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PERTH LEADERSHIP INSTITUTE

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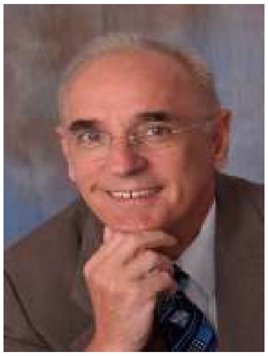
LEADERSHIP DEVELOPMENT STRATEGIES FOR A NO-GROWTH ERA



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The New Normal is No Growth

Leadership development approaches have an implicit assumption baked into them. That is that generally things are going up – sales, customers, profits etc – even if some of these might not be happening right at a particular time. What happens if the reverse is the case?

It has now become crystal clear that the US economy is in for several years of either low-growth, no growth or even negative growth. How does this affect leadership development and training generally?

The new normal is either no sales growth or even negative sales growth. This is being driven by ever-increasingly thrifty customers who are in a process of deleveraging. This deleveraging is going to take at least 10 years and probably longer. How do you train leaders to manage and guide organizations that must still increase shareholder value when overall GDP growth in real terms is zero?

This situation means that some traditional approaches of leaders who are facing growth or profit crunches can no longer be used. That means:

- No debt or much less debt
- No ability to throw capital around.
- Growth must come organically not just through M&A
- No "financial engineering" to paper over fundamental corporate problems
- Much less risk tolerance by boards

So most if not all of the traditional MBA bromides can't be employed.

"….How do you train leaders to manage and guide organizations that must still increase shareholder value when overall GDP growth in real terms is zero?…."

And now leaders can't even count on employees. Compensation is going to continue to decline in real terms. Employees will continue to be viewed ever-more as variable costs. There will be fewer of them. They won't have pensions. They will only get training when absolutely needed and this will increasingly be vocational, technical or tactical in nature. So employee loyalty will continue to diminish.

"Rational" Decision-Making Often Leads to Bad Financial Outcomes

The new normal coincides with another major trend. The behavioral disciplines are now revealing new findings in decision analysis. These demonstrate that most of the approaches that we consider to be "rational" are in fact driven by unconscious cognitive biases that skew our decisions dramatically away from what is truly rational.

This explains why apparently brilliant executives and leaders can make obviously wrong decisions that yield terrible results. We saw this in the US financial crisis. The Europeans have essentially the same problem. Firms such as Lehman and Bear Stearns that at the time were considered to be paragons of brilliant decision-making also demonstrate this effect.

The behavioral disciplines have discovered that there are numerous cognitive biases which lead to decisions being bad. One of these biases, the framing bias, where we tend to view decisions within the framework of what we unconsciously desire to be the case, means that in many situations, having more information actually leads to worse decisions.

Yet business education is still founded on the pillar of rationality and data analysis without consideration of how these real-world behavioral phenomena impact the decisions of leaders. Leadership development programs still focus on case studies that assume that we will act wisely and in everyone's best interests when we have enough information.

So we have two recent phenomena to consider. One is that the new normal is no growth. The second is that most decisions are skewed towards poor financial outcomes. Could these two be linked/ Could it be that bubbles are driven by unconscious biases that lead to terrible financial outcomes? That we are doomed to repeat these until we understand these behavioral phenomena?

"….Leadership development programs still focus on case studies that assume that we will act wisely and in everyone's best interests when we have enough information…."

Increasingly both researchers and experts are coming to see this as being the case. Authors such as Nouriel Roubini and Malcolm Gladwell have understood the zeitgeist in a way that many academics and political leaders have still not yet grasped.

In order to escape from the current economic trap of the new no-growth normal, leaders have to start understanding that they will be part of the problem until they understand their own behaviors deeply enough to show them how to compensate for their own cognitive biases..

Leadership development, executive training and corporate learning strategies have to develop new strategies for the new normal so that they can address the problem constructively. It is not an option to continue with the same learning and leadership development strategies that may well have caused the problems we have already experienced.

The "New Normal" Requires a Laser Focus on How Behavior Impacts Financial Outcomes

Before the new normal, leadership development was focused on bringing about improved team and corporate functioning and increased employee loyalty and engagement. These issues need to be addressed still.

But in view of the dramatically changed conditions of the new normal, there are even higher priority issues to be addressed. These center around how to create capital in no-growth and even declining markets.

In particular training needs to show leaders how to adjust and change their behaviors to focus specifically on those that create capital and how to reduce those behaviors that increase the risk of capital consumption including the risk of corporate failure. This feat must be accomplished while at the same time still accepting an appropriate level of risk so that rewards are not adversely impacted by behaviors that are overly cautious.

These issues include showing leaders and managers how to help:

- Employees and customers with capital creation through deleveraging behaviors
- Managers with capital increasing behaviors through more innovation and less resource utilization
- Partners and suppliers with capital-increasing behaviors
- Companies with capital increasing competitive-strengthening behaviors.

It is increasingly imperative that companies deliberately set out to develop:

- Innovator <u>behaviors</u> (as distinct from innovation processes)
- Cost leadership <u>behaviors</u> (as distinct from cost reduction processes)
- Lower-risk <u>behaviors</u> (not just lower-risk processes).

This training and development needs to focus on showing how some of the findings of the behavioral disciplines such as behavioral finance and behavioral economics can be leveraged to improve their decision-making and financial outcomes. This must also include increasing the sensitivity of leaders and managers to the cognitive biases that they have not hitherto recognized which will also impact them personally in their work and personal life.

Specific Actions to Address Leadership Challenges of the New Normal

Companies are going to need to develop and conduct new types of training courses for both emerging and existing leaders in order to address the new set of challenges of the new normal. Some of these are:

- Training in behavioral finance – how behavior impacts financial outcomes and how to leverage this knowledge to improve the value of companies in an era of no- or negative growth
- Awareness training in cognitive biases and what types of biases specific individuals are subject to, in order to improve their effectiveness in decision-making and in order to avoid unconscious biases which will lead them to making decisions with poor financial outcomes
- Training and development in business acumen – behaviors that lead to positive financial outcomes, and to show how to avoid approaches which depend purely on financial engineering which do not result in sustainable financial results since they are not behaviorally-based
- Training to show the precise links between cognitive biases, decision-making approaches and their impact on real-world financial statements
- Training via simulations which put these lessons into practice in real-world situations which highlight the difference between case-studies and behavior in real situations

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