POINT of VIEW

2016

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Privately held since 1956, we focus on delivering knowledge, insight and results through the collaborative efforts of a team of experts — now spanning 56 offices, 30 countries and more than 50 practice specialties. Boards and leaders consistently turn to Spencer Stuart to help address their evolving leadership needs in areas such as senior-level executive search, board recruitment, board effectiveness, succession planning, in-depth senior management assessment and many other facets of organizational effectiveness. For more information on Spencer Stuart, please visit www.spencerstuart.com.

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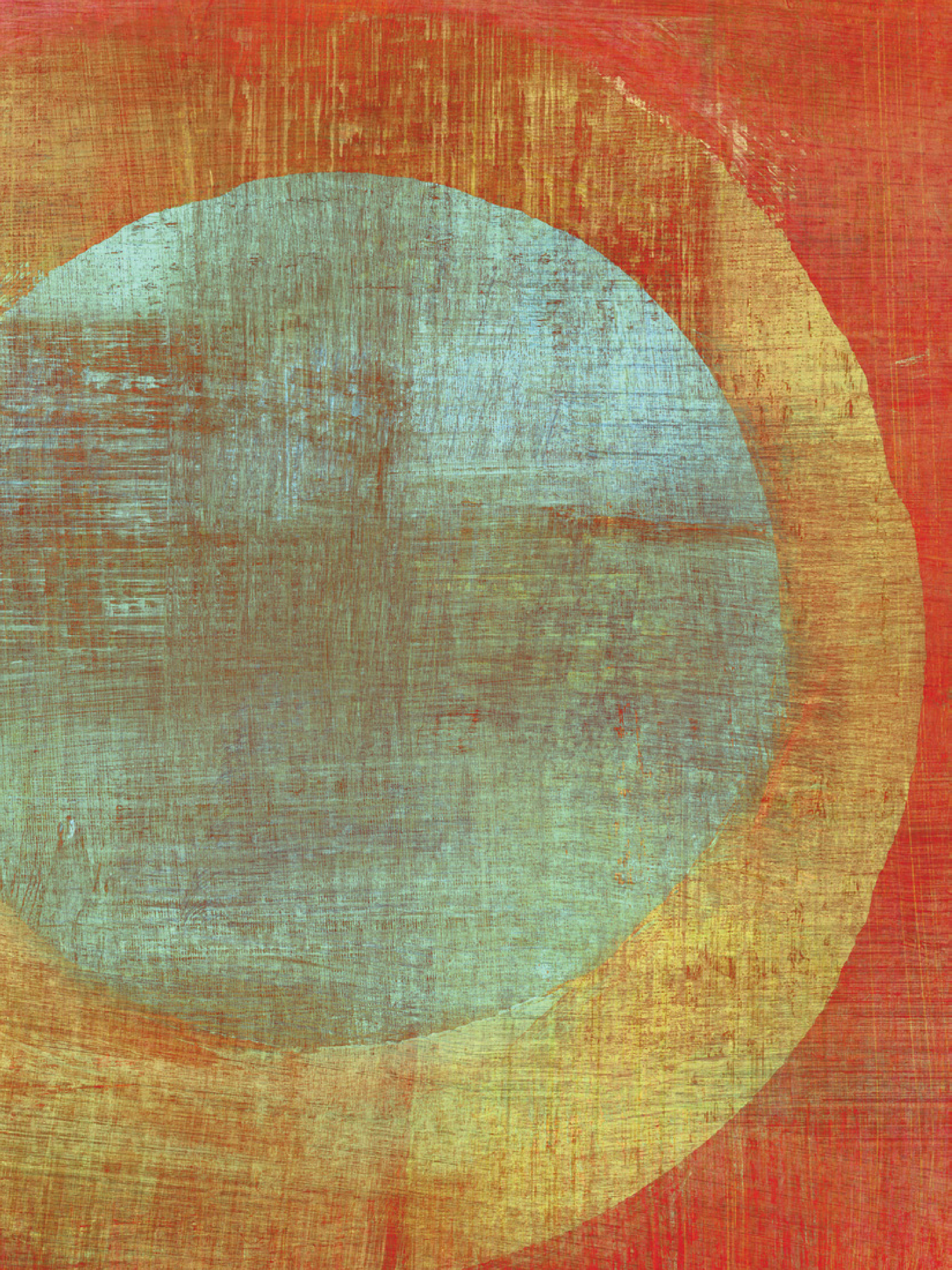


From our CEO

The dynamism of markets and competition today demands that organizations move at a faster pace than in the past and places a premium on the ability of businesses — and leaders — to adapt. Core to this is the ability to learn, both as individuals and organizations.

The most effective leaders actively seek out new ideas and contrasting perspectives, challenge their own biases and assumptions, recognize the need for and build new organizational capabilities and help create a culture that enables today's increasingly diverse, global workforce to change and adapt to new business priorities.

With this issue of *Point of View*, we explore the nature of learning in a business context and highlight what we and others have learned from experience — in digital transformation, leadership development and board governance, among other things.

We look at the concept of learning intelligence, why it matters and how leaders can enhance their own learning intelligence and the ability of the organization to learn and adapt. We consider the experience of early movers in digital, exploring what they did right, what they would do differently and how these experiences inform their future. Drawing on what we know about why some senior leaders have such a powerful impact on business performance while others do not, we look at how organizations can improve their ability to assess and develop executives for the most senior functional roles. We identify the questions boards should be asking to ensure that they are using assessments to remove barriers to better performance and look at the experience of dozens of CEO transitions to identify the hidden risks in CEO succession planning.

On behalf of all of us at Spencer Stuart, I hope you find articles in this issue of *Point of View* that spark an idea or highlight some useful learning. As always, we welcome your comments.

Kevin M. Connelly
Chief Executive Officer
Spencer Stuart

Performance in the Spotlight

Assessment and Board Effectiveness

Investor focus on board performance has reached new levels of intensity. The chairman and CEO of Vanguard, one of the largest mutual fund companies in the world, recently sent letters to the independent directors of its biggest holdings in which he outlined six principles of governance. "In the past, some have mistakenly assumed that our predominantly passive management style suggests a passive attitude with respect to corporate governance," he wrote, "Nothing could be further from the truth."

We have come to expect that kind of perspective from activist investors, who have long been assertive about board governance and composition. Now, large institutional investors are joining the chorus. Firms such as State Street, BlackRock and Vanguard are calling for greater transparency about how candidly boards are addressing their own performance and the suitability of individual directors. As the Council of Institutional Investors sums up, disclosure about assessment "is an indication that a board is willing to think critically about its own performance on a regular basis and tackle any weaknesses ... and can be a catalyst for 'refreshing' the board as new needs arise."

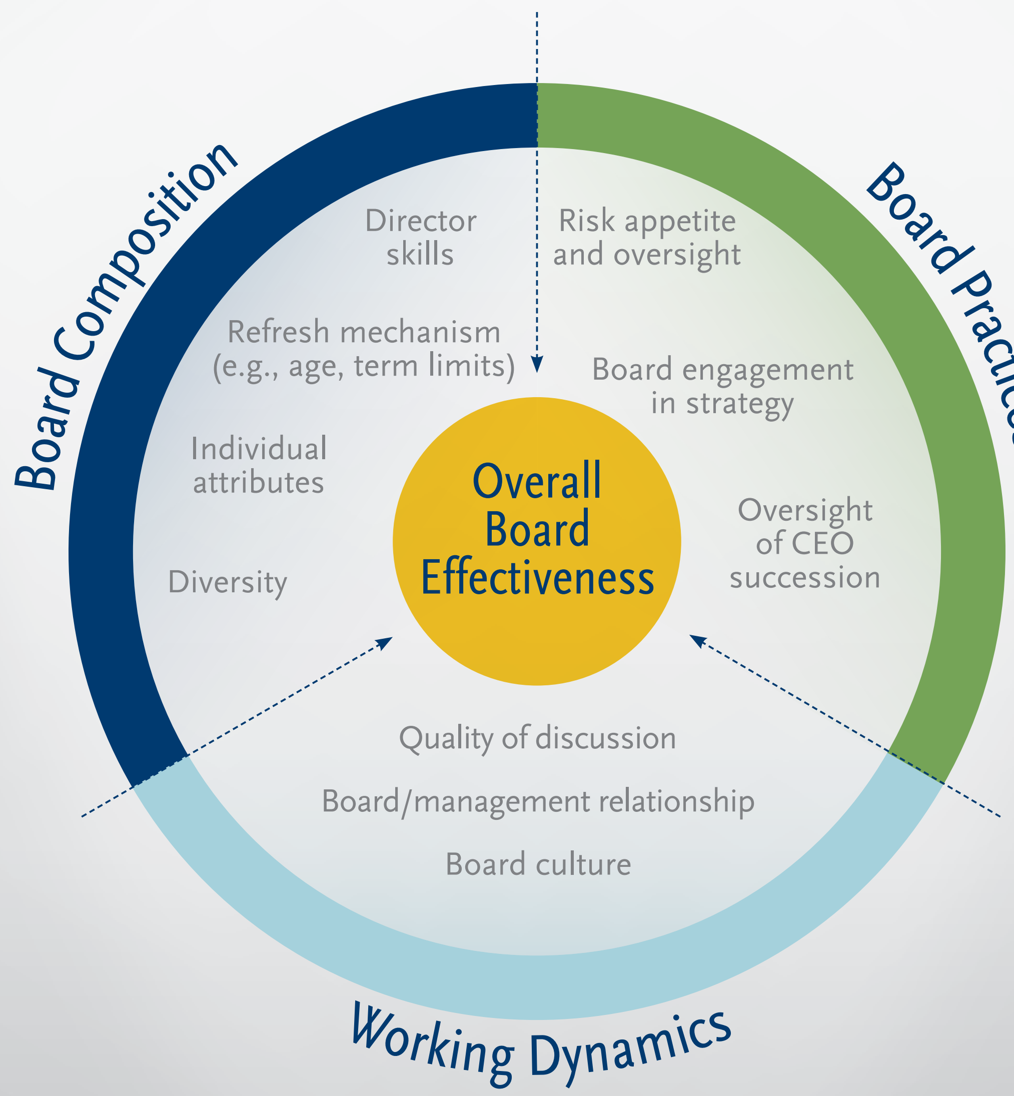
Annual board assessments have become ubiquitous, but are boards truly using them to ensure they are as effective as their shareholders expect them to be?

Some evidence suggests the answer to that question is no. For example, 39 percent of U.S. directors in the 2015 PricewaterhouseCoopers' Annual Corporate Directors Survey thought that someone on their board should be replaced. The primary impediments to replacing an underperforming director are board leadership's discomfort in addressing the issue and the lack of individual director assessments, previous research has found. The best boards are holding themselves to higher standards.

Boards that are committed to improving their effectiveness use the assessment process to get at six key questions:

- How effectively do we engage with management on the company's strategy?
- How healthy is the relationship between our CEO and board?
- What is our board succession plan?
- What is our mechanism for providing individual director feedback?
- What is our board culture and how well does it align with our strategy?
- What processes are in place for engaging with shareholders?

Board Effectiveness Assessment



Improving board effectiveness

When done effectively, board assessments provide the board with an opportunity to identify and remove obstacles to better performance and to highlight what works well. They give directors a forum to review and reinforce appropriate board and management roles, ensure that the board has the right perspectives around the table and bring to light issues brewing below the surface. A robust assessment can help ensure that the board is well-equipped to address the issues that drive shareholder value by focusing on the following questions.

How effectively do we engage with management on the company's strategy?

Oversight of the business strategy always has been a core responsibility of the board. But, today, the threats and opportunities facing companies are more dynamic. Digital transformation, business model shifts, the rise of new competitors and the impact of doing business globally require many businesses to change faster than in the past. So, regular strategic discussions have assumed greater urgency. The board should ensure that the management team is responding to emerging developments most effectively.

The CEO and his or her team "own" the strategy, but the board provides critical oversight. Directors should challenge assumptions and the soundness of the strategy, fine-tuning where needed, and measure performance against a set of agreed-upon objectives. The best boards ensure that the articulated strategy provides a forward-looking roadmap for the organization, including the specific levers to improve performance. A clear, sound strategy should serve as the foundation for all of the board's work, and high-performing boards are disciplined about making sure that it does.

The board conversation has increasingly drifted toward reviews of historical data — compliance reviews, financial reviews, safety reviews — that have less impact on business results, many directors report. This backward-looking review can come at the expense of forward-looking strategic matters where directors' expertise can be valuable in shaping future results. High-performing boards make time to focus on what matters, striking the right balance between important oversight responsibilities and forward-looking conversations.

How healthy is the "balance of power" between our CEO and board?

The relationship between the board and the CEO requires balance. The board is ultimately responsible for selecting the CEO, reviewing his or her performance, aligning CEO compensation with the performance of the business, and planning for the succession of the CEO. At the same time, the CEO is a close partner in many of these endeavors, sometimes taking the lead. For example, in succession planning, the CEO drives management succession at senior levels and serves as counsel to the board. The CEO's role diminishes as a transition nears, and the board moves toward selecting the next CEO. To minimize confusion about the respective roles of the board and CEO, it's helpful to have an open channel for communication. Effective use of executive sessions is part of the answer. Regularly meeting in executive session, both with and without the CEO, helps reduce the awkwardness that can arise when the board has executive sessions only on an as-needed basis. When the board meets without the CEO, it is best practice to debrief with the CEO immediately. The CEO evaluation also provides an opportunity for the board to assess aspects of the CEO's performance — including succession planning — that the board is ultimately accountable for overseeing.

What is our board succession plan?

In the words of F. William McNabb, Vanguard chairman and CEO, having the right directors on the board "is the single most important factor in good governance. ... Who they are, how they interact and the skills they bring to the table are critical from a long-term value standpoint." Boards should continually consider whether they have the optimum composition, given the company's strategic direction and the current business context. Boards should also establish mechanisms to identify the expertise that will be valuable as the context and strategy change. For example, in an industry that is rapidly consolidating, a board will want to consider whether it has the capability it needs to best oversee multiple acquisitions or the sale of the business in shareholders' best interests. The board of a company with a new first-time CEO may decide it needs someone to serve in a mentoring capacity to the CEO. Regularly reviewing the current composition and any gaps positions the board to take advantage of natural attrition from director departures and retirements. The best boards also forge agreement about the right degree of turnover and the mechanisms to promote board refreshment, including appropriate time frames.

What is our mechanism for evaluating the contributions of individual directors and providing director feedback?

On many boards, the elephant in the room is the performance (or lack thereof) of an individual director. Consensus is growing in support of conducting individual director assessments as part of the board effectiveness assessment — not to grade directors, but to provide constructive feedback that can improve performance. It can be difficult or uncomfortable to raise individual director performance issues, but high-performing boards expect directors to stay engaged and to contribute fully, and are willing to address under-performance. They establish a mechanism for surfacing and addressing issues and use director succession planning to encourage healthy turnover and accountability. They also create an environment that encourages individual directors to think critically about their contributions and the relevance of their skills to the company strategy.

The 8 Biggest Contributors to Board Dysfunction

1 Too much time spent on compliance and other backward-looking reviews at the expense of strategy

2 Lack of trust between the board and CEO

3 Weak or non-existent CEO succession plan

4 Lack of board succession planning

5 Disruptive or disengaged directors

6 Poor decision-making processes

7 Lack of a direct channel to shareholders

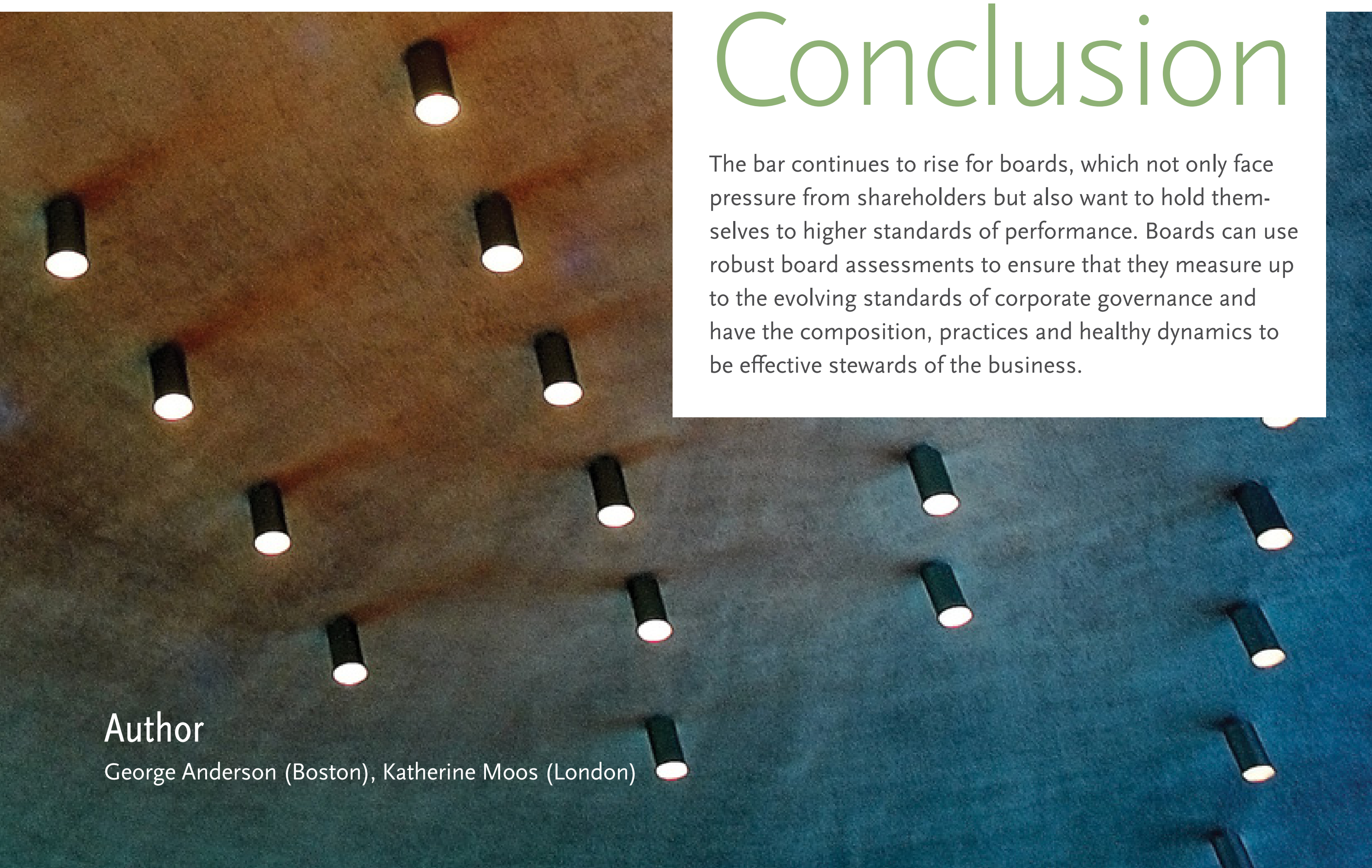
8 Too much board information and material

What is our board culture and how does it contribute to our ability to advise management effectively?

A really good board understands its own culture and how it impacts its decision-making and relationship with management. Despite the growing appreciation for the importance of culture, few directors are able to describe their board culture beyond "collegial" or "engaged." A deeper understanding of the culture of the board — how directors make decisions, handle disagreements, share information and the spirit in which they do these things — can improve the board's ability to advise management and provide appropriate oversight. In a fast-moving, highly dynamic industry, for example, the board needs to learn fast, remain open to alternatives and needs at least some directors with a more agile orientation. Culture can be shaped by influential figures, such as the chair, the CEO, the founder or long-serving directors; structural elements such as the format and conduct of meetings; selection and onboarding of new directors; or external events and the board's response to them. High-performing boards are willing to examine their culture more closely and assess its alignment with the needs of the business.

What processes are in place for engaging with shareholders?

Management is responsible for communicating with investors about the business, but shareholders increasingly want to engage with the board on a range of governance issues, including succession, compensation, risk oversight and other concerns. Often, it's not until after a board has experienced a challenge from shareholders — losing a say-on-pay vote, for example — that it concludes it needs to improve communication with shareholders. The most effective boards stay abreast of how the company is perceived by investors. They identify in advance who should take the lead from the board (whether a committee or individual board leader) in dialogue with shareholders and in responding to investor inquiries. Robust relationships with investors can help the board understand how the company is viewed externally versus competitors and can reduce the chance that the company will be surprised by activists or proxy votes. And when challenges do arise, the board is more likely to have built up a reservoir of understanding and support among large long-term shareholders.



Conclusion

The bar continues to rise for boards, which not only face pressure from shareholders but also want to hold themselves to higher standards of performance. Boards can use robust board assessments to ensure that they measure up to the evolving standards of corporate governance and have the composition, practices and healthy dynamics to be effective stewards of the business.

Author

George Anderson (Boston), Katherine Moos (London)

Getting from *Here* to *There*

Lessons learned from a decade of digital transformation

Transformation is on the agenda of nearly every company. Disruptive technologies and the accelerating pace of change are constantly threatening to undermine legacy businesses. No industry or geography is immune, and even pure-play companies that were among the earliest technology disrupters are being forced to re-evaluate their strategies.

However, some companies have been at this longer than others. Brick-and-mortar retailers continue to battle Amazon by creating and evolving e-commerce strategies. Travel and hospitality companies have adapted to decades of disruption from Expedia, Priceline and other early online travel businesses. Financial services organizations have been disrupted by E*Trade and others for years. The music industry has had to respond to challenges on various fronts — from illegal downloading and sharing to streaming services — while the publishing industry has had to adapt to the growth of digital reading devices and content aggregators.

What experience have these early movers gained that can help others as they undergo their own digital transformation? We spoke with six digital veterans about their experiences: What they did right, what they would do differently, what they learned along the way and how these experiences will inform their future. Based on these discussions, we have identified five key lessons for making faster progress on digital initiatives.

- Articulate a digital strategy that positions technology as a differentiator
- Structure for speed and agility: Challenge the org chart and standard processes
- Lead from the front: The CEO and senior team must champion change
- Inject change-makers and digital influencers throughout the organization
- Create a company culture that nurtures innovation

Business growth is a fragile endeavor. Cultures must constantly shift and leaders must adapt to new threats. Perhaps these lessons will help others avoid some common landmines.

With no playbook to draw on, leaders of companies that made the transformation to digital early embarked on a multi-year journey to transform the business, figuring things out as they went along. What they learned — and what remains true today — is that digital transformation is as much strategic, organizational and cultural as technological.

Articulate a digital strategy that positions technology as a differentiator

Changing consumer expectations is a key driver of digital strategy for many companies, which strive to provide an exceptional — and consistent — customer experience regardless of channel. Without a coherent strategy to guide how new technology is adopted and delivered to the consumer, technology solutions can be hammers in search of nails, and there can be a temptation to grab the "shiny new thing." The right strategy identifies the digital forces that are impacting the company — e-commerce, social media, big data, mobile devices, cybersecurity, the Internet of Things or cloud computing and storage — and addresses the opportunities or threats they represent. For some companies, the opportunity may be to bring products to market faster, gain efficiencies through automation or leverage new platforms for customer acquisition and engagement. Other companies may find their very business model under attack.

The desire to provide a consistent customer experience is spurring initiatives such as Wal-Mart Stores' "One Wal-Mart" and U.K. retailer John Lewis' efforts to build an omnichannel retail experience. These strategies help shape each business' digital identity, provide a vision around which to rally the organization, and influence decisions about culture, processes and IT investment.

"Digital isn't really about the pipes or the mobile device or the connectivity or the cloud or any of that. It's really about the collection of changed expectations, and those are the changed expectations of people, in their roles as consumers or members of the organizations that we're seeking to lead," said Neil M. Ashe, president and CEO of global e-commerce for Wal-Mart Stores.

A bold, well-articulated strategy puts the organization on notice that transformation is coming. Wolfgang Baier, former group CEO of Singapore Post Limited (SingPost), said a bold and clear vision to digitize the business is one of the most important decisions the board and management team have to make. "Initially, people smiled when presented with the e-commerce vision and did not believe it; when they saw how much we invested into pursuing the new area and the new talent joining, they realized that there was no turning back."

Motorola Solutions' "single view of the customer" strategy, articulated in a formal whitepaper, drove changes affecting every part of the company, including culture, talent decisions, organizational structure and, of course, IT investment. "I'm a big believer, as you embark on a transformation, in stepping back, working with the team to state a point of view for the company. We started that exercise by saying, 'Let's throw away the playbook and any preconceived notions about what the company is or is not, and think about how we would transform the company through the application of technology,'" said Eduardo Conrado, executive vice president and chief strategy and innovation officer.

Structure for speed and agility: Challenge the org chart and standard processes

As digital disruption accelerates change, many companies find that their traditional organizational structure and processes are incompatible with the innovation, speed and agility necessary to keep up. Speed is an imperative in a digitally driven world, said Baier. "As leaders, we cannot hesitate to make a decision; we must move quickly, check things out and learn. We need to fail fast, learn from failure and then move on."

In response, companies have moved to streamline their organizational structures and decision-making processes. Brazilian airline GOL moved away from a matrix organizational structure, which mired digital initiatives in lengthy approval processes, and created standalone innovation teams to facilitate faster implementation of new ideas and technology. "We had some cases of innovative projects that weren't released quickly due to the procedures of the matrix organization structure of the company," said CEO Paulo Kakinoff. With its more agile structure, GOL can move more quickly. "The distance between an idea and its digital realization is smaller."

Telecommunications company Axiata Digital Services re-engineered its processes to improve its agility and speed. "A nine-stage gate approval process for major decisions and five-page job applications were just too slow and cumbersome." Today, "if we have a great idea, we can test and launch quickly," said CEO Mohd Khairil Abdullah.

Motorola Solutions has adopted a two-speed approach, accelerating the delivery of customer-facing initiatives through the use of a faster, agile methodology, but maintaining the waterfall approach for back-office technology development projects. This approach drives creativity and speed, while offering stability to those parts of the organization that need it.

"Some paradigms must be broken, like the matrix organization structure for the approval of innovative digital projects associated with the waterfall development model. These are incompatible with the concept of disruptive innovation," Kakinoff said.

Also incompatible with innovation are functional and business silos that get in the way of collaboration, or communication protocols that slow decision-making. Digital at its core connects the customer and company, and this requires robust connectivity between functions within an organization. Functions and business units must work together as never before to plan and execute programs and remove barriers to information- and data-sharing.

Lead from the front: The CEO and senior team must champion change

For digital transformation to take hold, senior executives must lead and model change. "The CEO needs to be the chief digital officer of the company," argues Ashe. "You can't outsource it. It's not like a channel or another line of business. It's like water; it permeates the organization everywhere. How do you think holistically about your customer proposition, your associate population? How do you manage and lead? How do your HR systems support change? The deeper we get into it, the more everything gets exposed."

CEOs who "get it" spend time with digital teams. They pay attention to digital trends. They're curious. They're empathetic, because change is hard on the organization, and have the ability to bring people along on the transformational journey. They engage people at all levels of the organization on the need for change, and are willing to admit what they know and don't know.

"All initiatives for innovation must always be sponsored by the C-level leaders of the company," said Kakinoff. "This is the best way to foster new ideas, regardless of whether the agent of transformation is an old or new employee in the company. We encourage our leaders to make decisions and take risks."

Beyond being a visible champion for transformation, CEOs must change the way they assess culture and current leaders and hire new executives in order to drive organizational change. The first step is to define the elements of culture that must change to support the transformation agenda. Because the CEO and other top leaders have a disproportionate influence on the culture through what they emphasize and the examples they set, the CEO should prioritize the hiring and promotion of leaders who will serve as catalysts for change. These leaders should possess the style preferences of the ideal culture, but also have the influencing skills to model and bring along others in the organization.

Without the commitment and support of senior leaders, digital transformation is doomed to fail. So, CEOs should move quickly to make a change when a leader can't or won't support transformation initiatives. As one executive told us, a leader who does not have a change mindset may be more damaging to the transformation agenda than having no leader at all.

Inject change-makers and digital influencers throughout the organization

What skills are needed more broadly to lead change in a digital environment? Legacy companies have learned that a transformational mindset is a must, as is the ability to nurture innovation and make fast, nimble decisions. "I always hire based on a person having a transformational mindset. They need to have courage, digital understanding and be able to manage a P&L. We need leaders who can play the incubator rather than just the expert role," said Baier. And, at Wal-Mart, "digital is creating the need for a new type of manager, one who is able to work at this pace of change," said Ashe. Hiring innovators is far more important than industry experience. Innovation, by definition, drives first-to-market changes, so finding talent within the industry who has already driven this change is an oxymoron; companies must look outside to find the disruptor.

Communication skills are a key part of leading change and building a shared understanding of the customer. Paul Coby, IT director for John Lewis, notes that, despite the explosive growth of online shopping and the omnichannel revolution, the basics of his business have remained the same: "What you're trying to do is understand the customer's journey," which has always been the task of company leadership.

Injecting fresh skills into the organization through the infusion of new talent can serve as a spark for digital transformation. According to Conrado, Motorola Solutions evolved quickly after making the decision to bring on a new CIO with a different set of experiences, positioning IT teams to become partners in strategic conversations about the business. Similarly, Axiata began to evolve after hiring a new head of finance and creating teams devoted to innovation and strategy.

In addition to recruiting qualified leaders from outside their organizations, companies also must be able to identify potential leaders within. GOL actively seeks new leadership internally. “We observe initiatives aimed at digital and identify who are the agents of change within our company,” said Kakinoff. Creating teams with diverse skill-sets and moving people around the organization can expose more people to new ideas and get people working together on digital initiatives.

Create a company culture that nurtures innovation

Disruption, speed and agility are ingrained in the DNA of technology startups and other companies with roots in digital technologies. But for large companies with legacy non-digital businesses, whose success has come from optimizing a stable and efficient process to deliver incremental results, developing these traits requires a concerted effort by top leaders, moving people and hiring talent from the outside the organization to build the right culture. Resistance to the adoption of new ideas is a major impediment to success of digital initiatives, leaders agreed. Legacy companies have learned that culture can be an obstacle to keeping pace with change, and that a company culture that fosters and rewards creativity and risk-taking is necessary for innovation.

Encouraging innovation means giving people the freedom to try out new and revolutionary ideas — and the freedom to fail. At Axiata, this has involved rewarding new ideas, regardless of outcome. “We changed performance management to reward people who fail as long as they learn something,” said Abdullah. At the highest levels, the board gave leadership the freedom to experiment and take risks that might not pay off right away. According to Abdullah, “I was able to say to my group CFO that I will deliver you NOP after tax for the next few years — it’s just that in this case NOP meant ‘negative operating profit’ instead of ‘net operating profit!’”

Before launching its omnichannel shopping system, leaders at John Lewis had to overcome cultural resistance to change within the company. “People within the organization were thinking, ‘Why on earth would people go online if they could buy things in a store?’ You can’t try them on. You can’t see them.” Overcoming this resistance required a paradigm shift that came from the top down. GOL had to overcome similar internal resistance to its innovative paperless ticketing system. “The resistance to the adoption of new ideas and implementation of new technologies is one of the main impediments to success,” said Kakinoff. Its digital strategy a success, the company now needs to find ways to maintain the startup culture as the business scales ever larger.

How can companies evolve their cultures to nurture innovation? At SingPost, the leadership was able to transform the company culture quickly from the top down. "The board and management had a strong vision, five core values that include total customer-centricity and a one-team approach," said Baier. Communication was crucial to getting everyone on board, and worth the investment of time. "The biggest and most lasting change is that the organization has a can-do mindset. People have embraced the idea that they can really change things."

Ashe agreed that communication is essential. "You have to be able to find a way to find a common ground and build a shared understanding in order to achieve a common objective."

As part of its transformation, Motorola Solutions leaders concluded that they needed to invest in new collaborative technologies to match the culture they wanted to build. "We defined what we are and what we aren't, and that led to a redesign of all of our systems. We said, 'We're a mobile-first company. We're video first. We don't just collaborate on email, we're social-centric. We're going to minimize conference calls,'" said Conrado. "That led us to wall-to-wall wireless coverage, optimized for voice, data and video inside the company. We went 100 percent voice-over-IP in North America. We moved to video as our primary mode of communication in the company and put 600 video rooms in the company and ability to communicate via video from every employee laptop."

Finally, accept that transformation is an ongoing process

The experience of early movers suggests that, when it comes to digital transformation, questions about leadership, organizational structure and culture can be some of the most challenging — and critical to get right. Those organizations that are most likely to be successful place those issues front and center; they articulate a bold strategy; challenge organizational structures and processes that get in the way of change; have strong CEO and management team ownership of the transformation agenda; get the talent mix right; and build a culture that supports innovation and change.

But experience also shows that simply mastering the moment will not be successful over time, as technology and human behavior rapidly evolve. Digital transformation is not a "project" with a finite end. New disruptive technologies will emerge and customer behavior will continue to change, so organizations must be able to evolve and find new ways of doing business.

Success over time requires ongoing attention to leadership, processes and culture to ensure they continue to support the digital business strategy. Companies also should take a hard look at their talent management processes. The war for talent is real, and organizations that aren't able to recruit the best and the brightest are doomed to failure. The best organizations adapt their human resources practices to shorten recruiting time, think creatively about compensation and organizational structure, and continually assess the elements of culture that support and impede digital transformation.

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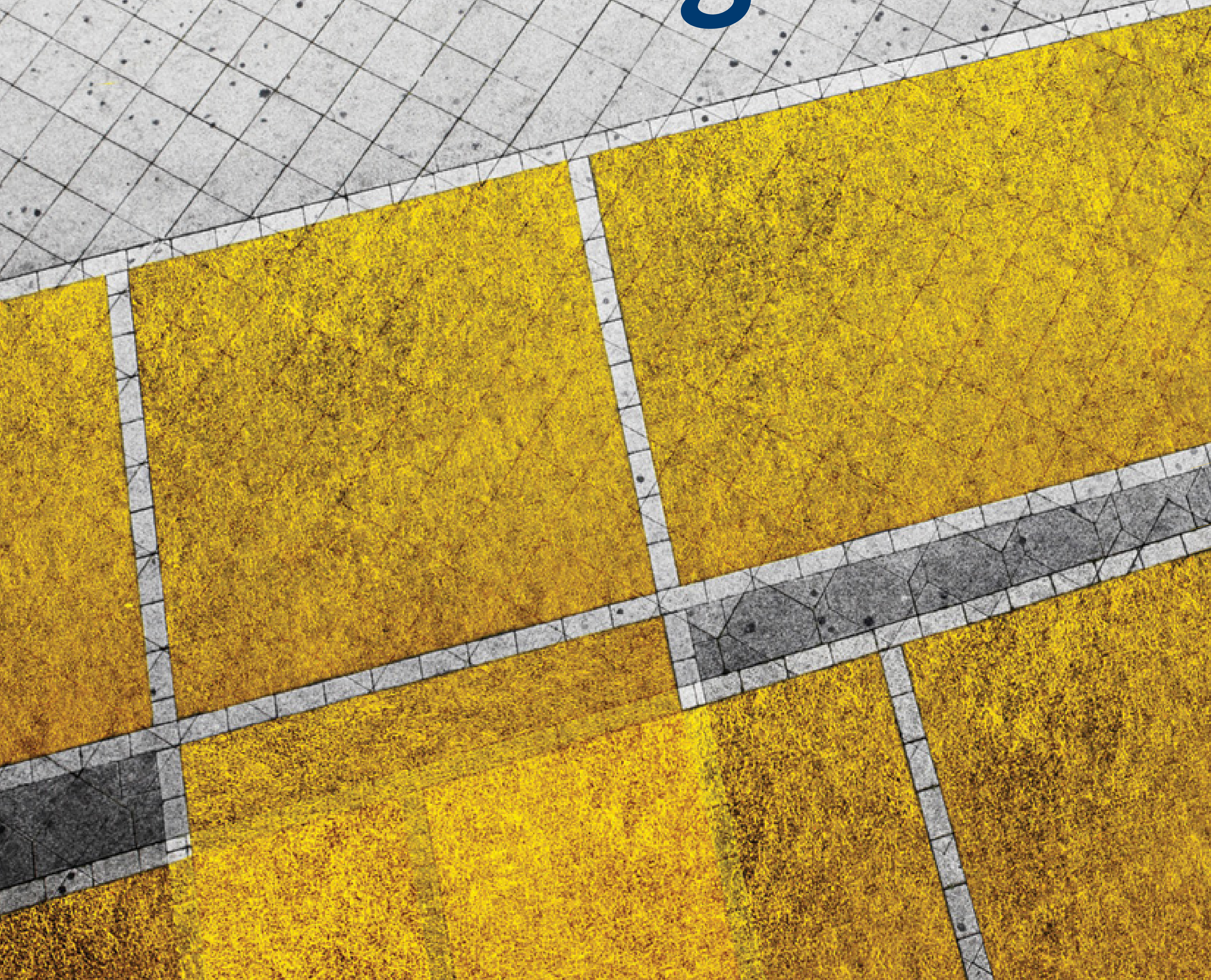
Why Senior Leaders Need to Rethink Learning Intelligence



Today's environment of rapid change and disruption demands executives who learn fast and apply that learning in order to succeed. While learning is a commonly discussed topic at many organizations, most theories and constructs do not provide a pragmatic description of the kind of learning that makes senior leaders successful — and could potentially predict their future performance. Most executives do not reach the top levels of an organization without being able to swiftly grasp vast amounts of material. But how strongly does this type of learning inform an executive's success, and, by extension, influence the organization's performance?

We have found that the characteristic of learning intelligence has a great impact on executive success by enabling leaders to respond appropriately to situations, and thus produce better results for the business. Learning intelligence is more than agility or the ability to absorb and apply new information. It is the ability to:

- look critically at one's own thinking, unconscious biases and actions;
- be open to, actively seek out and listen to new and contrasting perspectives;
- recognize how another viewpoint is better;
- change one's own perspective and actions in response (e.g., whether to abandon a struggling initiative despite significant sunk costs or to pursue new, untested avenues for growth); and
- know when to stand one's ground even in the face of contrary opinions.

Yet, most organizations cannot accurately identify and develop learning intelligence because they do not have the tools to precisely evaluate it. Often, organizations rely on self-reporting tools, which inherently lack objectivity. Or they focus exclusively on results rather than the underlying thinking that led to them — a much better indicator of future performance, but much more difficult to assess.

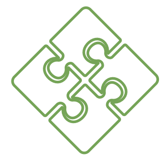
Context also matters. The impact of learning intelligence varies depending on the organization's unique challenges and culture. For example, leaders with high learning intelligence are critical when the organization's culture needs to change, especially if that culture does not prioritize learning. We will explore some common assumptions about learning, how learning intelligence can be recognized and assessed, and how it can be cultivated.

Learning intelligence: What it’s not

There are several common assumptions about what good learners “look like,” but they often focus on skill-sets or process rather than the full picture of what learning intelligence comprises. Learning intelligence is much more comprehensive and multi-faceted. Consider the following:

Smart people learn better.

Not all forms of intelligence guarantee a strong capacity to learn and adapt. Processing information well does not mean someone can act on that information and change his or her behavior. For example, the CEO of a financial institution graduated at the top of his class and is considered one of the world’s preeminent experts on banking and securities. Yet, he has not become as well-versed in the digital transformation of financial services as his industry counterparts. At the same time, those who can recognize shifting industry dynamics or analyze a situation and identify weaknesses are not necessarily good at learning from those analyses or acting on them. Many engineering leaders are taught to dissect and deconstruct projects and issues, but the ability to critique is not the same as being able to learn and adapt.



The more expertise you have, the better you are at learning.

Expertise is acquired through learning, so it stands to reason that those who have learned successfully in the past will continue to learn. However, some falsely believe their past expertise, however great, carries through to the future, regardless of changing times or the novelty of the situation. Tom Wujec, Autodesk fellow and global leader in 3-D design, demonstrates this principle in “The Marshmallow Challenge” design exercise: Build the tallest freestanding structure with sticks of spaghetti, tape, string and one marshmallow. Business school graduates were among the worst performers. Kindergartners, unencumbered by previous experiences and biases, performed better than most adults. The best problem-solvers and learners draw on their expertise while retaining a beginner’s outlook, which is characterized by openness and inquisitiveness. Additionally, people can acquire experiences without learning from them. Consider a senior executive who has lived in 10 countries in 10 years. Upon first glance, this experience might indicate she is culturally agile, but she also may have been unable to learn and adapt well enough to successfully live in a different culture more than a single year.

Intellectually curious, open people are good learners.

The CMO of a travel company is an avid reader of a wide range of topics, from behavioral economics to Renaissance art. During visits to the organization’s various offices, she makes a point of scheduling a team outing to an off-the-beaten-path attraction to learn how locals experience their cities. The CMO’s curiosity denotes a broad, cursory interest in a variety of subjects whereas learning is directed and more enduring, culminating in a change of behavior. Some can mistake focused information-gathering for intellectual curiosity — the HR leader of one global consumer products company touted its executives as being extremely intellectually curious but, in reality, they were simply dedicated to obtaining only the information they needed to complete a project, without any lasting alteration of their actions. Openness to learning is also important, but not enough. A CEO succession candidate believes that his global healthcare company must change dramatically if it is going to succeed in an evolving industry. He recognizes that the organization’s culture of risk aversion will stifle much-needed innovation. He has strong convictions about the direction the organization should take and knows he will need to strengthen his transformational leadership skills if he lands the top job. The candidate’s willingness to learn is a preference, not a capability.

While some individuals may be equally strong in each area, most people are stronger in one element or another. Most commonly, executives are strongest in openness, followed by honest contrast and then self-adjustment. You cannot adjust accurately without recognizing a clear and accurate contrast; and, in turn, you cannot identify a clear and accurate contrast without being open to new views.

When confronted with ideas or answers different from their own, leaders who are low in openness, honest contrast and self-adjustment dismiss them and often show no evidence of even processing them. They deny that other answers are better without a reason and are so emotionally invested in their own ideas that they ignore others. For example, an executive who scored low in ExI but had a track record of quick promotions vehemently disagreed with the findings of his assessment without asking why, demonstrating a weakness in openness and self-evaluation. Another executive helped lead the development of a product that failed on a massive scale, largely because it was based on a misperception of the consumer market. However, in later discussions, he cited this project as a key accomplishment despite clear facts pointing to the contrary. Leaders who score higher recognize that the perfect answer does not exist and therefore always ask for more answers, readily identifying positives and negatives in their own and other answers in order to build even better answers. They also greet stronger solutions with positive emotions and view them as opportunities. Putting these elements into practice, a CEO succession candidate we worked with would actively solicit constructive criticism on his leadership and communication skills, and then work with an executive coach to apply the feedback in his day-to-day interactions.

Recognizing and assessing learning intelligence

Learning intelligence is a key part of Executive Intelligence, which is the unique set of capabilities that enables executives to perform at the highest level. Both have a tangible impact on business performance. Companies with higher-scoring CEOs perform better: Spencer Stuart's proprietary methodology of measuring Executive Intelligence (ExI®) reveals that the CEO's score at time of appointment predicts 16 percent of the variation in profit performance two years later. Our analysis also shows that there is a correlation between higher revenues at organizations with senior leaders who are high in learning intelligence.

The elements that comprise learning intelligence are:

> **Openness**: The acceptance of differing or contrary opinions and perspectives

> **Honest Contrast**: The ability to identify differences between one's own perspective and those of others, and recognize the ways in which another's opinion may be better

> **Self-Adjustment**: The ability to shift one's own perspective, positively accept another's and treat it as an opportunity, and actively pursue and apply constructive criticism

The elements that comprise learning intelligence are:

> > Openness
> > Honest Contrast
> > Self-Adjustment

While it may seem counterintuitive, too much learning intelligence may not be a good thing. When leaders are extremely high in openness, honest contrast and self-adjustment, they can be overly willing to change their own points of view, unable to defend their stances and could be easily swayed by someone skilled at persuasion. This is where the other dimensions of Executive Intelligence and developed leadership capabilities are helpful. Our data shows that possessing a strong intellect combined with learning intelligence predicts executive growth more than either one alone. A developed sense of executive judgment based on experience gives leaders a better-informed view of the world to draw upon when making decisions.

Avoiding the CEO feedback trap

CEOs must be especially vigilant about maintaining and developing their openness, honest contrast and self-adjustment capabilities by actively seeking out alternative perspectives and establishing pipelines of new information. Chief executives tend to be insulated from ideas and information that contradict their thinking, either because they are farther away from the sources of new information or because others are more guarded about sharing potentially contradictory views. The new CEO of a financial institution was initially skeptical that the introverts on his team would avoid challenging him because of his extroverted personality and powerful influencing skills. Months later, he admitted he was wrong and adapted his behavior: He communicated to his team that in order to ensure everyone's voice was heard, he would first invite other perspectives before offering his own.

Another CEO deliberately hired a chief operating officer with a vastly different personality from his own so that his views would be tested. He had a conference room built between their offices as a forum to address conflict, with the rule that either could call the other in and neither would exit until they found a solution both agreed upon. His high learning intelligence imbued the entire organization. Although the broader sector tended to fluctuate, the company cycled more gently than others because it was able to recognize changes in the market and proactively shift into either efficiency or growth mode. The CEO also established a center with other companies in the region to foster mutual learning among executives about quality management.

CEOs with high learning intelligence also tend to consider failures as sources of success, exemplified by the legendary response of former IBM chairman and CEO Thomas Watson when asked if he was going to fire an employee who made a costly mistake: "No ... I just spent $600,000 training him. Why would I want somebody to hire his experience?"

How learning intelligence can be enhanced

Building learning intelligence across the organization starts with assessing and hiring executives with the trait, who, in turn, model learning behavior for others across the enterprise. In addition, these individuals create and are members of learning teams, which help foster a learning-oriented organizational culture. These efforts tend to be mutually reinforcing and, thus, present the greatest benefit when they take place at multiple levels.

At the individual level

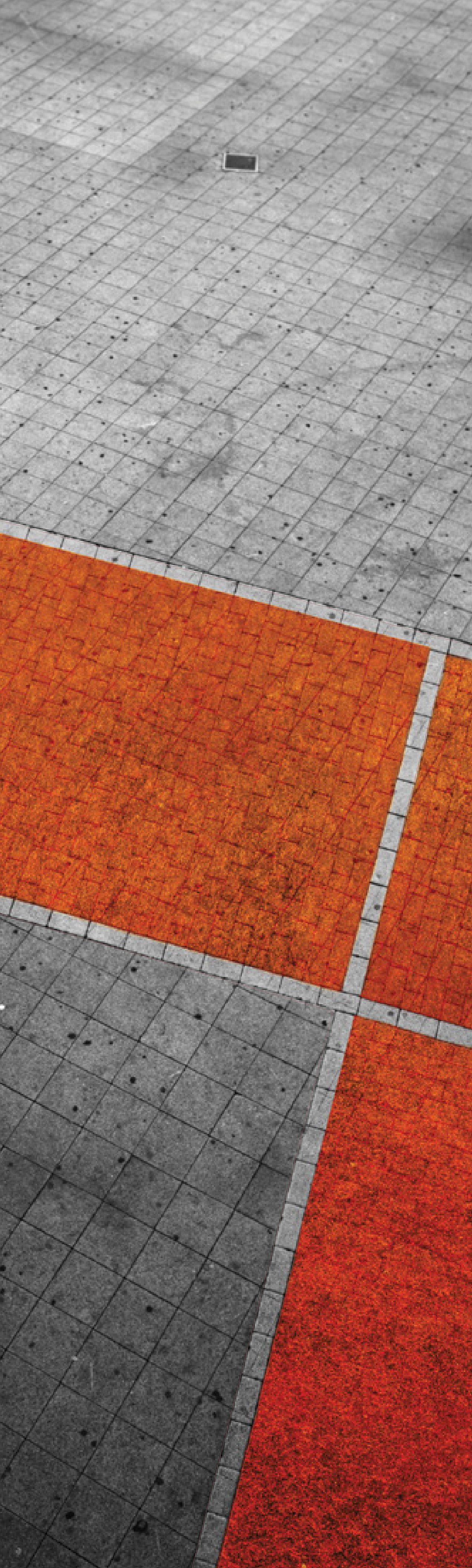
A combination of humility and inquisitiveness is not only key for effective communication, it is also a prerequisite for improving learning intelligence, noted Edgar Schein, professor emeritus at the MIT Sloan School of Management, in his book *Humble Inquiry*. An individual with learning intelligence does not need to be the smartest person in the room. To build their own learning intelligence, leaders can proactively seek out assessments and listen to constructive criticism in order to alert them to their blind spots, enabling them to become more self-aware going forward. Finding a coach who understands the different facets of Executive Intelligence can also be beneficial. For individuals who are already high in learning intelligence, conducting anonymous 360-degree reviews on an ongoing basis can ensure that they maintain their self-awareness and aren't falling victim to "the emperor's new clothes" syndrome. Leaders who learn from their teams also lead more effectively because they are engaging others as part of the learning process.

At the team and organizational level

In an age of big data and rapid change, senior leaders must rely on the teams around them to help distinguish what is of strategic importance from "the noise." While shifts at the organizational level are time-intensive, companies will see fast benefits by establishing strong learning teams — multidisciplinary groups assembled to teach and learn from each other. With its smaller scale, a team-learning process can be created over the course of a few months. Learning teams should spur networking and leverage the talents and knowledge of their members, making it beneficial to have representation from a variety of functions and backgrounds. The best learning teams are able to collectively problem solve, experiment and enact best practices based on their findings. They also proactively share information with and listen to one other, supported by guidelines that ensure information is offered and accepted respectfully. Strong learning teams can also acknowledge collectively or as individuals when they do not know enough about an issue without negative impact. They may have an acute awareness of whose knowledge is deeper in a given area and reflect that in discussions.

Organizational culture and structure are also crucial in nurturing learning intelligence. Organizations that do this well place leaders in situations where they are forced to learn, such as a new type of assignment, and then give them tools to help them learn. Learning-oriented organizations tend to have a systematic approach and infrastructure, with clear definition of roles and an environment that encourages the informal interactions that often lead to mutual learning. Organizations can create an environment that is more conducive to learning by examining people's reactions: For example, is risk-taking rewarded or punished? Spaces for tacit learning — in calendars, in performance goals and in emotions — further build learning intelligence throughout the organization.

Additionally, regular assessments and the creation of feedback loops within peer groups, the surrounding team and 360-degree relationships, including board members, allow everyone to learn from both successes and failures. Feedback should help the individual understand that applying a different decision-making process is not an arbitrary matter of preference, but can help him or her be successful. Organizations benefit from hiring leaders with high learning intelligence who can serve as an example for the entire enterprise. CEOs have the opportunity to use their decision-making power to make these capabilities come alive and shift the culture. However, senior leaders need realistic expectations: Changing the culture can be a slow process, albeit one with long-term benefits.



Conclusion

The understanding of how people learn and its role in executive and organizational performance will undoubtedly continue to evolve. We have found that senior leaders with high learning intelligence, strong learning teams and learning-oriented organizational cultures are essential in today's rapidly changing environment. Simply absorbing information is not enough; unconscious biases and staunch adherence to one's own ideas can obscure better, growth-producing solutions. Companies that are able to bypass common misconceptions in order to accurately identify and recruit leaders with learning intelligence, as well as build it at every level of the organization, stand at a distinct advantage. Learning intelligence enables senior leaders to make the best possible decisions — and deliver better results for the entire business.

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Can They Make the Leap?

What It Takes to Get to — and Succeed in — the Most Senior Functional Roles

What combination of leadership and technical capabilities, experience and aptitudes defines the highest-performing C-suite leaders? It's a question that CEOs wrestle with as they build their teams and think about the succession of top-team roles, and one that aspiring leaders consider when thinking about their careers.

One thing is certain: the demands on the top functional leaders continue to grow. With businesses operating in an environment of sustained uncertainty, intense competition and heightened expectations from employees, investors and other stakeholders, CEOs rely on top-team leaders to navigate unprecedented market complexity, risk and the rapid pace of change. Increasingly, achieving the strategic objectives of the business requires that functional and business leaders collaborate in new ways to plan and execute key initiatives and remove barriers to change. Senior functional leaders today also are more likely to engage with the board of directors, having to anticipate directors' concerns and perspectives on strategic issues.

These leaders can have a profound impact on the business. Those who excel are able to articulate a sound strategy and put in place the team, structure and processes necessary to actualize plans and achieve key objectives. Less effective leaders might get just part of the equation right, for example, helping to define the right strategy but failing to bring it to life for the organization, or they may be skilled at execution but unable to define a new strategy.

Selecting the right functional leaders today and ensuring that the organization is developing the next generation is all the more challenging for one important reason: The nature and scope of top functional roles — whether in finance, marketing, human resources, information technology, legal or supply chain — are markedly different than the roles reporting to these leaders.

The critical consideration when assessing next-generation functional leaders, then, is, "Can they make the leap?"

Making an impact: What we know about high-performing C-suite leaders

The ability to assess whether executives can make the leap to senior leadership roles is critical to the health of the business: Making the right leadership choices matters, especially at the most senior levels. Consider a couple of real-life examples:

Based on experience alone, the executive selected as the new chief human resources officer (CHRO) of a $50 billion technology company may not have seemed to be an obvious choice. She had not been a CHRO before, even at a smaller company, so therefore had not had much previous exposure to the board or the full breadth of HR issues. Nevertheless, she understood the culture, knew the business and was well-respected in the organization. In her assessment, she displayed exceptional ability in conceptual thinking and in reading complex organizational and people dynamics; she understood individuals' underlying agendas and could see the political dynamics at play in a situation. She leveraged these skills to help build alignment around key issues and kept everyone working effectively together. Colleagues would go to her for advice because she had something valuable to say. Having quickly earned respect and credibility with the board, CEO and management team, she had a big early impact on the business, especially on CEO succession planning — a place where CHROs can make a big difference in the organization or be sidelined when they lack influence with the board and CEO.

Conversely, having the right expertise on paper is no guarantee that an executive will have an impact on the business. A new chief information officer (CIO) hired to lead the digital transformation for a large industrial business had previous experience as a CIO and exceptional strategic thinking skills. He had the experience, knowledge and capabilities to do the job. And while he could inspire colleagues with his vision for the business, he lacked the ability to effectively influence and collaborate with other executives. Colleagues felt that he talked down to them and signaled that he was smarter than everyone else. The execution of the strategy failed under him because he couldn't build support for transformation initiatives. For the transformation to be successful, the company needed someone able to translate the vision for different roles and business units and have the patience to bring people along.

Why are some executives able to have such a positive impact on an organization, while others cannot? The specific business context, how well the individual fits the requirements of the role and the organizational culture, and the clarity of the objectives for the role all contribute to an individual's success. But we have found that the C-level leaders who are most able to make a difference in their organizations have well-developed leadership capabilities and the ability to adapt and grow with the job and the business.

Our research has identified the critical leadership capabilities that have the greatest influence on executive performance. For top functional leaders, three capabilities tend to be most important:

> **Collaborating and influencing** — identifying and building relationships with stakeholders and facilitating dialogue to forge consensus and collectively achieve objectives

> **Leading people** — managing, empowering and leading people, delegating roles and projects

> **Building capability** — gaining an understanding of individuals' capabilities and systematically developing people

In a matrixed business, for example, the ability to collaborate and influence the CEO and other management team leaders is a difference maker. It is far more difficult to influence and collaborate with executives outside of one's own functional domain who don't share the same language or perspective on the business. Executives who excel in this area have a strong understanding of the drivers of the business and find ways to engage and build partnerships with their colleagues. These executives also are most likely to end up in the CEO's inner cabinet; they become a counselor to the CEO and have a disproportionate impact on the senior team, the strategy and the broader organization.

Senior functional leaders who lack the ability to collaborate and influence risk becoming pigeonholed — the human resources leader who is stuck as the "people" person, the CIO as the "technology" person or the CFO who is regarded as the "accountant." Indeed, interviews with companies revealed that a primary reason for the failure of a new executive in the first 12 to 18 months is the inability to influence and collaborate across functions and business units.

Similarly, a strong capability in building teams is a cornerstone for success in top functional leadership roles. Among senior leaders who were highly successful in their first 18 months, the ability to build and empower highly capable teams was a primary reason. These executives place the right people in the right roles, making tough decisions when necessary. They pay attention to culture, individual roles and responsibilities, and identify the skill gaps and opportunities for improvement. They are able to create a team of highly talented people who work together and are more than the sum of their parts. This is important because many first-time functional leaders do not have previous experience managing large, multi-layered teams.

Succession planning: The capability gap

Despite the importance of these executive capabilities, hundreds of assessments of chief functional leaders and their direct reports reveal a wide capability gap between them. Direct reports of the top functional executives score significantly lower on the six core capabilities critical to success than the functional leaders themselves, the equivalent to three to four years of development. Promoting someone into a senior functional leadership role before they are ready creates a sort of "value gap," where the person is not able to have the full impact within their functional purview — or more broadly. This can happen because they are less skilled at influencing, lack knowledge about the drivers of the business or other functional areas, haven't been exposed to enough of the business, or fail to build and empower a strong team. Without the domain expertise and experience in the role, they may lack the confidence to engage in debate about the critical issues facing the business, limiting their ability to be a true adviser to the CEO and management team.

Promoting someone into a senior functional leadership role before they are ready creates a sort of "value gap," where the person is not able to have the full impact within their functional purview — or more broadly.

How can organizations get functional leaders the development time they need, short of placing them in the role? It's a fundamental challenge for companies, and one that can be difficult to solve. In many functions, the roles under the top leader are often highly specialized, making it more difficult to move within the function to gain experience. Many functional roles do not involve managing large teams of people or require much collaboration, so executives are not assessed on these capabilities as they move up in the organization.

Still, job rotation, P&L experience, exposure to other functional areas and business units do help prepare leaders for larger and more complex roles. When looking at business unit executives, who tend to have early P&L responsibility and broader exposure to the functions even at a regional level, we see a smaller capability gap between the top leader and his or her direct reports than the gap between functional leaders and their direct reports. These experiences develop leadership capabilities, building knowledge of the business and how different functions affect the business. The organizations that are most adept at developing succession-ready functional leaders identify high potentials early, so they have the most options for moving people around. When direct P&L experience is difficult to provide, it can be helpful to rotate high potential executives in functional roles within a business unit.

Senior functional leaders who lack the ability to collaborate and influence risk becoming pigeonholed — the human resources leader who is stuck as the "people" person, the CIO as the "technology" person or the CFO who is regarded as the "accountant."

Closing the gap: What does it take?

Demonstrated capabilities represent just part of the story when it comes to assessing executives for top functional roles. Knowledge and capabilities are not enough to predict how a senior leader might do in the most senior-level roles, which are more complex and ambiguous. As executives move higher in the organization, past knowledge and relationships become less effective tools for accomplishing business objectives and navigating the challenges they will encounter. The context changes, and executives must make sense of a much wider set of issues with less concrete information, and then conceptualize a clear plan, inspiring, engaging and motivating a large organization to act. Furthermore, no succession candidate is 100 percent ready for a senior functional leadership role, regardless of his or her preparation. There will be gaps in experience and knowledge.

For these reasons, it is important to understand an individual's ability to stretch beyond his or her current capabilities to continue to grow and change with the job and the company. We call this Executive Intelligence.

Executive Intelligence assessments measure five key dimensions: business intelligence, contextual intelligence, interpersonal intelligence, learning intelligence and conceptual intelligence. Executives with strong business intelligence are able to apply analytical judgment in complex and ambiguous situations. An executive with a high degree of contextual intelligence is able to consider issues from an organizational or social perspective, while someone with highly developed interpersonal intelligence has the ability to read and respond to others' emotional states so they can have constructive interactions. Conceptual intelligence enables leaders to produce big-picture insights from complex and disparate information. Finally, a high degree of learning intelligence allows individuals to change how they think and act in light of new information.

Executives with high Executive Intelligence scores have far more room to grow. Over time, they will bypass others who don't score as well. High ExI scores also correlate with faster executive promotions. An analysis of more than 700 CEOs, managing directors, COOs and CFOs globally found that executives with high ExI scores were promoted 22 percent faster than executives with low ExI scores. In other words, these executives were promoted one year earlier on average than those with lower scores.

Furthermore, new functional leaders with high ExI scores also are likely to be more effective advisers to the CEO and management team early in their tenure, before they have had the time to develop the knowledge base and domain expertise for their roles. These executives approach issues with clear structured thinking and are able to communicate succinctly and effectively, making them a strong partner in the debate and discussion of critical business issues.

Conclusion

Selecting the right leaders for senior functional roles is challenging because the nature and scope of these positions are markedly different than the roles reporting to them. By recognizing the capability gap, organizations can take concrete measures to build the skills of functional leaders to better prepare them for the most senior roles. But no new leader will be completely ready for all the demands of a top management position, so it is important to understand their potential to grow with the position and provide support for new leaders in the form of a strong team or an external coach.

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Leadership Development *Yesterday* and *Today*

Approaches that Work

Decades ago, formal training and development models, exemplified at the time by those at IBM, GE and Unilever, thrived and produced outstanding leaders who ran highly successful businesses. These organizations hired hundreds of graduates a year, who were rotated through different jobs, functions and geographies and sent through executive training. Twenty-five years later, if all went well, some portion of them became senior executives.

Much has changed since the heyday of programs like those, which, of course, have evolved over time. Several factors have influenced the evolution of leadership development:

- **Pace.** The pace of change is faster. Traditional leadership development and supply systems were designed for a world where change happened on a more predictable, linear course than the exponential change we see today. With market and competitive conditions changing so rapidly, how effective can long-lead development approaches be?
- **Mobility.** Careers in general are more mobile and one of the tradeoffs is that individuals have had to assume greater responsibility for their own personal development.
- **Culture.** Appreciation has grown for the important role of corporate culture in guiding the everyday decisions and behaviors of employees that contribute to — or detract from — business performance. What's the role of leaders in shaping the culture, and how are leaders influenced by the organizational culture that surrounds them?
- **Organization.** Strict hierarchies have given way to flatter, more dispersed and flexible (and often global) organizations at most companies, while the emergence of "boss-less" or self-management structures at several high-profile companies have some questioning the relevance of traditional notions of leadership.
- **New models.** Of course, companies born in the computer era like Apple and Google have developed their own approaches to talent and leadership development to fit their cultures and business models, in some cases creating their own versions of the corporate university.

In light of these shifts, how has leadership development evolved, and what does it mean to be a leader today?

We would argue that a leader's ability to help the organization adapt to a changing business context is especially important today. CEOs and other senior leaders always have had to scan the external environment for forces that could affect the business and translate those risks and opportunities into strategy. Today, given the dynamism of markets and competition, organizations must respond at a faster pace, requiring leaders who are able to quickly build new organizational capabilities and create a culture that enables a diverse, global workforce to change and adapt to new business objectives.

"The point where the past and the future come together is leadership," according to Sandy Ogg, a former operating partner in Blackstone's Private Equity Group and former chief human resources officer for Unilever who founded executive advisory firm CEO.works. "Leaders have to help bring strategy and culture together. The role of leaders in an exponentially changing world is to bring people with them."

Not surprisingly, no single, prevailing model has emerged for developing leaders with the breadth of knowledge, skills and experience that top leaders require. To explore how leadership development has evolved, we spoke with several accomplished thinkers and experienced practitioners in leadership and executive development. What emerged were four critical drivers of the most effective leadership development approaches today.

1

CEO ownership and participation

Though General Electric's management development institute in Crotonville, N.Y., opened in the mid-1950s and continuously evolved, the institute emerged as a critical tool for promoting business and cultural change under CEO Jack Welch. Welch invested in Crotonville and devoted significant time to participating in programs there, which was renowned for producing top leadership talent.

"Leadership development programs are only as good as the CEO wants them to be," says Bill Conaty, GE's most senior human resources leader for nearly 15 years and now an adviser on talent issues for private equity firm Clayton Dubilier & Rice. "If a CEO really believes in leadership development initiatives, then the rest of the organization has to step up and make it happen. If the CEO is not really supportive and doesn't serve as a visible role model, the rest of the organization fakes it and these programs eventually fall off the cliff."

Leadership coach Marshall Goldsmith tells the CEOs he works with that they must do more than support talent development initiatives, they must model the behaviors that they want other leaders to embrace.

"What I always tell CEOs is, 'If you want everybody else to do this, you go first. Let them watch you do it. Before you start preaching to everybody else, let them see that you're serious about this and you're doing it yourself,'" Goldsmith says. "After that, then they can begin to address the development of the next level of management so that they're also role models at their level, ultimately spinning it out in a larger sense so the whole company is going in the same direction."

Defining and measuring leadership success

A failing of many leadership development programs is that they don't measure whether executives have actually become better leaders, Goldsmith argues. "What typically gets evaluated in a leadership development program? The speakers, the lunch that was served, the room where the program was held. What almost never gets evaluated is the leaders!"

Goldsmith co-authored a study of leadership development programs in eight major corporations that employed a variety of development methodologies, including off-site training, coaching, classroom-based training and on-the-job interaction. The companies went beyond measuring "participant happiness" at the end of a program and instead measured the perceived increase in leadership effectiveness of participants over time in the eyes of their co-workers and stakeholders. Regardless of the training method, the executives who showed the most improvement were those who discussed their improvement priorities with co-workers, and then regularly followed up with these co-workers. Leaders who did not pursue ongoing feedback from colleagues showed improvement that barely exceeded random chance, the study found.

Measuring leadership performance was central to Ogg's work at Blackstone. After joining the firm in 2011, he set out to improve the firm's track record of hiring for senior roles, especially CEOs of its portfolio companies. In addition to re-engineering the hiring process to be more evidenced-based — improving the success rate of their selections — he began to define the leadership activities that led to higher portfolio company returns and to track what he calls the "return on a change in leadership" and the "speed to value" of new leaders.

"What we looked at was, does the job deliver what we expect it to deliver with this person in it? There is a history of return before the arrival of the new leader, so we can see whether the person changes the trajectory of the investment. We were looking to take these businesses from linear growth to exponential growth, so looking at the metrics of return on a change in leadership and the speed to value, we were able to identify what the 'curve beaters' do, and think about ways to help other leaders do this work," Ogg said.

Leadership design that supports the strategy and desired culture

"Culture eats strategy for breakfast — in the absence of leadership," Ogg argues. CEOs and management teams sometimes underappreciate their ability to influence the organization's culture and change-readiness through leadership design.

"If you want to change a company quickly, the highest leverage point is the leadership and management culture. What sits behind the leadership and management culture is leadership design: What is it that we actually do? How do we select leaders, train leaders and promote leaders? What meetings do we have? How are decisions made? How is power allocated?" Ogg said. "There are a finite number of things that make up the leadership DNA of a company. Most people assume that those things are already decided and they are what they are, but if you are the CEO, you can change the design."

The way a company identifies, promotes and develops future leaders communicates a lot about the culture an executive team is trying to build, so the board and CEO should think carefully about how the company is developing and promoting emerging talent, especially those who may be contenders for the CEO role. To make sure that the next generation of executive talent aligns with the culture that the company wants for the future, talent management and development programs and employee evaluations must reflect the mindsets, behaviors and capabilities that will be needed. For example, if the organization needs to move to a more driven, results-focused culture, then training, development programs, the way meetings are run and how executives communicate all may need to evolve to signal to emerging leaders how to be successful in the future culture.

Small bursts of highly relevant executive training

Even companies that do a great job of hiring can fall down when it comes to assessing, developing and retaining their most promising people. Leadership development primarily results from experience on the job — learning by doing — and watching and learning from bosses and colleagues, including receiving coaching and feedback. Formal executive training represents a smaller but important third component of leadership development. Given the speed of change today, however, corporate training models that take people out of work for a couple weeks or more have given way to shorter, more targeted and concentrated training experiences that some compare to making fuel stops on the highway.

Technology, including online learning, and the shift toward shorter, more targeted training promises to improve the relevance of training programs and increase retention in a world where attention spans are short and the way people consume information has changed.

"In the past, you might go to a week-long program this year and another one next year. Many of those were wonderful programs, but, first, I would question the retention after a week-long program and, second, typically there was no follow-up to measure whether people were adopting what they learned," Goldsmith explains. "Today, especially with the advent of new technology, it's possible to give people shorter bursts of content and build in ongoing follow-up and measurement, so that these programs can actually focus on execution. It takes a lot of work to keep something in somebody's head today because we are barraged with emails, voicemails, and most people today feel busier than they ever felt in their entire lives."

For companies, investing in executive training provides the benefit of motivating and breeding loyalty in the leaders tapped for the programs — something Conaty saw at GE among those selected for programs at Crotonville and he still believes is valuable today. "You can attract great talent to an organization, but in my mind there is some obligation as a hiring company to further develop and assess those individuals. Many companies don't do such a great job at that, and then those people are back on the talent market in a couple of years."

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Effective hands-on leadership and mentoring has never been more crucial, and its impact directly correlates to overall business performance. In an environment of rapid change, leaders must lay the path for organizations to adapt to a continually changing business context. The leadership development approaches that are most likely to produce these executives have several common elements. In these situations, the CEO directly supports and participates in development efforts, and ensures that the overall leadership design and culture aligns with the leadership development goals. Results of development initiatives must be continually measured. And the best executive training must always remain relevant and highly targeted. Finally, the most effective leadership training and development approaches must evolve over time as the needs of business change in order to nurture the next generation of great talent.

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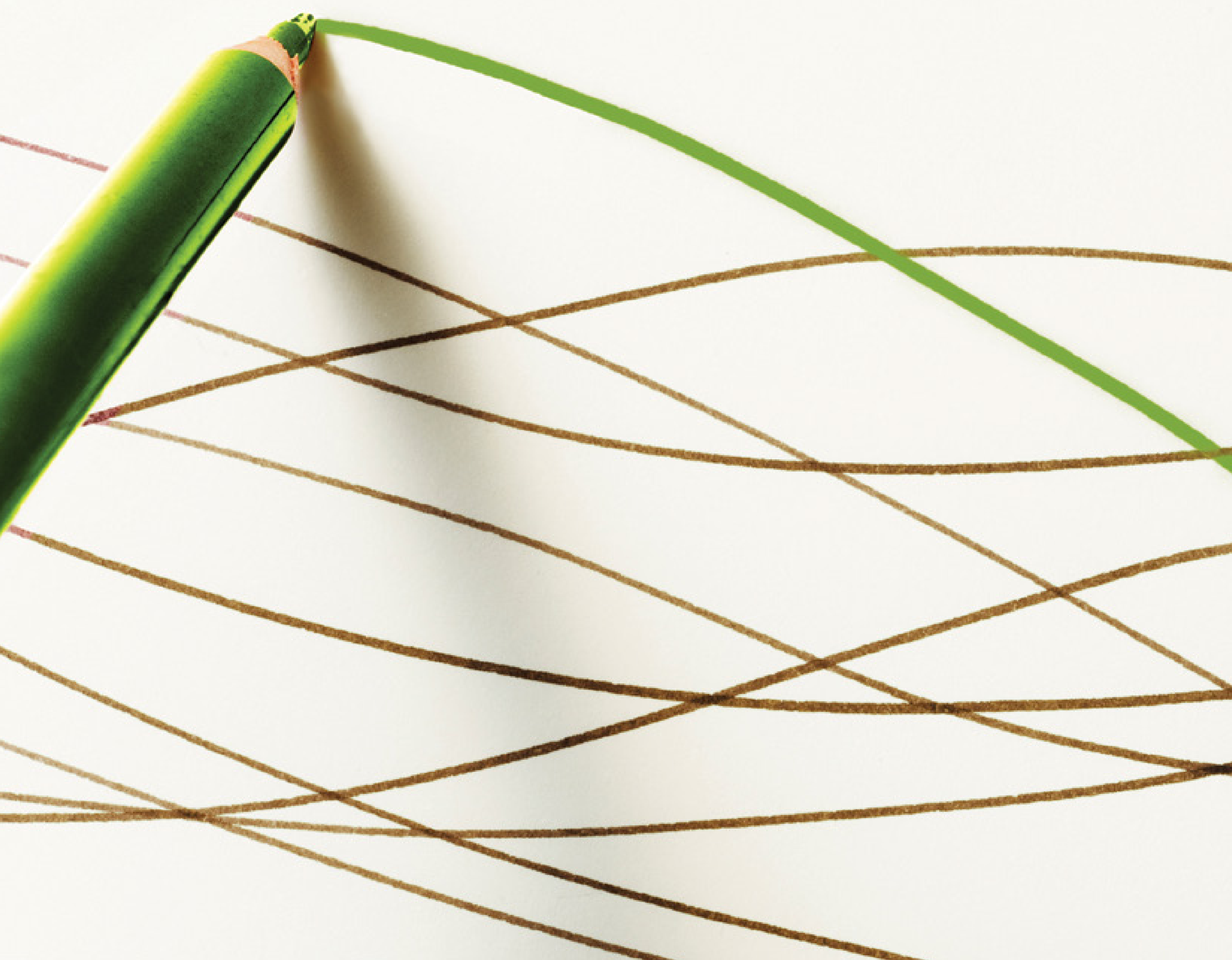
The Four Biggest Hidden CEO Succession Risks and How to Avoid Them



Improving the Odds of Having a CEO-Ready Internal When the Time Comes

When it goes well, CEO succession planning produces a strong internal successor who, in the short term, is well-received by the organization and Wall Street and, in the long run, has the right vision and strategy for the business and drives the company to achieve above-market growth and shareholder value creation. Most boards strive for a best-in-class process that maximizes the future readiness of internal talent, aligns directors behind the ultimate selection and, of course, identifies the best candidate for the CEO role.

When the board manages a long-term well-executed process that results in a great internal successor, everyone feels good about the outcome. However, CEO succession planning can be fraught with hidden risks and challenging dynamics that, if not recognized and managed, can derail the process and destroy value.

Getting succession planning right is not a hypothetical consideration for most companies. Consider that, in the four-year period from 2012 to 2015, 74 percent of the new CEOs appointed to S&P 500 companies were promoted from within, an increase from 63 percent during the 2004-2007 period. And 91 percent of those CEOs had no prior CEO experience.

This article draws on an analysis of more than 100 CEO transitions in the past seven years and conversations with 25 chairmen, lead directors, and incoming and outgoing CEOs involved in recent CEO succession situations at companies with revenues ranging from $2 billion to $50 billion. The analysis reveals hidden succession risks and identifies the characteristics of the processes that achieve the best succession outcomes.

#1

Losing your best internal candidates

Losing a strong internal succession candidate is a greater risk than many boards appreciate. You should assume that the strongest internal candidates frequently receive calls about opportunities at other companies. When they trust the succession process and timeline, they don't take recruiter calls — but that can change abruptly. All too often, the CEO and board do not know enough about what's on the minds of these executives. There can be many reasons why a leading internal candidate might begin to mistrust the process. Insiders often have too little transparency into the succession process and the relative roles of the board and CEO in developing and selecting the CEO successor. But the turning point for many is a comment (often off-hand) from the CEO suggesting a change in the timeline. A casual comment about "staying a year longer" can be enough to create uncertainty.

Don't leave potential insider candidates with a lack of clarity about the succession process and general timeline, or certainty about their value to the organization. One of the most important things the board can do is to establish an open line of communication with potential successors. This begins by creating opportunities for executives to interact with the board directly. The stated purpose of these interactions is simply to ensure the board gets to know key leaders and that the leaders get to know the directors. The CEO should make this happen by suggesting recurring check-ins, which should occur more often as a CEO transition approaches, in conjunction with each board meeting, for example.

Because some CEOs can be sensitive to the board wanting to meet directly with potential successors, which can make them feel like a lame duck, it is safest and most natural to focus the conversations on the business or function the executive is leading today, and individual development plans. For example, it can be effective to have a director spend a day with an executive reviewing the business or addressing the team, which provides a platform for a more natural interaction outside of the formal board meeting environment. This is your opportunity to let the executive know how much the board values him or her. If you create a safe environment and build a strong relationship, the executive will feel comfortable sharing his or her plans and concerns.

"I had not been taking calls for years, but then after the CEO mentioned he might stay a couple more years, I started taking calls. It only lasted two days, and then, by chance, I ran into the lead director in the office. He told me how much the board appreciated my impact and, when I asked, he assured me that the timeline was not changing as far as the board was concerned. Fortunately we had this conversation before I got a call for a great CEO role."

Internal CEO successor

Board engagement with internal candidates can provide an additional benefit as the succession process nears its conclusion: When the board has been actively engaged with internal candidates and garnered their trust during the process, it will be in a stronger position to approach the runner-ups after the selection about their future plans. Every CEO transition carries the risk that executives who are critical to the success of the business will leave the company, especially if they vied unsuccessfully for the CEO role. When the lines of communication have been open, directors can have authentic conversations with runners-up about their value to the company, increasing the chance that they will be willing to stay.

#2

Overlooking the best internal options

Boards have a very narrow window of observation on internal candidates. As a result, internals are often pigeonholed — force fit into a simple narrative. For example, the strong operator with weak communication skills may be viewed as insufficiently strategic. This kind of generalization is natural given the limited information available to the board. If an executive does not make a great impression in the limited interactions with the board, lacks charisma or is not the best verbal communicator, directors have a hard time seeing that person as a viable CEO successor. In fact, we have seen cases where the board (and the CEO) were enamored of a very polished, charismatic leader, whom they assumed to be more strategic, and discounted a less charismatic leader's track record of consistently outpacing the industry as, "He can handle slow change and incremental growth, but he is not strategic enough to handle all the change that lies ahead for us."

> "The board does not have enough insight to select internal candidates. They just don't have it. They come in once a quarter for one-and-a-half days. There is no way to know insiders through the board's typical interactions with insiders."
>
> Outgoing CEO

In other situations, boards fail to entertain the high-potential candidate at the next level down. We have seen many situations where a more junior executive with enormous potential has been promoted to the CEO role and outperformed the company's peer group. This is only possible when boards are willing to cast the net wide enough to consider executives who have more potential over the long term but require more development time. A longer process provides the time to uncover and develop these "unexpected" candidates, allowing the board to get to know them and become more comfortable with promoting the next-generation leader into the CEO role.

Internal CEO Successors

136 were promoted from within the company over four years

91% were first-time CEOs

47% were promoted from the chief operating officer role

24% were promoted from division CEO

8% were promoted from the chief financial officer role

42% served on a public company board before becoming CEO

Source: Spencer Stuart study of internal CEO successors in S&P 500 companies from 2012 through Q3 2015.

The remedy for these risks is a formal executive assessment of potential internal successors, ideally by a credible and objective outside third party. A formal assessment should provide a baseline understanding of insiders' capabilities, developmental gaps and potential long before a decision needs to be made. Assessments of executives should include a review of their track records leveraging strategic and operational capabilities similar to what the next CEO will need, as well as their ability to stretch into the more complex, demanding and ambiguous CEO role. From there, executives can be provided specific development opportunities and support. Many companies find it useful to tap an outside expert who can establish an appropriate process for a specific set of development needs. Boards should be aware of the biases that can form about internal candidates — assuming a stellar operator isn't a strategic thinker, for example — and challenge themselves to be specific about the development needs and action plans for the key internals, observe their growth over time, and be open to new narratives about individuals.

#3

Insufficient time to close the developmental gaps of internal candidates

When boards do not have a good handle on the timing of the CEO's retirement plan or a strong sense of the internal succession candidates, they can find themselves in a bind when the CEO's departure is rapidly approaching. It's a frustrating scenario for boards: The CEO plans to retire in less than a year and assessments reveal significant gaps in the top contender's capabilities or experience, or the board simply does not feel comfortable with the readiness of internal candidates to step into the top role. This can happen when the CEO gets ahead of the board, honing in on a particular succession candidate, when the board and CEO disagree about the strength of that internal candidate or when the process did not start soon enough to provide sufficient time to identify and address the development needs of internal candidates. It also can be the result of the unexpected emergence of an activist who forces an accelerated CEO transition. When internal candidates have "unfixable" weaknesses or lack the time to address developmental needs in time for the transition, it increases the likelihood that the board will have to look externally.

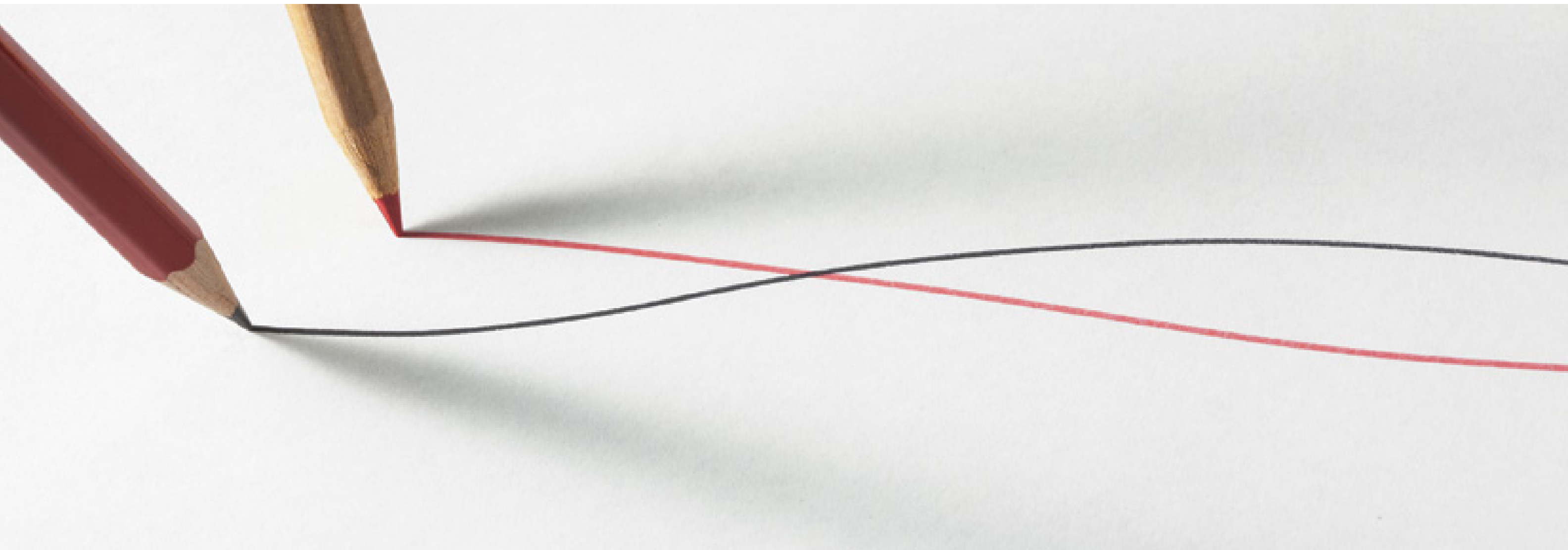
> "We had a sense at some point the CEO planned to retire, but the announcement was abrupt, lacking in forethought and transition planning. We'd had conversations about potential successors, but the board hadn't engaged in a way it should have. When the CEO made his announcement, we were in disarray."
>
> Lead director

Again, starting the process early is critical. Conducting formal assessments of internal candidates early provides high-potential internal talent the time they need to develop; potential successors may need to be assigned to new roles to gain experience, and prove that they can be stretched. Potential successors are much more likely to be ready if development plans are set early and are based on a clear understanding of individuals' strengths and gaps, and the board has a chance to observe progress against goals. A minimum of one year is required to make meaningful and sustained progress in key developmental areas, and even more time is needed to close gaps in experience.

It also is valuable for directors to deepen their understanding of the external talent market. Confidential external benchmarking — which identifies outside talent that might be considered for the CEO role, typically without contacting those individuals — can provide directors with a good sense of the relative strength of the internal candidates, and help them see any experience gaps more clearly. In short, external benchmarking is another step in the process that boards should take when evaluating CEO succession candidates in order to feel comfortable that they are making the right decision.

An internal succession candidate rarely will be entirely ready, but the board will be much more comfortable betting on the individual's continued progress if directors have seen growth and a sense of his or her trajectory over a longer development period. By monitoring executives' progress on an ongoing basis, the board can observe patterns of performance and develop a more nuanced point of view on their strengths and weaknesses. When this is the case, boards tend to be much more aligned as a group and are more confident that they are making the best decision. This is critical to the next CEO, who will inevitably hit rough patches. The next CEO deserves to have a board that is aligned behind him or her.

> "I have found that the idea of promoting from within can be tough for the board because directors are looking at candidates who have never done the job before. Many directors are instinctively disposed to getting someone who already has been a CEO. An objective process that gets directors to focus on the real factors that will drive success helps build consensus among directors."
>
> Board chair



BOARDS KNOW THEY SHOULD START EARLY, SO WHY DO THEY WAIT?

Boards today understand that they are responsible for CEO succession and, when companies are performing well, want to oversee a strong succession process that produces an internal successor who is ready to move into the top role. This does not mean that boards find it easy to initiate discussions about succession with the CEO.

For many directors, there never seems to be a good time to raise the issue. In high-performing companies, boards can be reluctant to raise the topic for fear of signaling to the CEO that it wants a change at the top. Paradoxically, in under-performing companies, directors often want to avoid rocking the boat and causing the CEO to worry about his or her job security at a sensitive time. Sometimes, the board just wants the current CEO to stay in the job longer. As one CEO recalled, "I had to convince my board that I was leaving. I kept telling them, but they did not act on it." In addition, boards sometimes avoid raising the topic of succession because they want to be respectful of the CEO's role in developing leadership talent.

Ironically, the least awkward time to start the conversation about succession may be shortly after a new CEO takes over, although this rarely happens, even among the most enlightened boards. However, several directors voiced strong support for starting succession planning in a new CEO's first year; the board and CEO have a fiduciary responsibility to address enterprise risk, and few risks are more important to the business than CEO turnover.

At a minimum, the board should own the succession transition two to three years before an anticipated transition. If the board hasn't started succession planning, it can ease some of the tension surrounding the issue if the initial conversation with the CEO focuses on the emergency/contingency plan — the "name in the envelope" in case of an unexpected health or family emergency. From there, it can be easier to extend the discussion to the CEO's time line, making clear the expectation that the CEO will inform the board of his or her plans two or three years in advance to allow for an orderly succession plan.

> "I know we should start the process now, but we are all too fatigued from the most recent succession process."
>
> Lead director

As the transition nears, the board and CEO will want to define a more concrete time line for succession. The CEO should be encouraged to shift his or her mindset from "what am I leaving" to "what am I building" and think in terms of the legacy left by preparing the next CEO and handing over the reins at the right time, and this includes making room for the development of succession candidates.

#4

A bumpy handoff and slow start for the new CEO

Even boards that manage an effective succession planning process resulting in the promotion of an internal successor sometimes "wing" the actual transition between the departing and new CEOs. The immediate transition can involve a wide range of activities: communicating with a variety of stakeholders, developing a transition plan for the outgoing CEO, negotiating compensation for the new CEO, meeting SEC reporting requirements, and planning retention strategies for non-selected candidates and other key management players. In one succession situation in which we were involved, the successful internal CEO candidate was encouraged to develop plans for three phases of the transition: before the announcement was made, between the announcement and taking over the role, and after becoming CEO, focusing on four stakeholder groups — investors, customers, suppliers and employees.

> "As opposed to a big bang, we had a gradual transition of responsibilities. We developed a matrix of what was changing and shared it with the senior leadership team so they knew what to expect."
>
> Internal CEO successor

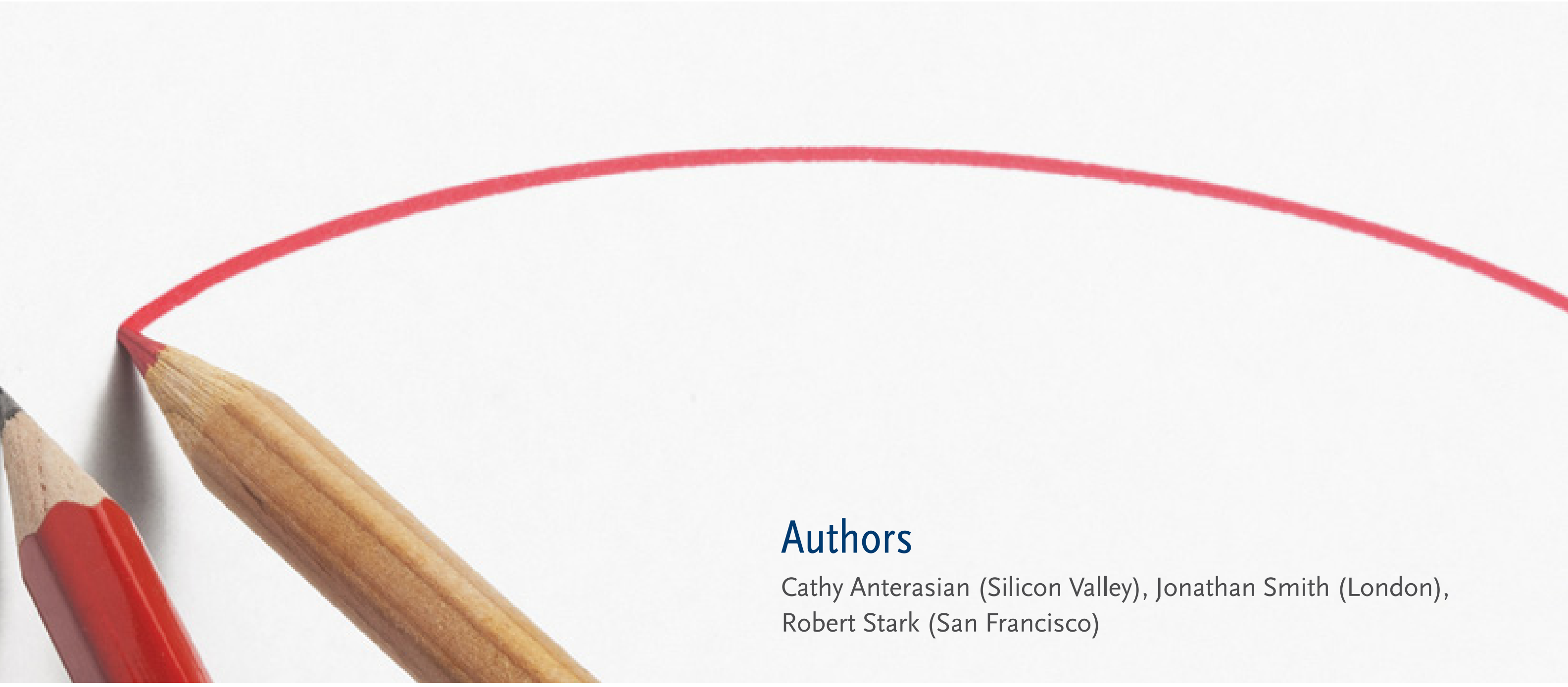
Without an engaged board to provide guidance, the outgoing CEO may become too hands on — interfering with the transition or acting out in other ways as the organization pivots to the new leader — or too hands off, not providing the necessary support to the new CEO. The board can be invaluable in advising the outgoing CEO to play an appropriate role in the transition and coaching the incoming CEO through the initial transition period.

Avoiding the succession risks

CEO succession represents a critical turning point for companies when tremendous value can be created or destroyed. Furthermore, succession planning is complicated, requiring the board to manage through the complexity and risk of the decision and the different ways in which events may unfold over time. Succession planning also can be a highly personal and charged topic, particularly for the CEO. Part of the board's role is to diffuse these issues and minimize the emotion of the process.

When done right, directors have maximized the chance that the company will have a ready internal successor; made a great decision about the next CEO; and fully aligned behind the next CEO. But without a thoughtful plan, there are big risks, some obvious, others hidden, suggesting three main themes for the board.

1. Start early and review the plan regularly. In the best processes, objective, third-party assessments of internal talent occur early enough to provide candidates time to develop and the board time to build a fuller, more nuanced view of internal players. The board should review the plan and candidates' progress at least once annually.
2. Build and maintain trust in the process. Once they have been through it, directors often remark on the power of the succession process to align the board around the strategic direction of the business, the capabilities needed in the next CEO and in the ultimate CEO successor. This only happens when the board oversees an effective, transparent process, ensures that the stakeholders understand the process and maintains an open line of communication with internal candidates.
3. Remain vigilant even after a decision is made. The board should stay involved in the CEO transition to ensure the incoming CEO establishes a clear plan for the early days of the transition and that it is executed in a disciplined manner. The board also should make sure that the outgoing CEO provides the necessary support to the new CEO without seeming to interfere.



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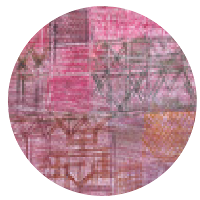

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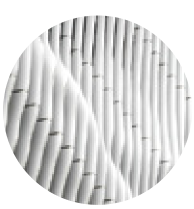

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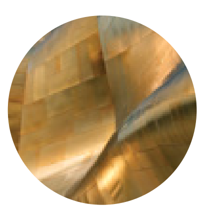

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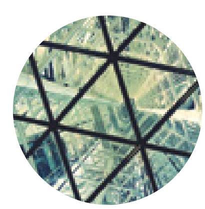

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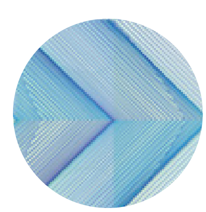

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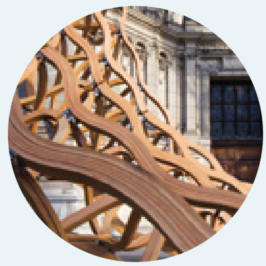

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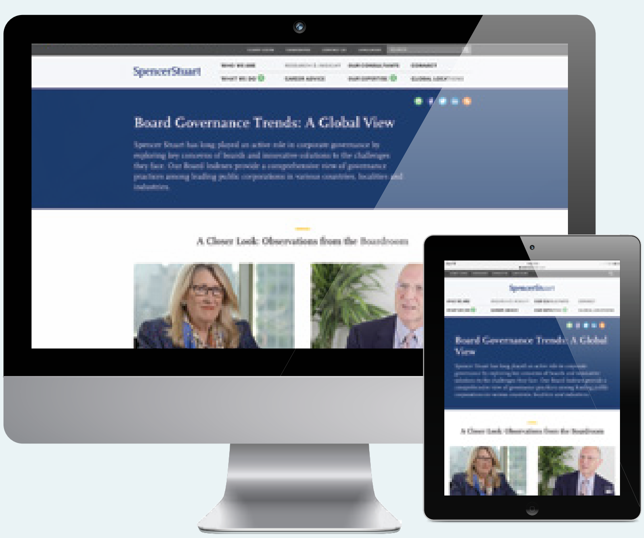

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