PERTH LEADERSHIP INSTITUTE

WHITE PAPER

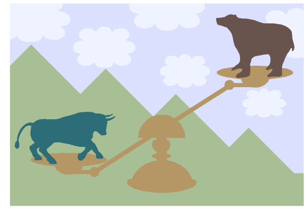
<u>SUSTAINABLE</u> GROWTH – THE NEW GOAL FOR LEADERSHIP DEVELOPMENT

As we exit the recession, we have to focus on what we teach future leaders so that they ***don't repeat the monumental*** *mistakes* that got us here. The goal now is ***sustainable*** growth. It has to look beyond purely short-term profitability and particularly towards ***benefiting the next and future generations***.

September 2009

(352) 333 3768
www.perthleadership.org

Executive Summary



*<u>Part One: Old Growth Era was **growth at all costs**</u>*

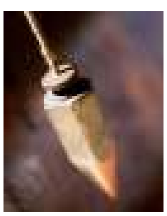
…Previous leadership development approaches did not prevent the crisis.

Now the need is for <u>sustainable</u> growth. The end of the recession is an opportunity to change to new models of growth-focused leadership development.

*<u>Part Two: Innovation means **something different** now…</u>*

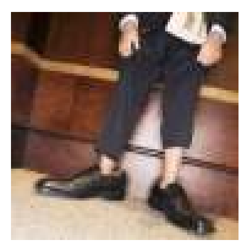
…Innovation can be good or bad. We must show future leaders how to tell the difference. We are here to benefit future generations, not just ourselves.

We must develop leaders who do not needlessly consume more resources on innovation than are merited.



*<u>Part Three: New Growth Era **requires business acumen with the long view**</u>*

Leadership development must educate future leaders in business acumen. Business acumen is more than making a profit. We must develop leaders who have common-sense and not just a high level of financial literacy.



*<u>Part Four: Sustainable growth means integrating **innovation with business acumen**</u>*

Innovation without business acumen leads to busts. Innovation with business acumen leads to sustainable growth. We have to develop future leaders with these new mindsets in order to leave a real legacy to succeeding generations.

Table of Contents

SUSTAINABLE GROWTH – THE NEW GOAL FOR LEADERSHIP DEVELOPMENT

Part 1 Old Growth Was Growth at All Costs

The New Post-Recession Challenge – Sustainable Growth

We have just undergone a wrenching economic crisis whose effects will be with the country for at least the next few decades. It will leave its indelible mark on the debts that must be paid by succeeding generations of Americans. At a societal level we have all made fundamental mistakes. Executives, managers, consumers, home buyers, governments, unions, business – all were a part of a shared delusion that we could have growth with no pain; that growth could be ultra-fast, sustainable and without penalty, personal, professional, monetary, psychic.

"…The price for escaping the crisis is major financial burdens on us and our successors…."

As we pick up the pieces, we now know that we were wrong. The price for escaping the crisis is major financial burdens on us and our successors. We can only meet and solve this challenge by growing again so that we can build up wealth in order to pay back our massive debts. To do this, we need to grow sustainably, something we have not done since the recession of 1992, if not before.

Yet the mindsets, management approaches and philosophies which have been taught and inculcated in management incorporate both conscious and subliminal drivers which are based on models of unsustainable growth. From exotic financial instruments, to unsustainable M&A strategies, credit techniques and sales approaches, much of the current mindset is still based on the strategies of unsustainable growth that landed us in trouble in the first place.

There were numerous causes of the economic crisis. There is no point in assigning blame here because there were so many factors, and everyone was involved in it in some shape of form. But one that must share the blame is leadership development approaches. Our leaders were clearly totally unprepared for what happened. Leadership development approaches were too.

SUSTAINABLE GROWTH – THE NEW GOAL FOR LEADERSHIP DEVELOPMENT

The task for leadership development is clear. It must focus on new and fresh approaches which prepare leaders to create growth that is sustainable and sustained. It cannot just repeat the same methods as were applied in the status quo ante. It must learn from its mistakes in the past and acknowledge that it did not produce leaders who could address this problem properly.

As we exit the recession we will get growth. The challenge is to make it sustained. This is the new challenge for leadership development.

Leadership Models Did Not Prevent Unsustainable Growth Mindsets

"…As we exit the recession we will get growth. The challenge is to make it sustained…"

We must face some unpalatable truths about how we trained our future leaders before the recession. What specifically are these truths and how can we profit from these lessons?

1. Conventional leadership approaches did not prevent unsustainable growth mindsets that led to an economic crisis at all levels of organizations and society.
2. **High financial literacy and training approaches to improve it in companies did not prevent the crisis and indeed may have made it worse.**
3. Training in risk reduction did not prevent systemic problems in financial services companies.
4. The lack of awareness and training in behavioral risk was present at most levels of the private sector, government and nonprofits

1. Conventional leadership approaches did not prevent unsustainable growth mindsets that led to an economic crisis at all levels of organizations and society.

Most of the companies affected by the crisis had leadership development programs. They have been tested under fire and have been found wanting.

Most leadership programs focus on soft versus hard skills. It is not that such programs are inappropriate. Rather they are missing a vital component, namely concerning the business aspects of leadership. The crisis showed that leadership programs need vastly more emphasis on these aspects including business acumen and behavioral finance.

Leadership development programs did not focus on the business issue of sustainable growth and its relationship to leadership behaviors, irrational and otherwise.

2. **High financial literacy and training approaches to improve it in companies did not prevent the crisis and indeed may have made it worse.**

Wall Street was populated by executives and managers with the highest levels of financial literacy in the world. Instead of helping curb financial excesses, these qualifications and the misplaced confidence they instilled in their owners actually added fuel to the flames. Many companies – not just on Wall Street but Main Street companies too - routinely send their senior executives to corporate training course in universities to learn more about financial subjects and to increase their financial literacy. This clearly did not prevent the crisis and probably exacerbated it.

Nor was financial literacy focused on the dangers of over-confidence, and its impact on exacerbating imprudent behaviors which could lead to unsustainable growth. The assumption indeed was that high financial literacy in a turbocharged environment would automatically lead to even faster and sustained growth. Leadership developers equated financial literacy with prudent growth when in fact there may have been an inverse relationship.

3. **Training in risk reduction did not prevent systemic problems in financial services companies.**

All Wall Street companies had supposedly sophisticated risk management systems in place. Yet this did not prevent the crisis either. **These systems were technically- rather than behaviorally based.** These systems were based on the premise that if the right technical systems and methods were put in place, that risk could be kept within acceptable bounds. This philosophy has been proved to be tragically incorrect.

> "…Leadership developers equated financial literacy with prudent growth when in fact there may have been an inverse relationship…"

The popular literature is now focused on the problems thus exposed, namely problems of **irrationality in financial behaviors**. These were not understood by the Wall Street companies.
Leadership development must incorporate training in these areas if we are not to repeat the same problems in the next 10 years or earlier.

In the pre-recession period, since the issue of irrationality and irrational behaviors was being ignored, leadership and leadership development also ignored the issue of current growth models being inherently unsustainable. Future leaders were taught that providing the right technical approaches were followed, behavior did not matter since it would just do as it was told. History has demonstrated the tragic error of this heroically flawed assumption.

4. The lack of awareness and training in behavioral risk was present at most levels of the private sector, government and nonprofits

It was not just financial services companies either that were affected. It included everyday Main Street companies that gravitated to the apparently promising new models of debt, derivatives, hedging and other exotic approaches. Neither did their risk management systems work as planned.

"…Business acumen was ignored as being less important than other issues such as the ability to command and lead, irrespective of financial and growth outcomes…"

Almost all companies assumed that a technical approach to financial risk would be effective. They completely ignored the behavioral aspects of risk at a formal level. In the end these proved to be instrumental in causing, exacerbating and extending the crisis.

Yet current leadership approaches are almost silent on these topics. In any case few leadership courses teach participants anything whatsoever about the behavioral bases of financial risk.

The lack of attention to behavioral risk permeated all levels and sectors of society. This led to regulators and overseers ignoring risky behaviors which would lead to unsustainable growth. Business acumen was ignored as being less important than other issues such as the ability to command and lead, irrespective of financial and growth outcomes.

Will Leadership Development be More Effective This Time Around?

Major economic slowdowns and recessions undergo highly predictable patterns. Just before the slowdown occurs, the market is at a peak; there is a great deal of complacency amongst companies, employees, shareholders and investors. Money is easy to get and much is therefore wasted. Behaviors in financial matters are relatively lax and investment quality declines across the board, not just at the company level but with individuals and shareholders.

Since most people do financially well in such a market, even those people with low business acumen are successful. It is difficult to use financial performance as a guide for discriminating between good and bad financial behaviors since both seem to be equally well rewarded in such halcyon times.

As economies move into a growth phase again, companies tend to progressively value business acumen less, since the crisis is now over and they feel less need for it. They are lulled into a false sense of security by the improving business climate. At this point the seeds are being set for the next crisis.

“…As economies move into a growth phase again, companies tend to progressively value business acumen less, since the crisis is now over and they feel less need for it. …. At this point the seeds are being set for the next crisis….”

Even as this White Paper is being written, the seeds are being sown for the next economic crisis to the extent that future leaders and leadership educators believe that the crisis has now passed.

We are now exiting the recession. Training budgets, which have been cut drastically during the recession, will now start to rise again. Leadership development now has the chance to make things right, to change their modus operandi and to move to models and approaches which take into account the weaknesses we have identified above.

But the question is now: will these changes be made? Will companies and those responsible for the leadership development function actually make changes? The danger now is that no changes will be made and that leadership development will simply perpetuate the same old models and approaches that supported the very problems that led to the crisis.

Now is the time for companies, organizations, their executives, and their HR and leadership development areas to stand up and to be counted. If the world is truly to learn the lessons it has been given, they need to grab the reins and start making these changes now. There will not be a second chance.

> "…..Will companies and those responsible for the leadership development function actually make changes?..."

If and when the economy moves into a bull phase again, which is not unlikely, if no changes are made, then we can expect to see a return of the same types of factors that led to this crisis. By making the changes now, organizations can help short-circuit this process.

Part 2 Innovation Means Something Different Now

Old Growth Era Innovation Cost More than It Generated

The pre-recession period created many innovations. Chief amongst these were financial services innovations. For a while it looked like these innovations had put us into a new world of productivity and wealth. We now know they did the opposite. We now know that the costs of these innovations outweighed the benefits.

It is clear that we need to rethink the relationship between innovation and growth. In particular:

- The New Growth Era requires a new type of innovation perspective
- Innovation must have a positive intergenerational impact
- Innovation must not crowd our prudent use of resources

The New Growth Era Requires a New Type of Innovation Perspective

Once a recession ends and the company has survived, the attention turns once again to growth. Many of the company's competitors have been weakened or disappeared. The need is for fast moves to take advantage of the new situation and to search out new approaches than can provided competitive advantage and growth to fill the gaps that competitors have left.

Growth could come from expanding demand or from innovation. For many if not most companies it will come from the post-recession demand kicker; for far fewer it will come from innovation.

As we will show, the innovation driver is a necessary but not sufficient basis for New Growth Era sustainable growth. For growth to be sustainable it needs to be based on a type of innovation which goes beyond that accepted in the Old Growth Era.

> "..The goal of leadership development is to develop sustainable innovation and discourage fashion-based innovation.."

In any long-term growth perspective, innovation is the driver of growth. Innovation leads to higher value-added, increased gross margins and hence higher profitability and increased market value for the company.

But from the sustainability perspective, there are **two types of innovation**. One is the type that is based on fashion and produces growth, but just in the short-term. Option ARMS and subprime mortgages are an example. The other is based on longer-term fundamentals and produces long-term and sustainable growth. Examples are broadband and Web 2.0.

These two types of innovation are driven by different behaviors and have different outcomes. **The new goal of leadership development is to develop sustainable innovation and discourage fashion-based innovation.** To do this it needs to understand the behavioral drivers behind these. It needs to understand the difference at a deep level so that it can make the distinction credibly and in away that discourages "bad" innovation and rewards and encourages "good" innovation that leads to sustainable growth.

Innovation Must Have a Positive Intergenerational Impact

Innovations by definition change things. The issue is how long they change things for.

"Bad" innovations change things but only for the short-term. They do not have permanent impact on the economic and social landscape. Thus they do not have a sustained impact and do not result in sustainable growth, even though they are innovations in the usually-accepted meaning of the word.

An innovation could create capital over a longer period within the current generation, but the capital creation ceases by the end of the generation. In that case there is nothing left over for the next generation. In that case, we the current generation have consumed all the capital produced by the innovation. So this innovation produces growth only for the current generation but not the next. An example is the financial services "innovations" of the last few years.

> "…Better mouse-traps may create short-term profits but they do not create social and intergenerational capital…"

Where the innovation produces capital only for the current generation but does not do so for the next generation, it may seem to have created sustainable growth, but that sustainability is experienced only by the current generation. From the perspective of the next generation the growth is not sustainable since it has not stretched out in time enough to benefit it.

Where an innovation does not benefit the next generation it has not produced sustainable growth, viewed from a longer-term perspective. From a New Growth Era perspective, it must therefore be termed "bad" innovation.

Innovation is generally seen as a competitive phenomenon. The iPhone kills the Blackberry (maybe); hybrids beat gas guzzlers and so on.

But on our criterion of creating capital and with an intergenerational perspective, the perspective changes. If the innovation does not create capital on a net-net basis, (that is intergenerational, in all forms of capital), the doo-dad is not really an innovation, it is really just a better mouse-trap.

Better mouse-traps may create short-term profits but they do not create social and intergenerational capital. The option ARM was a better mouse-trap, micro-credit is almost certainly an innovation on a net-net basis. The iPhone is nice but we have yet to see whether it is more than a better mouse-trap. The Apple app store may well indeed stand as an innovation on this score.

The lesson is that one crucial criterion for judging innovation is its impact on creating capital, wealth and assets for the next generation. **We define this wealth not only in financial but also in social and environmental terms**.

On this criterion, must of the innovation before the current recession was bad innovation. It has in fact led to a vast consumption of capital to clean up the mess which will reduce the level of wealth, social and environmental assets left to the next generation.

"…Sustainable growth ….must create a net level of wealth which is available to the next generation.."

Sustainable growth requires good innovation. It must create a net level of wealth which is available to the next generation. Leadership development must firmly show the difference between the two in educating and developing future leaders so that we can avoid the level of intergenerational losses we are bequeathing to our successors as we speak.

Innovation Must Not Crowd Out Prudent Use of Resources

Generally innovation is seen as good in itself. **But the vast majority of innovations fail and do no good**. Only a tiny proportion of innovations succeed.

The vast majority of innovations actually consume capital and lose money
Most people given the job of innovation are not innovators and will not create an innovation, much less a "good" one in the sense of this White Paper.

Most people who are innovative both in a narrower and a broader sense, will end up using vastly more resources on the innovation than will ever be recouped, in a financial or in a social sense. Most innovators behaviorally use a high level of resources.

Research shows that high spending on R&D has no correlation with the level of commercially successful innovations actually produced. The biggest companies with the highest R&D budgets invariably are significantly less innovative than companies that spend a much smaller amount on R&D. Overspending on innovation consumes resources that could be used for other purposes that would lead to sustainable growth.

It is counter-productive to promote high innovation without an accompanying focus on resource utilization. If this is not done, innovation initiatives simply tend to consume capital and actually weaken the competitive position of the company. Innovation without such a focus will render growth less sustainable than otherwise, even if the innovation is successful commercially.

Sustainable growth requires innovation that is also focused on a prudent level of resource utilization. What constitutes “prudent” cannot be inferred from the practices of the Old Growth Era. Prudent resource utilization requires a different standard of judgment for resource use that needs to be defined and codified on a case-by-case basis by wise managers who understand the complex tradeoffs involved.

In sum, innovation is tough and generally consumes far more capital than will ever be recouped from most of it. Of course, that is not an argument for not innovating. It is simply an argument for doing it a lot better and avoiding the many traps that await the unwary.

In the current end-recession scenario, innovation and growth initiatives will be greatly different from those practiced in good times.

> “…innovation can be either a positive or a negative force for sustainable growth…”

- In good times they tend to be generously resourced; in exiting a recession they must be frugally resourced.
- Good-time initiatives will be run for periods that are excessive or imprudent; those at the end of a recession will have tightly bounded timeframes.
- The types of people who are chosen to implement them will be vastly different; those chosen in good times will tend to be imaginative high resource utilizers with relatively low levels of business acumen; in the early growth period of the next cycle those chosen to lead the initiatives will tend to be people who are more focused and frugal.

Innovators in the early growth period will have high business acumen or will have been trained to have it. This raises a new set of challenges to leadership development organizations which have never been put formally in the position of having to identify, develop and nurture such traits.

The task of leadership development is to promulgate the attributes of good innovation within an environment of resource utilization standards that contribute to sustainable growth rather than detracting from it.

Leadership development needs to promote innovation not as a good in itself but in a critical manner. It must demonstrate **how innovation can be either a positive or a negative force for sustainable growth**. Future leaders need to be shown the difference. They need to develop the mental tools that will allow them to discern when innovation will be good for sustainable growth, and when it will be bad for it.

New Growth Era Requires Sustainable Innovation Perspective

The implications for HR and leadership development are:

1. Leadership development must educate future leaders on good and bad innovation; that is the types of innovation which lead to sustainable growth and those which do not.
2. Leadership development must also focus on intergenerational impacts of innovation. Intergenerational impacts must become a far high priority than they were in the Old Growth Era.
3. Future leaders must be shown the difference between innovation that creates capital and innovation which consumes it inappropriately. They must be aware of the behavioral differences than drive such innovations.

Part 3 New Growth Era Requires Business Acumen with the Long View

Old Growth Era Ignored Business Acumen

What is notable about the run-up to the economic crisis is the disregard by so many of our leaders as to the basic concepts of business viability and reasonableness.

"…Intergenerational impacts must become a far high priority than they were in the Old Growth Era…"

Some of the largest corporations were being run based on almost negligible capital. Government-backed corporations such as Fannie Mae also had minimal capital but did not know it. Financial statements did not reflect the dangerously undercapitalized state of many of our most important companies. In sum, basic tenets of business acumen were being disregarded at the highest levels throughout the land and this was routinely ignored even by governments and regulators.

Sustainable growth needs business acumen. There are powerful lessons to be learned:

- Leadership development must include business acumen.
- Business acumen is way more than just making a profit.
- It must incorporate intergenerational payback.

- Financial models and data must meet the test of common sense
- Business acumen dictates that growth should not be zero-sum
- Social and environmental capital creation must be included

Leadership Development Must Include Business Acumen

Conventional leadership development focuses mainly on interpersonal and emotional skills and job competencies. Most of the leadership approaches in use derive from theories that are up to a century old. Approaches based on them have a psycho-analytic, anthropological and social rather than a financial basis.

These theories were developed before the development of modern economics and financial theories. This does not mean that they are irrelevant to leadership. It means that they do not address specific and crucial problems of business and financial behaviors. They were never designed to do that and in any case there was never any business or financial behavioral framework to build on to address such issues.

Modern scholarship has started to address these issues through the development of new disciplines, particularly behavioral economics and behavioral finance. But so far these lessons have not been recognized and absorbed by leadership development.

These new theories are based on the principle that financial and economic behaviors are not necessarily rational and are often irrational. They explain at a high level precisely why we tumbled into the recent economic crisis. However leadership development professionals have still not absorbed these models and they have not yet been used to fill the **yawning gap in leadership concerning financial behaviors and the role of irrationality in decision-making.**

> "…behavioral economics and behavioral finance…..so far …have not penetrated leadership development…"

As a result of this, leadership development programs in the vast majority of cases still do not incorporate business acumen approaches; they mistakenly equate financial literacy and business acumen. The recent crisis should have decisively put an end to that misconception since it has become crystal clear that the possession of financial literacy, right up to the level of a Nobel Prize, did not help players foresee or solve the issues.

If anything, high financial literacy

may have been a part of the problem, not a part of the solution. **Right now the need is for business acumen, not for financial literacy.**

But the bias of modern corporations to accept MBA degrees as being a proxy for sound financial behavior has meant that this gap is proving difficult to address. HR and leadership professionals in the vast majority of cases have had a background in psychology and psychoanalytic disciplines rather than in financial disciplines and most feel decidedly uneasy in this area.

This has turned out to be a major impediment to overcoming the bias in corporations in favor of using psycho-analytic and non-financial behavioral approaches to leadership; even though the evidence is now that this is actually reducing the credibility of these leadership efforts and programs. Moreover this gap is also leading to a loss of credibility for many of these programs as the business side of companies sees the problem and takes sides. This is particularly the case post-recession.

"...high financial literacy may have been a part of the problem..."

The fundamental problem in the last few years has been a lack of business acumen. As we exit the recession and start to aim for growth yet again, the key issue will be how to achieve growth that is prudent. How to inject business acumen into growth efforts is now becoming the crucial factor to address for almost all organizations globally.

Business Acumen is Way More than Just Making a Profit

What do we mean by "business acumen"? The usual definition would be a knack for making money or profit. But as can be seen this White Paper puts a far broader and even radical construction on this term.

Our definition of "business acumen" is the propensity to create capital. But in our definition, "capital" refers not just to financial capital, but also to other forms of capital including social, environmental and political capital. The notion of sustainable growth refers to the creation of capital in all of these areas and additionally for the benefit of future generations, not just our own.

It might be thought that this also contradicts the White Paper's thesis that we must develop business acumen and apply it particularly in innovative settings. Surely business acumen is precisely the use of financial criteria to growth projects to ensure that we make money and are consistently profitable?

However this is to misunderstand the true nature of business acumen. With true business acumen, we are not just trying just to turn a profit. **We are trying to create capital, be it financial, social or political.** And in the case we are setting out here, a crucial use of that capital is to benefit the next generation, which means taking into account the social and environmental capital outcomes of our growth efforts, which sometimes actually reduce it.

So in a sustainable growth approach, we are recognizing that even if we make profits in our generation, we can still end up reducing overall intergenerational capital and thereby further impoverishing the next generation, even if we ourselves get by for the moment.

Of course, this is not to say that we aren't trying to turn a profit. **But we must recognize that there are good and bad profits.** Those profits that reduce the sum of capital for the next generation, not just financial, but also social, political and environmental, are bad profits. Those that increase it are good.

On this criterion, the apparent profits made by the many industries in the pre-recession period, were bad profits. Our aim is to generate good profits. This requires leaders who have vision and wisdom that far transcends the technical financial models that are so heavily relied on by most organizations.

Leadership development needs to have a far more sophisticated understanding of what constitutes business acumen, capital generation and intergenerational equity if it is to produce the leaders what are now so sorely needed. It needs to incorporate business acumen into leadership development courses. Furthermore it needs to show that business acumen is more than just about profitability and show future leaders the implications for management and strategy of these concepts.

It Must Incorporate Intergenerational Payback

What do we mean by payback and the period in which it should be achieved? Should it be an arbitrary period such as 2 or 5 years? Should it be a financial definition such as time to meet a certain ROI? Or should it be something broader, tied to social or even environmental concerns?

> "...vision and wisdom that far transcends the technical financial models..."

Our view is that we must take a broader view. If we take the narrower view of payback, we tend to run into the problem that the investors are paid off but the company went bust, the same problem that we have already experienced in this recession. Any definition that allows a small segment to profit but the rest of society to lose cannot be admitted since it is inherently nihilist – it allows society potentially to be destroyed even if the project was a success

We are all acutely aware that the cost of this recession will have to be met over a period over at least one and probably two or more generations. The responsible approach is to say that whatever we do must lead to the next generations not having to pay for our mistakes. We cannot mortgage these next generations. So the criterion for payback must be a social one. Thus if we create growth, it must be such as to leave at least the next generation better off, not worse.

Those who believe in the primacy of modern financial theory may have a problem with this since it goes against many of the established criteria developed for to judge the financial worthiness of investments and projects. But almost everyone has children and we all have a responsibility for them. Likewise we have the responsibility to leave a planet that hopefully will be in better shape than we found it. Only by taking a broader social and environmental view can we meet the twin goals of growth with responsibility. This is the only way to achieve sustainability.

Leadership development must not only develop business acumen in future leaders. **It must also introduce the idea of intergenerational equity** and educate them in how to apply it in management. It must leaven the technical financial formulas for payback that are taught to business students and MBAs with the broader ideas of intergenerational equity which are becoming more important now as the resources used by our generation increasingly detract from the opportunities for the next.

Financial Models and Data Must Meet the Test of Common Sense

There has been a progressive divergence between financial theory and business acumen over the course of the last couple of business cycles. Increasingly what appears to be good in the financial view is at odds with the view of the common man and what constitutes sound business practice.

> "…Growth manias tend to become uncontrollable…"

This has underscored the need that we must teach our future leaders not just about academic models; we must also teach them common sense. Academic theories tend to view business acumen as being a less-advanced and informal form of financial thinking even though modern scholarship is now showing this to be an outdated view. Yet it is precisely by reverting to basics that we can avoid many of the problems that have plagued us over the past few years.

<u>SUSTAINABLE</u> GROWTH – THE NEW GOAL FOR LEADERSHIP DEVELOPMENT

If you can't understand the mechanisms behind growth, then you should not adopt them. This might seem to be an obvious precept, but it was widely ignored in the run-up to the economic crisis and was crucial in causing it.

Many of the financial innovations that led to the crisis failed this test miserably. That is not to say that many were not worthwhile. It was just that in the heat of the moment, the envelope was pushed way too far.

Growth manias tend to become uncontrollable. If certain methods of growth seem to work, it can be difficult for others to gainsay them. But it is precisely in these situations that true leaders stand up to critique them.

How many leaders were prepared to use common sense instead of the exotic approaches that were dreamed up by the quants and the eggheads? How many leaders were prepared to ignore the financial lessons they had learned at business school and call a halt to what now appears as lunacy?

Business acumen is a matter of behavior rather than of learned knowledge. Most people do not have high levels including and possibly especially managers with high levels of financial literacy.

Leadership development needs to **inject common sense into the leadership equation**. It needs to develop approaches to guard against group-think and herd mentalities. It needs to develop critical thinking about some of the doubtful new improvements in financial literacy and techniques.

Leadership development needs to incorporate the new findings of behavioral economics and finance so that it integrates our new advances in understanding irrational behaviors. This will help leaders of the future avoid being massively blindsided, which seems to happen with unfailing regularity at least once every generation. It needs to understand that business acumen is much more a state of mind that can be developed, rather than a university degree, and take appropriate steps to develop it.

Business Acumen Dictates that Growth Should Not be Zero-Sum

By "zero-sum" we mean growth that is offset by a decline in another part of the industry or area. This stricture sounds a little bit too obvious – the growth should not be at the expense of other competitors. Isn't that what competition is all about?

"...Leadership development needs to inject common sense into the leadership equation..."

At a social level, if growth is zero-sum, then society essentially goes nowhere and there is no net growth. In that case, the growth does not meet the basic criterion that we have set ourselves, namely that the growth should last at least more than our generation. That way the next generation actually gets to benefit from our efforts and we have paid down some of the mortgage we left to them. In a zero-sum game that does not happen.

Zero-sun growth occurs when companies and organizations set as their goal growth that is set **purely to strictly intra-generational financial measures** such as paying back an investment or meeting a certain investment hurdle rate. The company may meet this criterion, but on our wider measure, it has not helped pay down the mortgage left to the next generation.

Non zero-sum approaches to growth include the following:

- Attempting to grow markets, not just aim for a redistribution of profits in them to our own organization
- Formally measuring whether our efforts create capital for the next generation
- Formally measuring whether we are creating capital after we take into account social and environmental externalities

Leadership development must develop future leaders who can see beyond the zero-sum mindset. It must show the fallacies of the zero-sum mindset. It must teach future leaders that their efforts as managers must benefit their unborn successors and that zero-sum is just a fancy way of taking from them that to which they have a right to expect.

Social and Environmental Capital Creation Must be Included

> "…it is vital that future leaders be taught a formal approach to business acumen so that they can view these issues within a commonsense financial context…"

As we now understand very well, fast growth has major costs, although these are often not reflected in financial data. Economists call these costs externalities. The goal of sustainable growth is to reduce and eliminate these externalities.

We are now very well aware of some of the environmental externalities. We understand the danger to the environment and the planet of uncontained growth. However what we have not yet addressed is how to harmonize the twin goals of sustainability and business acumen.

This is a very difficult subject. Yet it is at the heart of the environmental sustainability issue. Leadership development needs to ensure that these issues are addressed so that neither side gets out of hand. It is clear that there is at least some possibility of environmental concerns swamping business acumen, just as it is that business issues will swamp environmental concerns.

This means that leaders must have a clear model of what business acumen is and how these tradeoffs can be identified and measured formally. In this way leaders can assess and judge the business tradeoffs involved in environmental and social concerns and make reasonable and defensible tradeoffs.

Issues such as health reform and the deficit are bringing these issues into sharp relief. Future leaders must be taught a formal approach to business acumen so that they can view these issues within a commonsense but broad financial context and again make decisions which are reasonable and defensible.

Part 4 Sustainable Growth Means Integrating Innovation with Business Acumen

This White Paper has discussed two basic areas of leadership development. These are innovation and business acumen. To date, these have been treated as different and generally unrelated topics. The experience of the economic crisis has shown that they are integrally related.

"…business acumen also deals with payback at an intergenerational level…"

The Old Growth Era treated innovation as a good in itself. We have argued that there is good and bad innovation and that these need to be discussed and included in leadership development curricula so that managers can understand the difference.

Business acumen has almost totally been ignored in leadership development. This White Paper shows that was a major factor in the economic crisis. Future leadership development needs to formally include business acumen so that we can show leaders how to avoid the problems of its absence in the future.

But we have also shown that business acumen can be viewed on two levels. One is business acumen at a purely financial level that has a relatively short-term focus. The second view is the broader view, that business acumen also deals with payback at an intergenerational level, and that capital is defined not just as being financial, but also as being social and environmental.

These realizations pave the way for recommendations for leadership development in the future. Above all they point to the need for addressing them as integrated topics.

Sustainability Needs Different Leadership Development Paradigm, Different Mindset

If leadership development in corporations restarts off where it left off, then the opportunity will be missed. In that case our future leaders will not be provided with the different paradigms and mindsets they need to achieve sustainable growth.

These changed paradigms and mindsets include:

1. Introducing the broader intergenerational, social and environmental goals of the New Growth Era into leadership development.
2. Re-working innovation programs to make them more realistic and more focused on broader intergenerational objectives.
3. Implementing programs to develop business acumen defined both in the narrower and in the broader sense.
4. Integrating business acumen and innovation programs.

1. Introducing the broader intergenerational, social and environmental goals of the New Growth era into leadership development.

Develop formal programs to introduce these wider concepts into leadership development. This course should stress the limitations of purely technical financial criteria and the pitfalls that can occur when they are taken too far. It should particularly focus on the responsibility for future generations and leaving them with a viable stock of capital so that they can benefit from the efforts of this generation, not suffer from them

"…Future leaders need to be shown what happens when innovation goes wrong, as it frequently does…"

2. Re-working innovation programs to make them more realistic and more focused on broader intergenerational objectives.

Innovation programs need to be reworked so that they examine the pitfalls and traps in current innovation models and perspectives. Future leaders need to be shown what happens when innovation goes wrong, as it frequently does, and how to get the ship back on course. Participants need to be taught the broader social and intergenerational issues in innovation as well as the purely competitive approach.

3. **Implementing programs to develop business acumen defined in the wider sense.**

Leadership development needs to formally conduct training in business acumen so that future leaders know how to avoid the sort of problems that have occurred in the past few years. They need to be shown the broader ramifications of business acumen in its application to social and environmental capital and to it application to intergenerational transfers and intergenerational capital outcomes.

4. **Integrating business acumen and innovation programs**

Innovation and business acumen programs need to be combined so that the tight connection between the two can be appreciated. Future leaders must be shown how innovation without business acumen can lead to massive and avoidable social dislocation and costs, especially those to the next generation.

Some High Leverage Initiatives for Leadership Development

The recession has ended. Now is the time to act. The lessons of the past are clear. Leadership development should act rapidly to take the initiative. Some of this initiative needs to be aimed at spurring fast action to sensitize management to the new sustainability model. **Some of them need to spur action within HR and leadership development.**

So what can HR and leadership development do quickly to take advantage of the new growth opportunity? We would suggest some of the following:

- Get a thought leader in the areas of innovation and business acumen to present to top management.
- Do a fast business acumen program with the CEO and the top management team.
- Conduct an integrated innovation and business acumen program for a sympathetic business unit head and his/her top managers.
- Introduce business acumen concepts into traditional leadership development programs.
- Conduct business acumen onboarding with new executives.
- Conduct a seminar on the implications for intergenerational equity of some of your latest innovations.
- Carry out an inventory of business acumen in the top innovation team as part of a sustainable growth initiative