Performance Improvement Quarterly, 18(3) pp. 26-36

Can Boards of Directors Think Strategically? Some Issues in Developing Direction-givers' Thinking to a Mega Level

Bob Garratt
Cass Business School

ABSTRACT

The author argues that current corporate government legislation and practice is weighted too much in the direction of "board compliance." It is, therefore, in danger of reducing the risks taken by boards of directors. In the long term this could slow significantly the growth of capitalism. He proposes a rebalancing of the fundamental board dilemma—how to strike a dynamic balance between driving the enterprise forward and keeping it under prudent control—in favor of "board performance" and raising the competence of "Mega-thinking" on the board. This requires integrated board developmental activities so that their directorial accountabilities and liabilities are differentiated from the executive's, and that the requirement for rigorous strategic thinking has total commitment. Often fear and irritation by newly-promoted executives has to be overcome here. The author introduces the "Learning Board" model and its associated annual rhythm for a board's year. Three approaches to developing strategic thinking are discussed including the Thinking Intentions Profile, and an updated version of the PPESTT analysis.

Introduction and Terminology

Oscar Wilde was right, Britain and the US are countries kept apart by a common language. This is especially true in the area of corporate governance when the same words can mean very different things on either side of the Atlantic. So before I get into the heart of this chapter let me clarify my use of words by giving some definitions. Here I use the term "director" in its strict legal sense—a statutory member of the board of directors charged with driving their enterprise forward (giving direction) whilst keeping it under prudent control—the classical "directorial dilemma." The term "director" is often abused in the US by referring to two quite distinct jobs. On the one hand is the correct usage as a member of the board of directors. But it is used also to define an executive one level below a Vice President. As the US corporation tends to be executive-led in its business thinking with a consequent down-playing of the importance of directors, this double use of the term creates confusion in the minds of many.

How Directors Avoid Thinking About the Future

Most board directors do not budget time for, nor have little sustained interest in, thinking regularly and rigorously about the future health of their businesses. This surprising finding comes from my own work on the preferred thinking patterns of statutory directors in the UK (Pierce, 2000), the work on "Directoral Dashboards" by my colleague Ram Ramakrishnan in South East Asia (2003), my colleague Clive Morton's work published in *By The Skin Of Our Teeth* (2003), and my empiric observations through working with boards of directors in Europe, East Asia, Australia, and the US over many years. Even a cursory check of the amount of time budgeted by a board for its proper direction-giving roles of formulating policy and developing strategic thinking, as distinct from trying to micro-manage the company from the boardroom table, should prove this.

Why should this be so? The tendency for a board of directors, especially those comprised of existing or previous executives, is to try and micro-manage the business from the boardroom table, while avoiding their key task of developing strategic thinking. If we accept that the term *mega* (originally *meta* in ancient Greek) means both larger, and above the mean—defined by Kaufman (2000) to include societal impacts and consequences, then mega-thinking demands both a change of board priorities and a concerted effort to sustain it. This means raising their eyes for even short periods of time away from the immediate, executive world of instant delivery and instant gratification to one where they reach the paradoxical, more reflective, and yet more proactive world of strategic thinking. Psychologically one should help directors reframe their role so that they feel it both necessary and legitimate to budget time on these reflective activities and so develop their "helicopter view" competencies. Taking this further, the development in both the individual director, the board, and the total organization of such "double loop" learning (Watzlawick, Weakland, & Fisch, 1974; Argyris, 1999) is a way of rising above the daily pressures of the executive treadmill to fulfill the true, long term, directorial role. It demands that the direction-givers are capable not only of regular and rigorous scanning of their socio-political environment but have then the capacity to assess the strategic risks associated with their analyses, and be bale to take wise decisions on the broad deployment of their scarce resources to benefit the long-term health, and prudent control, of the business thus maintaining their legal *fiduciary duty* to their owners.

Executive life is rarely like this, especially in US corporations. In my UK studies less than twenty percent of the directorial population has either the interest or innate capacity to rise to the "mega" level of thinking. I find that there are three main reasons for this:

- Ignorance of, and a lack of ability in, differentiating between the executive and direction-giving roles in an organization
- Confusion over the legal position and liabilities of direction-givers as distinct from executives
- Fear and irritation in effective executives at the suggestion that they would have to learn new attitudes and skills to become an effective direction-giver

But before we review these let me comment on the present unhealthy position of many US corporations.

A Caveat on US Corporations

My experiences have come from the common law systems of the UK, East Asia, Australia and South Africa—the Commonwealth nations. The US has developed the commercial aspects of common law in a way which diverges from the rest of the Commonwealth and has, I argue strongly, led itself into an unhealthy and potentially corrosive dead end. Many US corporations seem to display acute schizophrenic tendencies when confronted with the requirement to develop "mega-thinking." On the one hand executives are rewarded well for being obsessively fixated on instant gratification through their delivery of their *quarterly* performance figures. Their willingness to tolerate this short-term perspective is compounded by four interacting factors.

> ***Many US corporations seem to display acute schizophrenic tendencies when confronted with the requirement to develop "mega-thinking."***

First, the common practice of a Chief Executive Officer insisting in his or her employment contract that they are also Chairman of the board effectively castrates the board and leaves it with one dominant director, regardless of the legal position. This alone makes collegial mega-thinking difficult if not impossible. Second, it is almost impossible for the shareholders to sack directors of quoted corporations, especially those many registered in Delaware, especially because of the "plurality" rule. Third, given the rate of "churn" of shareholders and funds in any one year, it is increasingly difficult to identify who "the owners" are at any one time and so, despite the noticeable rise of shareholder activists, the political issue of protecting shareholder rights is seen as a minor one. Fourth, the rushed legislation of the Sarbanes-Oxley Act 2002 (SOX) is damaging US business because it is focusing executive and directorial behavior on such detailed control and "single point of accountability" issues that it causes directors and executives to avoid risk increasingly and so reduce their time for mega-thinking. Yet risk is the very essence of capitalism. I argue that Sarbanes-Oxley will have damaging effects on the US economy unless it is amended. The US has already perfectly good fraud laws. The immediate and deeper problem is how to get US directors out of their current "compliance" mindset and back into adding shareholder value by designing their company's future. Currently SOX seems to be inhibiting the development of mega-thinking at US board level.

Developing the Directorial Mindset Toward Mega-Thinking and True Corporate Governance

Agreeing the Meaning of "Policy" and "Strategy"

Effective direction-giving is always a dilemma. On the one horn is the act of driving the enterprise forward. On the other horn is the act of keeping it under prudent control. It is the prime task of the board of directors to keep these in dynamic balance. And they will never get it completely right. The difference between the two is the risk that the directors take in their governing role. Mega-thinking helps reduce these risks by setting them in wider and more dynamic contexts and creating a feedback system for rapid learning from them.

The directorial dilemma is as old as time. If we look at the ancient Greek definition of "governance" (*kubernetes/helmsmanship*), then there are two intellectual foundations for creating effective organizations which have been around for some three-and-a-half millennia. The Greeks used the terms "policy" and "strategy" to define those higher levels of thinking above the day-to-day "tactics" which nowadays we tend to call "operations." Many corporations either are ignorant of these terms or are arrogant enough to assume, Tweedledum-like, that any word means what they say it should. This was lays madness. Let us look more closely at these two "mega" words.

Policy is the highest level of intellectual thought in an organization. It comes into the English language from the ancient Greek "polity." It concerns the board's understanding of the wider "political" environment which allows the energy niche within which their organizations exist currently. It is not, therefore, "policy-as-organizational-rules" (e.g., who gets which vacations, which parking slot, etc.). This is an abuse of the term perpetuated still by some business schools and consultancies. Policy Formulation demands that the board budgets time, and develops the intellectual capacity, to understand the complex inter-relations between their company and the wide environment energizing their business. This includes finding ways of tracking changes in, at the very minimum, the following environments:

- political,
- physical,
- economic,
- social,
- technology,
- trade (world),

and then being able to make some sense of them in relation to the business' Purpose, Vision and Values, and then adding of shareholder value.

Many business folk balk at this "PPESTT" concept. Indeed many say that they want as little to do with the "policy/political" world as possible. I am not arguing here that directors must be party-political, nor be seen to support a specific political grouping. I am arguing that they must be sensitive to changes in the wider "policy" environment, and to develop organizational nimbleness if they are to have the competitive intelligence to ensure the long-term future of their business.

Strategy comes also from the Greek and was defined originally as "the world of the military general." Later it became better known as meaning "the broad deployment of scarce resources to achieve our Purpose." The generals accepted, or debated, the political wish to achieve national Purpose, then they deployed their forces to achieve this. Nothing much changes over time, except our misuse of words. The *mega-thinking* concept seeks to reverse such misuse. But at present the adjective "strategic" is one of the worst abused because many executives believe that attaching it in front of a phrase makes that phrase more important and less open to critical questioning. My colleague Henry Mintzberg wrote the delightful book *The Rise and Fall of Strategic Planning* (1994) in which he differentiates between "strategic planning" and "strategic thinking." He argues that strategic planning is a dangerous oxymoron, a contradiction in terms like "friendly fire" and "fun run." We both argue that planning in any organization is crucial—but that it is the start of the executive round, not the role of the board. The board's role is to derive broad strategy from their policy formulation and foresight. Then they debate this with the executives who commit to the strategy and take it as the basis of their planning. The acid test is whether this strategy is implemented, and whether the associated rate of learning is equal to the rate of change in the external environments. Strategy has to be flexible in a dynamic and uncertain world. Strategy must never be set in concrete. What worries me about many of the corporations with whom I work is the lack of awareness of the importance of strategic *thinking*—the conscious or unconscious avoidance of "mega" level. I and colleagues have written about this in detail separately in *Developing Strategic Thought* (Garratt, 2003a).

Such "mega-thinking" is about developing the board's understanding of the wider policy context, which by definition will always be risky and difficult to quantify, and then encouraging them to *learn* consciously on a regular and rigorous basis how to broadly deploy their scarce resources to achieve their Purpose. This is expressed most clearly through their strategy statement which must include a combination of the five classic elements of strategy:

- Where we will advance (products, services, geographic areas)
- Where we will retreat (short-term redeployments)
- Where we will hold our ground
- Where we will make alliances
- Where we will withdraw totally

Toward the Learning Board

When creating a regular and rigorous system of board learning many organizations across the word have found it helpful to adopt the *Learning Board* model and process (Garratt, 2003b). This develops the fundamental notion of the board having to balance continuously Board Conformance (keeping the business under prudent control) and Board Performance (driving the enterprise forward). It uses the horizontal axis of time and the vertical axis of internal or external perspective (see Figure 1).

"Board Performance" covers the right-hand quarters of *Policy Formulation/Foresight* and *Strategic Thinking*. "Board Conformance" covers the left-hand quarters of *Supervising Management* and the *Accountability* of the board of directors. Figure 2 takes this basic framework into the detail of the full Learning Board model.

Using the model I urge boards to develop their mega-thinking by focusing with their executives on two key interfaces of the Learning Board (the arrowheads in the right-hand quarters):

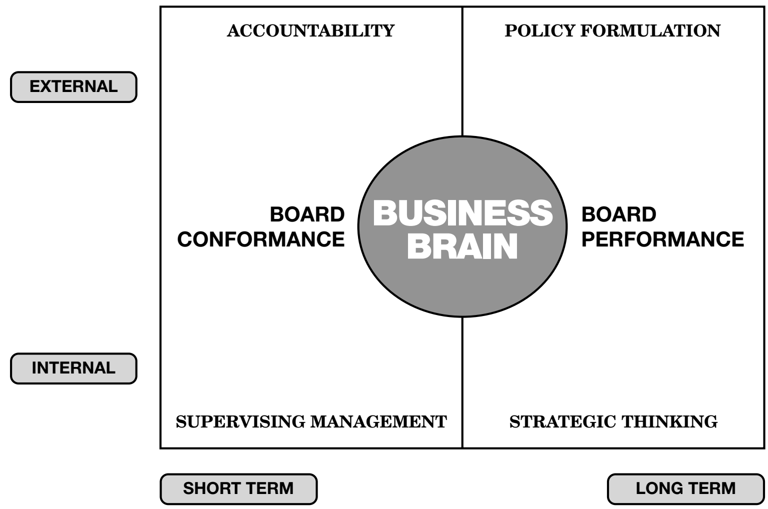

Figure 1. The Learning Board: Basic Framework.

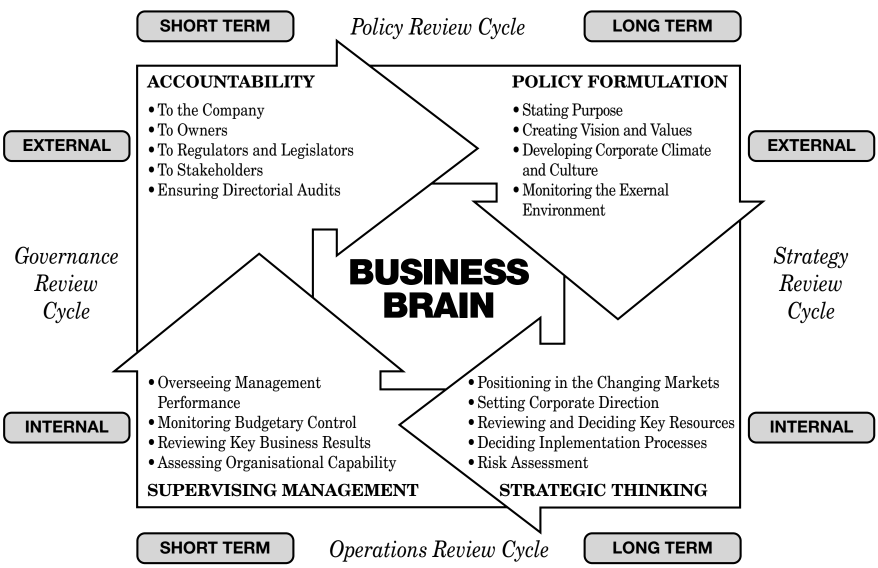

Figure 2. The full Learning Board model.

- The mega-level debate between the results of their *Monitoring of the External Environment* (PPESTT et al.) and their subsequent *Positioning In The Changing Markets*
- The debate between *Implementing the Strategy* and *Ensuring Organizational Capability* (Garratt, 2000). This is where the effectiveness of a strategy is tested, often to destruction. My work on UK director's preferred thinking styles reinforces this point and will be discussed in more detail later in this chapter. Often the lack of interest by a board in developing effective mega-thinking and subsequent strategies with the executives, combined with an unwillingness to hear bad news from those implementing strategy, leads to the sub-optimization of the strategy and at worst business failure. In complexity theory terms they can fool themselves into believing that they are winning when the truth is that they are losing in a changed environment (Monks, 1998).

But there is more to developing board effectiveness through mega-thinking than understanding a quadrant. The essence is not in the content but in the board's learning process. Accepting that there is an annual *rhythm* to a board's year is crucial. In its simplest form this means that the chairman ensures that:

- The board starts its year with an "away day" which checks out Purpose, Vision and Values, and Corporate Culture (all of which are measurable) before getting into the deep mega-thoughts on monitoring the external environment
- The board has at least quarterly "away days" to develop its strategy by taking the results of its Policy monitoring and debates into the key issues of organizational capability, strategic implementation and rapid learning systems
- Ensuring that the monthly "numbers" session is restricted to no more than one hour so that there is not tendency for the board to try and micro-manage the executives form the boardroom table. With current software this is possible even for multinationals
- Ensuring that at month nine of a financial year there is an "away day" to ensure that the much accountability demanded now by legislators and regulators is on track for the annual report in three months time. The days of desperately post-rationalizing at month thirteen are now over.

This is not rocket science. But it does give the board a regularity and rigorous discipline, within an agreed picture of an annual process, which allows them to understand better their role, especially the importance of the mega-thinking aspects of it. And it gives them "homework" to do, which I shall return to later.

Opening-up the Board's Mega-Thinking Process

Where is the wisdom we have lost in knowledge? Where is the knowledge we have lost in information?

—T.S. Eliot, *The Rock,* 1934

The essence of ensuring mega-thinking in the boardroom is to allow sufficient "blue skies" time to ensure that the board is not dominated by data-overload. SOX has already made this more difficult. Indeed the attempt by President Bush's team to "stop the bad guys" fraudulent practices has threatened the core notion of capitalism—business judgment based on thoughtful risk. SOX seem based on the notion that better business judgment is based on increasing data complexity followed by order and control. This is a delusion. Effective corporate direction-giving is not about security. It is about the skill of judging risk based on hard and soft facts, and then committing to it. It is about developing corporate wisdom.

How can this be addressed? My experience is that the generation of a level of humility in board members and executives in breakingoutoftheir executive behaviors, plus a reframing of their approach to their thinking processes, pays dividends. Humility is necessary to accept that many of the thinking and behavioral styles which allowed executives to scale the greasy pole become dysfunctional when they strive to become strategic thinkers. Whereas before their "shaping" behavior (Belbin, 2003) their focus was on the short-term micro-politics at the top of their corporation (Garratt, 2003c), and a public stance of having to be seen as omniscient has proved successful (Garratt, 2003c), the opposite is true when they are trying collegially to ensure the long-term health of their business. If such earlier non-collegial behaviors are brought into the boardroom, then the chances of mega-thinking are reduced and the chances of interpersonal political conflict increased.

There are three areas of directorial thinking, and subsequent learning, by which the mega-approach can be developed.

Using Intelligent Naivety

First, a useful start is to develop around the boardroom table the acceptability, indeed the necessity, of using *intelligent naivety* (Revans, 1982). This is a powerful concept which says that in this group it is OK to say "I don't know, tell me more." It assumes that the people sitting around the boardroom table are bright, but that many will be uninformed about the technical details of the different specialist executive functions. Once established as a group norm through the chairman it helps stop "techno-babble" in a group (i.e., the deliberate overuse of technical terms in the hope of intimidating into submission the non-specialists around the table). This can be made much worse if there is also a tacit agreement in the group that no specialist will question another specialist's area. This is the opposite of what a board of directors is meant to do. So the chairman must encourage those who do not understand, or doubt, what has been said to have

***First, a useful start is to develop around the boardroom table the acceptability, indeed the necessity, of using* intelligent naivety.**

the courage and collegial support to say just that and to ask for a simpler explanation. Often this causes other directors to say that they had been wondering about this also and, with luck, the techno-babble unravels and the air is cleared for some mega-thinking.

Developing Divergent Thinking Styles

Second, many critics of current executives, and the business school's approach to the education process of MBA students, point to the analysis-only fixation of the programs (Hayes & Abernathy, 1980; Mintzberg, 2004). The consequent "analysis-paralysis" is often applied thoughtlessly in practice. This is hardly surprising as the notion of "convergent thinking" is deep in our secondary and tertiary educational institutes (Hudson, 1970). The idea that the only way of problem-solving is to focus sharply on one element, strip out all the contextual information and go for a single "right" answer, is still deep in many executives' and professionals' mindsets. This explains in part why the business school and consultancy worlds, are dominated by quadrants as key instructional tools. Quadrants demonstrate two-dimensional thinking well. But the world is four-dimensional, so quadrants have limited use. Having trained with architects I am used to thinking in three and four dimensions, along with many physicists and mathematicians. Most executives are not.

The approach here is to encourage "divergent thinking"—where C.P. Snow's two cultures (Science and the Arts; 1993) are integrated (Hudson, 1970). This does not exclude "convergent thinking" but ensures that the contexts are explored well *before* convergent thinking allows for risk-assessment and strategic judgment. Even then an effective strategy will always have contingencies built in so that fast feedback from its implementation will allow rapid modification of it.

Divergent thinking is the core of the board's "homework." They are paid to keep a constant watch on trends in the external environment and to feed these into the board's quarterly "away days" and their consequent mega-thinking. A simple start is to take the PPESTT framework and then have the board directors form "buddy pairs," either two directors or a director and an executive. Each pair takes one element of the PPESTT (political, physical, economic, etc.) and for three months monitors the trends that they see. These are reported back briefly at the quarterly strategic thinking away days, debated, and then their portfolio is handed to another pair whilst they take a different one. Over an eighteen month period this alone transforms the quality of mega-thinking on a board.

Profiling Thinking Intentions

Third, it is possible to quantify a person's thinking *preferences* (i.e., the preferred sequence of a person's thoughts) as they attempt to solve a problem. This happens in a person's mind before they open their mouth and before they are seen by others to behave. The best instrument I know for this the *Thinking Intentions Profile* (TIP) from Effective Intelligence

Ltd. It is a self-assessment instrument which reviews three elements for effective thought:

- Judgment
- Description
- Realizing

"Judgment" is essentially past-orientated and builds on a personal blend of logic and rationality, and values and commitment. "Description" is present-focused and builds on a personal blend of hard, quantifiable facts and "soft facts" (sensing the immediate political climate in a person or group). "Realizing" is future-orientated and is about making the future happen. It is a personal blend of vision, and ingenuity.

These six elements of the TIP are then broken down into twenty-one subsets which I shall not go into now. However, I am now analyzing a data-base of five hundred UK board directors and already there are some worrying findings (Pierce, 2000; Garratt, 2003c). At least eighty percent of the population (male and female; private and public sectors) has a distinctive pattern. They are strongest in the "soft facts" areas and their thinking thrives on the micro-politics which surround them. This is backed by a high second preference to use logic and rationality. So a tendency to post-rationalize strongly what they have just done micro-politically is evident. For me this begins to explain why mega-thinking often fails to get started. If one then looks at the *least* preferred thinking styles of the board directors in the sample, they are dealing with the hard facts, and last, having the ingenuity to want to make the future happen. This seems entirely paradoxical for direction-givers. More research is required but, if true, this is an indictment of the training and development of the current generation of board directors. Having worked with directors on five of the six continents I would say from empirical observation that this holds true for the majority whatever their nationality.

Conclusion

Mega-thinking cannot be developed in direction-givers without having a strong intellectual framework to make sense of their increasingly complex and interacting external environment. Developing such understanding requires both a regular and rigorous process of continuous learning by the board. Here the *Learning Board* is useful. Such continuous learning also requires regular annual appraisal of the board as an effective working group, of each board committee, and of each individual director—as is now the regulation for UK listed companies (Financial Reporting Council, 2003).

Ultimately, mega-thinking occurs in private, behind the boardroom door. If the directors have a strong chairman who understands the legal notion of each director being an equal colleague with the duty to comment critically on what the company and its executives are doing, and accept that ultimately they as directors are accountable, then there is a sporting chance of their business having a healthy future. If there is a dominant figure who censors open thinking, critical review and intelligent naivety, then the corporation is stuck in a "bad learning" cycle and is doomed finally.

But even in a "good learning" cycle there can be no certainty. Director's thinking is always about dilemmas (Hampden-Turner & Trompenaars, 1994) and trying to balance two opposing notions. It has to be. So I leave the final sentence to F. Scott Fitzgerald:

> *The test of a first-rate intelligence is the ability to hold two opposed ideas in the mind at the same time, and still retain the ability to function.*
>
> —The Crack-up, 1936

References

Argyris, C. (1999). *On organizational learning* (2nd ed.). Oxford: Blackwell Publishers.

Belbin, M. (2003). *Management teams: How they succeed or fail*. London: Butterworth Heinemann.

Financial Reporting Council. (2003, July). *The combined code on corporate governance*. Retrieved from http://www.frc.org.uk/documents/pagemanager/frc/combinedcodefinal.pdf

Garratt, B. (2000). *Twelve organisational capabilities: Valuing people at work*. London: Harper.

Garratt, B. (Ed.). (2003a). *Developing strategic thought.* New York: Harper Collins.

Garratt, B. (2003b). *The fish rots from the head.* New York: Harper Collins.

Garratt, B. (Ed.). (2003c). *Thin on top: Why corporate governance matters*. London: Nicolas Brealey Publishing.

Hayes, R.H., & Abernathy, W.J. (1980, July-August). Managing our way to economic decline. *Harvard Business Review.*

Hampden-Turner, C., & Trompenaars, F. (1994). *The seven cultures of capitalism: Value systems for creating wealth in the United States, Britain, Japan, Germany, France, Sweden, and the Netherlands*. London: Piatkus.

Hudson, L. (1970). *Frames of mind: Ability perception and self-perception in the arts and science.* London: Penguin.

Kaufman, R. (2000). *Mega planning: Practical tools for organizational success.* Thousand Oaks, CA: Sage.

Mintzberg, H. (1994). *The rise and fall of strategic planning.* New York: Free Press.

Mintzberg, H. (2004). *Managers not MBAs.* London: FT Prentice Hall.

Monks, R.A.G. (1998). *The Emperor's nightingale*. London: Capstone Books.

Morton, C. (2000). *By the skin of our teeth.* London: Middlesex University Press.

Pierce, C. (Ed.). (2000). *The effective director.* London: Kogan Page.

Ramakrishnan, R. (2003). Directorial Dashboards: The New Board Metrics. In B. Garratt (Ed.), *Thin on top: Why corporate governance matters*. London: Nicolas Brealey Publishing.

Revans, R. (1982). *The origins and growth of action learning*. Bromley: Chartwell-Bratt.

Snow, C.P. (1993). *The two cultures.* Cambridge: Cambridge University Press.

Watzlawick, P., Weakland, J., & Fisch, R. (1974). *Change: Problem formulation and problem resolution*. New York: Norton.

BOB GARRATT is a Visiting Professor in Corporate Governance at the Cass Business School, City University London, Chairman of Board Performance, Ltd. in London and Singapore, and has written extensively on corporate governance, board development, and strategic thinking. His books include *The Fish Rots from The Head: The Crisis In Our Boardrooms* (1996 & 2003), *Thin On Top: Why Corporate Governance Matters* (2003), and *Developing Strategic Thought* (Editor; 1995 & 2003). *E-mail*: garratts@btconnect.com