

# Monetizing Leadership Quality

By Susan Dunn and Bruce J. Avolio

**Who controls the assets that have the most sway with equity analysts? If you said senior talent leaders, you'd be right — but likely puzzled, as well, given what most analysts talk about when they refer to the critical assets of a business.**

Two respected research houses, Corporate Branding LLC and IPSOS Mori, each surveyed equity analysts from around the globe and both confirmed a surprising insight — that the most important factor they consider in determining an organization's stock price is not short-term operational efficiency, sales productivity or cost-effectiveness; it's the quality of the organization's leadership and how it contributes to firm performance.

In the first phase of a two-stage research project, we interviewed 50 analysts from equity markets around the globe and asked them to describe the way they assessed leadership quality in calculating a firm's worth. What data did they look at? Where did they get this data? How did they weight it? Although these analysts were from a broad range of regions, industries and tenure, they shared a similar approach.

They gather 20 years of cash-flow data from the organization they are following and adjust these figures to reflect their unique insights and knowledge. For years one and two, the analysts review the operating plan and assess the probability that the frontline will meet their targets. For years two through 20, the analysts lack confidence in predicting organization performance. They are unable to cut through uncertainty around technology changes, consumer needs, new competitors and regulatory shifts. Instead, they look at the top management team (TMT), forecast their ability to capitalize on these types of uncertainties as they arise and adjust the cash flows accordingly.

In forecasting the TMT's ability to capitalize on uncertainty, the analysts rely on three criteria:

- **Track record** — Previous roles where they face similar challenges and the results achieved
- **Reputation** — Experiences, stories, books and articles that describe the leader's approach, character and confidence
- **Presence** — Effectiveness in articulating the way forward, addressing opportunities, questions, concerns, crises and disruptions in plans

In a follow-up global survey of 305 analysts, we asked how much they had changed the stock price based on their assessment of the TMT. The average was an astonishing 16 percent! For most organizations, this is equivalent to five to seven years of organic growth.

The majority of analysts said they typically did not receive information from the organization that was useful in forming their judgment about leadership quality. Instead, analysts gathered information about a specific leader's effectiveness from external sources including peers, social media, articles, books, websites and trade-shows. They also interviewed competitors, suppliers and recruiters.

Our results also reveal that analysts do not just take a quantitative approach to valuing leadership. Instead, they rely on their "gut sense" to evaluate leadership. We asked investor relations leaders why this was the case. One explained that "analysts recognize that leadership is too complex to be explained by a set of numbers."

Despite their reliance on external sources, though, the analysts said they would welcome more information from the companies they cover. In fact, 80 percent said they could be more accurate in judging leadership with better information from the organization.

After we completed our research, we shared our findings with several senior leaders responsible for talent management. They were surprised that analysts ranked management or leadership strength so high on the assessment criteria. They described potential implications for their role and actions they could take, including:

- Partnering with Investor Relations to determine how analysts who follow their industry view the organization's leadership strengths
- Identifying two or three concerns the analysts raise and building them into the leadership-development agenda
- Considering analysts' perspective when making recruiting and succession decisions.

Many talent managers expressed concern around their readiness to take on this opportunity, while all recognized the significance. One talent leader captured it well: "There aren't many things we can do as an organization that adds 16 percent to our equity value overnight."

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