Sustainable leadership practices for enhancing business resilience and performance

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Implicit in the decision process of corporate leaders is a central question: what and who is this business here for? Many subscribe to the belief that the primary goal of leadership is to maximize shareholder value; their decisions determine whether shareholder value will be enhanced in the short term, the long term, or some combination of the two.

But the shareholder-first approach that originated and prevails in the Anglo/US world has received heavy criticism from a number of well-regarded management researchers.[1] Almost two decades ago, French economist Michel Albert wrote that in its extreme form, the sole pursuit of profit is a threat to neoliberal capitalism itself because the focus on short-term profits discourages long-term thinking, investing, and planning.[2] Charles Handy reminds us that the purpose of a business goes beyond making a profit to something better, a higher level purpose: ''Owners know this. Investors don't care.''[3] A few years ago in *Strategy & Leadership*, Michael Raynor[4] debunked the premises on which the shareholder-first model rests, and a few months ago Michael Porter[5] criticized the current belief that looking beyond the business is bad for business. In the January/February *Harvard Business Review* he argues that companies should be considering other stakeholders, and so generate economic value by creating societal value.

These respected thinkers offer another answer to the question about the purpose of a business: the firm should see itself as an interdependent part of a community that consists of multiple stakeholders whose interests are integral to business success. In this view, an enterprise can be seen as a system of long-term cooperative relationships between affected parties. These include the firm's managers and employees, customers and clients, investors, suppliers, the towns, states and nations where the firm is located or sells goods and services and even future generations of stakeholders.[6] In such a system, stakeholder influence generates pressure for the organization to behave in ethical and environmentally and socially responsible ways, and in turn, this interdependency helps the firm be sustainable and resilient.[7]

This alternative approach to leadership is variously referred to as ''sustainable,'' ''Rhineland'' or ''honeybee'' leadership. By sustainable we don't just mean a firm is being green and socially responsible. Research and observations in over 50 firms around the world, including in many listed corporations, suggest that sustainable leadership requires taking a long-term perspective in making decisions; fostering systemic innovation aimed at increasing customer value; developing a skilled, loyal and highly engaged workforce; and offering quality products, services and solutions.[8] What senior executive would reject these as legitimate goals for an enterprise seeking to both thrive and endure?

To some cynics, sustainable leadership – a management approach aimed at delivering better and more sustainable returns, reducing unwanted employee turnover and accelerating innovation – sounds too good to be true. They dismiss it as just another form

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of humanistic management, merely good management practices, or as following old-fashioned values. There is some truth in each of these characterizations. Certainly, sustainable leadership embraces aspects of humanistic management in that it includes valuing people and considering the firm as a contributor to social well being. The individual practices of sustainable leadership are not new:

- Warren Bennis advocated recruiting, training, and employing an effective top leadership team rather than just relying on the heroic CEO. He also proposed that firms become financially transparent as a step to becoming more ethical.
- Peter Drucker wanted managers to promote change and allow innovations to come from all over the organization, thereby enabling ordinary people to make extraordinary things happen.
- Stephen Covey urged using the knowledge and engagement of a firm's employees.[9]

What is new is the understanding that these practices form a self-reinforcing leadership system that enhances the performance of a business and its prospects for survival. What is also significant is that sustainable leadership practices are diametrically opposed to the typical shareholder-first approach, which business schools, management journals, the media, and many practitioners continue to promote.

The ties that bind

Under sustainable leadership, firms become very savvy in leveraging common long-term interests that bind various stakeholders together. For example, they choose suppliers not just on the basis of low cost, but they also value the added benefits that long-term relationships with innovative and reliable suppliers can bring to both parties. Automaker BMW, for example, did not take advantage of the global recession by squeezing its long-term suppliers; instead it lent them money to help them through the crisis. This contrasts sharply with the Anglo/US practice of only awarding work to the lowest bid and then pitting suppliers against each other by calling for new tenders every few months rather than fostering long-term relationships.

Other stakeholders, particularly employees, also benefit from long-term relations with a company. Part of the implicit deal with stakeholders involves the enterprise behaving ethically and responsibly towards both the environment and the community. In return, stakeholders support the enterprise. Examples of this support include customer loyalty, investors leaving their dividends in the business, and employees accepting lower wages and/or shorter working hours in difficult times, as occurred during the recent global financial crisis.

In short, the objective of sustainable leadership is to keep people, profits, and the planet in balance over the life of the firm, and in so doing ensure that the business generates the social capital needed to weather downturns. Many management writers are calling for businesses to reinstate the moral and social dimensions of what they do.[10] Responsible leaders aim to achieve excellent outcomes for their own organizations and other stakeholders over the long term. In contrast, when a firm's leaders manipulate short-term profit results and fail to invest resources effectively, they jeopardize the firm's and others' long-term future.

Sustainable leadership practices

Several authors have pointed out the advantages of the sustainable leadership approach over its short-term shareholder-first counterpart.[11] Avery and Bergsteiner[12] have identified and investigated these principles, showing how they differ in practice. Using a sample of 14 European organizations operating on principles diametrically opposed to the shareholder-first philosophy, Avery[13] first identified 19 leadership practices, distinguishing what she then referred to as the Rhineland and Anglo/US approaches. She found that these two approaches comprise two diametrically opposed sets of practices that form self-reinforcing systems. Avery then tested the 19 criteria on a sample of 14 organizations from other parts of the world that adopted sustainable Rhineland practices to varying degrees. She demonstrated that enterprises led this way can flourish in diverse industries and locations ranging from the developed world of the USA, UK, Australia, Europe, and Scandinavia to emerging economies in South Africa and Thailand. Avery and Bergsteiner[14] expanded the list of practices to 23 as shown in Exhibit 1, by adding four elements. Exhibit 1 contrasts the extremes for the sustainable ''honeybee'' leadership approach and the shareholder-first or ''locust'' approach on every practice. (Although these are referred to as practices, some more precisely reflect broad principles or attitudes).

Exhibit 1 Criteria distinguishing typical sustainable leadership and shareholder-first perspectives

Leadership elements	*Sustainable leadership ''honeybee'' philosophy* Sophisticated, stakeholder, social, sharing	*Shareholder-first ''locust'' philosophy* Tough, ruthless, asocial, profit-at-any-cost
Foundation practices		
1. Developing people	Develops everyone continuously	Develops people selectively
2. Labor relations	Seeks cooperation	Acts antagonistically
3. Retaining staff	Values long tenure at all levels	Accepts high staff turnover
4. Succession planning	Promotes from within wherever possible	Appoints from outside wherever possible
5. Valuing staff	Is concerned about employees' welfare	Treats people as interchangeable and a cost
6. CEO and top team	CEO works as top team member or speaker	CEO is decision maker, hero
7. Ethical behavior	''Doing-the-right thing'' as an explicit core value	Ambivalent, negotiable, an assessable risk
8. Long- or short-term perspective	Prefers the long-term over the short-term	Short-term profits and growth prevail
9. Organizational change	Change is an evolving and considered process	Change is fast adjustment, volatile, can be *ad hoc*
10. Financial markets orientation	Seeks maximum independence from others	Follows its masters' will, often slavishly
11. Responsibility for environment	Protects the environment	Is prepared to exploit the environment
12. Social responsibility (CSR)	Values people and the community	Exploits people and the community
13. Stakeholders	Everyone matters	Only shareholders matter
14. Vision's role in the business	Shared view of future is essential strategic tool	The future does not necessarily drive the business
Higher-level practices		
15. Decision making	Is consensual and devolved	Is primarily manager-centered
16. Self-management	Staff are mostly self-managing	Managers manage
17. Team orientation	Teams are extensive and empowered	Teams are limited and manager-centered
18. Culture	Fosters an enabling, widely-shared culture	Culture is weak except for a focus on short-term-results that may or may not be shared
19. Knowledge sharing and retention	Spreads throughout the organization	Limits knowledge to a few ''gatekeepers''
20. Trust	High trust through relationships and goodwill	Control and monitoring compensate for low trust
Key performance drivers		
21. Innovation	Strong, systemic, strategic innovation evident at all levels	Innovation is limited and selective; buys in expertise
22. Staff engagement	Values emotionally-committed staff and the resulting commitment	Financial rewards suffice as motivators, no emotional commitment expected
23. Quality	Is embedded in the culture	Is a matter of control

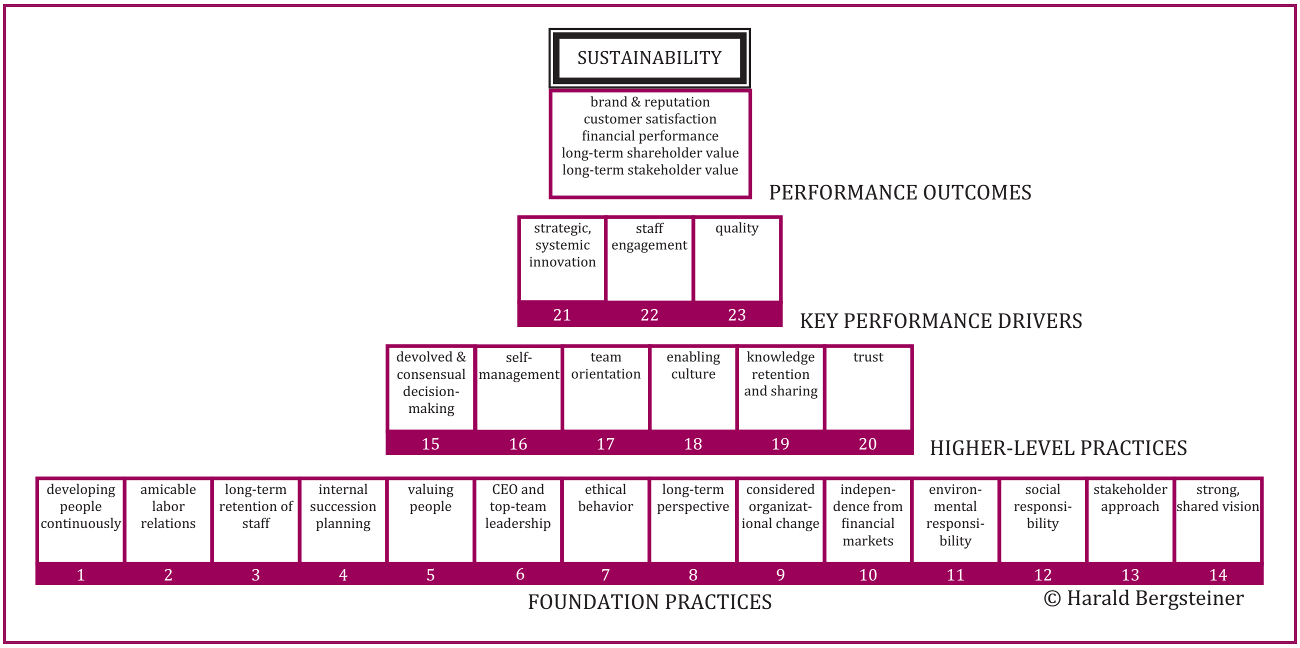
Source: Avery, G.C. and Bergsteiner, H. (2010) *Honeybees and Locusts: The Business Case for Sustainable Leadership.* Sydney: Allen & Unwin, pp. 36-37

It became evident that US management experts, among others, had been calling for managers to implement these ''honeybee'' practices for many years, but these calls go unheeded in locust firms. The research evidence also suggested that each ''honeybee'' practice could add considerable value to a business – including to its bottom line. In addition, many managers do operate on sustainable leadership, as Avery and Bergsteiner's[15] observations of around 45 enterprises show.

The 23 ''honeybee'' practices have been arranged in the form of a pyramid to serve as a guide for intervention (Exhibit 2). The practices form three groups in the pyramid: foundation practices, higher-level practices, and key performance drivers. A fourth level crowning the pyramid contains performance outcomes that research shows contribute to sustainability:

1. Foundation practices form the lowest level of the pyramid. They can be introduced at any time management decides to do so. The 14 foundation practices include programs for training and developing staff, striving for amicable labor relations, staff retention (avoiding layoffs), succession planning, valuing employees' experience and their contribution to customer loyalty and to innovation, deciding whether the CEO's role is to be that of hero or top team member, ensuring ethical behavior, promoting long-term thinking, managing organizational change sensitively, striving for independence from the financial markets, promoting environmental and social responsibility, balancing multiple stakeholder interests, and ensuring that a shared vision drives the business.
2. Higher-level practices form the second layer of the pyramid. These six practices cover devolved and consensual decision making, creating self-managing employees, harnessing the power of teams, developing a trusting atmosphere, forming an organizational culture that enables sustainable leadership, and sharing and retaining the firm's knowledge. The pyramid has been developed on the idea that when relevant foundation practices are in place they facilitate and support the emergence of the higher-level practices. For example, it is unwise to simply decree that employees will become self-managing unless the people involved have received the appropriate training to enable them to self-manage, know and share the firm's vision, have been with the firm for some time (and so understand the culture and have established networks), be empowered to make decisions, and feel valued. Similarly, trust cannot simply be enhanced the way that skills can be developed because trust depends on the operation

Exhibit 2 The Sustainable Leadership Pyramid from Avery and Bergsteiner[18]



> “Sustainable leadership embraces aspects of humanistic management in that it includes valuing people and considering the firm as a contributor to social well being. These practices form a self-reinforcing leadership system that enhances the performance of a business and its prospects for survival.”

of many of the foundation practices. Hence, in the pyramid, self-management and trust appear as higher-level practices that emerge from a combination of multiple foundation practices.

3. Key performance drivers create the third level. The elements of innovation, staff engagement, and quality essentially provide what end-customers experience and so drive organizational performance. The key performance drivers in turn emerge from various combinations of the foundation and higher-level practices. A body of research[16] indicates, for example, that a team orientation, skilled and empowered employees, and a culture that supports knowledge sharing and develops trust all enhance quality. These practices in turn depend for their existence on various foundation elements being in place. Thus, the key performance drivers emerge from both sets of lower level practices.
4. Performance outcomes. The apex of the pyramid contains five performance outcomes that create sustainable leadership. The 23 elements from the various levels in the pyramid collectively drive:
   - Integrity of brand and reputation.
   - Enhanced customer satisfaction.
   - Solid operational finances (all firms have to survive financially including in the short term).
   - Long-term shareholder value.
   - Long-term value for multiple stakeholders.

The pyramid is intended to be dynamic in all directions. Interactions between the elements not only flow bottom-up and top-down, practices on the same level also influence each other. Furthermore, how the 23 practices are actually implemented leaves enormous scope for variation, avoiding a one-size-fits-all approach. For example, it is clearly a matter of long-run survival to operate ethically (think of Enron and many other firms), but there are many ways in which senior executives can ensure that this happens operationally.

Sustainable leadership relies on complex interconnections between multiple practices. In the short run, it may be simpler to lead using the Anglo/US or shareholder-first model. However, considerable research attests to the sustainable leadership or Rhineland model leading to better performance outcomes over the long term than the Anglo/US model.[17]

That said, a sustainable leadership system is vulnerable in the sense that it can be disrupted by a range of external events, such as mergers and acquisitions, by taking on additional major shareholders who do not appreciate sustainable values, or by the arrival of a CEO who subverts the existing system. This can involve major disruptions such as suddenly laying off staff or taking a short-term view on an issue. It can lead to cuts in training, reducing environmental protection or social responsibility programs, or violating ethics to satisfy investors in the next quarter. Short-termism can also lead to other non-sustainable practices such as reducing investment in research and development or ignoring the interests of stakeholders other than investors. Almost inevitably, sacrificing long-term success for short-term wins will be associated with unanticipated organizational change and disruption to a sustainable culture.

On the other hand, by maintaining an informed long-term perspective that commits to being adaptive and innovative, a company can attract and educate patient investors. If the firm can adapt to changes in its markets and new competitors, staff will be retained, training will continue, the firm's innovation and levels of quality will be maintained, its knowledge retained, stakeholders' interests (including those of the environment and community) acknowledged, and abrupt ill-considered change averted.

Using the pyramid

The Sustainable Leadership Pyramid provides a framework for examining an organization's current practices. It depicts a system in which the elements mutually influence each other in different directions. For example, trust, one of the higher-level practices, can be expected to develop in the presence of certain other practices and to be jeopardized in their absence. Trust enhancing practices include amicable labor relations, developing people, empowered decision making, long-term retention of staff, and caring for people. In addition, ethics, long-term perspective, environmental and social responsibility, a stakeholder approach, and a shared vision contribute to creating trust.

The beneficial financial effects flow both up and down the pyramid. For example, when savings from recycling practices boost financial performance. As a top down effect, a profitable manufacturer could decide to invest the surplus in reducing toxic waste or recycling. In this example, financial success drives environmentally-friendly initiatives. Research shows that firms that perform well financially invest more in corporate social responsibility than underperforming firms.[19] This does not mean that only rich firms can afford environmental and social responsibility, but that sustainable practices are linked in complex ways to financial performance.

At each level of the pyramid the practices reinforce, and are reinforced by, other practices at that level. For example, devolved decision making reinforces all five of its higher-level companion practices. This mutual reinforcing of elements at the same level occurs at all levels of the pyramid, including among performance outcomes. For example, shareholder value is created when the brand is protected and customers and investors are satisfied.

Sustainable leadership in practice

Sustainably-led organizations have been identified across different sectors, countries, institutional contexts, and markets.[20] Examples of successful enterprises that consistently embrace sustainable leadership principles abound, particularly among privately-held firms and SMEs. Unlisted companies displaying virtually all of the 23 characteristics of a sustainable enterprise include: in the USA, WL Gore & Associates (Goretex® and other products) and SAS (software); in Germany, Giesecke & Devrient (bank notes and securities) and Kärcher (cleaning solutions); and in Switzerland, Endress & Hauser (flow technologies) and Migros (retail conglomerate).

However, it is likely to be more difficult for listed corporations or private equity groups to operate on sustainable principles because of the pressures on them to achieve short-term performance goals. Yet numerous listed enterprises manage to operate sustainably, if necessary by standing up to or managing their relationships with the financial markets. Well-known examples include Germany's Munich Re from the finance industry; Colgate (consumer goods) based in the USA; Britain's BT Group (telecommunications); the Thai construction corporation, Siam Cement Group, and its competitor from Switzerland, Holcim.

How Wal-Mart implemented sustainable leadership

In 2005, Lee Scott, ex-CEO and President of Wal-Mart Stores and now Chairman of its Executive Committee, announced that the company would essentially adopt sustainable leadership principles going forward, although he did not use that term. Financial performance was solid, but the company was the target of many complainants – employees, local communities, suppliers, and environmentalists. Scott decreed that Wal-Mart, one of largest *Fortune* 500 corporations, would become more ethical, and more socially and environmentally responsible. The company would use its political might to benefit ordinary Americans in healthcare and energy savings, and make people's lives better. Scott even advocated paying more for products from ethical suppliers – an extraordinary reversal by an enterprise built around a low-cost strategy. In the years since, Wal-Mart has experimented with environmentally-friendly stores and other socially-responsible measures.[21] Interestingly, its bottom line has not suffered during this process, posting net sales increases for the past five years, according to Wal-Mart's 2009 annual report. In recent months, in a move to improve the healthiness of its products, the firm announced plans to reduce the fat and salt in its house brand groceries and cut prices on fresh produce.

Does sustainable leadership pay off?

A considerable body of evidence shows that sustainable practices are more likely to enhance business performance than the shareholder-first approach. First, various writers have examined and compared the Anglo/US system with its Rhineland counterpart, concluding that Rhineland principles are more sustainable and lead to better outcomes than the shareholder-first approach.[22] Second, Avery and Bergsteiner have gathered extensive evidence for each of the individual practices in their pyramid model, showing how they are more likely to contribute to positive business outcomes than their counterparts under the shareholder-first model. For example, a major difference between shareholder-first and sustainable practices lies in whether they retain people or lay them off when times get difficult (See the sidebar ''Staff retention: how sustainability supports competitive advantage''). Staff retention is regarded as a foundation element in the pyramid because conditions aimed at keeping staff can be initiated at any time. However, retaining staff supports various higher order outcomes in the pyramid; it allows knowledge to be retained, and supports quality, trust, and innovation, for example, and enhances financial performance, as well as staff and customer satisfaction. Similar cases can be made for the other 22 elements.

Where to start implementation

Changing the purpose of a firm from shareholder-first to being a highly performing contributor to society is not easy, especially for large corporations where systems, processes, the culture, investor and employee expectations, and other elements in the leadership system have been aligned to the Anglo/US approach. Sustainable leadership requires a major shift in mindsets, values, and assumptions about how business works. This is not easy when managers have been educated to make shareholder value the immediate and overriding goal.[23]

In terms of where to start using Avery and Bergsteiner's model, it is wise to begin with an audit of how the members of an organization perceive the current status on the 23 practices. Some elements may already be in place, but others may be seriously lagging, and intervention should be targeted appropriately.

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Staff retention: how sustainability supports competitive advantage

Turnover of valuable staff is costly, and it can also lead to intangible losses. On the cost side, replacing talented senior staff costs between one and two year's salary and benefits.[24] Whether employees stay or not can make a difference to the bottom line as a six-year study of 904 university graduates hired by six public accounting firms showed. The difference in related human resource costs depended on the various firms' organizational values, but was assessed at about US$6 million.[25] Estimates like these generally exclude hidden costs such as lost productivity while the new employee is learning the job, training costs, and time spent conducting exit interviews and briefing search consultants or advertising agencies. Losing employees means that knowledge and expertise not only disappear, but they may end up serving a competitor. Similarly, laid-off staff can take customers with them, which given that the estimated cost of acquiring a new customer is up to five times the cost of retaining an existing one,[26] can be costly. Adding these costs together makes layoffs quite expensive.

On the plus side, retaining employees can generate unique competitive advantage for a firm, derived from the linkages that form between long-term employees that enable ideas and skills to be shared in firm-specific ways.[27] Job security promoted by retaining staff contributes to higher productivity,[28] and lowers rates of absenteeism, sick leave, and ''internal migration'', all of which are often associated with layoffs and are costly to a firm.[29] Furthermore, retaining staff adds to company value. Low voluntary turnover contributes about 3.2 percent to a company's value and a strong commitment to job security adds an additional 1.4 percent, according to global research.[30] Overall, firms shedding staff tend to experience more long-term financial difficulties than their counterparts, beyond the obvious short-term improvements.[31] Another consequence of staff layoffs can be damage to the firm's reputation, as a study of *Fortune's* most admired companies in America showed.[32] Interestingly, although executives rated the laying-off firms negatively, financial analysts were even more negative in their appraisals of downsizing firms. Thus, laying off value-adding employees tends to produce medium to long-term losses once hidden costs are taken into account. Although layoffs are sometimes unavoidable, employers who continue to invest in and care for their people can minimize negative effects, such as productivity losses and absenteeism.[33]

Change can begin by ensuring that dysfunctional foundation elements are addressed first. Next, company leadership can promote the advantages of the higher-level practices and key performance drivers. Realistically, top-line performance is not likely to improve unless the foundations are in place. For example, executives can't command their staff to be more innovative and so simply issue an edict and increase the R&D budget. Without some of the lower-level practices, systemic innovation is unlikely to become widespread. These include taking a long-term perspective underpinned by a strong vision; and retaining, skilling, and valuing employees. Supportive foundation practices in turn foster the six higher-level practices that systemic innovation depends on. Innovation is stimulated by many things, including having an appropriate culture that supports and values systemic and systematic creativity; effective teamwork and collaboration; as well as self-managing employees willing to initiate ideas, make autonomous decisions, and share knowledge. Trust also supports the long-term perspective required for systemic innovation to work. Innovation and staff engagement mutually reinforce one another – engaged staff tend to be more innovative, and a highly innovative culture boosts staff identification with the organization, in turn supporting engagement. Hence, a virtuous circle begins.

After anchoring the foundation elements, support can then be given to developing and institutionalizing the six higher-level practices. When all of this and the supporting systems and processes are in place, increased innovation, staff engagement, and quality in products and services can be expected. Establishing a successful innovation culture can take 10 years or longer.

The cost of not changing

Other competitive forces, including the need to collaborate with the best suppliers and attract and retain customers and talented employees, may impel change. However, perhaps the major force brought to bear on a recalcitrant management will be the increased cost of doing business in an unsustainable way. The financial sector could exert enormous pressure for change if it chose to, valuing people-centered, innovative, ethical and stakeholder-based leadership practices over current business-as-usual practices. Major global players, such as Munich Re, have already integrated sustainability into their corporate strategy and now invest their own funds-under-management almost exclusively in sustainable equities and property. As this policy spreads to pension funds and other long-term investors, top executives will be forced to consider a more sustainable model simply to maintain the firm's share price (and their own compensation packages). The costs of borrowing for unethical firms will increase because of the potential risk to their reputations, and hence to their finances and other forms of sustainability. No doubt, in addition to stiff penalties, BP has experienced very high costs of all kinds following its 2010 oil spill disaster in the Gulf of Mexico. A combination of optimizing business conditions, gaining stakeholder support, and protecting the firm's reputation should make sustainable leadership practices an obvious choice.

If self-interest fails to motivate enterprises to change, governments can intervene to prod them, as has already happened in the UK. Unsatisfactory levels of social responsibility displayed by British firms led the government to take action in the early 21st century. The British government created a sustainable development strategy with the specific objective of furthering socially responsible behavior in business. The strategy aimed at ensuring minimum levels of environmental protection and performance in health, safety, and equal opportunity.

Challenges

There are many obstacles in changing to sustainable leadership. First, sticking with conventional wisdom is comfortable and easy – it's business as usual. Second, change is disruptive and initially creates both financial and intangible costs, although as the Wal-Mart case shows these may not slow growth and profits. Third, most people disregard hard evidence and make their decisions on the basis of ideological beliefs. Managers are no exception to this human foible despite their training and experience in decision making. Fourth, major change involves risks, bringing with it the chance of a drop in short-term performance, so stakeholders need to be prepared to focus on the long term. Finally, radical change can take a long time to embed and then maintain. A major Australian bank converted from a shareholder-first strategy to a sustainable leadership model. The change took a decade to take hold, with outstanding results, but unraveled in only a few years to under a new CEO with a different agenda.

The choice to adopt a more sustainable strategy, one that research and practice show leads to higher resilience and performance over the long term, remains in the hands of each executive team. Unfortunately, executives remunerated on a short-term basis may have no incentive for seriously pursuing long-term change, to the detriment of shareholders and other stakeholders. This is where the fundamental short-term focus of the shareholder-first or business-as-usual model begins to destroy shareholder value and endanger a firm's very survival.

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