



Beyond the boom

A crisis is on the cards for top management as baby boomer leaders reach retirement age and there are too few people to replace them. **Robert P. Gandossy** and **Marc Efron** argue that developing a culture of leadership and setting different reward levels is vital for the future success of top companies.

At his first meeting with IBM's Senior Leadership Group in 1996, Lou Gerstner, the new CEO charged with saving Big Blue from the brink, issued an edict: Go back to school! The directive must have surprised and angered more than a few of the 300 senior executives he faced – many of whom had been with the technology giant for decades.

But Gerstner hadn't been recruited to make friends. His immediate challenge was to save an institution that had been placed on a 24-hour deathwatch. When Gerstner told the executives in the room that they would be participating in a programme focused on developing their own leadership capabilities, they knew they'd better listen.

A downward spiral had taken IBM from a \$6 billion profit in 1990 to an \$8.1 billion loss by 1993. In an industry that was rapidly expanding, IBM had lost half of its market share since 1985. The stock price stood at an all-time low and competitors like Hewlett-Packard and EMC clawed at its market share. And on April 1 1993, the day Gerstner took charge, IBM's stock was just \$13 per share, down from a high of \$43 in 1987.

for IBM's amazing turnaround, he clearly recognised himself that the company's leadership strength extended far beyond his office. Leaders were held accountable for growing leaders, and good leadership was viewed as a critical asset to be carefully managed.

And Gerstner's mandate could prove to accomplish far more than merely saving IBM. With the company facing likely retirement of as much as 75 per cent of its senior management team by the year 2007, Gerstner's investment in a powerful leadership development and succession management process may prove to be vital if IBM is to retain its regained crown and Gerstner's turnaround legacy is to last.

Reaching boiling point

As Gerstner's story demonstrates, it is the development of a strong leadership team, rather than the actions of a single individual that sets one organisation apart from the rest. The facts are indisputable. Great leadership teams build trust and confidence among their people. They motivate and

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The organisation that had long held court as America's most admired company was forced to abandon its guarantee of lifetime employment, sending tens of thousands of workers in search of new jobs. Many of those workers found employment within the legions of new dot-coms and undoubtedly snickered at IBM as a dinosaur that would soon be extinct. However, it wouldn't be the dot.com millionaires but Big Blue that would have the last laugh.

The phoenix and the market

Just as Wall Street was preparing to throw the first shovelful of dirt onto IBM's casket, something miraculous happened: the giant rose from the dead. In 2001, profits reached over \$8 billion on revenues of \$83 billion, and shares hit an all-time high. The company once credited by *The Washington Post* for inventing the computer industry was back – with a vengeance. And, in an instance of supreme irony, *Business Week* declared IBM the largest dot-com in the world. Gerstner and his team had pulled off the turnaround of the century, leading IBM back to profitability – without chopping up the company into separate operating units, a plan that had been in the works when he took over as chief executive.

While Gerstner has been given much of the credit

inspire. They anticipate challenges and redirect the enterprise in timely and appropriate ways, unifying the workforce behind a single cause and driving the kind of performance that allowed a Southwest Airlines to soar or an IBM to reboot itself. Simply put, they deliver better business results.

The opposite is true as well: an incompetent leadership team wreaks serious damage and creates inflexible bureaucracies, often destroying shareholder value and dooming the organisation to failure. The corporate landscape is littered with hundreds of overly managed, poorly led institutions.

It's clear now that there is a cause and effect – great returns for those organisations that invest in leaders and failure for those that do not. After decades of largely paying lip service to building great leaders, executives everywhere have begun to think more seriously about their own leadership processes.

Baby boomer bubble

This new awareness arrives at the right moment as daunting demographic trends loom. From the 1970s to the 1990s, companies became spoiled by the enormous baby boomer generation which provided millions of talented, dedicated workers. The mindset that you could "buy" a leader when needed became ingrained in many firms. "Twenty years ago," says Jeff Sonnenfeld, associate dean at

Yale's School of Organization and Management, "only 7 per cent of major firms hired CEOs from the outside. Now it's over 50 per cent."

But ageing boomers are retiring and there is a smaller pool to take the workforce from. As the

We started our research by surveying CEOs and human resources executives at 240 of the world's top 500 multinational companies, asking questions about a broad variety of topics that would influence how leadership strength is built. We conducted in-

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bubble bursts, we will see a 15 per cent drop in the number of men and women of key leader age – those in the 35- to 44-year old range. As everyone knows, when supply of a desirable product decreases, its price increases. Companies looking to pay the market price for an executive may soon find the quality they want is not in their range.

And that's not all. Boards of directors and shareholders have increasingly less patience with leadership teams that do not produce results. In 2001, a record number of 555 CEO departures were recorded. In 2002, nearly 100 CEOs of the world's largest 2,500 companies were replaced for performance reasons, almost four times the number asked to leave in 1995. Leaders who can draw out multiple perspectives and lead diverse teams effectively will be a rare, valuable commodity through the "boomer trough."

depth interviews with leaders at more than 50 companies. In 2003 we added a global perspective, surveying hundreds of companies in Europe and Asia as well as in the US.

Unlike some previous studies, we emphasised that there had to be a relationship between great leadership and superior financial results. So we passed all data through a financial screen. In the 2003 study we used the five-year compounded growth rate of earnings before income and taxes (EBIT) as this screen. Those that failed to perform at or above their industry median over a five-year period from the study date were eliminated. Surprisingly, this knocked out many well-known firms with reputations for strong leadership programmes.

In the second phase of our study, we went back to the top companies and interviewed nearly 100 senior executives and high-potentials, including a

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Sowing the seeds

The combination of demographics and economic challenges means that companies no longer have the luxury of taking a trial-and-error approach to building leadership quality and depth. They need tried and tested methods and tools that fit with their organisation's culture. Unfortunately, many companies find that fact-based, clear guidance is in short supply.

Our research discovered that narrowly-focused studies on topics like succession planning, executive education, and performance management were widely available, but no study looked broadly and systematically at the combined factors that enable companies like GE, IBM, or Colgate to be so successful in growing great leaders. And that combination of factors seems to offer the best possible explanation for the consistent stream of great leaders at top firms. After all, it was more than great leadership development programmes that produced GE's three CEOs in waiting.

number of CEOs, to better understand – from their perspective – what makes the difference in companies that build great leaders.

Many of our own preconceived notions about leadership were challenged. There are no silver bullets or formulas to steal and embed in your organisations. There are patterns, however – and the patterns are what we were after. The top companies share a combination of values and results-oriented practices for identifying, nurturing, and rewarding future leaders. These elements form the cornerstone of their programmes and set them apart from the vast majority of organisations today.

Three fundamental truths of building great leaders

These elements aren't best practices, but they capture what we call a leadership truth. A truth can be thought of as an inviolable rule of building leaders – a foundation element of top companies. We believe that all three truths must be in place for a company to consistently build leadership quality and depth. →

→ Leadership Truth #1: CEOs and boards of directors at top companies provide leadership and inspiration

Without the passionate and visible commitment of the CEO, developing great leaders is not possible. It seems intuitive that CEO involvement would be a critical success factor. After all, the support of senior management has proven to be critical for a wealth of corporate initiatives to succeed. But top-down support has become such a catchphrase in recent years that the real meaning has grown fuzzy. Involvement takes on an entirely new meaning in the realm of growing great leaders.

It is imperative that chief executives not only support the programme, but also actively participate in it and communicate passionately and frequently about it. CEOs at the top companies are intimately involved in their talent review processes – reviewing top candidates and ensuring that key roles are filled with top people. When we met with Bob Nardelli, CEO at The Home Depot, he was preparing to visit every division for several days each for business and talent reviews. CEOs of the top companies can spend a quarter or even half of their time devoted to leadership. They do so because they know there is a direct link to results.

The financial consequences are compelling. When a CEO is actively involved in leadership development, the organisation averages a 22 per cent return to shareholders over a three-year period. Without direct leadership from the top, the numbers

Leadership Truth #2: Top companies have a maniacal focus on the best talent

Many of these companies have built a respected marketplace image, reputations for developing talent, and innovative and selective recruiting processes, ensuring a full and powerful pipeline. Southwest Airlines receives over 200,000 unsolicited applicants per year. It may only hire 5,000; 2 per cent of those who apply.

Learning that top companies focus on developing their high-potential talent should not be, in and of itself, particularly surprising. But they not only spend considerable time identifying and evaluating their high-potential people, they also focus heavily on matching leaders with jobs and providing cross-functional experiences.

Sometimes when we explain these developmental moves, people get the wrong impression. Make no mistake – these are tough, challenging assignments with difficult goals. These companies intentionally take leaders out of their comfort zone and stretch them to test their capabilities and their capacity to grow. And while support is provided – unlike the Darwinian sink or swim models we see in some companies – there is tremendous challenge and pressure to succeed. Being high-potential in the top companies often means you're held to a higher standard.

Top companies also recognise the immense value these people bring to the organisation. Studies have

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drop to an astonishing negative 4 per cent. Even in down times, these companies consistently out perform the market by 1 to 2 per cent. This equates to billions of dollars in market capitalisation.

Perhaps that's why board members are so dedicated to leadership development at the top companies. And boards will be even more active in the future, coming on the heels of legislative and regulatory reform and shareholder pressure. Getting the board involved not only gives high-potential people better coaching, but it also keeps pressure on the CEO to continue doing the same.

Take Procter & Gamble. Every year, CEO Alan Lafley reviews the top 150 people with the board. "They get exposed to our top talent in a lot of ways," says Lafley. "They not only see them make presentations to the board and in social situations, but also see them in action in their category and country businesses." Scott Cook, CEO of Intuit and a P&G board member, arrives a day early for board meetings so he can get to know P&G's highest-potential employees and see how they behave.

consistently shown that top performers produce in value at least 100 to 150 per cent more than average performers in similar jobs. People who fall into this category should have compensation opportunities significantly above their lesser-performing peers. If they only see 5 or 10 per cent pay increases, it isn't particularly motivating. Top companies differentiate pay between high-potentials and average performers in the same role. This frequently entails at least 75th per centile pay and perhaps even as high as 90th per centile pay. While that may sound excessive, it's a bargain considering the value that these star performers bring to the table.

Leadership Truth #3: Top companies put in place the right programmes, done right

Even the most soundly designed leadership practices can be undermined by inconsistent implementation or lack of integration with other

leadership processes. What sets the best firms apart from the rest is not just careful design of the right process but a relentless dedication to executing these flawlessly. And that means ensuring what they do is integral to the business.

GE's performance and succession planning process, known as Session C, has been a model for companies throughout the world. Not only does Session C provide a forum for leaders to discuss GE's talent and the opportunities to strengthen it, but it also provides a place for candour and debate and reinforcement of priorities and cultural norms and values.

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GE employees complete an online self-assessment, listing their accomplishments, adherence to GE's values, developmental goals, and career aspirations. They also update their internal resumes – jobs they've held and educational experiences. Supervisors and managers then complete similar evaluations which flow upward, in a reverse cascade, through every department and function. The dialogue is rich and open.

These strategic priorities are inseparable from the discussion of talent. But the focus is clearly on the development of leaders to meet the business challenges ahead. "Do people like working for her?" CEO Jeff Immelt will ask. "Who has she brought along? What does he want to do next?" If the executive is ready for a move, cross-business assignments are facilitated. The process is an integral part of running GE's \$130 billion business.

Few have achieved and sustained what GE has for so long, even though GE's formula for winning the war for talent is simple: hire outstanding talent, create an intense performance culture, and rigorously assess performance. Just words to many. But at GE, they back it up. They continuously

supply chain management and customer relationship management have done. Each of these critical processes are reinventions of predecessor functions that were necessary but of marginal value. Over the last decade, using technology and revamping tired, disconnected systems, they have become core to the modern enterprise.

At top companies, managing and developing talent is running the business. HR builds the systems and processes, but the line drives it. This is what happens at Colgate. "The line owns leadership development," says Lois Juliver, Colgate-Palmolive's chief operating officer, "we work with HR to get all the

tools, and they put in place the mechanisms. But if the line doesn't own it, it's not going to happen."

The result is a company with a reputation as a place where leaders want to work – a "leadership brand," that will ultimately separate the winners from the losers in the battle for leadership talent. For the best talent, it's always a seller's market, and they can pick and choose from the best available opportunities. Those organisations that have cultivated a strong leadership brand will be far better positioned to attract and retain top leadership talent.

Meeting the challenge

The three truths are important, but they don't quite capture the whole situation. There are a number of subtleties that account for substantial differences between top companies and those below them. Leadership Truth #1 emphasises the importance of the CEO and the board in developing great leaders, but it goes well beyond them – everywhere you turn, the importance of finding and developing talent permeates the organisation. It is a way of operating. A manager of

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evaluate performance and differentiate pay and opportunities between the best and the least effective. They "sell" careers and they have the infrastructure and the discipline to do what they say.

In *Human Resources for the 21st Century* several contributors suggest that the future value of HR rests on its ability to integrate its activities more directly into the heart of the business – much like

one department will willingly part with their best people to grow capability in the organisation as a whole. They take calculated risks to test new skills, strengthen others, and build the confidence needed for senior executive roles. This movement of talent across businesses, functions, and geographies creates a network that facilitates learning and a pride in the larger whole, not its parts. →

→ Individuals develop strong ties and a desire to give something back to the organisation and to the people who helped them.

Top companies are well on their way to preparing themselves – and their people – to meet future challenges head on. They are a step ahead of the rest and are not complacent. No executive we met felt they had the problem solved – none have crossed off “developing leaders” from their priority list. That is yet one more differentiator for the best companies and the best leaders – they are less cynical, less complacent and always aware that there is more work to be done. ■

Resources

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This article is based on Chapter 1 of *Leading the Way* (John Wiley, 2004) by Robert Gandossy and Marc Efron

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