ago. Using open-source software and cloud computing, for example, a startup that might have once required $5 million to get off the ground can often do it for $500,000 today.

This plays to the strength of angels, who prefer smaller deals and are typically quicker to make decisions than venture firms backed by institutional investors. In fact, angel investors — usually individuals or small groups of wealthy investors who use their own money — now suppy the overwhelming majority of high-growth startups with their first money after the founders have tapped family and friends.

According to Jeffrey Sohl at the University of New Hampshire, angels invested $22.5 billion in more than 60,000 high-growth U.S. ventures in 2011. Traditional venture capital firms invested slightly more total money, about $28.4 billion, but they poured it into just 3,673 deals — a tiny fraction of the number of companies financed by angels.

This offers major new opportunities for entrepreneurs seeking seed capital. But it’s easy to misunderstand how angel investors work and what they want. Having studied and watched many angels firsthand, I offer seven basic insights:

UNDERSTAND ANGEL NETWORKS.

Angel investing is a personal business, and angels rely heavily on personal networks of like-minded investors. Many angels work in groups, jointly vetting proposals and putting high value on others’ opinions. Even when angel investors work separately, they share ideas and listen closely to one another. The most important key to raising money from an angel is often the good word from another angel.
LOOK CLOSE TO HOME.
Most angel investments are within 50 miles of the investor, and angel networks are often in geographic clusters. There’s no mystery here: Early-stage investors need to stay close to the people they are betting on. Silicon Valley and Boston have particularly big clusters, but many other cities have them, as well. If you don’t live near an angel cluster, consider moving.

SHARED ROOTS ARE IMPORTANT.
Maxim Faldin and Kamil Kurmakayev, two Russian-born Stanford graduates, had no luck raising seed money from traditional VCs for Wikimart, an eBay-like site in Russia. Then they targeted their search for investors with natural affinities: those with Russian roots or international experience, and people with experience in e-commerce. That led them to Fabrice Grinda and Jose Marin — professional angels with extensive expertise in e-commerce and global markets. Today, Wikimart is thriving.

ANGELS WILL HUNT FOR THE FATAL FLAW IN YOUR PLAN.
You may have a perfectly reasonable plan for a $10 million business. But angel investors are looking for companies that can ramp up to $50 million or $100 million in revenues. Likewise, they aren’t looking for incremental improvements over the competition. They want “disruptive” ideas that will upend existing business models. If your idea is disruptive, however, can you hold on to it? Can copycats and incumbents jump in as soon as you’ve shown the way?

YOUR TEAM MAY BE MORE IMPORTANT THAN YOUR CONCEPT — OR EVEN YOU.
Angel investors want people who can execute the plan. They will place heavy weight on not only your track record, but also your management team. Beyond looking at résumés, angel investors want evidence that the team can work together when the going gets tough.

ANGELS ARE EVOLVING FAST.
The success of traditional angels has spurred a new breed of “superangels” or “micro VCs.” Like traditional angel groups, these funds invest in seed-stage companies but are structured more like traditional VC firms that raise capital from outside investors.

We also hear a lot these days about accelerators, such as Y Combinator and 500 Startups. Their approach also seems to work well; for example, Y Combinator has graduated approximately 430 companies, including top-notch startups like Dropbox. Saeed Amidi, founder of accelerator Plug and Play, is now setting up similar structures around the world.

This may just be the start. The Jumpstart Our Business Startups Act — or JOBS Act — now allows small companies to market directly to individual investors through crowdsourcing over the Internet. This one regulatory change could be the biggest change yet for early-stage investing. One thing is for sure: Brand-name venture capital firms are not the only game in town.

Ilya A. Strebulaev is an associate professor of finance at Stanford GSB.
The former CEO of Young & Rubicam explains why searching for virtue is a winning business strategy.

BY LOREN MOONEY

For nearly his entire life, Peter Georgescu has been obsessed with the struggle of good versus evil in human nature. “Why is it possible for people, most of whom can also be loving and compassionate, to do terrible things?” wonders Georgescu, author of *The Constant Choice: An Everyday Journey from Evil Toward Good* and chairman emeritus of Young & Rubicam.

His curious preoccupation stems from personal experience: As a young boy in World War II-era Romania, Georgescu was subjected to human evil firsthand. His father, who managed the largest oil-producing region of Romania for Esso (which later became Exxon), and mother were in New York at Esso headquarters when the Soviets dropped the Iron Curtain of communism on Eastern Europe. Georgescu’s parents were forced to stay in New York. His grandfather, a former Romanian governor, was arrested and murdered in prison. “Not long after his arrest, my brother and I were placed into hard labor,” says Georgescu, who was nine years old at the time. “For years I spent 10 to 12 hours a day, six days per week, cleaning sewers, as I was small enough to fit into the pipes.” Later, he was forced to do high-voltage electrical work. “I suffered frequent incidents of painful shocks that knocked me to the ground — that was my education! We were offered no schooling whatsoever.”

Peter Georgescu, the chairman emeritus of Young & Rubicam, received his MBA from Stanford GSB in 1963.
FREEDOM
Peter Georgescu (right) and his brother, Costa, reunite with their parents, mother Lygia and father Valeriu, in 1954 in New York City after six years of forced labor in communist Romania.
After six years, Georgescu and his brother were released with intervention from President Eisenhower and a congresswoman, Frances Payne Bolton, and came to America to be reunited with their parents. "My gratitude and respect for this country, with its bountiful freedoms, which are still the envy of the world, will never diminish," he says. Yet, he says, as he worked his way through the business world, again he saw forms of evil — not the blatant human cruelty he'd experienced, but a force more subtle and insidious. It was a “me first” attitude that all too often went beyond merely wanting to succeed above the competition, and became narcissistic greed and cheating, all in the name of “maximizing shareholder value.”

In the past few decades, he says, the corporate vision has increasingly narrowed to focus on short-term gains sought by short-term shareholders and financial institutions. “The other stakeholders — customers, employees, the surrounding community, the environment — are now largely excluded from the corporate, decision-making table,” says Georgescu. But there is another, better way to strive to do good in business, just as people do in their personal lives. “Enlightened self-interest,” he calls it. “We have a choice to make every day, countless times a day, and we can choose between doing good, living by a higher set of values, or doing something that harms other people. Good intentions are simply not good enough. We must be responsible for the ultimate results of our actions.”

In addition to being the right thing to do, making decisions this way is good for long-term growth and success, he says. “The new winning companies — the Googles, the Apples, the Starbucks, and the Patagonias — are demonstrating how practicing values is a winning strategy in business, not merely because it’s the right thing to do but because it’s the only way that works now.”

**GOOD FOR EMPLOYEES**

There’s an old business management book called *The Customer Comes Second*, which runs counter to the popular guiding principle of putting the customer first. “But it makes sense,” says Georgescu. “How can the employees treat customers with respect when the organization doesn’t treat them with respect?” Beyond basic decency and improved customer service, providing a supportive, positive environment for employees fosters creativity and innovation. By having a greater sense of fairness in the workplace, Georgescu says, companies can achieve “sustainable creativity,” an ethos practically required to achieve the level of innovation necessary to compete in today’s economy.

**GOOD FOR THE CORPORATION**

“The average tenure of Fortune 500 CEOs is just over three years,” says Georgescu. With the shortened horizon, “investment in brand building is diminished in favor of short-term tactics to drive up sales and profits.” More companies need to be playing the long game in order to thrive into the future. Georgescu recalls a point in the mid-’90s, when he was CEO of Young & Rubicam, and management decided
to take the company public. Senior managers held most of the company shares at the time. “The concern was that, assuming a successful IPO, a good many of these executives would retire and the next generation of management would not be enfranchised in the ongoing enterprise,” he says. With the future of the company in mind, the senior executives redistributed some 30% of their shares to the next generation of managers. The move helped with talent retention, as well as cemented a culture of sharing incremental results more broadly and deeply in the company, and, in the end, “proved to serve the enterprise, and all its stakeholders, including shareholders, very well.”

GOOD FOR THE COMMUNITY
The political and economic conditions of the past several years have caused a “huge socioeconomic chasm that threatens the U.S. and other developed nations,” says Georgescu. Several economists have predicted dire consequences for our entire way of life if we don’t address the issue of income inequality. While political action will be a necessary part of the solution, business leaders have an obligation to help, too, says Georgescu, by wisely balancing the interests of all corporate stakeholders. There is a better path to long-term success, he says. And it begins with the choices made today. Δ
The Quotable
Mary Barra

The new head of General Motors discusses cars, leadership, and the best advice she ever received.

EDITED BY LOREN MOONEY
On her management style: “Collaborative. When we have to make tough decisions, giving direction and setting the strategies for the products of General Motors, there should be constructive tension. We should have vigorous debates. ... At the end of the day, when the decision has to be made, if we don’t have complete unanimity, I have no qualms about making it. But I want that tension in a constructive way to make sure we evaluate things from every angle. I am pretty hands-on as well. I will call a chief engineer when I am driving a vehicle.” Interview with the Los Angeles Times, December 11, 2013

On management: “If we win the hearts and minds of employees, we’re going to have better business success.” Fortune video conversation, October 16, 2013

On the best advice she ever received: “I'm reminded of a plant manager who asked his lead engineer to explain her hiring process. She said, ‘Well, we fill a bathtub with water and we offer the applicant a teaspoon, a teacup, or a bucket. Then we ask him or her to empty the tub.’ ‘I get it,’ the manager said. ‘A go-getter would use the bucket because it’s faster.’ ‘No,’ the engineer said, ‘a go-getter will pull the drain plug.’” Inforum, women’s professional development organization interview, March 14, 2012

On taking GM’s corporate dress code from 10 pages to “dress appropriately” as head of HR: “It really became a window into the change that we needed to make at General Motors, because I’d have managers sending me emails or calling me saying, ‘I need you to write it down.’ So I would take them through and say, ‘OK, what do you do?’ You know, ‘I run a group of 20 people. I’m responsible for $10 million of budget, etc.’ And I said, ‘I can trust you with $10 million of budget and supervising 20 people, but I can’t trust you to dress appropriately, to figure that out?’ It was kind of a step in empowering. Because we found that sometimes people hid behind the rules and didn’t like them, but didn’t necessarily step up. So this really encouraged people to step up.” Fortune video conversation

On the auto bailout and transition: “The biggest lesson I learned, and I take it to everything I tackle now, large or small, inside of work and outside: If you have a problem, you’ve got to solve it. Because that problem is going to get bigger in six months. It could get bigger in two years. But it’s not going to get smaller with time.” Inforum, women’s professional development organization interview, March 14, 2012

On a woman in leadership: “I think there are more women in more senior roles than in 1980 when I started. But from my career perspective, I don’t go into a room and take count. I want to be recognized for my contribution and for what I do. Yeah, there were probably times it was to my benefit, and there were probably times when it was not to my benefit. But that is true for everyone. There are always things that potentially impact how you are received. And I just don’t focus on it. I don’t focus on what you can’t control.” New York Times, December 10, 2013

On mentorship: “You get to a new position, you work really hard and you earn people who are willing to support you, because they see how hard you’re working and they’re willing to extend a bit of their personal capital to say, ‘Yes, I know so-and-so is going to do a great job in this new role.’” Inforum interview

On being results-oriented: “I’m reminded of a plant manager who asked his lead engineer to explain her hiring process. She said, ‘Well, we fill a bathtub with water and we offer the applicant a teaspoon, a teacup, or a bucket. Then we ask him or her to empty the tub.’ ‘I get it,’ the manager said. ‘A go-getter would use the bucket because it’s faster.’ ‘No,’ the engineer said, ‘a go-getter will pull the drain plug.’” Kettering University commencement address, 2013

On replacing traditional business executives with leaders who have technical expertise: “We went back to really empowering the individual who knows every aspect of that vehicle and knows every trade-off they’ve made to get a great vehicle on the road. ... So every vehicle has its own chief engineer, and it’s single-point accountability. ... I have seen a real transformation in just the short few months since we’ve made that change, in the sense of ownership and the commitment. Before we had some confusion as to who was really accountable and who was making the call. There’s no confusion now.” Autoline This Week interview, October 12, 2012

On failure: “As Charles Kettering said... ‘The only time you don’t fail is the last time you try something and it actually works.’” Kettering University commencement address

On change: “Not everything needs changing. Some things need protecting. And that can be just as important, challenging and rewarding as changing the world.” Kettering University commencement address

On fostering a culture of work/life balance: “Everybody does a better job when they’re able to balance. It might mean on a certain day I’ve got to leave a little early because I want to see my daughter play volleyball. That doesn’t mean that after we go home, and after we’ve eaten dinner and the kids go to bed, I’m not going to take out the computer and catch up on what I missed. We need to provide that environment. In a world now with our BlackBerries and our smartphones, we’re always on. We need to find the opportunity not to do everything, but to do the important things.” Inforum interview

On strategic innovation in a large company: “If anyone could predict exactly where we’re going to be in five to 10 years, they’d be very popular. That’s why we’ve got to be prepared. For many years now, General Motors has had an energy diversity policy. We have work going on with CNG [compressed natural gas] vehicles. We have continued work with fuel cell vehicles, with batteries, with improving the internal combustion engine, with hybrids, etc. I really believe it’s not going to be one silver bullet, but it’s going to be many things.” Autoline This Week interview

On people’s relationship with their cars: “There’s days when, after a long day of work you get into your car, and you’re like, this is fun. I get to drive this home.” Stanford magazine, September/October 2011 A

Mary Barra received her MBA from Stanford GSB in 1990.
When entrepreneur Gregg Renfrew set out to take on the traditional cosmetics industry by founding a company specializing in nontoxic beauty-care products, the biggest challenges didn’t come from her competitors in the $80 billion global industry. Surprisingly, they emanated from within her fledgling venture just as it was about to take flight.

In this issue of Stanford Business, we begin a three-part series following Renfrew through the most difficult moments of the launch of her company. H. Irving Grousbeck and Sara Rosenthal first recounted Renfrew’s journey in a 2012 case study. What follows are extensive excerpts from the case, first published by the school’s Center for Entrepreneurial Studies.

We hope the experiences of this serial entrepreneur will prompt discussions and feedback from you, just as they spark students to consider what they would do if they were in Renfrew’s shoes. At the end of each of the three sections, spread over the next three issues of the magazine, we will include questions we hope you will answer on our Facebook page or by sending your responses to us at the email address listed on the following page. Some of the names and details have been fictionalized, but this is a story of real business leaders facing real start-up dilemmas.

Women should not have to compromise their health in the name of beauty.
— Gregg Renfrew, Founder and CEO, Beautycounter

From the cleaning business she started on Nantucket Island in college to the bridesmaid dress company she launched after graduation, Gregg Renfrew had had entrepreneurial aspirations for as long as she could remember. Therefore, in 1997, when she identified an opportunity to buy The Wedding List, a U.K.-based wedding registry service, she went for it. Renfrew licensed the idea from its founder, Nicole Hindmarch, with a vision to enhance and build out the personalized registry service via an online wedding registry, expanded product showrooms, and a radically more user-friendly experience than what was currently available. Though the company achieved early success, the dot-com bust in 2001 created financing challenges, and Renfrew was forced to sell her company to Martha Stewart Omnimedia, where she served on the executive management team for the next nine months.

Upon leaving her job at Martha Stewart at the end of 2001, Renfrew felt ready to launch yet another venture, this time her own retail consulting practice where she would work directly with some of the biggest retail brands in the country to help shape their customer-facing identities. She subsequently led or advised brand, marketing, and merchandising engagements for J. Crew, Bergdorf Goodman and Intermix, among others. In 2006, she was recruited to the position of CEO of Best & Co., a well-known children’s retail group, to help revive the traditional brand and develop its multichannel distribution strategy. In March 2008, she left Best & Co. and moved to Los Angeles, where she resumed her retail consulting practice, through which she was connected with Jessica Alba, the Hollywood actress.

Alba was interested in launching an organic baby-apparel company, and she hired Renfrew to develop the business model and market strategy. Renfrew had recently gained in-depth knowledge of the nontoxic (i.e., free of known carcinogens, mutagens, and other harmful chemicals) goods space and had begun to make significant changes in her personal life based on what she had learned. As she and Alba worked together, they expanded the original concept beyond organic to a full line of nontoxic baby products that would ultimately become known as The Honest Company. This work affirmed Renfrew’s personal passion and ignited a professional commitment to bring safer, healthier high-quality products to market.
Renfrew immediately called her friend Bryan Wolf, a lawyer at one of Los Angeles’ largest entertainment firms, who had first become intrigued by Renfrew’s desire to build her brand, in part by leveraging celebrity and media channels. The two had already committed to working together, and Renfrew was excited to share her revelation with him. As it turned out, Wolf had also long been compelled by direct sales and agreed that it was the perfect fit for their new venture. Within days, Wolf had pledged to contribute up to $200,000 to fund the early stages of the startup, and further committed to spend 40 to 60 percent of his time helping manage the new company. Renfrew and Wolf would share 50/50 in the voting rights and ownership stake, with both diluting their shares equally as new investors came on board.

Renfrew and Wolf were able to corral another $1.8 million over the next several months by pooling capital from friends and family ranging from $25,000 to $350,000, while maintaining a controlling ownership share in the company. The partners also assembled a five-person board of directors, with voting rights distributed evenly among the members.

The Challenge: What hurdles will Renfrew face as she tries to break into the $80 billion beauty-products industry? What marketing tactics will persuade women to drop their current beauty products and trust their skin to a newcomer, offering a safer but expensive alternative? Is there room on the playing field for this startup? What do you think of Renfrew’s choice of a business model? Tell us your thoughts at www.facebook.com/stanfordgsb using #StanfordGSBCaseStudy or email us at StanfordBusiness@Stanford.edu

Next Issue: Like many entrepreneurs, Renfrew turned to a network of trusted and talented friends and former colleagues to take her venture out of the gate. But will her loyalty to them derail her dream of providing women with safer skin-care products?

As Renfrew surveyed the space in the fall of 2010, she saw several areas, including food, apparel, and cleaning products, with well-established brands and significant shelf space represented by nontoxic products. In contrast, beauty and personal care, an almost $80 billion global industry, appeared to be largely overlooked. A handful of companies such as Burt’s Bees, Tata Harper, and Alba Botanica were beginning to make names for themselves, but very few were going after the more sophisticated, high-end corner of the market. Renfrew began to articulate her vision for a company whose products were “chic like Chanel, safe for your body, and performed like a traditional brand.”

She also began to explore the various distribution channels through which she could sell. One day over lunch, a friend suggested she look into the direct selling model, and after an afternoon’s worth of research, Renfrew knew she had landed on exactly the right sales channel. As she explained, “This story — the story of healthier products and how important they are — needs to be told person to person. This is a story told between friends. On top of it, direct selling provides economic opportunities and enables the empowerment of women. It is perfect for beauty products.”

What hurdles will Renfrew face as she tries to break into the $80 billion beauty-products industry?
Parents: Help Your College Students Launch Their Careers

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Change lives. Change organizations. Change the world.
"We want to help developing economies use their natural strengths and resources as innovations in the value chains."
—Hau Lee, PAGE 58
PASSIONS

The Art of Collecting: How three enthusiasts built their world-class collections

For Guy Ullens, it all started as a hobby and a desire to support the work of the artists he saw when his business took him to China in the 1980s. Some 20 years later, in 2004, he and his wife, Myriam — worried there would be no major event to support the exploding Chinese art community during the 2008 Beijing Olympics — decided to build a Chinese contemporary art museum. “We went way beyond our budget, but we had our first major show in November 2007,” says Ullens, who lives in Switzerland and graduated from Stanford GSB in 1960. One of the pieces in his collection, The Last Supper by Zeng Fanzhi, sold for a record $23.3 million last year.

Ullens still collects the works of young Chinese and California artists. Today the Ullens Center for Contemporary Art in Beijing’s 798 Arts District is run by an American “superqualified head curator” and plans an exhibit of young Los Angeles artists next fall. “When I meet an artist or a piece of art I love, I cannot sleep for a few days,” Ullens says. His best advice for other collectors? “When you start, go for the best honest advisers, and go for the best quality.”

—DEBORAH PETERSEN
121030
by Wang Guangle, 2012
The Answer
by Ludwig Deutsch,
1883
Terence Garnett: “Trust Your Instincts.”

Were it not for a photograph taken with a Brownie camera of his father as a young man, Terence Garnett might have never gathered an art collection, and especially one that has reached some of the world’s most significant museums, including the J. Paul Getty Museum in Los Angeles and the Musée d’Orsay in Paris.

The image of his father in Cairo while serving in the British Army in the Middle East helped inspire the younger Garnett’s intrigue with that part of the world, and, eventually, with the artists in the 1800s who captured its sublime desert landscapes, as well as the bold, ornate dress, weapons, and mosques of that era.

Garnett, cofounder of a venture capital firm in Silicon Valley, is not drawn to the 19th-Century Orientalist depictions of harems. Instead, he collects the more masculine, historical pieces of the genre. He has done extensive research to bring his collection to what it is today, but choosing art is more than an intellectual or financial pursuit. “What I’ve gone after is what I love,” says Garnett, who earned his MBA at Stanford GSB in 1988. “At the end of the day, you have to go with your gut instinct and go with what you like. That kind of trumps everything,” he says. “If you are going to make a significant investment, whether it is in a company or in a piece of art, you’ve got to have the conviction and trust your instincts.”

—DEBORAH PETERSEN

Sergio Autrey: “Art Can Change Many Things.”

Sergio Autrey grew up in Mexico City, tagging along with his mother when she bought antiques for the family’s home. Those outings marked the beginning of a lifelong passion for art that has led him to become a kind of modern-day Mexican Medici. After he received his MBA from Stanford GSB in 1978, Autrey returned to Mexico City and began collecting and commissioning art. “I decided to sponsor my generation of painters,” he says, adding that these artists have become his friends. In turn, those artists have created more than 1,000 paintings for his collection, some of which Autrey lends to exhibitions and museums. For Mexico’s bicentennial in 2010, he commissioned 26 artists to produce large paintings that reflected his country’s 200 years of independence and the Mexican Revolution. (All the paintings are at www.akaso.com.mx)

“I think art can change many things,” says Autrey. “It can change people’s views. Some of the art is not what it first appears to be. There’s a lot of violence behind many of the paintings. You look and say, what a beautiful thing! But underneath there is darkness.”

—KERRY A. DOLAN
MOON SHOTS

“The Frontiers of the Unknown”

An investor in the space and satellite industry heads to the desert with his own rockets and looks to new heights.

BY MICHAEL FREEDMAN AND STEVE FYFFE

SPECTACLE
Launching rockets in Nevada’s Black Rock Desert
Steve Jurvetson has spent the better part of the last two decades identifying and investing in some of the world’s foremost entrepreneurial ventures. In his time off, he does something quite different: He heads out to California’s Central Valley, Nevada’s Black Rock Desert, and other less populated areas to launch rockets. At first it was just the small ones — about a decade ago, he picked up a rocket kit at a hobby store, assembled it, and launched it with his kids. Over time, he went bigger — much bigger — assembling custom designs with esoteric materials, plus onboard cameras, computers, and other electronics to measure performance.

What’s the appeal? For starters, there’s the community. “You’re surrounded by a bunch of other geeks, generally, science, engineering types who love to talk about nose cone design and computational fluid dynamics,” he says. There’s also the satisfaction of physically building something with one’s own hands. And then, of course, there’s the spectacle. There are no limits on rocket speed, and virtually no barriers to size, cost, and complexity. He knows of launches that have reached 330,000 feet. (Those sorts of altitudes require FAA approval.) He, too, has built his share of impressive ones. His skinny carbon fiber rocket hit Mach 2 several times. In some instances, the launch ignites a solid 10-foot-tall plume of fire. In one case, he used a titanium sponge propellant and created a pyrotechnic shower in the desert that spewed fire 80 feet into the air.

Jurvetson’s interest in rocketry goes beyond being a hobby. He invests in low-Earth-orbit satellites and space exploration businesses such as Elon Musk’s SpaceX, where Jurvetson sits on the board. The idea behind the satellite investment is, essentially, that it used to cost so much to build and launch a satellite that it had to stay in orbit for years to recover the cost. Doing so meant flying the satellite far from Earth so that it didn’t de-orbit. Now, with the size and cost dropping dramatically, satellites can orbit closer to Earth, which means improvements in applications like telecommunications and imagery. “The entire constellation costs a fraction of the old model but provides a much better service,” he says. “If you’re looking with cameras at the Earth, you fly in close to the Earth; you get a better picture. If you have hundreds of them up there, you see the entire Earth every day. You don’t have to have a big, expensive telephoto lens off in the distance. You have a bunch of little ones. That’s just a smarter way to do it.”

That insight, he says — to have almost disposable satellites — would have been unthinkable in the past. “People are used to building satellites that cost a half billion dollars,” says Jurvetson, a partner in the Menlo Park venture capital firm Draper Fisher Jurvetson. “They’re the size of a Greyhound bus. They’re now being shrunk down to the size of a shoebox that costs tens of thousands of dollars, and you put hundreds of them up there.”

Underlying all of this, Jurvetson says, is this notion that “we, as humans, like to imagine what could be and explore what hasn’t been explored — to go to the deepest depths, to go to the highest heights.” In every startup, he says, there’s an entrepreneur who has some dream or vision, a star he or she sees on the horizon. “They often have taken a number of pragmatic steps to get there, like building rocket engines and then building rockets, then building a spacecraft.” But it is the dream of the prize — “in the case of SpaceX, it’s colonizing Mars” — that carries and motivates the entrepreneur, the team, and the investors, through years of hard work. “The people who push humanity forward, to the frontiers of the unknown,” he says, “are some of our greatest heroes.”

We as humans like to explore what hasn’t been explored — to go to the deepest depths and to the highest heights.

Steve Jurvetson, a partner at venture capital firm Draper Fisher Jurvetson, received his MBA from Stanford GSB in 1995.
TRAVEL

Bringing Sustainable Tourism to Rural China

A group of researchers explore a new way to alleviate poverty in the Chinese countryside.

BY MELISSA LEAVITT
For Chinese professionals leading hectic lives in crowded, polluted city centers, a vacation in the countryside provides a rare opportunity to slow down and breathe fresh air. These tourists also potentially offer a much-needed source of income for rural families who subsist largely on scant revenue from small-scale farming.

Yet, so far, China’s farmers have found homestay tourism difficult to develop and sustain. Few have the means to furnish high-quality lodgings, nor the experience to successfully market and manage a tourism business. Local governments do not have the expertise or the financial resources to promote small villages as vacation destinations. And financing from investors outside the community comes with its own problems.

Enter researchers working with the Stanford Institute for Innovation in Developing Economies (SEED, for short) on value chain research aimed at integrating more local products and services into emerging markets. They have developed a new approach to rural tourism in China that would preserve the authenticity of the region, meet the needs of urban travelers, and turn rural farmers into entrepreneurs. By making crucial changes to the supply chain for homestay tourism, they hope to alleviate poverty in rural communities in an economically, socially, and environmentally sustainable way.

The challenge, in essence, is that traditional tourism supply chains largely rely upon intermediaries such as hotel operators and travel agents. Particularly in rural markets, the researchers found that nonlocal businesses dominated the tourism industry. While these investors may be able to construct hotels and other accommodations that bring in wealthy tourists, this type of development can lead to uncontrolled growth that harms the environment and disrupts local culture. In addition, few of the economic benefits ultimately trickle down to the local community.

A case in point is Old Town Lijiang, a historic town in southwest China and a

Hau Lee is the Thoma Professor of Operations, Information, and Technology at Stanford GSB and the faculty director of SEED. For a full list of the researchers working on this project, go to http://stnfd.biz/ubVxE
In Old Town Lijiang, commercial success has come at the cost of environmental damage.

UNESCO World Heritage Site. The town receives more than 15 million tourists, generating more than $3 billion in tourism revenues annually. But commercial success has come at the steep cost of environmental damage and cultural degradation. As Old Town Lijiang’s ancient waterways became contaminated with sewage, and its cobbled streets transformed into a red light district of bawdy nightlife, much of the indigenous Naxi population began to flee the town. “Relying on outside investors to develop tourism is very common in emerging markets, but causes leakage of economic benefits to outsiders,” said Hans Galland, a member of the Stanford research team with 10 years’ experience as a tourism investment professional in China.

The researchers hope their model, which consists of providing farmers with a lodging product financed by microloans, will be more “community-centric,” says Vivek Garg, who focused on entrepreneurial innovation in his native India before coming to Stanford. Their concept, he says, will not only grow the economic pie but enlarge “the community’s slice of it.”

In a recently completed pilot project, the researchers focused on Puxing, a mountain village in southwest China dotted with tea shrubs and fruit orchards. Despite boasting the natural and cultural attractions city dwellers desire, Puxing residents generated just 10% of their income through tourism. Situated 20 minutes away from the Mount Emei and Leshan Giant Buddha Scenic Area, which drew nearly 300 million visitors in 2012, Puxing, the researchers knew, had the potential for tourism development, especially for vacationers who wanted to escape the crowds and enjoy Puxing’s unsullied way of life.

On a farm homestay, tourists could join their host family in farm chores, such as picking tea leaves, and learn how to prepare traditional cuisine. They could tap into the area’s spiritual heritage by partaking in Buddhist traditions, or time their vacations to coincide with the annual Peach Blossom Festival, which draws as many as 200,000 visitors to the town every spring.

The researchers also found that a few Puxing families had tried to host tourists in their homes, but the homes weren’t up to the standards of urban visitors. Typically made from clay, area homes tend to be poorly maintained and energy inefficient. Even if their houses had been in better condition, farmers would have found it difficult to effectively market them to attract a constant stream of visitors, say the researchers, who also discovered that many families resisted the idea of turning their homes over to strangers, wary of the intrusion that tourists would bring. To overcome these impediments, the researchers plan to introduce a new product into the value chain: a 24-square-meter modular pod placed on the farm premises, which farmers could purchase through a loan.

For tourists, pods offer a combination of modern conveniences and small-town hospitality. They get a taste of the farming lifestyle without causing the family any disruption or displacement. They also get to experience Puxing from the best possible vantage point, because pods can be placed in the most appealing and scenic locations on the farm grounds. Each pod, which includes a bed, sitting area, and bathroom, would cost farmers approximately RMB 80,000 (the equivalent of $13,000), and they may be able to obtain a loan on preferential, perhaps even interest-free, terms. “As the owner of both the farm and the homestay pod, farmers are incentivized to make socially optimal decisions and prevent environmental degradation, as unsustainable tourism would create a cost to their farming business,” said researcher Tilky Xu, a Stanford doctoral student in economics.

Another critical change to the traditional tourism supply chain involves centralized operations. Bearing in mind the difficulties of past attempts at rural tourism, the researchers would incorporate industry leadership and expertise. Farmers in this new model are to be responsible for day-to-day operations and interactions with visitors, but key management functions, such as marketing, quality control, and training, would be centralized and financed through a cooperative. Under the guidance of the research team and the local tourism bureau, the centralized platform would help ensure a quality, authentic homestay experience. The idea is to optimize participation from the local community while still welcoming the expertise of tourism professionals to produce a profitable, sustainable model. Projections from the pilot study showed that a pod-based homestay model could increase household income in Puxing between 35% and 55%.

Many questions remain if this is to be a sustainable model. For starters, the community itself may not be structured to support this model, as it is fragmented and has little precedent for cooperative organization. In addition, rural property rights in China are undergoing considerable change, and land issues could erupt if farmland becomes the basis for commercial tourism revenue. Moreover, although this model involves significant participation from farmers, they must still purchase the pods from an outsider and work with a centralized operating platform that may not have the trust or cooperation of the community.

Researchers plan to address these challenges and put their homestay model to the test by building several sample pods in Puxing. In January, the research team embarked on their third field trip to China to prepare to roll out their prototype. If their projections turn out to be correct, their test case could turn an impoverished farming community into a rural tourism market that offers farmers a sustainable source of supplementary income and that preserves their land and traditions. The study could also point the way to increasing income in rural areas around the world.

“We want to help developing economies use their natural strengths and resources as innovations in the value chains,” says Hau Lee, faculty director of SEED and a supply chain expert. “This is an example of how local people can use their own livelihoods — the landscape, their farms, and local foods — to create economic value.”
“Do what you love and you will have a good chance of doing something great.”
— Stanford GSB lecturer Rob Siegel, speaking at Stanford GSB’s Strategic Management of Technology & Innovation class.

“Choose to see beauty in everything you do. That will help you change the world.”
— Jane Chen, a 2008 Stanford MBA graduate and founder of the Embrace infant warmer device, speaking at Stanford GSB’s Social Innovation Summit.

“It takes the same amount of energy to dream big as to dream small. So dream big but stay humble.”
— Anheuser-Busch InBev CEO Carlos Brito, speaking at Stanford GSB. He received his MBA from the school in 1989.

“Happy people are people who always have a project. They’re pursuing meaningful life goals.”
— Sonja Lyubomirsky, a 1994 Stanford PhD, speaking at the 2013 Roundtable at Stanford in October.

“Great entrepreneurs have a genuine passion and belief that what they’re trying to do is change the world.”
— Theresia Gouw, a 1994 Stanford GSB MBA graduate now at venture capital firm Accel Partners, speaking at the Stanford Alumni Entrepreneur Reunion.

“Leaders need the courage to follow through on their own convictions before everybody agrees.”
— Professor Robert Burgelman at Stanford GSB’s Strategic Management of Technology & Innovation class.

“Don’t chase success. Chase a dream.”
— Richard Fairbank, the founder of Capital One and a 1981 Stanford MBA graduate, speaking at Stanford GSB.

Join the conversation @StanfordBiz
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#### NAMES AND ORGANIZATIONS

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