THE LEADERSHIP VALUE CHAIN

Linking Leaders to the Fate of Organizations

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SUMMARY

The Big Idea

There is little question that leadership is vital to organizational effectiveness. Lots of studies show that changes in leadership are followed by changes in company performance. But it isn't clear – among leadership scholars or HR leaders alike – *how* leaders impact the fate of firms.

I propose that we can identify, understand, and even measure the active ingredients that connect leaders to organizational effectiveness by applying value chain logic to the problem.

This presentation describes the *Leadership Value Chain*, a framework that links characteristics of individual leaders to their leadership style; leadership style to impact on unit processes; unit processes to unit results; and unit results to effectiveness across a broad range of firm-level performance measures.

The point of the *Leadership Value Chain* is to lay out the sequence of key variables and considerations that relate individual leaders to organizational effectiveness. Of all the things we *could* measure, these are the things that we *must* measure to determine the value of leadership. Moreover, the framework is an aid to thinking strategically about key leadership decisions and investments.

Key Points

Who leaders are determines how they lead. We can measure the personal characteristics of leaders – their inherent attributes like personality and cognitive abilities; their acquired characteristics like knowledge, experience, and skill; and their social capital in the form of networks and relationships. Likewise, we can also measure their leadership style – the actions they take and the choices they make. These metrics tell us who leaders are and what they do.

We also need to look at the impact of leadership. Since leaders get results through other people, it makes sense to look at how they affect processes separately from the outcomes achieved by the units for which they are responsible.

In terms of impact on processes, there are three levels of analysis to consider. At the employee level, we can assess how leaders affect attitudes, engagement, and job performance. At the team level, we can examine how leaders affect team dynamics and the climate around the work group. And at the organizational level unit goals, staffing, and policies are affected by leaders. Taken together, how leaders affect employees, teams, and their units tell us "how they played" and give us a point of reference for why the unit achieves what it does – or doesn't.

Further downstream are unit or team outcomes. Following the balanced scorecard, we can identify a range of outcome metrics that indicate unit effectiveness. These include measures of productivity, financial performance, customers, and human resources.

Leaders should be held accountable for the performance of their unit in terms of both how their team plays (processes) and what it gets done (outcomes). Note, however, that the unit of analysis here is not the leader; leadership effectiveness is about the performance of a *team*.

Finally, at the organizational level, effectiveness is a product of the performance of distinct organizational units and is the responsibility of the CEO and the top team. I propose productivity, financial, customer, human resources, and a new category, "purpose," for measuring the impact of leadership at the firm level.

Applications

The *Leadership Value Chain* can be used to guide critical talent management activities. For instance, it can provide an integrated basis for decisions about selection and succession, training and development, performance appraisal, compensation, and organizational development interventions.

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Robert B. Kaiser, Kaplan DeVries Inc.

We take it for granted that leadership matters. And for good reason: beyond our everyday intuition, rigorous research has documented a link between leaders and organizational effectiveness. For example, one study of the financial utility of executive leadership estimated that high performing executives add, on average, $25 million in value more than average performers over a typical tenure.[1] Another study concluded that CEOs account for 14% of the variability in firm financial performance. To put that in perspective, industry sector accounts for 19%.[2] Thus, deciding who will lead is nearly as consequential as the choice to sell pharmaceuticals, undergarments, or automobiles.

It is one thing to know that leaders play a decisive role in the fate of organizations; it is a different and more helpful thing to know *how* they make a difference. I have spent much effort combing through the business press and the academic literature looking for data-based models that explain how leaders make a difference. There are many frameworks that capture pieces of the puzzle; but I have not found anything that gives the whole picture.

In this paper, I describe a framework to fill this void. I call it the *Leadership Value Chain* because the basic concept comes from value chain logic.[3] The goal is to identify the sequence and classes of variables that transform a particular input (individual leaders) into a valued output (organizational effectiveness). The reason for doing this is that understanding the value of leadership is important yet not well developed. It is also a complex problem. My goal is to cut through the difficulty of the task by distinguishing, amid all of the many different things we *could* consider, what are the essential things that we *must* consider to determine the value of leadership?

After providing a bit of background, I describe the elements in the *Leadership Value Chain* and suggest ways to measure them. At the end, I acknowledge limitations to the model and close with examples of how senior HR and talent managers can apply the framework in thinking strategically about key leadership decisions and investments.

Background

It may be helpful to describe my interest in measuring the value of leadership. I'm an odd species, neither fish nor foul: I spend my time as both a leadership scholar and as a consultant coaching individual leaders, developing assessment systems, and helping organizations frame problems and then do research to address them. I come at the question of the value of leadership both practically and scientifically. And I don't accept that there are lower standards for practice than science. After all, since the practice of leadership carries implications for thousands of employees and the local economies that are the foundation of communities, shouldn't we use a higher bar?

Simplifying the Complex

There were two needs that prompted the development of the *Leadership Value Chain*. First, our R&D team needed a way to think about criteria for validating new leadership assessment tools and development interventions. Second, the question of how leaders add value is on everyone's mind, but the problem seems hopelessly complex. As I looked to both the scholarly and practitioner literatures, I was disappointed by the lack of a comprehensive framework.

And then struck necessity, the mother of invention. It became evident in a research project for a client organization that the various stakeholders were not on the same page. Our goal was to identify the things managers did to boost and depress the engagement of their employees. But the stakeholders seemed to be talking past each other: The HR folks were interested in behaviors; the senior leaders emphasized engagement scores; and the middle managers, skeptical of the concept, wanted to know if engagement was related to the bottom line. We needed a common mental model.

We put forward an early version of the *Leadership Value Chain* as a way to call attention to these distinct components and how they fit together. With the team on the same page, we could more effectively communicate and design, execute, and interpret the study.

It was striking how this framework facilitated our group task. When I first presented it at a professional conference, the reactions were equally surprising.[4] As my colleague, Amy Webb, said, "Any savvy HR person could sit down and draw this out. The fact that you took the trouble to do so is a big help." I can only hope she is right.

Fair warning: the *Leadership Value Chain* and the discussion around it are not simple. This framework goes well beyond a 2 x 2 matrix. I am forsaking the value of simplicity in deference to the complexity of the topic. My hope is that as you go through all of the moving parts you will find what Oliver Wendell Holmes called "the simplicity on the other side of complexity."

Defining Leadership

All discussions of leadership rest on an assumption about what the term means. The thinking behind the *Leadership Value Chain* is guided by the view of leadership put forth by Robert Hogan.[5] According to this view, based on an analysis of human origins, leadership is an evolved solution to the adaptive problem of collective effort. Fundamentally, leadership concerns influencing individuals to transcend their selfish short-term interests and contribute to the long-term performance of the group. Thus, the essence of leadership is building a team and guiding it to outperform its rivals.

There are two important points about this definition. First, leadership is not about individuals called leaders; it is about the team for which the leader is responsible. The second point follows the first and is that an evaluation of leadership effectiveness should concern team performance.

This may seem obvious. Yet a recent study we did suggests it is worth emphasis. We reviewed the psychological literature on leadership and examined how researchers define effectiveness. We created a classification system for measures of leader effectiveness and then counted how often they were used in over 1,500 statistical analyses.[6] The results were telling of an individual bias: the majority of measures of leadership effectiveness (57%) had nothing to do with team or group performance and instead reflected evaluations of the individual leader. They had to do with variables more concerned with the manager's career success (e.g., ratings of potential, "promotability," overall job performance). Moreover, of the minority of studies that examined team performance, nearly three-quarters were concerned with team processes (e.g., subordinate job satisfaction, motivation, and commitment; team cohesion). The least used measures of leader effectiveness concerned business results – unit productivity, profitability, customer satisfaction, and so forth.

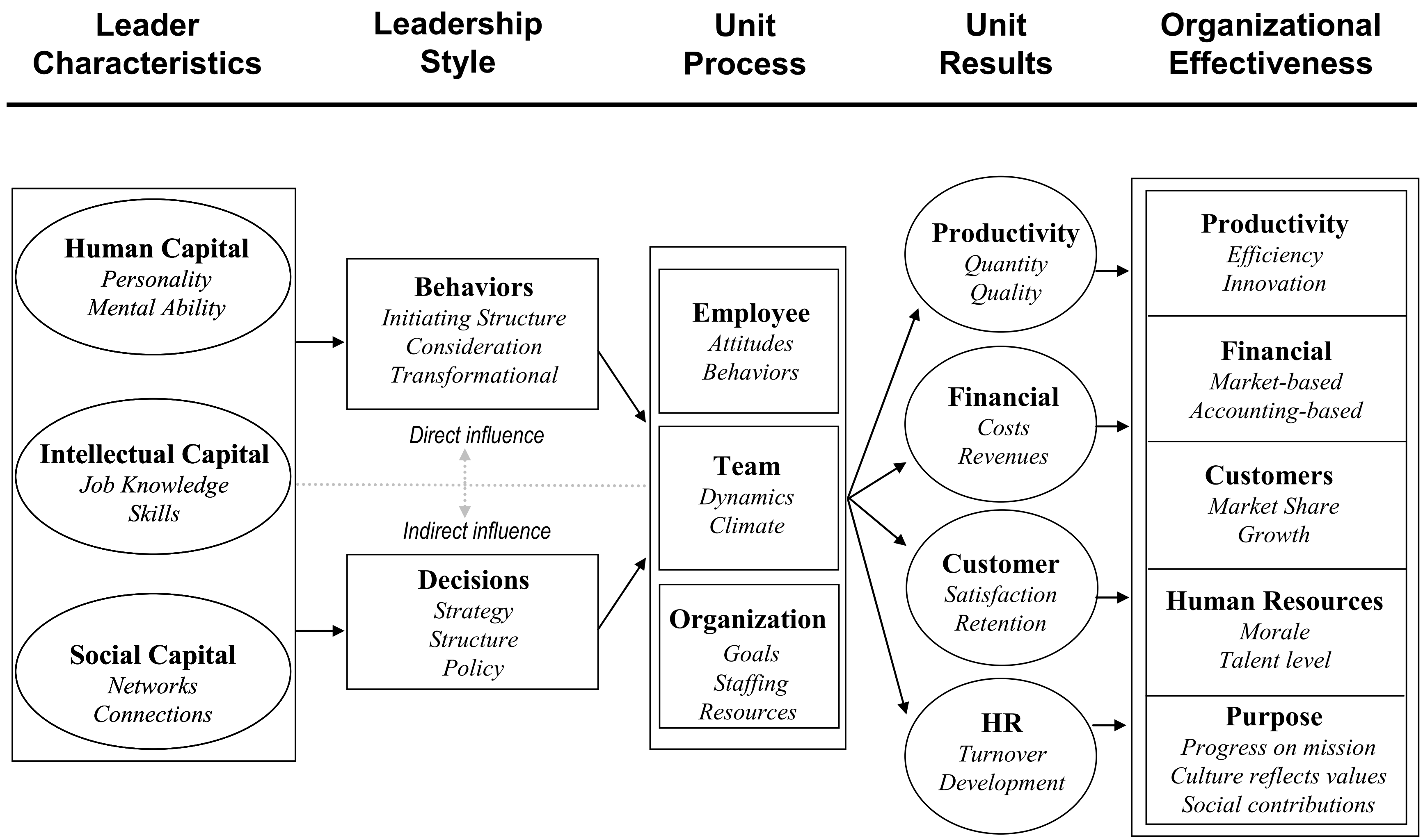
The point is that even professional researchers often make a mistake in measuring the value-added of leadership by focusing on the leader as the unit of analysis. If the purpose of leadership is to unite people in the pursuit of a common purpose, then the bottom line is how the team is doing at reaching that goal.

The Leadership Value Chain

Figure 1 (on the next page) presents a visual representation of the *Leadership Value Chain*. The label "value chain" is used to connote that the framework is intended to classify distinct variables and represent how their inter-relationships transform inputs into valued outputs. The idea is familiar to managers and seems apt to the question of how leaders contribute to organizational effectiveness.

At first glance, this schematic may appear to be just another taxonomy – a confusing and overwhelming list of variables. But if we take each of the categories one column at a time, they will each make sense as will the relations among them.

Figure 1. ***The Leadership Value Chain***



Note: Specific variables (*in italics*) within each domain are meant to be illustrative and not definitive. The important feature of the framework is the classification of each domain as residing in a particular stage in the sequence linking individual leaders to organizational effectiveness.

Leader Characteristics

The *Leadership Value Chain* begins by considering the things that make individual leaders different – their knowledge, skills, abilities, and personality characteristics. These individual differences represent who leaders are.

One way to organize this domain is provided by the various types of capital discussed in the HR literature.[7] Perhaps due to their relative youth, the terms human-, intellectual-, and social capital appear to be used inconsistently. It makes sense to me to distinguish them as follows: Human capital refers to inherent person characteristics like personality and mental abilities; intellectual capital considers things acquired through experience like job knowledge and skills; and social capital includes relational characteristics like networks and professional contacts.

Regardless of how the individual differences are categorized, each class can be quantified. For instance, consider human capital. Modern personality assessment is quite robust and effective. Perhaps the best tools for use at work are those from Hogan Assessment Systems. When used according to the underlying theory, the evidence is compelling that these tools measure personality and are highly valid at predicting a wide range of dimensions of job performance, including leadership and derailment.[8] General mental ability, or IQ, is also a robust predictor of leadership.[9] There are many well-developed and easy-to-administer measures of IQ, including the Watson-Glaser Critical Thinking Inventory and the Wonderlic.

Emotional Intelligence is more suspect; most supposed measures of EQ are nothing more than repackaged personality scales. However, there is one particular instrument, the Mayer-Salovey-Caruso Emotional Intelligence Test, which measures EQ as a true mental ability that is both distinct from IQ and personality and also makes a unique contribution to the prediction of job performance.[10] It is worth noting that this test was developed by the scientists who first introduced the concept and were subsequently ignored as the popular press ran wild with the idea.

Intellectual capital is more difficult to measure and well-validated, standard assessment tools are harder to find. However, the biodata method appears promising for measuring experience. And assessment centers, with high fidelity simulation and trained observers, may be a good method for assessing knowledge and skills. Measures of social capital are least developed; it appears that more conceptual and empirical research is needed to quantify social relationships. Nonetheless, the task should bear fruit; as the old adage goes, it is not what you know but who you know.

One critical individual difference variable that is difficult to categorize is learning orientation. Perhaps it is best seen as a bridge between human capital and intellectual capital. At any rate, the importance of learning and continued self-development cannot be overstated.[11] There are good measures of learning style and learning agility. There is also a compelling psychological literature on learning and underlying motivations to learn, but further development is needed to capitalize on this knowledge in practice.[12]

An important point about these variables is that they may be the best measure of potential. They are transportable characteristics and no matter where you go, there you are. This suggests that these measures can be used to measure the talent level of an individual or of an employee body. Moreover, since these characteristics represent who leaders are, they are the drivers of leadership style.

Leadership Style

Individual differences are relevant to the extent they are expressed in how the leader leads. I take an interdisciplinary view of leadership style and see two key aspects: behaviors (the actions leaders take) and decisions (the choices they make).

The psychological study of leadership has focused on behaviors – being considerate, showing initiative, transforming followers, exchanging transactions, and so on. Management research emphasizes decision making in such domains as strategy, structure, policy, and so forth.[13] The behavioral and the decision-making aspects of leadership style are complementary; they serve unique influence functions. Direct influence is a face-to-face, interpersonal matter involving behavior whereas indirect influence is a relatively impersonal process of guiding people by setting direction, implementing systems and structures, and establishing formal policy.[14] Both types of influence are important to leading a high performing team.

This distinction is represented in Figure 1 by a line distinguishing direct influence as concerning the behaviors that directly motivate employees and galvanize teams – versus the behaviors that demoralize employees and weaken teams. Below the line, indirect influence is portrayed as making decisions about strategy, structure, and policy that has its indirect influence on employees by providing guidance and constraints by shaping their work environment.

The behavioral view of leadership style is the predominant one; it is the basis for most research measures as well as the ubiquitous 360-degree feedback tool. The decision-making aspect seems to deserve greater attention, especially given how we all intuitively understand the important role of judgment in leadership. Furthermore, there is a good deal of research in the management sciences that demonstrates how leaders have a fairly consistent preference for certain kinds of strategic decisions (e.g., whether to grow or defend a position), structural designs (e.g., centralized vs. decentralized), and fiscal policy (e.g., acquisition through cash or stock).

This leads to a difficulty in measuring leadership style. On the one hand, measures of leader behaviors are commonplace. On the other hand, measures of preferred decisions are less common and less well-developed. A lopsided assessment strategy that only picks up the behavioral piece is inherently limited.

Another difficulty in measuring leadership style is that it is routinely done with coworker ratings. The problem is that ratings do not measure behaviors – ratings measure *perceptions* of behavior. Thus, they are susceptible to all kinds of perceptual biases. One problem that severely compromises the use of ratings is that they are saturated with liking; several studies have shown that a substantial portion of differences in ratings is due to how much the rater likes the person being rated.[15] Thus, relying on ratings alone amounts to a *de facto* popularity contest. And as we all know, sometimes leaders have to go against the grain.

What are the alternatives to ratings? From a pure measurement perspective, job simulations and assessment centers may be viable. Admittedly, their cost relative to ratings may yield little utility. Leadership style may well be the weakest link in the *Leadership Value Chain*.

A final concern about measuring leadership style, especially with ratings, is that it reflects how leaders are seen in their current role. Thus, they say very little about potential and likely performance in a different role. This becomes paramount in promotion decisions because the behaviors that lead to success in an executive job, for instance, are dramatically different from those associated with success in a middle management job.[16] Therefore, succession planning efforts that exclusively rely on assessments of current performance are ill-advised. Certainly current (and historical) performance should be considered, but the smart money is to do so in the context of how role requirements may differ in the next job.

Of course, assessments of how one leads are important for understanding the performance of the team one is currently responsible for.

Unit Process

The behavioral and decision-making aspects of leadership style impact organizational performance through their effects on the organizational unit. Put simply, leaders get things done through other people. Influencing people, teams, and organizational features is the proximal effect of leadership; like falling dominoes, the proximal effect leads to business results as a distal impact. If unit processes reflect how the team plays, then unit outcomes indicate their win/loss record.

It is important to conceptualize the impact of leadership on how the team plays at multiple levels of analysis. Three distinct levels include the individual employee, the team, and the organization itself.

Leader behaviors have a direct influence on individual employee's attitudes (e.g., job satisfaction), motivation (engagement), and behaviors (performance). Leader behaviors also affect team dynamics and climate – for instance, by facilitating communication and coordination, rewarding or sanctioning certain behaviors, and modeling norms and interaction patterns. Leader decisions also indirectly influence employees and teams by defining such organizational features as goals, who to put in what role, and how to allocate resources. These expressions of strategy, structure, and policy shape the organization which delimits and guides employee choices and actions.

The measurement of unit processes becomes increasingly more difficult as you move from the employee to team to organizational levels. At the employee level, important things to consider are job satisfaction, engagement, and job performance (e.g., quantity/quality of individual output). At the team level, dynamics and climate should be assessed. Team dynamics refer to how the team functions as a group and includes such things as cooperation, communication patterns, cohesion, and group confidence. These can be measured through surveys that ask employees to describe the team or group as a whole. Unit climate considers the environment surrounding the team and can be assessed with climate surveys that tap such things as stress, customer service orientation, support for innovation, and so forth.

Like measuring leader decisions, measuring leader impact on the organization poses difficulties. The development of measures of phenomena at this level has been slow-going. One possible solution is to ask more senior leaders – who presumably have an adequate frame of reference and basis for judging – to evaluate the unit's goals, staffing, and use of resources.

Thus, the mechanisms through which leadership style drives unit results operate at the employee, team, and organizational level of analysis. Collectively, a leader's impact across these three levels can be seen as creating a context for performance, because the leader's job is to facilitate team performance. On the one hand, this promotes an internal focus – with an emphasis on activities within the unit. On the other hand, because contexts can be more or less conducive to performance, this explains why a team achieves what it does, which is directly reflected in unit outcomes.

Unit Outcomes

The next category pertains to the results the unit produces over a given period of time. I believe that unit results are the best measure of leader effectiveness. And I find it surprising how infrequently unit performance is explicitly measured and reflected in the evaluation of managers. It is often said that results are affected by things beyond a leader's control – changes in the market, regulations, suppliers, and the like. This argument makes little sense; as Robert Hogan puts it, "Spin is about why we lost." And leaders are paid to win. Moreover, unit results are the primary contribution each individual leader makes to the fate of the overall institution and so represents tangible value.

There are several distinct kinds of unit performance indices and none provides a complete picture; however, a range of financial and non-financial metrics can collectively provide a balanced scorecard. The standard scorecard template put forth by Robert Kaplan and David Norton and adopted and adapted by many Fortune 500 companies includes four general categories: productivity, financial, customer, and human resources.[17]

Productivity measures of unit performance concern the quantity and quality of goods and/or services produced by internal business processes. Another class concerns financial results – measures like revenues, costs, or the ratio of revenue to costs (i.e., profitability). Increasingly important are customer-oriented measures of unit performance – customer satisfaction, retention, and growth. Finally, human resource-based measures of unit performance include such variables as safety/accident rates and rate of voluntary turnover. In the modern era of scarce talent, it also makes sense to index the extent to which leaders are developing their subordinates into future leaders.

There are two things worth emphasizing about unit-level results. To compare results across units, it is important to put the measures on a common scale. For instance, straight measures of unit revenues will not provide an even comparison between leaders of units of different size. Common techniques for equating in such a case include computing the ratio of revenue per employee or revenue as a percentage of budget. An alternative technique is to express these metrics in a percentage reflecting what was achieved relative to objectives (i.e., percent of plan).

The second point is that the choice of a specific type of measure for representing the productivity, financial, customer, and human resource categories should be grounded in the nature of the organization, its industry, and strategic orientation. For instance, in a highly commoditized industry, an emphasis on costs may be more relevant than revenues. In a growth-oriented business, customer metrics may dominate.

A recent article by John Boudreau and Peter Ramstad describing a new paradigm of decision science for HR suggests how the optimal choice of business unit metrics may vary from organization to organization.[18] They provide guidance and emphasize how the decision sciences provide a flexible architecture in which choices about what to measure can be more tailored and strategic yet still focused and disciplined.

Although perhaps not exhaustive, these four categories of business-unit results seem adequate for classifying the majority of measures reported in the research literature. Moreover, they reflect the metrics used by best-practice organizations to monitor unit performance. As the term "balanced" scorecard suggests, it is imperative to employ a broad range of measures because the real world of leadership is fraught with trade-offs and conflicting values.

Organizational Effectiveness

In the final analysis, what matters to enduring value and the fate of organizations is effectiveness at the overall institutional level. This is effectively the "unit" for which the CEO and the top team are responsible. Theorists take a gestalt view of performance at this the organizational level and see it as more than simply a linear sum of the performance of the various units.

Thus, although the performance of individual business units contributes to organizational effectiveness, it is a larger concept. It does, however, involve similar content. In the *Leadership Value Chain,* organizational effectiveness is represented with the same four general categories used at the unit level, although using alternative measurement techniques within each. Also, there is a fifth category having to do with the realization of the firm's purpose, its reason for being.

Broadly conceived, organizational productivity reflects the efficiency of business processes in transforming inputs (capital, people, materials) into outputs (goods and services). Indicators here are derived from those at the unit level (e.g., quantity and quality). Rate of innovation could also be included. Note that these measures reflect an internal perspective and overlook the fact that organizations compete against one another.

Consider the Harbour Report, which tracks productivity in the automobile manufacturing industry. The most recent release indicated that productivity increased for General Motors (GM) by reducing the time it takes to produce a vehicle in its North American plants to 34 hours. However, it also reported that Toyota's North American plants took only 28 hours to produce a vehicle.[19] It is more informative to compare within-organization measures of performance to a meaningful external standard, such as the industry average or a competing organization's standing on comparable figures. In this example such a comparison helps to explain why, despite productivity gains, GM continues to lay off employees, lose market share, and post declining profits: its rate of efficiency improvement lags behind that of its rivals.

Thus, measures of organizational effectiveness should be put on a normative metric to be interpreted.

The second category of organizational effectiveness measures concerns financial indicators. It is important to consider two types of these, market-based and accounting-based. Market-based measures are thought to be forward-looking because they represent perceptions of both current and potential wealth creation. They concern profitability and shareholder value and are represented by such measures as total shareholder return (TSR), price-to-earnings ratio, and Tobin's Q ratio (market value divided by cost to replace assets). There is general agreement that market-based measures are superior to accounting data because they are less subject to manipulation.[20] Nonetheless accounting data can provide meaningful and unique information. They differ from market-based measures in that they reflect an historical perspective. Common examples include earnings per share, return on investment or assets or equity, earnings growth rates, and economic value added (EVA, operating profit less taxes and the cost of capital).[21]

Customer service indices comprise the third category of measures of organizational effectiveness and, like unit results, concern customer satisfaction, retention, and growth. Market-share is another example of such a measure often applied at the organizational level. The fourth category, human resource-based measures, reflects how well the organization is managing talent. Aggregate indices in this group include rate of turnover and morale. A case can also be made for including bench strength – the number and quality of future leaders. Like the other metrics, customer and human resource measures should also be normed to industry standards.

An important point about customer and human resource-based measures is that, while they are not reflected directly on the "bottom line," they are crucial to the sustainability of current levels of productivity and financial performance. That is, when hard results are achieved in a manner that alienates customers and demoralizes employees it is likely that the organization will suffer a reversal of fortune.

The final category of effectiveness measures concerns achieving the organization's purpose. This class of variables is conceptually the more ambiguous and difficult to articulate. By definition, it is essentially an idiographic construct – key organizational stakeholders define its *raison d'être* and it doesn't necessarily require reference to external standards. Typically, an organization's purpose is codified in its mission statement and these usually refer to intangible, value-laden aspirations that may defy precise quantification.[22] Nonetheless, progress toward the mission tells us whether the organization is doing what it set out to do and provides a larger sense of meaning for employees, customers, and even society.

A concept that is often discussed in close association with purpose and mission is core values. These refer to deeply held beliefs and feelings about the right way to be. How do we know if an organization is living its values? By its culture. It has been said that culture is "the way we do things around here," implying that it may or may not be consistent with the values espoused by key stakeholders.[23] Organizational culture is a function of senior leadership and they have responsibility for ensuring that the kinds of things that get modeled, rewarded, and reinforced are consistent with the company's core values. There may be nothing more demoralizing than working for a company that claims to believe in one set of values (e.g., diversity, fairness) yet consistently practices another (e.g., good ol' boy networks).

Finally, assessments of organizational purpose should also consider what the company does for the community. Corporations were originally given charters to enhance the local economies and societies in which they operated. The reason is more pragmatic than ideological: there is a symbiotic relationship between organizations and communities, such that the health of one affects the health of the other.

Taken together, these measures of business results map the domain of organizational effectiveness, perhaps the ultimate measure of the value of leadership.

Caveats

Having laid out this conceptualization of the complex set of variables needed for measuring the value of leadership, we should turn to a few limitations of the framework. These are mostly concerns related to context. Organizations do not exist in a vacuum; they are part of a larger environment and the implications of this are worth noting.

One obvious factor is that the unit results and organizational effectiveness measures pertain to for-profit businesses. The *Leadership Value Chain* was created for use in work with these kinds of concerns. It would seem to apply to privately held, for-profit companies as well. But application to non-profits and government organizations like the military and educational institutions will require further refinement and customization.

I believe, however, that the front half of the model, from leader characteristics through impact on unit processes, applies to all organizations. There is, however, one qualification for this: the relationship between leadership style variables and the impact on unit processes and outcomes may vary by hierarchical level. Research I have done with Bart Craig shows how the effectiveness of various leader behaviors varies dramatically as a function of level.[24] For instance, for middle managers, a directive and non-empowering style appears most effective; the exact opposite spells success for executives.

Another limitation is that not every variable relevant to leadership and value is here. Rather, I have tried to identify the more critical variables that must, by necessity, be considered. Einstein is said to have claimed, "The problem with a map with a scale of one mile equals one mile is that you no longer need a map." This is to say that models like the *Leadership Value Chain* are heuristic devices; they are decision aids that try to reduce complexity to a manageable set of considerations that the human mind can deal with. Some factors are no doubt neglected. My only hope is that I've specified the most important ones, and if I haven't, then perhaps someone will kindly point out my oversight and direct us toward a more useful framework.

Applications

At this point, we have covered a lot of ground in conceptual terms. Perhaps it would help to describe specific applications of the *Leadership Value Chain*. In this final section, I will focus on examples of applying the framework in practice.

The primary use of the *Leadership Value Chain* is to identify and specify the full gamut of factors that must be considered in understanding how individual leaders contribute to organizational effectiveness. The model intentionally includes many components, and that can be both a strength and a weakness. It seems fair to say that most of us prefer simple models – the ever-present 2 x 2 matrix, for instance, like the one made popular by GE that juxtaposes results by values to capture what leaders get done and how they do it. Or selection decisions that are made with implicit criteria that go something like this: "We need leaders who are participative – this candidate isn't very participative, so she is disqualified."

The problem with these kinds of mental models is that they only cover a subset of the important ground linking leaders to organizational effectiveness. In evaluating leadership and trying to understand why it matters, these models tend to stop prematurely. Not every talent management decision or value calculation problem necessarily requires that we consider all of the pieces to the *Leadership Value Chain*. But having them laid out before us at least raises the question of what needs to be considered and helps us guard against overlooking critical factors.

One application is in leader selection and succession decisions. A full range of categories to cover in a blended assessment of candidates is suggested by the *Leadership Value Chain.* The best practice is to start with a clear definition of the role based on what the organization needs from the particular unit given its strategic outlook. For instance, is it a turn around situation? A start up? A mature industry? Is morale low and turnover a problem? Based on the role requirements, you can work backwards through the value chain to define the ideal leadership style for the situation. And this naturally suggests the required human-, intellectual-, and social capital. Now we have a clear sense of the job qualifications to look for in a candidate. A full assessment would require sizing up personality and relevant mental abilities, taking stock of relevant work experiences and skills, and getting a sense of networks and other connections that are helpful. Where possible, it is also helpful to understand the individual's track record: if the person has held a similar job in a similar situation, what kinds of productivity, financial, customer, and HR results were achieved? How did the leader impact employees and the way the team functioned? And what kinds of behaviors and decisions did the leader employ? Taken together, this kind of information on each candidate provides for a more informed selection decision – far more than is typically the case.[25]

The *Leadership Value Chain* also lends itself to training and development decisions. For instance, when unit results are not as desired, it raises the question of unit processes and how they are affected by leader behaviors and decisions. A diagnoses of whether the issue is a goal, structural, or resource problem versus an attitude, motivation, or behavior issue with individual employees or troublesome dynamics within the team can help direct T&D efforts most efficiently to the aspects of how the leader is leading that offer the most leverage.

Performance appraisal is another activity that can be informed by the *Leadership Value Chain*. It seems that a full leadership physical ought to include assessments of unit outcomes and unit processes at a minimum. Institutional measures for the outcomes should be fairly easy to compile. Unit processes may be more difficult, but can be accomplished with climate surveys for employee and team functioning and with the judgment of superiors about goals, staffing, and resource utilization. For the conversation to be developmentally-oriented, some focused assessment of the individual's leadership style – both behaviors and decisions – is also needed. The best source of data may be the subordinates of the work unit, as in an upward feedback process.

Similarly, the *Leadership Value Chain* is relevant to compensation decisions. Tying variable pay to unit outcomes and unit processes is a sure-fire way to put a laser focus on adding value and doing so in a way that is sustainable.

Finally, it seems that organizational development interventions at least implicitly rely on something akin to the *Leadership Value Chain.* When organizational effectiveness comes up short, the natural next step is to get a reading on how the various business units are performing. For those that are found wanting, a follow up assessment of what is going on in the unit is warranted. And problems here may be traced back to leadership. If the issue is with the leader, then it raises the question: is it a selection or a development problem?

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Rob has over 60 publications, presentations, and workshops on leadership, assessment, personality, executive development, and organizational effectiveness. His article on measuring and developing leadership versatility with Bob Kaplan in the *Sloan Management Review* won an award from MIT and Pricewaterhouse Coopers in 2004.

Rob also has an active consulting practice; he specializes in coaching high potentials. And he offers a unique service of contract research to help companies frame, study, and solve vexing leadership issues – from creating corporate leadership models to revamping internal assessment systems to linking development investments to strategic business goals.

Rob earned a B.S. in Psychology and Sociology and an M.S. in Industrial-Organizational Psychology from Illinois State University. He lives in Greensboro, NC with his wife, Molly, and their children, Claire and Ben.

Endnotes

1 Barrick, M. R., Day, D. V., Lord, R. G., & Alexander, R. A. (1991). Assessing the utility of executive leadership. *Leadership Quarterly, 2*, 9-22.

2 The estimate of the impact of CEOs on financial performance comes from: Joyce, W.F., Nohria, N., & Roberson, B. (2003). *What really works: The 4+2 formula for sustained business success*. New York: Harper Business. The estimate of the impact of industry is from: McGahan, A.M. & Porter, M.E. (1997). How much does industry matter, really? *Strategic Management Journal, 18*, 15-30.

3 My use of value chain logic is inspired by: Porter, M. (1985). *Competitive advantage: Creating and sustaining superior performance*. New York: Free Press.

4 The *Leadership Value Chain* was first presented in a conference symposium I chaired on *Making Leadership Research More Relevant*: Kaiser, R. B., & Ferrell, S. G. (2005, April). *Leadership and the fate of organizations: On the measurement of effectiveness*. Presented at the 20th Annual Conference of the Society for Industrial and Organizational Psychology, Los Angeles, CA.

5 Hogan first made this case in a widely read article: Hogan, R., Curphy, G. J., & Hogan, J. (1994). What we know about leadership: Effectiveness and personality. *American Psychologist, 49*, 493-504. We have emphasized the point in subsequent papers, including: Hogan, R., & Kaiser, R. B. (2005). What we know about leadership. *Review of General Psychology, 9*, 169-180.

6 The research was reported in the presentation described in Endnote 4: (Kaiser & Ferrell, 2005, *Leadership and the fate of organizations*).

7 For instance: Boudreau, J. W., & Ramstad, P. M. (1997). Measuring intellectual capital: Learning from financial history. *Human Resource Management, 36*, 343-356.

8 See, for example, an impressive meta-analysis demonstrating notably higher validity coefficients than is typically reported for personality in: Hogan, J., & Holland, B. (2003). Using theory to evaluate personality and job performance relations: A socioanalytic perspective. *Journal of Applied Psychology, 88*, 100-112.

9 For a meta-analysis of the validity of cognitive ability in leadership see: Judge, T. A., Ilies, R., & Colbert, A. E. (2004). Intelligence and leadership: A quantitative review and test of theoretical propositions. *Journal of Applied Psychology, 89*, 542-552.

10 Information on the MSCEIT and a wealth of validity research on the ability-based model of emotional intelligence is freely available at: http://www.emotionaliq.com/

11 The pivotal role of learning as revealed in research on executive development is summarized in: McCall, M. W., Jr. (1998). *High flyers: Developing the next generation of leaders*. Boston: Harvard Business School Press. The importance and assessment of learning agility is described in: Lombardo, M. L., & Eichinger, R. W. (2000). High potentials as high learners. *Human Resource Management, 39*, 321-330.

12 This work on learning motivation was inspired by: Dweck, C. (1986). Motivational processes affecting learning. *American Psychologist, 41,* 1040-1048.

13 For an encyclopedic reference to research on leader behaviors see: Bass, B. M. (1990). *Bass and Stogdill's handbook of leadership: Theory, research, and managerial applications* (3rd Ed.). New York: Free Press. A summary of research on leader decisions is provided by Finkelstein, S., & Hambrick, D. C. (1996). *Strategic leadership: Top executives and their effects on organizations*. St. Paul, MN: West Publishing.

14 For the distinction between direct and indirect influence, see: Zaccaro, S. J., & Horn, Z. N. J. (2003). Leadership theory and practice: Fostering an effective symbiosis. *Leadership Quarterly, 14*, 769-806.

[15] Both field experiments that examine performance appraisal ratings and scientific studies of coworker ratings collected for theory testing have demonstrated the large influence of liking. For example: Varma, A., DeNisi, A. S., & Peters, L. H. (1996). Interpersonal affect and performance appraisal: A field study. *Personnel Psychology, 49*, 341-360. And: Brown, D. J., & Keeping, L. M. (2005). Elaborating the construct of transformational leadership: The role of affect. *The Leadership Quarterly, 16*, 245-272.

[16] Interestingly, of seven distinct leader behaviors in this study, only learning orientation was a consistent positive predictor of effectiveness for supervisors, middle managers, and executives: Kaiser, R. B., & Craig, S. B. (2004, April). *What gets you there won't keep you there: Managerial behaviors related to effectiveness at the bottom, middle, and top*. Presented at the 19th Annual Conference of the Society for Industrial and Organizational Psychology, Chicago, IL.

[17] The surging popularity of the balanced scorecard holds out promise for advancing our understanding of how to assess the value-added of leadership: Kaplan, R. & Norton, D. (1996). *The balanced scorecard: Translating strategy into action*. Boston: Harvard Business School Press.

[18] Boudreau, J. W. & Ramstad, P. M. (2005). Talentship and the new paradigm for human resource management: From professional practices to strategic talent decision science. *Human Resource Planning, 28(2)*, 17-26.

[19] As reported in: *The Economist* (2005, June 11-17). General Motors: The lost years. *375*, 60.

[20] For a useful discussion of accounting measures and examples of how they can be manipulated, see: Anderson, J. R., & Tirrell, M. E. (2004). Too good to be true: CEOs and financial reporting fraud. *Consulting Psychology Journal: Practice and Research, 46*, 35-43.

[21] EVA is quickly becoming the preferred measure of firm performance: Stern, J. M, Shiely, J. S., & Ross, I. (2001). *The EVA challenge: Implementing value-added change in an organization*. New York: Wiley.

[22] An excellent discussion of the importance and difficult-to-grasp nature of values and organizational purpose is provided in: Collins, J. C. & Porras, J. I. (1997). *Built to last.* New York: Harper Business.

[23] This quote is often attributed to Ed Schein, but it also appears on p. 277 of: Burke, W. W. & Litwin, G. (1989). A causal model of organizational performance. In J. W. Pfeiffer (Ed). *The 1989 annual: Developing human resources*. San Diego: University Associates. Nonetheless, Schein's work on culture is a classic in the field: Schein, E. H. (1985): *Organizational culture and leadership*. San Francisco: Jossey-Bass.

[24] See the research described in endnote 16 (Kaiser & Craig, 2004, *What gets you there*).

[25] Research we did at the Center for Creative Leadership examining over 300 executive selection decisions revealed that the state-of-the-art left much to be desired: Sessa, V.I., Kaiser, R.B., Taylor, J.K., & Campbell, R.J. (1998). *Executive selection: A research report on what works and what doesn't*. Greensboro, NC: Center for Creative Leadership.