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The Leadership Value Chain

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There is little question that leadership is vital to organizational effectiveness; however, there is a lack of comprehensive models of the processes and intervening factors that explain the link between individual leaders and organizational performance. This article concerns an evidence-based framework, the *leadership value chain*, that traces the characteristics of individual leaders to their leadership style; leadership style to effect on team and unit processes; team and unit processes to team and unit results; and team and unit results to effectiveness across a broad range of organizational-level performance measures. The point of the leadership value chain is to identify the sequence of key variables and considerations that relate individual leaders to organizational effectiveness. Of all the things to consider, these are the things that must be considered to determine the value of leadership. The authors use examples to show how this framework can provide a heuristic for thinking strategically about key leadership investment decisions and organizational development interventions.

Most people take it for granted that leadership matters. Beyond everyday intuition, research has documented a link between leaders and organizational effectiveness. For example, one study estimated that high performing executives add, on average, $25 million in value more than mediocre performers over a typical tenure (Barrick, Day, Lord, & Alexander, 1991). Another study concluded that chief executive officers account for 14% of the variability in firm financial performance (Joyce, Nohria, & Roberson, 2003). To put that in perspective, industry sector accounts for 19% (McGahan & Porter, 1997). Thus, deciding who will lead is nearly as consequential as deciding whether 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

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difference. We have searched the business press and the professional literature for research-based models that explain how leaders make a difference. There are many frameworks that capture pieces of the puzzle, but none gives the whole picture.

In this article, we propose a framework to begin filling this void. It is called the *leadership value chain* because the basic concept comes from value chain logic (cf. Porter, 1985). 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 purpose is that understanding the value of leadership is important yet not well developed. It is also a complex problem. Our goal is to cut through the complexity by distinguishing, amid all of the many different things we could consider, what are the essential things we must consider to determine the value of leadership? We also take an evidence-based approach, choosing only factors demonstrated by empirical research to link leaders, leadership, and organizational performance.

After providing a bit of background, we describe the elements in the leadership value chain and suggest ways to assess them. Ultimately, we acknowledge limitations to the model and close with examples of how consulting psychologists, human resources and talent managers, and researchers can apply the framework in thinking strategically about key leadership investments and organizational development.

BACKGROUND

Our interest in leadership comes from our work in business organizations. Therefore, much of the following pertains to leadership in the context of for-profit businesses. The basic logic and key concepts are likely to pertain to leadership of government, military, education, community, and nonprofit organizations; however, some of the organizational performance variables we discuss may need to be adapted to those contexts.

Simplifying the Complex

There were two needs that prompted the development of the leadership value chain. First, our research and development 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—it is central to such issues as the return on investment of executive coaching and the debate about executive compensation—but the problem seems hopelessly complex. In examining both the scholarly and practitioner literatures, we were struck by the lack of a comprehensive framework. This prompted us to attempt to create one.

Fair warning: the leadership value chain and the discussion around it are not simple. This framework goes well beyond a 2 × 2 matrix. We are forsaking the value of simplicity in deference to the complexity of the topic. Our hope is that as one examines the framework by understanding each phase one at a time and then considering how they all link together, one will find what Oliver Wendell Holmes described as "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 articulated by Robert Hogan (Hogan, Curphy, & Hogan, 1994; Hogan & Kaiser, 2005). According to this view, on the basis of an analysis of human origins, leadership is an evolved solution to the adaptive problem of collective effort (Van Vugt, Hogan, & Kaiser, 2008). Fundamentally, leadership concerns influencing individuals to transcend their short-term self-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 competition.

There are two important points about this definition. First, leadership does not primarily concern individuals called leaders; rather, leadership is primarily concerned with the performance of the collective for which the leader is responsible. The second point follows the first and is that an evaluation of leadership effectiveness should focus on group performance.

The foregoing may seem obvious. Yet, a recent study we did suggests it is worth emphasis. We reviewed the research literature and examined how scholars operationally define *leadership effectiveness*. We created a classification system for measures of leader effectiveness and then counted how often they were used in 1,695 statistical analyses conducted with 1,124 independent samples that included more than 285,000 leaders (Kaiser, Hogan, & Craig, 2008). The results were telling of an individual bias: The majority of measures of leadership effectiveness did not reflect team or group performance and instead reflected evaluations of the individual leader. Common measures included ratings of the manager's overall job performance, the average rating across an inventory of behavioral items or competencies, ratings of potential, being nominated or selected for a leadership role, and rate of career progression. These variables are more concerned with the individual's career success, and they reveal very little about the performance of his or her team. Moreover, of the minority of studies that did examine team performance, most were concerned with team processes (e.g., subordinate job satisfaction, motivation, and commitment; group cohesion). The least used measures of leader effectiveness concerned results—group 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 and guide them in the pursuit of a collective purpose, then the bottom line is how the group is doing at reaching that goal.

THE LEADERSHIP VALUE CHAIN

Figure 1 presents a visual representation of the leadership value chain. We use the label *value chain* to connote that the framework is intended to classify distinct kinds of variables and represent how their interrelations transform inputs into valued outputs. The idea is familiar to managers and seems apt to the question of how leaders affect organizational effectiveness.

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

Leader Characteristics

The leadership value chain begins by considering the things that make individual leaders unique—their personalities, abilities, knowledge, skills, and relationships. These individual differences represent who leaders are, and have implications for how they lead.

One way to organize the domain of individual differences is provided by the various types of capital discussed in the human resources literature (cf. Boudreau & Ramstad, 1997). Perhaps because of their relative youth, the terms *psychological capital*, *intellectual capital*, and *social capital* are often used inconsistently. One way to distinguish them is as follows: *Psychological capital* refers to inherent and enduring person characteristics such as personality and mental abilities; *intellectual capital* refers to knowledge and skills acquired through education and experience; and *social capital* refers to relational characteristics such as networks and professional contacts.

Regardless of how the individual differences are categorized, they can be quantified. For instance, consider psychological capital. Modern personality assessment is quite robust, thanks in large part to the development of the Big Five, or Five-Factor Model. A recent meta-analysis of 73 studies of the relationship between personality and leadership shows that when the Big Five personality dimensions are considered as a set, the multiple correlation with leadership is .48 (Judge, Bono, Ilies, & Gerhardt, 2002). The results indicate that good leaders seem emotionally stable (confident, calm under stress), extraverted (energetic,

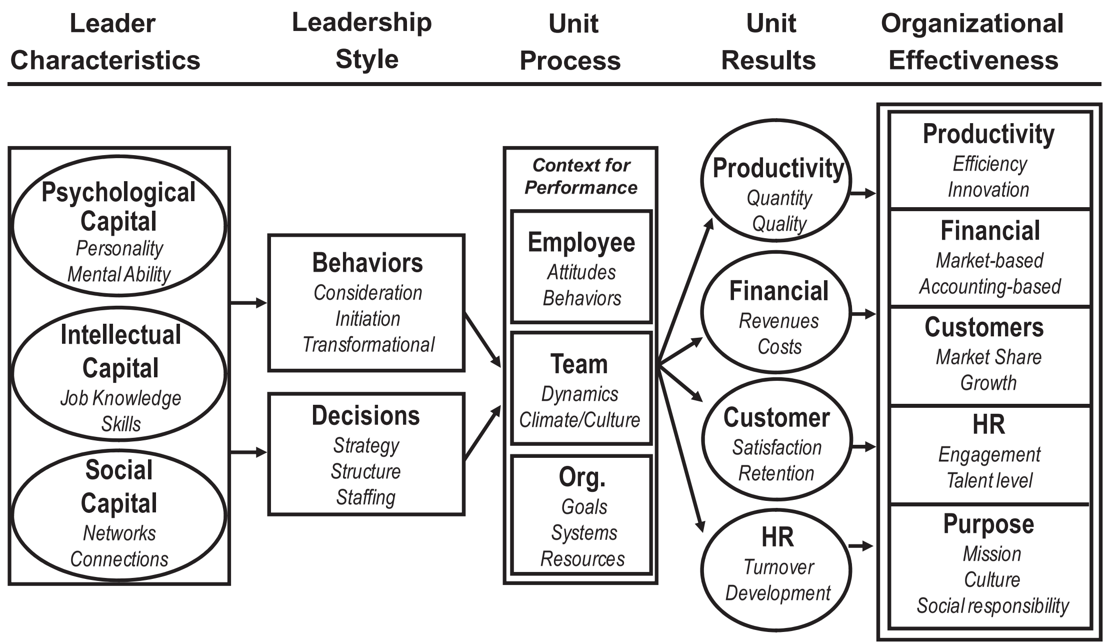

FIGURE 1 The leadership value chain. Specific variables within each domain (*in italics*) are meant to be illustrative and not definitive. The important feature of the framework is the classification of each domain as residing in a particular stage in the sequence linking individual leaders to organizational effectiveness.

assertive, outgoing), conscientious (self-controlled, organized, hard working), open (creative, visionary, flexible), and only somewhat agreeable (considerate, but also tough minded).

Recent advances in personality research show that counterproductive dispositions and values can shed further light on understanding effective, and ineffective, leadership. For instance, so-called "dark side" dispositions have been conceptualized as counterproductive, extreme versions of the Big Five that undermine leadership effectiveness because they disrupt relationships and corrupt judgment (e.g., when extreme stability is seen as arrogance, when extreme conscientiousness leads to a fear of making mistakes; Hogan, Hogan, & Kaiser, 2010; Kaiser & Hogan, 2007). Another aspect of personality important in leadership is values. Values are deeply held beliefs about what is important and desirable and therefore motivate particular behavior patterns and choices (Hofstede, 1980; Rokeach, 1968). Several studies show how leader values predict what they will reward, sanction, and ignore, as well as the kinds of goals, strategies, and processes they will select, and even the types of information they will and will not attend to (Finklestein, Hambrick, & Cannella, 2009). Values also have implications for organizational fit, because leaders whose values are congruent with the values implicit in the organizational culture are more committed and productive (Schein, 1992).

Other psychological capital variables related to leadership include mental abilities. A recent meta-analysis of 151 studies reported a correlation of .27 between general mental ability, or IQ, and leadership (Judge, Ilies, & Colbert, 2004). General mental ability can be easily quantified with cognitive tests, of which there are many well-developed and easy-to-administer measures. Emotional intelligence (EQ) is more suspect; most supposed measures of EQ are little more than repackaged personality scales that do not represent it as a truly distinct mental ability (Mayer, Salovey, & Caruso, 2008). However, measures that represent EQ and its components as a true mental ability are sufficiently distinct from IQ and personality to make a unique contribution to the prediction of job performance (Daus & Ashkanasy, 2005). Alas, the research on ability-based measures of EQ and leadership is too sparse to draw strong conclusions at this stage.

Another key individual difference variable in leadership is learning orientation (Lombardo & Eichinger, 2000; McCall, 1998). A recent survey found that two thirds of companies consider learning orientation when identifying high-potential candidates (Silzer & Church, 2009). Unfortunately, the same article reported that there seems to be a lack of good assessment measures for learning. However, there is a compelling psychological literature on learning and underlying motivations to learn (cf. Dweck, 1999), and it seems promising that this work can be expanded upon to develop practically useful assessment tools.

Intellectual capital refers to knowledge and skills learned through education and experience. The importance of intellectual capital is underscored by the

Lessons of Experience research conducted at the Center for Creative Leadership, which determined that the majority of leadership development occurs on the job as managers face new work challenges (McCall, Lombardo, & Morrison, 1988). Factors such as job knowledge and functional skills are difficult to measure, and well-validated, standard assessment tools for use with leaders are hard to find. One promising approach developed for the selection of high-level military personnel includes a battery of problem-solving tasks that tap into creative problem-solving skills, contextual awareness skills, and social judgment skills (Zaccaro, Mumford, Connelly, Marks, & Gilbert, 2000). The biodata method also appears promising for measuring experience; a recent study demonstrated that a measure of the variety of developmental assignments combined with learning orientation can predict leadership competencies (Dragoni, Tesluk, Russell, & Oh, 2009).

Measures of social capital are less developed; more conceptual and empirical research is needed to quantify social relationships. There is currently an explosion of research on social networking analysis, and it is likely that this research will yield sorely needed measures of social capital. As the old adage goes, it is not what you know but who you know. A study of 20 General Electric executives who went on to become chief executive officers at different companies found that tapping into their social networks to staff their new teams was pivotal. When the new team included three or more members the chief executive officers had worked with previously, the companies generated on average 15.7% higher annualized returns compared with those of similar firms in their market; companies whose top teams included fewer members the chief executive officers had worked with generated an average of 16.6% lower annualized returns (Groysberg, McLean, & Nohria, 2006).

An important point about psychological, intellectual, and social capital variables is that they may be the best measure of potential. They are transportable characteristics and no matter where you go, there you are. These measures can be used to forecast likely performance in a larger role or gauge the bench strength of an employee body. Moreover, because these characteristics represent who leaders are, they are useful for understanding how leaders lead.

Leadership Style

Individual differences are relevant to the extent they are expressed in how the leader leads. We take an interdisciplinary view of leadership style and see two key aspects: *behaviors*, the actions leaders take, and *decisions*, the choices they make (Kaiser & Hogan, 2007; Kaiser et al., 2008).

The psychological study of leadership has focused on behaviors—being considerate, showing initiative, transforming followers, exchanging transactions, and so on—whereas management research emphasizes decision making in such domains as strategy, structure, systems, and so forth (Bass, 1990; Finklestein et al., 2009; Yukl, 2010). 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 social behavior—for instance, when a leader clarifies performance expectations or makes an emotional appeal to motivate employees—whereas indirect influence is a relatively impersonal process of guiding people through key decisions that shape their work environment—for example, by setting direction, structuring roles, implementing systems, and establishing formal policy (Kaiser & Hogan, 2007; Zaccaro & Horn, 2003). Both types of influence are important to leading a team.

These different forms of influence are represented in the leadership value chain by distinguishing direct influence as concerning the behaviors that directly motivate employees and galvanize teams—versus the behaviors that demoralize employees and weaken teams. Indirect influence is portrayed as making decisions about strategy, structure, and staffing that have an indirect influence on employees by providing guidance and constraints in the work environment.

The behavioral view of leadership style is the predominant view; it is the basis for most research measures as well as the ubiquitous 360-degree feedback surveys. The decision-making aspect seems to deserve greater attention, especially given the crucial role of judgment in leadership. Further, research suggests that as many as half of all management decisions fail (Nutt, 1999). Research in the management sciences shows that 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; e.g., Bertrand & Schoar, 2003). Furthermore, these preferences are a function of personality and experience (Miller & Toulouse, 1986; Prince, 2005).

This disparity poses a difficulty in measuring leadership style. Measures of leader behaviors are commonplace. Measures of preferred decisions are less common and less well-developed. An unbalanced assessment strategy that only measures the behavioral aspect of leadership style 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 and rater errors (Murphy & Cleveland, 1995). One problem that compromises the use of ratings is that they are saturated with liking; studies have shown that a substantial portion of differences in ratings is due to how much the rater likes the person being rated (Brown & Keeping, 2005; Varma, DeNisi, & Peters, 1996). Thus, relying on ratings alone amounts to a de facto popularity contest, despite the fact that leaders have to sometimes make unpopular decisions.

What are the alternatives to ratings? From a pure methodological perspective, job simulations and assessment centers may be viable. Quantification of naturalistic observations made by subject matter experts is another option. It is true that 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. Performance ratings say little about potential and likely performance in a different role (Silzer & Church, 2009). 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 (Freedman, 1998; Kaiser, Craig, Overfield, & Yarborough, 2010). Therefore, succession planning efforts that exclusively rely on assessments of current performance are ill-advised. Certainly current (and historical) performance should be considered, but it should be considered 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 for which one is responsible.

Team or Unit Process

The effect of leaders on organizational performance is mediated; the behavioral and decision-making aspects of leadership style affect organizational performance through their effects on the team or 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 results as a distal effect.

It is important to conceptualize the effect of leadership on team or unit processes at multiple levels of analysis. Three distinct levels include the individual employee, the team, and the organization itself. Meta-analyses document how initiation, consideration, transformational, and transactional leader behaviors have a direct influence on individual employee's attitudes, motivation, and performance (Judge & Piccolo, 2004; Judge, Piccolo, & Illies, 2004). Other studies, including a meta-analysis, show that these leader behaviors also affect team dynamics, norms, and climate (Burke et al., 2006; Peterson, Smith, Martorana, & Owens, 2003; Taggar & Ellis, 2007)—for instance, by facilitating communication and coordination, resolving conflict and building trust, rewarding or sanctioning certain behaviors, role modeling, and building shared mental models through group learning. Leader decisions also indirectly influence employees and teams by defining organizational features such as goals, systems, and routines for processing work, whom to put in what role, and how to allocate resources (Finklestein et al., 2009; Zaccaro & Horn, 2003). These expressions of strategy, structure, and staffing shape the organization which guides and constrains employee choices and actions (Kaiser & Hogan, 2007).

The measurement of unit processes becomes increasingly more difficult as one moves from the employee to team to organizational levels. At the employee level, important things to consider are attitudes and motivational factors like job satisfaction, trust in management, and engagement, as well as behaviors such as job performance, citizenship, and counterproductivity. At the team level, dynamics and climate can be assessed. Team dynamics refer to how the team functions as a group and includes such things as cooperation, communication patterns, cohesion, conflict, 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 what it feels like for members to be a part of the team. Climate can be assessed with surveys that tap such things as stress, psychological safety, customer service orientation, support for innovation, and so forth.

Similar to measuring leader decisions, measuring the effects leaders have on the organization poses difficulties. The development of standardized 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 strategy, structure, and staffing vis-à-vis what the larger organization needs from this particular team or unit.

In sum, the mechanisms through which leadership style drives unit results operate at the employee, team, and organizational levels of analysis. Collectively, a leader's effect across these three levels can be seen as creating a context for performance because, as Hackman (2002) put it, the leader's role is to set the stage for group performance. On the one hand, this promotes an internal focus—with an emphasis on activities within the team or unit. On the other hand, because contexts can be more or less conducive to performance, this helps explain why a team achieves what it does, which is represented by unit outcomes.

Team or Unit Outcomes

The next category pertains to the results the team or unit produces over a given period of time. Results may be the best measure of leader effectiveness. As Peter Drucker famously observed, "Effective leadership is not about making speeches or being liked; leadership is defined by results not attributes." Yet, it is surprising how infrequently unit performance is explicitly measured and reflected in the evaluation of managers. It is sometimes argued that results are affected by things beyond a leader's control—changes in the macroeconomy, regulations, competitor moves, and the like. This argument makes little sense; if results are beyond a leader's influence, then it shouldn't matter who is chosen to lead. Of course, the robust literature on leadership succession shows clearly that changes in leadership are followed by changes in organizational performance (Day & Lord, 1988), which makes the case that leaders do affect results. Moreover, unit results are the primary contribution each individual leader makes to the performance 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 nonfinancial metrics can collectively provide a balanced view. The balanced scorecard methodology 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 (Kaplan & Norton, 1996).

Productivity measures of unit performance concern the efficiency of internal processes and are reflected in the quantity and quality of goods and/or services produced. Another class concerns financial results—including 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. Last, human resource-based measures of unit performance include such variables as safety/accident rates, rate of voluntary turnover, and learning and development. In the modern era of scarce talent, it is important to index the extent to which leaders are developing their subordinates into future leaders.

Recent research substantiates how leadership style and unit process relate to unit outcomes. For instance, leader behaviors have an effect on employee attitudes and motivation, which in turn predicts financial, productivity, customer, and human resources outcomes (Harter, Schmidt, & Hayes, 2002). Further, economic research indicates that leader choices about basic management practices—operations (e.g., process improvements, internal communication), targets (goals, rigor and transparency of setting goals), monitoring (tracking and following up on performance), and incentives (linking pay and performance)—predict a broad range of performance metrics (e.g., productivity, profitability, sales growth, survival rates; Bloom & Van Reenen, 2007).

Two things are 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., percentage 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.

An article by John Boudreau and Peter Ramstad describing a new paradigm of decision science for human resources suggests how the optimal choice of business unit metrics may vary from organization to organization (Boudreau &

Ramstad, 2005). They provide guidance and describe a flexible architecture in which choices about what to measure can be tailored and strategic yet still focused and disciplined.

These four categories of team or business-unit results—productivity, financial, customer, and human resources—account for the majority of measures reported in the research literature. Moreover, they are 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 imperatives.

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 chief executive officer and the top team are responsible. Theorists often take a gestalt view of performance at 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. Unit performance and organizational performance, however, do 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 that transcends unit performance and has to do with the realization of the firm's purpose, its reason for being.

Broadly conceived, organizational productivity reflects the efficiency of internal processes in transforming inputs (capital, people, materials) into outputs (goods and services; Katz & Kahn, 1978). Indicators here are derived from those at the unit level (e.g., quantity and quality). Rate of innovation could also be included. Team or unit performance measures like these often reflect an internal perspective and overlook the fact that organizations compete against one another (Kaiser et al., 2008). Therefore it is useful to compare these internal metrics to external standards, such as industry benchmarks or the performance of rival organizations.

The second category of organizational effectiveness measures concerns financial indicators. It is important to consider two basic classes of financial indicators, 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, 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-based measures because they are less subject to manipulation (Anderson & Tirrell, 2004). Nonetheless, accounting data can provide meaningful and unique information. They differ from market-based measures in that they reflect an historical perspective—they reflect how the organization has performed. Common examples include earnings per share, return on investment or assets or equity, earnings growth rates, and economic value added (operating profit less taxes and the cost of capital; Stern, Shiely, & Ross, 2001).

Customer service indices comprise the third category of organizational effectiveness metrics 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.

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 progress on the organization's purpose. This class of variables is conceptually the more ambiguous and difficult to mesure. By definition, it is essentially an idiographic and existential construct—key organizational stakeholders define its raison d'être and it does not 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 (Collins & Porras, 1997). 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. 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" (Burke & Litwin, 1989, p. 277), leaving open the question of whether that way is or is not consistent with the values espoused by key stakeholders. 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 (Schein, 1992). 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).

Last, an assessment of organizational purpose involves social responsibility and 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. Thus the sustainability of organizational performance depends, in no small part, on the sustainability of the larger social community and environment.

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

CONTEXT

Of course, leadership does not take place in a vacuum, but rather in a particular context. Thus, the leadership value chain framework depicted in Figure 1 is enveloped in multiple layers of context. Surprisingly, the field lacks an integrative and generally accepted taxonomy of key contextual factors. A recent review article, however, identified at least seven distinct aspects of context that have been studied (Porter & McLaughlin, 2006): Culture/climate (e.g., norms, values), goals/purpose (strategy), people/composition (demographics, capabilities), processes (types of tasks, governance, policies), state or condition (stability or crisis), structure (organizational level, degree of centralization), and time (point in history, stage in life cycle).

Contextual factors need to be taken into account to make the components of the leadership value chain relevant and applicable in a particular case. For instance, the choice of measures to reflect unit results should be grounded in the nature of the organization, its industry, and strategic orientation. The relevance of various organizational effectiveness measures depend on the stage in the organizational life cycle. Further, recent cross-cultural research indicates that although much of what constitutes desirable leadership is universally accepted, there are critical cultural differences in how these behaviors are regarded depending on how they are expressed (House et al., 2004).

Although the research literature on how contextual factors affect the relations among variables in the leadership value chain is piecemeal, it can be instructive. For example, the relationship between leadership style variables and the effect on unit processes and outcomes appears to depend on hierarchical level. Research shows how the effectiveness of various leader behaviors varies dramatically as a function of level (Freedman, 1998; Kaiser et al., 2010). For instance, for middle managers, a more directive and less empowering style appears most effective; the exact opposite spells success for executives. There are other examples but they are isolated; the literature could benefit from a systematic integration of the research on how contextual factors moderate the effects 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. One obvious limit 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. However, application to non-profits and government organizations such as the military and educational institutions will require further refinement and customization. We believe, however, that the front half of the model, from leader characteristics through effect on unit processes, applies to most, if not all, organizations.

Another limitation of the leadership value chain is that it may not represent every variable relevant to leadership and value. Rather, we have tried to identify the major classes of variables, and identify the most critical variables in each class, that must be considered. Albert 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.

The leadership value chain is also limited in that it is not a dynamic theoretical model of how leaders cause organizational performance; rather, it is simply an articulation of the major classes and sequence of variables relating leaders to organizational performance. Figure 1 may suggest a simple, linear flow of effects beginning with leaders and ending with organizational performance. In reality, the relationships among these variables are multi-directional and reciprocal. For instance, follower behaviors and attitudes can prompt leaders to adjust their style (see Bass, 1990, pp. 345–360) and organizational performance can influence employee attitudes just as attitudes can influence organizational performance (Schneider, Hanges, Smith, & Salvaggio, 2003). At the same time, there is also support for the implied causal flow of variables in Figure 1. Research on succession clearly indicates that changes in leadership are *followed* by changes in organizational processes and results (e.g., Bertrand & Schoar, 2003; Day & Lord, 1998). Simply put, leadership and organizational performance are complex phenomena involving dynamic human systems that allow for multiple sources of causality over time.

APPLICATIONS

In this final section, we describe different applications of the leadership value chain framework for solving common talent management and organizational development problems. The primary use of the leadership value chain is to identify and specify the range 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 2×2 matrix, for instance, such as the one made popular by General Electric 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 the pieces laid out 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 (Sessa, Kaiser, Taylor, & Campbell, 1998). For instance, is it a turnaround situation? A start up? A mature industry? Is morale low and turnover a problem? Based on the role requirements, one can work backwards through the value chain to define the ideal leadership style for the situation. This naturally suggests the required psychological, 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, relevant mental abilities, and learning orientation; taking stock of relevant work experiences and skills; and getting a sense of networks and other connections that are relevant. 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 human resources results were achieved? How did the leader affect employees and the way the team functioned? And what kinds of behaviors and decisions did the leader employ? Taken together, this information on each candidate provides for a more informed selection decision—far more than is typically the case (Sessa et al.).

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 training and development 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. An adequate appraisal of performance should include how one leads and both how and what one's team or unit accomplishes. Measures for the unit outcomes should be fairly easy to compile, provided the organization tracks performance. Unit processes may require more effort, 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 appraisal 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 performance across a balanced range of unit outcomes and unit processes is an effective way to align incentives with sustainable organizational performance.

Last, 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. 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?

There are many other applications of the leadership value chain framework, just as there are many questions about the value, importance, and accountability of leaders. We do not assume that this framework is the final word on how leaders affect organizational performance. However, we do hope it is helpful for thinking about the question in solving real-world problems concerning the management of leadership talent and the enhancement of organizational performance.

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