The Role of Leadership in States of Transition

Honors Capstone Thesis

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Table of Contents

Introduction

The state of the global economy teeters on the brink of chaos. Large, powerful nations helplessly watch money drain from their stock markets. The current situation reaches every corner of the country and leaves no business, organization or person untouched. While government officials search for a solution in the form of debt restructuring and bailout packages, other influential players must step up to play a role in the rebuilding of the global economy. Corporate executives must take the responsibility and the challenge upon themselves to pull their businesses out of this pit of sinking sand. It seems that every action taken by the government causes the nation to sink a few more inches into a recession. Although the first instinct is to claw your way out, the best way to survive this natural hazard is to stand still. This prevents objects from sinking faster and provides more time to locate the best solution. Our nation's leaders should adopt the same mentality. They should fight the urge to struggle and instead remain still. Not everyone seems to agree, however. Recently the Securities and Exchange Commission accused Bank of America CEO, Kenneth Lewis, of knowing about Merrill Lynch's losses and not disclosing them to the B of A shareholders before the merger vote. Under normal circumstances this SEC violation would be considered fraud. Lewis and the New York Attorney General claims that "the Treasury secretary at the time, Henry M. Paulson Jr., and the Federal Reserve chairman, Ben S. Bernanke, put pressure on him to complete the Merrill merger while keeping quiet about the losses until an additional government bailout" (Davidoff). In this case, Bank of America argues that the government prevented Lewis from applying his own leadership philosophy and pressured the CEO into making a decision that might be detrimental to his career. Accurately assessing the situation plays a significant role in finding the best solution and the best leadership style to pull the economy out of this sinkhole of a recession.

It is not a question of if the economies bounce back but when. Executives must recognize their role in rebuilding the economic strength of the United States. One biblical verse states “God grant me the serenity to accept the things I cannot change; courage to change the things I can; and wisdom to know the difference.” Otherwise known as the serenity prayer used by recovering alcoholics, the statement can be applied to the United States current financial situation. Corporate executives and government officials alike need to accurately identify the things that are in their control. Once identified, leaders will be able to apply the appropriate leadership style and make suitable decisions. The leadership style chosen by the executives will be dependent on the current situation and thus, leaders will be pressured to deviate from the leadership styles that are familiar to them. The theory of contingent leadership argues that no one leadership style applies or is best for every situation. Managers who excel at contingent leadership possess the ability to switch between varieties of styles depending on the needs of the situation.

Analyzing the Situation

In order to know what the situation calls for, managers should have the ability to recognize the environment both in and outside of the organization. Tushman and Romanelli identify phases that an entity passes through in a management article published in 1986. Their basic descriptions provide relevant insight as to what factors influence the organizational contexts outlined below. They hypothesize that a range of two independent factors determines the current phase of the organization: change and implementation time. Figure 1 shows the relationship between the time needed to execute organizational changes and different levels of organizational changes.

Convergent States

Tushman and Romanelli define convergent states with long periods of steady development and stability. The organization experiences few ups and downs in regards to overall performance. Nominal fine-tuning generally occurs during these phases and allows the organization to address small issues and adapt to the continuously changing environment. However, one article recognized that “the combination of prior history of success and inertia often inhibit leaders’ ability to initiate a needed reorientation.” (Eggleston and Bhagat. October 1993) Convergent states have the potential to last too long and affect the organizational negatively by creating lethargic leaders and a reactive workforce. Abigal Adams once said of John Quincy, “ These are the times in which a genius would wish to live. It is not in the still calm of life, or the repose of a pacific station, that great characters are formed. The habits of a vigorous mind are formed in contending with difficulties. Great necessities call out great virtues. When a mind is raised, and animated by scenes that engage the heart, then those qualities which would otherwise lay dormant, wake into life and form the character of the hero and the statesman.” Lack of stimulation and proactive change prevents the organization from progressing. Challenges stimulate necessary changes.

Transition States

The transition phase begins with poor performance and the deterioration of business ratios and other quantifiable measures. No clear distinction exists between the convergent and transition phase. It is crucial, however, for management to recognize when it occurs because at that point, the organization is vulnerable and at the mercy of the industry, the economy or any other outside stimuli. The transition is particularly relevant to executive management due to the unpredictable nature of the environment and susceptible condition of the organization. During this stage, a variety of leadership styles must be utilized to address a variety of situations quickly.

Reorientation States

The same is true for reorientation states. Monumental transformations followed by periods of successive stabilization distinguish the reorientation state. This phase is a product of an environmental stimulus in the transition stage and is characterized by organization-encompassing change. During the reorientation phase, any management decision has the potential to quickly lead to decline and failure. Management decisions alter significant parts of an organization such as strategy, mission, vision, core values, organizational structure and policies. At this time, leadership must take an active role in guiding the organization using appropriate leadership styles that establish new organizational aspects and restore legitimacy to management and the entity. If leadership fails to act appropriately, the organizational risks falling into permanent decline and eventually ending in failure. Managers who use contingency theory and who apply the appropriate leadership style, will move the organization from the reorientation state to a new convergent state defined by new norms, policies and other core features.

In one article, the authors argue in favor of the contingent leadership theory stating that a “relationship exists between organizational contexts and leadership requirements.” (Eggleston and Bhagat. October 1993.) Thus once the situation has been identified, the appropriate leadership can be used.

United States of America

Using Tushman and Romanelli's phases, we will determine the current organizational context of the United States. We seek to observe the nation's current economic state and all types and forms of entities ranging from non-profits, to Fortune 500 companies to the public sector. After identifying the organizational context of the country's economy, we will better postulate what leadership styles and abilities will be required of future leaders and under what situations.

The Washington Post sites the beginning of the financial crisis in the late 1900's when mortgages were granted to people who could not afford them. These sub-prime mortgages enabled thousands of unqualified people to purchase overly priced homes. The housing bubble continued to grow, especially with the burst of the tech bubble following September 11, 2001. After a drop in interest rate by the fed, banking investors bought mortgage-backed securities, which promised a more stable return. However in 2004, the housing market collapsed and suddenly the value of these homes dropped leaving people could not afford to pay their mortgages. Default and foreclosure plagued the banking industry and created toxic assets on the books of these institutions that gobbled up mortgage-backed securities. These banks then wrote off these accounts receivable lost millions of dollars causing their shareholder value to plummet. According to one Washington Post article, "The MSCI Emerging Markets Index dropped 53 percent from January to November 2008, compared with 33 percent for the S&P 500" (Quinn). Unemployment increased to 8.5% as of mid-April. Organizations all over the country cut jobs daily in order stay out of the red.

Having considered the previous information, it is obvious that the US is currently in the transition phase. The types of change occurring and the timeline at which things are happening rule out the convergent phase. Everyday the American public witnessed a new bailout plan, bank restructuring or merger. The situation is tumultuous, unpredictable and complex. It is unclear as to when exactly the decline actually started, which is also characteristic of the transition phase. We have yet to see a period of stabilization and can eliminate reorientation as a possible context as well. Thus, having identified the appropriate phase, we can discuss several leadership styles and determine which styles U.S. leaders should apply in the upcoming months.

Leadership Styles

An organizational behavior textbook defines leadership as having four communalities: "1.) Leadership is a process between a leader and followers, 2.) Leadership involves social influence, 3.) Leadership occurs at multiple levels in an organization and 4.) Leadership focuses on goal accomplishment." (Kreitner and Kinicki. 2007.) Using these four statements, we will discuss and classify several leadership styles and relate them to both contingent leadership theory and organizational context.

Leadership is a process between a leader and followers

Leadership styles fall among a spectrum of many different factors. In regards to working with subordinates, power distance plays a role in the classifying three major styles: autocratic leadership, laissez-faire leadership and participative style. Power distance is a term used by Gerard Hofstede, the famous Dutch writer who sought to uncover the differences between cultures. In his book Cultural Consequences, he wrote “power distance is a measure of the interpersonal power or influence between a boss or subordinate as perceived by the less powerful of the two.” (Hofstede. 2001.)

Autocratic leaders, for instance, have a style dependent on power distance. The subordinate perceives the leader to exercise total control over decisions that affect both the organization and the member. Followers participate very little in change and feel little to no ownership in a laissez faire type organization.

Participative leadership seeks to include every member of the team. The manager or executive recognizes the important of information exchange and idea generation. Those subordinates who work with participative leaders perceive a balance of managerial decisions and team-led decisions. In relation to the OB definition, a moderate balance permits the follower to experience a feeling of ownership and control over what happens to both the organization and his position within the organization.

On the opposite side of the spectrum, laissez-faire leadership pertains to managers who allow their subordinates to operate and make decisions on their own. This is successful with highly skilled and proactive teams. This “hands off” approach facilitates creativity and the transfer of knowledge while requiring frequent and concise communication.

Leadership involves social influence

Social influence plays a large role in motivating team members to perform in an organization. A manager’s leadership skill set should include the ability to establish legitimacy and to use that power to motivate followers. Leadership styles that cultivate this type of reaction are charismatic and transformational leadership.

Sociology in our time states that charismatic leadership is "power legitimized on the basis of a leader's exceptional personal qualities or the demonstration of extraordinary insight and accomplishment, which inspire loyalty and obedience from followers." (Murray and Linden. 2000.) Teams depend heavily on charismatic leaders because they inject dedication, passion and energy into their followers. People who exhibit this type of leadership are a rare breed. Losing them tends to handicaps the team, leaving them without direction and lack luster.

Transformational leadership capitalizes on all elements of social influence. They spend time forming significant relationships with subordinates through various communication mediums. Transformational leaders stress the importance of synergy and the group welfare. By attending to the health of the group and the attitude of the followers in regards to moral and motivation, transformation leaders build strong bonds with subordinates. These bonds foster commitment to the leader as well as the organization.

Leadership occurs at multiple levels in an organization

Earlier we addressed the multiple stages of an organization as described by Tushman and Romanelli in order to best identify the current phase in the United States. We argue that through the use of appropriate leadership styles and contingency theory, leaders will be able to resolve the economic situation plaguing the economy. Leadership, however, occurs at all levels of the organization beginning at the top and working its way down to the individual. A line employee may be a charismatic leader who encourages fellow employees to work to their potential. The motivational role played by these employees is crucial to the success of all levels of the organization. Even an intern can become a leader and inspire fellow employees.

Every level of an organization needs a bureaucratic leader. Detailed oriented and concerned with following procedures, these people hold organizations together. They cover all the bases and ensure that the appropriate rules are followed. These leaders help establish the structure of an organization by enforcing policies and traditions. Their consistent actions and performance create the perception of a just work environment.

Leadership focuses on goal accomplishment

Perhaps the most quantitative aspect of leadership, goal accomplishment provides a tangible measurement of the success of a leadership style. Both task-oriented leadership and transactional leadership styles pertain to the completion of a job. Task-oriented (TO) managers focus on completing the job at hand. TO leaders have a tendency to be tunnel-visioned in regards to their work and as result, exemplify autocratic management practices such defining work, member roles and group structure. Task-oriented managers must be wary not to ignore social influence and the importance of maintaining those relationships. This type of leadership is often characterized by low motivation because managers focus too much on the task as opposed to the people performing the work.

The foundation of transactional leadership stems from a basic labor agreement. A subordinate agrees to take on a job and will dedicate their time to the completion of a task. Similar to bureaucratic leadership, transactional leaders are "by the book" and expect an established standard of production. These types of leaders also emphasize the presence of consequences if followers do not meet standards. Due to the demand for consistent, high levels of performance and focus on task completion, this type of leadership doesn't necessarily inspire creativity or proactive solutions.

It would follow then, if these four statements define leadership and each style of leadership applies to only part of the definition, it would be appropriate to state that no single style best defines leadership. Like every aspect of business, leadership styles have negative and positive aspects of which leaders must be aware. By knowing themselves, their dominant leadership style and how to identify the situation, leaders will be well equipped to apply the contingency theory to their everyday work.

Contingency Theory

The contingency theory arose from the works of Fred Fiedler, who in the mid-90's developed his own contingent leadership theory. He argues that leadership can be broken down into two parts: the least preferred co-worker (LPC) scale and situational favorableness. After connecting task-oriented leadership styles and relationship-based leadership styles, he states that there is no one style that best applies to every leader and every situation. The environment and the organizational context play a large role in determining what style will be appropriate. By knowing and applying the different techniques and styles, leaders today have the ability to be well-rounded executives and managers. Knowing other styles not only allows a leader to adapt to several situations but helps them better understand their team members actions and decisions. Leaders who employ contingency theory capitalize on the leadership abilities of the their followers as well opportunities presented by the situation at hand.

Leadership for the United States

As was previously discussed, the United States is currently experiencing a time of transition. The transition stage is defined by sudden change and poor organizational performance. Although it is difficult to pinpoint when the problems started, it is evident whom both the government and the public thinks should fix them. Corporate executives are being held personally responsible for the deterioration of their companies. Whether it is because of their role in the organization or the inflated compensation packages they receive, these corporate leaders are being barraged with threats, criticism, and questioning. For instance, a congressional committee asked that Rick Wagoner of General Motors to step aside as part of the government's bailout strategy. Pressure from the public and the government on companies to perform brings a host of new challenges to organizational leaders. For some companies, obstacles arise daily and set backs are common practice. There is never one solution to the problem and it will take a culmination of efforts to survive over the upcoming months. Managers alone cannot save a company. It will be the commitment and teamwork of every stakeholder including investors and employees. Leaders must be able to capitalize on every decision; they must be able to restore legitimacy to management decisions. The threat of change coupled with the fear of unemployment can seep into a workforce, brewing an atmosphere of distrust and self-preservation. Especially in a transition state, executives must take on a gross roots role. They must be agents of change in the organization. Executives must be able to motivate and inspire employees to embrace change. The contingent theory of leadership allows executives to choose the leadership style most appropriate for the situation. For instance, charismatic and transformation leadership play a role in building employeremployee relationships, which is particularly important in transition states. Managers must employ each style to capitalize on their role as a leader.

Business Ethics

In times of uncertainty, it is easy for executives to search for easy solutions. Answers that appear to be the most efficient or the most cost competitive are often the opposite. Easy solutions are like band-aids on a broken arm. With the much bigger problem hidden inside, it is difficult for someone to see and attend to the injury. The same is true for the United States economy. Very few people took note of the diseases stewing inside of our banks and loan institutions. Now that it has taken hold, corporate executives are being asked to dig deep and purge their companies of toxic assets and unnecessary costs. Strong leadership will be needed in these situations as executives have the responsibility of facilitating the changes. Maintaining employee reliability, commitment, and performance will be hard when faced with possible layoffs and pay cuts. Quick, rash decisions that require multiple corrections and attention doesn't inspire faith in a leader's decision ability and it further contributes to the chaotic, uncomfortable environment in the work place.

Furthermore, executives must eliminate conflicts of interest. The purpose of an organization is to create value for their shareholders. Owners in the firm want a return on their investment. As a result, they nominate a board of directors to represent their ownership in the corporation. The executive positions within the company represent the interests of the corporation and its stakeholders like employees. When one person occupies a leadership position on the board of directors as well as in the company, it may be difficult for them to separate their roles. How can the CEO, who is also the chairman of the board, act on behalf of the shareholders if he is also representing the employees? Is it ethical? These are hard questions. Many companies still operate under this type of structure. Samuel Palmisano of IBM plays the role of CEO, Chairman and President. Ronald Sugar is the CEO and Chairman of defense contractor, Northrop Grumman. In these types of situations, leaders must take great care to use the contingency theory of leadership. Faced with the task of representing a variety of different stakeholders, executives must be able to adapt to every situation. They must effectively manage their relationships and navigate organizational challenges without alienating a group of stakeholders. Contingent leadership enables executives to switch between styles in order to capitalize on the environment and the players involved.

One example of how contingent leadership plays a role in business ethics is the story of U.S. Commerce Secretary, Gary Locke. Prior to being elected to Obama's cabinet, he served as Washington's governor. Large companies such as Microsoft and Boeing donated thousands of dollars to his campaign for the governor. 500 companies gave money to Locke over the course of 8 years totaling $800,000.00. His charismatic leadership style, combined with his focus on results made him a significant asset to the state. He brought both jobs and revenue to Washington. Although this is permitted according to state laws, as secretary of the commerce Locke is under considerable pressure to eliminate his stake in Microsoft. The contingent theory of leadership enables Locke to move from one group of stakeholders to another. He keeps each group happy while accomplishing his tasks. A purely task-oriented or purely relationship based style would lead to either organizational failure or destruction of business relationships, respectively.

Compensation

If the American public criticizes one thing about leadership today, it would be their inflated executive compensation packages. Typical compensation includes three components: a base salary, bonuses, and long-term incentives (LTI). According to an article published by the Society of Human Resources Management, Standard & Poor's executives received on average $10.5 million a year in compensation in 2008. Does the leadership style of today's executive warrant $10.5 million dollars per year? In order to better understand, the public should understand how companies award compensation. Executive salaries are fixed and tax deductible for the company if they fall under $1 million dollars. As a result, compensation packages rarely consist of salaries exceeding the ceiling. Bonuses are considered variable pay and are based on annual performance. Long-term incentives are meant to encourage executives to remain at the company for a longer period. These stock options and restricted shares can only be exercised during a certain period. By prolonging compensation, companies hope to focus executives' energy on long-term sustainability. The SHRM article stated "typical allocation is salary, 18 percent; bonus, 24 percent; and LTI, 58 percent." (Grossman.) These packages are proposed by committees and set by boards.

With the onset of the financial crisis and credit crunch, shareholders and the government alike want to know why these struggling companies awarded their executives such high pay when stock prices plummeted on their watch. It seems that compensation has moved away from pay for performance. Today, compensation benefits those leaders who exhibit strong tendencies toward styles characterized by social influence. Charismatic and transformational leadership styles establish legitimacy without actually performing. Their communication skills and ability to navigate social situations help build a reputation and image. In contrast, pay for performance plans tend to benefit the transactional and task-oriented leaders, who focus on accomplishing set goals and benchmarks. It would seem that pay committees moved away from rewarding executives for their results and began compensating for status and perceived personal risk. The current state of the economy, however, brought to the light the inflated paychecks. Shareholders and government officials alike have taken a heightened interest in the pay of executives, especially those receiving federal aid. An article in the Wall Street Journal said, "Shareholders at roughly 400 companies that accepted federal aid will conduct advisory votes this year on those companies' compensation plans. Congress later this year may require such "say-on-pay" votes at all companies. The results are not binding, but can pressure boards to alter pay practices" (Dvorak). Investors including the United States government want to ensure that their money is being well spent and funneled towards the company, not the exorbitant life styles of the company's leaders.

Exemplary Leadership

"Individual decisions within IBM generate more revenue than entire countries" (The New Face of IBM). International Business Machine has gone through the gamut. They have seen every stage of an organization and adjusted their business strategy to fit the industry environment. Two CEO's that come to mind are Louis Gesner and Samuel Palmisano. Louis Gesner recognized a period of transition for IBM. He took advantage of the markets need for mid-size main frames. He changed the corporate structure and focused research and development on engineering based on customer needs. Gesner used his ability to capitalize on industry opportunities. He recognized the state of the organization, identified the opportunities, and adapted his leadership style to lead IBM to a new era of customer relationship focus.

Sam Palmisano states on his IBM webpage, “To capture the biggest economic opportunities or to tackle society's most daunting problems—to imagine what the world might be, and actually to build it—people have sought something more fundamental: a unique ability to conceptualize opportunities, to analyze developments, to tackle and overcome grand challenges” (Palmisano). He embraces a variety of leadership styles learned at Johns Hopkins University and as senior managing director in Japan. Palmisano also prides himself on being a selfless leader. He views his career as an unstructured learning process and an accumulation of experiences, which contribute to his leadership ability. In an article on CNNMoney.com, he states, “I've noticed that some of the most effective leaders don't make themselves the center of attention. They are respectful. They listen. This is an appealing personal quality, but it's also an effective leadership attribute. Their selflessness makes the people around them comfortable. People open up, speak up, contribute. They give those leaders their very best.” By introducing himself to as many experiences as possible, Palmisano enhances his ability to recognize and adjust to a variety of situations and modify his leadership style.

Conclusion

Leadership manifests itself in many different ways. People naturally gravitate towards specific styles of leadership as a result of their personalities and personal experience. Regardless of what style a person prefers, leadership always consists of the four major concepts: 1.) Leadership is a process between a leader and followers, 2.) Leadership involves social influence, 3.) Leadership occurs at multiple levels in an organization and 4.) Leadership focuses on goal accomplishment. With these things in mind, it is important for leaders today to recognize the importance of familiarizing themselves with all of the styles of leadership. By being a well-rounded leader, a person can act according to the situation and environment. It would follow then, that it is equally important for a leader to be able to accurately gauge the state an organization. The contingent theory of leadership depends upon the correct interpretation of management information and employee motivation. In the current economy, ignoring the signs of a transition state like deteriorating business ratios is fatal to the company. Adjustments in business practice and corporate attitude depend on the tone set by the executive. The recent criticism of executive compensation leaves a bitter taste in the mouth of stakeholders and the American public. For example, AIG filed for bankruptcy, and their managers received $165 million in bonuses. An award not based on performance but with the purpose of keeping the manager in house inflates not only compensation packages but also the egos of the leaders. Future executive compensation should seek to reward leaders such as IBM's Lou Gesner. His innovative thinking, willingness to fail, and ability to lead placed IBM on the forefront on their industry. Gesner, however, is just one example. Leaders today must recognize the potential within themselves. Executives must learn to utilize the contingent theory of leadership because in the United States' transition state, who knows what challenges they may face.

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Richard Newman. . "Relief at what cost? " McClatchy - Tribune Business News 5 April 2009 ABI/INFORM Dateline. ProQuest. American University Library. 15 Apr. 2009 http://www.proquest.com/

9. Appendix A – Figure 1: Periods of Change