The Achieving potential series: gaining the leadership edge

The new global mindset
Driving innovation through diverse perspectives
Executive summary Cultural diversity offers the flexibility and creativity we need to recreate the global economy for the 21st century.

The new language of leadership This is far more encompassing of the entire human experience, and leads to a global viewpoint.

Understanding the vocabulary Diversity of thinking is key to today’s global business, but a new study from the Economist Intelligence Unit shows companies falling short on cultural goals.

Q&A: Ernst & Young’s Global Chair and CEO, James Turley, talks with Fareed Zakaria, Editor of Newsweek International, about why uniformity is the enemy of the new leadership.

Q&A: Ernst & Young’s Americas Inclusiveness Officer, Billie Williamson, asks Haila Wang, CEO of France Telecom R&D Beijing, about the roles of diversity and innovation—and leaving the comfort zone.

Letting it all go: unleashing diversity leads to idea generation throughout the organization.

Rutgers University Professor Farrokh Langdana offers an economic point of view.

Reading between the lines The new rules of leadership await codification. But here are four consistent themes:

Lesson 1: stir the pot
Lesson 2: anticipate the Next Big Thing—or better yet, drive the Next Big Thing!
Lesson 3: nurture a spectrum of talent
Lesson 4: get the mindset

Q&A: Ernst & Young’s Global Leader, Diversity and Inclusiveness, Pierre Hurstel, speaks with leading intercultural authority Milton Bennett, Ph.D., about the value of diversity training and programs.

The last word: cracking the code Step back, take stock and get comfortable with the diversity mandate.

References
Executive summary

Cultural diversity offers the flexibility and creativity we need to recreate the global economy for the 21st century.

Innovating was never easy. But it’s more difficult than ever in a globalized world that is struggling to recover from a major economic crisis. Differing voices and viewpoints are powerful factors in steering innovation. If an organization does not leverage the potent weapon of diversity, it risks limiting its creative potential and ultimately losing its competitive edge.

In the evolution of leadership, diversity is not defined just by race or gender. It also encompasses the whole human experience – age, culture, education, personality, skills and life experiences. Managed effectively, this cultural diversity offers the flexibility and creativity we need to recover from the economic crisis and confront the many forces challenging us: economic and social upheavals; major demographic shifts; globalization; an urgent need to innovate to renew economic growth; and increasing demands for diversity from our partners, clients, customers and other stakeholders. A recent Ernst & Young study, Redrawing the map: globalization and the changing world of business, reveals that the boards of many global companies lack the diversity to deal with intercultural challenges. At the same time, they cite the need for internationally experienced staff as the most important cultural factor in conducting business globally (see “Diversity of thinking is most important in global business,” page 7).

Becoming a great leader in any country or culture takes time, but translating the new inclusive idiom will quickly reveal four imperatives for success:

1. Stir the pot. Research shows that diverse viewpoints generate the lively debate that can create new ideas.
2. Anticipate the Next Big Thing – or better yet, drive the Next Big Thing! Diversity powers innovation, helping your business generate new products and services.
4. Get the mindset. Focus on transformational leadership.

Leading companies have shown that visible benefits to the bottom line result from leveraging inclusive ways of thinking. But an inclusiveness strategy should not be implemented rashly. Leaders must first cultivate the insight to recognize and understand differences and their power to bring about profound cultural shifts in organizations. This mental transformation is critical to developing transformational leadership capabilities. It is the single most important step toward becoming a successful player in the global arena.
The new language of leadership

Hema Hattangady takes diversity seriously.

As Managing Director of Schneider Electric Conzerv, the Indian business division of the Germany-based global energy management giant, Hattangady oversees the parent company’s diversity initiatives in India. One of the very first actions that Schneider President and CEO Jean-Pascal Tricoire took after his company acquired Conzerv was to set up a steering committee for diversity. He wasn’t just paying lip service to the concept. Not only did the Indian subsidiary actively recruit people from all over India and from different educational backgrounds, but it also considered them key players in innovation, which Hattangady calls the “engine” of her business.

“When you start recruiting people from the different regions, at senior leadership levels, you get a much broader perspective on business issues,” Hattangady says. But to manage the process effectively, senior management must set the right tone throughout the organization, she adds. “The necessary approach is tough love. You’ve got to be firm and kind and patient enough to persuade the key people, ensuring that they are genuine ambassadors for diversity.”

Hattangady and Tricoire are among many business leaders in the vanguard of a dynamic new approach to leadership, one that uses diversity as an essential tool to innovate and as a key element to achieve a cultural shift in the organization. It is fast becoming the most effective leadership style to steer companies to success in today’s global business environment. But it also means being willing to jettison traditional management wisdom and learn what may even be called a new thought process: the thought process of global or intercultural competency. Like many mindsets, this one has its own rules, nuances, challenges and, all too often, baffling exceptions. Yet it leads to the global viewpoint that is best prepared to drive innovation.
Understanding the vocabulary
The word “diversity” has traditionally been branded as a “human resources” term, associated with fair hiring practices or enhancing an organization’s image as a good citizen. But it has the power to be so much more. Research shows that a diverse organization enjoys quantifiable business benefits that homogeneous firms do not. Like any strategy, diversity can backfire if handled badly; managed artfully, it can deliver remarkably positive results. The leaders of the future will need to view diversity much as they do other social and political issues – such as privacy, the environment and product safety – that are increasingly important to corporate strategy and that have major financial implications for global companies.

It is important to note that diversity today no longer means just differences in race or gender. It is far more encompassing of the whole human experience. Multiple dimensions, such as age, culture, personality, skills, training, educational background and life experiences, need to be considered. To thrive and innovate in the global economy, we require flexibility, creativity and imagination – qualities that can be nurtured only by a diversity of viewpoints bringing different voices to the table and that we urgently need as we emerge from the worst economic crisis in decades. Several forces are actively shaping the new mindset of inclusiveness that we must learn:

**Economic and social forces.** Deep recessions often inspire profound changes in leadership styles. The Great Depression of the 1930s, for example, resulted in the creation of the New Deal in the US and policies that led to the social democracies of Europe. After World War II, the rapid growth of science and technology in the US, Japan and Europe launched new industries that demanded new styles of management and organization. In the UK, the recession of the late 1970s and early 1980s paved the way for the restructuring of many manufacturing industries, the creation of more flexible labor and capital markets, and eventually, the privatization of state-owned businesses. Corporate leadership styles mirrored these shifts. For instance, the autocratic bosses of the 1950s and 1960s who commanded hordes of “organization men” gradually gave way to the consensus-building managers of the 1980s and the easy-going dot-com leaders of the 1990s.

**Demographics.** The numbers speak for themselves. The latest statistics from the United Nations show that the population is aging in much of the Americas, Europe and Asia. At the same time, the numbers of children and young people have hit an
all-time high in developing economies. In the US, people entering the workforce are significantly younger, more ethnically diverse and (or) foreign-born; by 2016, 68% of new entrants into the US civilian labor force will be women or people of color. These demographic upheavals will have a significant impact on workforce hiring and management and the way that we all approach our customers and clients.

Globalization. The global financial landscape is beginning to shift as emerging-market countries undergo a period of rapid expansion. Since 1990, cross-border capital flows have grown at a compound annual rate of 14.2% (up from 8% in the prior 10 years), and have reached their highest levels ever. The United Nations Conference on Trade and Development reports that in 2008, US investments overseas dropped 18% and those from the European Union plunged 30%. By contrast, emerging economies increased their foreign direct investment – in the case of China and India, by a hefty 30% in 2008. Geographic and economic barriers are crumbling everywhere, exposing formerly insular nations to new cultures, new opportunities and new challenges. Competition comes from unexpected quarters and collaboration spans borders and time zones. In the “flat” world of the 21st century, the traditional view of diversity through the lens of gender or race is too narrow – as is the old view of leadership.

The innovation imperative. The connection between innovation and economic growth is a time-honored one. Beginning with the work of the Nobel Prize-winning Economist Robert Solow in the 1950s and culminating in modern Keynesian and supply-side theories, economic models generally view innovation as a key factor in economic success. History teaches us that even the deepest economic downturns afford opportunities to innovate: DuPont, Hewlett-Packard (HP), Polaroid and RCA discovered or developed major new technologies during the Depression years and beyond. The ability to repeat this performance in troubled times depends on how effectively business leaders can develop a global mindset and harness diverse perspectives to drive innovation.
Globalization is the buzzword of the 21st century, but what does it mean in practical terms? Ernst & Young explored that question in a recent report – *Redrawing the map: globalization and the changing world of business* – based on a survey that the Economist Intelligence Unit (EIU) conducted for us.

Our research defined globalization as the level of a country’s integration with the world economy through the exchange of goods and services, movement of capital and finance, movement of labor, exchange of technology and ideas, and cultural integration. Using statistical data, the EIU developed a globalization index that measured the performance of the world’s 60 largest countries on 20 separate indicators of cross-border integration. In addition, 520 senior business executives were surveyed worldwide, and 30 respondents were interviewed in depth.

One of our key findings was that most companies fall short on the diversity of thought and culture needed to handle global business. Nearly 40% of the businesses surveyed obtain more than half their total revenues from global markets; in three years’ time, 54% of respondents expect to do so. But boards of directors seldom reflect the global reach of their businesses. Almost half of the companies operating in 25 or more countries admitted that they had at most only a couple of foreign nationals on their boards. Yet they cited globally experienced staff as the leading cultural factor in conducting business around the world.

“The most important thing is diversity of thinking,” pointed out Ahmet Bozer, President of the Eurasia and Africa Group, Coca-Cola Company. That means having executives who understand both emerging and developed markets. “You have to operate at a different level where you can deal with the full range of business opportunities and issues.”

Managing those issues will require agility and a spectrum of viewpoints. Our survey shows that although globalization reversed briefly during the financial crisis, it will resume as the world’s economies recover. Governments and regulators will play a dominant role in pushing for integration. “Our globalized world demands greater global coordination and consistency in corporate governance, accounting and auditing standards,” says Beth Brooke, Global Vice Chair, Ernst & Young. “Achieving that goal would make it easier for the business and investment community. It would also improve the quality of decision-making upon which we all rely.”

In the post-crisis world, companies will still expand geographically, but will rebalance local and global strategies while innovating. Emerging-market firms will profoundly alter the business outlook as they ramp up the pace of domestic growth and branch out into developed markets. In this context, a lack of diversity of thinking and experience at the senior management level could leave firms behind as they race to compete.

Which of the following factors do you expect to be the most important issues over the next year when trading goods internationally in developed markets? (% of respondents)

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<th>Factor</th>
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<tr>
<td>Extent of tariffs, quotas or other formal trade barriers</td>
<td>30%</td>
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<td>Currency volatility</td>
<td>40%</td>
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<td>Cost of goods being sourced</td>
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<td>Shipping costs</td>
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<td>Degree of customer clearance bureaucracy</td>
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<td>Import licensing requirements</td>
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<td>Quality of border infrastructure, such as ports, airports, roads and rail</td>
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Roughly what proportion of senior management located either at your company’s headquarters or where you are currently based are nationals of another country? (% of respondents)

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<td>Below 5%</td>
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<td>5-14.9%</td>
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Uniformity is the enemy of the new leadership

Creativity goes hand in hand with uncertainty. Diversity brings leadership challenges. How can organizations compete and innovate in this environment? James Turley, Global Chairman and CEO, Ernst & Young, discussed that question with journalist and political commentator Fareed Zakaria, Editor of Newsweek International; author of several books, including, most recently, The Post-American World; and host of CNN's Fareed Zakaria GPS.

James Turley: In The Post-American World, you say that globalization has led people worldwide to put their own spin on modern culture, resulting in “an efflorescence of the local and the modern.” Do you see this as evidence that diversity of life experience promotes newness and growth?

Fareed Zakaria: In the first phase of globalization, modernity was defined by American brands. Now we’re in a second phase of globalization, where countries are more comfortable seeing themselves as modern. They are searching within themselves for expressions of modernity by combining local tastes and preferences, and this interaction between the local and global versions of modernity is going to produce new products, new trends, new fashions. You’ll see Bollywood influence Hollywood as much as vice versa. Movies in China will start having an impact on global culture; music and dance in Brazil will have an impact as well. They will offer competing visions of modernity. But competition produces fusion, which means great new energy.

James Turley: To what extent does diversity of thinking serve as a source of innovative ideas that can help countries gain or keep a strategic advantage?

Fareed Zakaria: Diversity is the crucial source of ideas. I’m on the governing board at Yale University, and we observe that the most interesting research happening right now is taking place at the intersection of different fields: biology and engineering, engineering and chemistry, etc. People in these fields have diverse training, viewpoints and skills, and it’s making them think, “Wait a minute, if we can use an engineering technique to design a molecule just so, maybe it will have some biological application.” That’s where the future of science is moving.

The question is how you leverage diversity. We separated science into these disparate buckets, and now we’re trying to reunite these separated disciplines to create new and
innovative ways of looking at the world. What’s key is the ability to do something with diversity – to turn it into innovation and insight.

James Turley: You say in your book that “America’s edge in innovation is overwhelmingly a product of immigration.” What can we do to help educational and immigration policies generate innovative ideas?

Fareed Zakaria: America greatly benefits from having a diverse educational system. Everyone competes all the time: for research grants, for top students, for the best professors. This competitive environment, in turn, exposes us to different ways of doing things. In education, uniformity is the enemy of innovation.

As for immigration, the US has the dynamism it does because each year it welcomes roughly one million legal immigrants from all over the world. These are people from different backgrounds and ethnicities and nationalities, and they’re learning how to work together. Immigrants stretch themselves. Say you’re an immigrant from Vietnam studying mechanical engineering in the US. You have to find a way to keep in your head both the village you came from and the engineering department at UCLA. That forces you to be more inventive and productive. I remember this, being an immigrant myself: I had to stretch myself by embracing two cultures and two ways of looking at the world. It’s incredibly difficult but powerful, and it’s why immigrants do so well at start-up businesses; they have to be comfortable with newness, innovation and uncertainty. Being comfortable with uncertainty is a key to success in life. When you settle for certainty, you’re settling for some lower-performance outcome that gives you stability.

James Turley: China is a huge engine of economic growth, but how might it benefit from a broader spectrum of ideas to drive innovation?

Fareed Zakaria: China has enormous regional diversity, and could easily take advantage of that. I think China has done an extraordinary job marshalling resources and human capital, but largely it has executed ideas that were developed elsewhere. China is far ahead of India in terms of growth, but if you think of global brands, you think of Infosys, Wipro, Tata – Indian companies. For China, you scratch your head and come up with Lenovo – partly because they bought ThinkPad from IBM – and maybe Haier. China’s economy is three times as large as India’s, but it has not been able to get the entrepreneurial part of it moving at the same speed. It will have to embrace and encourage diversity rather than try to create uniformity. The question is whether, with China’s emphasis on social stability, it can live with the disorder that diversity can sometimes produce.

James Turley: In The Post-American World, you talk about the shortcomings of some political systems. To be competitive in producing innovative ideas, you argue that we must address these failings. How?

Fareed Zakaria: The crucial disease of democracy is that decision-makers have difficulty imposing short-term pain in exchange for long-term gain. No one wants to be unpopular. Governments may need to enact structural reforms, but it will mean union protests and a difficult political year or two. You’d get an employment boost eventually, but the the long-term payoff is not what gets anyone elected. That is the core problem for democracy. It’s also a problem for CEOs: how to pursue a strategy regardless of the effect on your quarterly stock price. You’re really trying to create incentives for leadership to take the long view.

James Turley: So what’s the answer?

Fareed Zakaria: For various reasons, most elections take place on the margins. If you could create incentives to focus on the middle, that would be great. A lot of it has to do with leadership. One definition of leadership is an ability not to be distracted or dazzled by short-term popularity, and to push for long-term objectives. Call it the Warren Buffett approach to managing a company, pushing for long-term value rather than trying to pump up the stock price every quarter.

James Turley: What should CEOs choose to focus on to encourage innovation and new ideas?

Fareed Zakaria: The first thing is to ask, “What is the central way in which this company will stay competitive in the future?” Focus on your core competency. Also, ask, “How do I get there in 5 to 10 years?” Don’t look at the next quarter; that pushes you toward financial engineering and public relations. The transformational stuff is going to take time. You’ve got to set out that long-term goal and make it happen. “To govern is to choose” means you have to get rid of a bunch of stuff you’re doing, or de-emphasize it. Now, in a corporate environment, you can say, “This is what’s working; here’s where I’m doubling down.”

James Turley: How do we do this on a global level?

Fareed Zakaria: Companies must embrace diversity and recognize that there are lots of markets, business models and types of human capital out there. So many companies now are getting 50% and 60% of their top-line growth from “the rest of the world.” But of the top 20 people in the company, how many come from the rest of the world? Maybe two or three. On the board? One, maybe. That tells you that they haven’t truly embraced diversity, that they’re not yet global companies. The next phase has got to be to turn into truly global companies, drawing strength from diverse origins, viewpoints and markets.
Leaving the comfort zone

Talk to any global leader involved with diversity initiatives, and the subject of creative tension inevitably comes up. Billie Williamson, Americas Inclusiveness Officer, Ernst & Young, spoke at length on this subject with Haila Wang, CEO of France Telecom R&D Beijing and a champion of the role of diversity in innovation.

Billie Williamson: What role does innovation play at France Telecom?
Haila Wang: We’re very focused on innovation. Among the world’s mobile operators, we have one of the biggest research centers. Our focus is on convergence services, mobile multimedia and other areas. We have a large research and development (R&D) budget and about 4,000 R&D staff in China. Initially, our research operations were very focused on France. Ten years ago, there were few overseas operations. Today, it’s different: more than half of our global revenue comes from outside of France, and our research centers are located all over the world. We think that R&D and innovation will not necessarily come from a single place. Our strategy is open innovation, and that will come from many places.

Billie Williamson: Does the company deliberately try to create diverse teams to spur innovation?
Haila Wang: Yes. We see innovation as a global process, so we have people working on projects from different countries. Diversity comes naturally when you work this way: people who participate in the projects have different views and different backgrounds. In the corporate headquarters, they regard diversity as very important, so we have a talent-sharing program that rotates people to different countries. It’s a good way to enrich the team because we can get different views from diverse areas of the world.

Also, we split our advanced R&D into about 30 different segments. One segment, called research object terminals, is located at our Beijing lab. All terminal-related research worldwide is managed and approved there. Placing different research segments in locations around the world is a good way of ensuring that we get diverse perspectives on our R&D efforts.

Billie Williamson: What must corporate leaders do to move companies toward greater diversity and the innovation it can help generate?
Haila Wang: Innovation is different for big companies than for small ones. In big companies, most new ideas are killed before they get off the ground, but the ones that survive are more likely to have a big impact because they have the resources of a big firm behind them. Leaders at large companies must therefore select the right innovations. Small companies, although they can generate many ideas, have limited resources, so their innovative ideas are usually killed, not by the company itself, but by the market. It’s not that leadership is less important at small companies, but that they will be led to innovation in a more natural way.

Billie Williamson: How does diversity affect innovation?
Haila Wang: For us, it’s obvious, because we’re in China and our target market is Europe. Every day we are confronted with the diversity issue, in that sometimes we have difficulty convincing people who aren’t in China of our value proposition. Sometimes people can’t see what’s happening outside of their own country – they don’t realize there are other ways of thinking, other business models. People need to be taught to embrace diversity, to develop their capacity to accept change and to understand others who are different from them. So it’s important, through this combination of different perspectives, to push different teams – and sometimes to push ourselves – into an uneasy position. In other words, if we’re always comfortable, there is no innovation.
Supporting diversity isn’t only good citizenship — it’s also good economics. Both Keynesian and supply-side economists agree, for example, that greater productivity leads to more innovation, which fuels growth in the economy. Innovation, in turn, is often the result of diversity.

“There is a positive correlation between diversity and innovation,” says Dr. Farrokh Langdana, Professor of Finance and Economics at Rutgers University in New Jersey. One way to get started on innovation, he believes, is for company leaders to focus on promoting diverse thinking, using personality tests to evaluate employees for such traits as creativity and risk tolerance. Those whose test scores show innovative or entrepreneurial tendencies should be paired with those who are practical, deadline-oriented and budget-conscious. Mixing people together in this way would allow companies to create teams with diverse skills and ways of looking at problems, distributing a company’s idea-generation capacity more evenly throughout the organization. And it’s important, Langdana notes, to get the right balance of perspectives. “Pairing visionaries with pragmatists will ensure that we don’t just have 25 superb ideas that never see the light of day,” he says. “It’s better to have two ideas that make it to market.”

The mother of invention

Such methods of spurring innovation may actually be easier to implement during a downturn, in Langdana’s view. “Everyone’s thinking, ‘What can I do to stay employed? What can I do to make sure that my company survives?’ You don’t need too much motivation in a recession.”

To realize their innovative potential, companies should exploit diversity and view it as a strategic advantage. “Diversity is a resource we have to mine,” Langdana says. “We need a more strategic way to create the diversity that can spark innovation. And government can help by eventually reinstating a regulatory climate that fosters innovation. The creative potential is already there; we just have to unleash it.”
Reading between the lines
The new rules of leadership await codification. But sifting through the growing amount of research on the topic, we found that certain themes emerge repeatedly. To be competitive in the global economy, leaders must:

1. Stir the pot: leverage conflict (sparked by differing viewpoints) to generate new ideas
2. Anticipate the Next Big Thing — or better yet, drive the Next Big Thing! Use diverse perspectives to develop new products and services
3. Nurture a spectrum of talent: find talent in unexpected places and forge creative collaborations
4. Get the mindset: focus on transformational leadership

Lesson 1: stir the pot

“Polite” organizations that strive for consensus and send the cowboys to classes to squash personal conflict are due for a management rethink.

Researchers are increasingly finding the opposite: that open clashes of ideas boost a company’s energy and creativity. “Most leadership experts argue that the best way to manage change is to create alignment, but our research indicates that for large-scale change or innovation initiatives, a healthy dose of dissent is usually just as important,” say the authors of a recent article in the *Harvard Business Review* (“How to Pick a Good Fight,” December 2009). In fact, they add, “a peaceful, harmonious workplace can be the worst possible thing for a business” because it leads to complacency, the biggest predictor of poor company performance.

Other research bears out the healthy-conflict theory:

- Diversity can improve an organization’s performance by enhancing creativity or team problem-solving. By “stirring the pot” in positive ways, diversity encourages the intellectual debate and conflict that lead to innovation (Cornell University, Stanford University).
- In a study of 28 teams, heterogeneous teams solved complex tasks better than homogeneous teams. The diverse teams exhibited a higher level of creativity and a broader thought process (Henley Management College, UK; Ford Germany).
- Heterogeneous groups produced more creative results and communicated better than homogeneous groups in a study of 15 groups (Tilburg University and I-NET Internet Services, The Netherlands).
It’s no coincidence that effective leaders look to diverse perspectives – and the conflict they may spark – to produce exceptionally creative thinking that may not occur otherwise. Nancy J. Adler, a scholar of organizational behavior and one of the world’s leading researchers on cultural diversity, cites the example of a Swedish pharmaceutical firm that benefited from intercultural conflict. Adler quotes a company executive as saying: “We traditionally carried out product design at our Stockholm headquarters. Once, by accident or design, we brought in an international team to discuss the design of a new allergy product. Due to extreme differences in opinion on what constitutes good medical practice, the team designed the new product with maximum flexibility to suit the requirements of each country. We later discovered that the greater flexibility was a huge advantage in developing and marketing a wide range of internationally competitive products” (International Dimensions of Organizational Behavior, 5th edition, 2008).

Adler goes on to emphasize that creative thinking is what diverse teams do best. “Cultural diversity provides the biggest potential benefit to teams with challenging tasks that require creativity and innovation,” she observes.

Lesson 2: anticipate the Next Big Thing – or better yet, drive the Next Big Thing!

The idea that diversity propels innovation has been proven time and again in cross-cultural research. In particular, the work of Scott Page, Professor of Complex Systems at the University of Michigan at Ann Arbor, shows that diverse groups tend to outperform homogeneous groups, even if the members of the latter group are more capable. Furthermore, diversity fires up innovation. According to Page, “innovation provides the seeds for economic growth, and for that innovation to happen depends as much on collective difference as on aggregate ability.

If people think alike, then no matter how smart they are, they most likely will get stuck at the same locally optimal solutions. Finding new and better solutions, innovating, requires thinking differently. That’s why diversity powers innovation.”

It is critical to note here that Page is talking about diversity in its broadest sense – as a collection of different viewpoints. Research across a variety of countries and multinational companies has shown that diverse teams generate ideas that result in better products and services. For example:

- In a study conducted in Germany, higher levels of innovation and R&D correlated with higher levels of cultural diversity (German Federal Employment Agency, 2006).
- In a study of 45 teams from five high-tech firms in the US, teams composed of people with different functional specialties worked more effectively with other internal teams and showed a
higher product innovation rate (Research Technology Management, 1990).

Where innovation is critical, companies should construct teams with equal proportions of men and women so that they can benefit from the most diverse talent pool (London Business School).

Some of the most successful companies of our time were founded on the power of diverse viewpoints – and have used them to drive far-reaching innovations. The story of Microsoft is one of inclusive, no-holds-barred striving not to create, but to be, the Next Big Thing. Since 1981, when Nokia pioneered car phones, it has been at the forefront of telecom innovation; to develop the next generation of mobile devices, the company actively seeks input from numerous sources, including consumers, its own business units and external collaborators. Diversity of ideas and talent is also the thinking behind “open innovation,” a term coined in 2003 by Professor Henry Chesbrough of the University of California-Berkeley. Companies that embrace open innovation look outside the boundaries of their own organizations to gain access to the best knowledge, ideas and technology. Today, the idea has broadened to include collaboration across borders, functions and even industries.

A report from the innovation research and advisory firm Nerac notes that “open innovation is giving way to open business models, where all phases of the innovation lifecycle are subject to external thinking” (Open Innovation: Facts, Fiction, and Future, September 2008). That’s precisely what Philips had in mind when it opened up its internal R&D campus in Eindhoven, The Netherlands, to other companies—including IBM, ASML and NXP—and their R&D groups, with whom Philips collaborates and shares ideas. Another champion of open innovation, Procter & Gamble (P&G), has pushed the concept even further. On its Connect + Develop website, it invites submissions for innovations from everyone, including individuals, companies, universities, government labs and other organizations. P&G looks for new ideas in all aspects of its business, from trademarks to package design to engineering. Recently, the company bought the technology for an antimicrobial product from an unknown company that had submitted an unsolicited proposal through the website.

Lesson 3: nurture a spectrum of talent

While new and improved products and services will matter, the biggest corporate battle of the next decade will be fought over talent. When McKinsey & Company updated its famous 1997 study, The War for Talent, in 1997 and 2001, the firm found that almost nothing had changed in a decade. Companies remained just as unprepared to find and retain capable talent as they had been 10 years earlier. What’s more, they expected the competition for talent to continue to be the most important global challenge over the next decade.
Reading between the lines
Smart leaders cannot afford to ignore this problem. Being open to new opportunities and perspectives, and taking advantage of the flexibility that a diverse talent pool offers, are key ways to address the skills shortage. Women, in particular, are coming into their own as an economic force. (We address this issue in detail in other Ernst & Young special reports, Groundbreakers and Scaling up, ey.com/groundbreakers, ey.com/scalingup.) Although they own about 30% of all private businesses and account for 40% of the labor force globally, women lag behind men on such measures as educational attainment, wages, political empowerment and economic participation, especially in developing countries. Yet research shows a significant statistical correlation between gender equality and countries’ economic development. In addition, studies reveal a strong positive link between corporate financial performance and the presence of women in senior management. Two of note are:

1. A study of 101 large corporations showed that companies with three or more women in senior management functions scored higher than companies with no women at the top on nine criteria of organizational excellence, including key factors such as leadership, accountability and innovation (McKinsey & Company).

2. Among Fortune 500 companies, firms with the highest representation of women board directors outperformed those with the lowest, as measured by return on invested capital, return on equity and return on sales (at 66%, 53% and 42%, respectively) (Catalyst).

On the upside, while it is still slow to take root, the trend toward diversity in senior management has been gaining steam. Several companies in the Fortune 100 now have foreign-born CEOs: examples include PepsiCo’s Indra Nooyi (India), Alcoa’s Alain Belda (Brazil), Altria Group’s Louis Camilleri (Egypt), Hartford Financial Services Group’s Raman Ayer (India), Citigroup’s Vikram Pandit (India) and Coca-Cola’s Muhtar Kent (Turkey). The executive pipeline will continue to become more international as many MBA programs now fill their classes with more foreign students (BusinessWeek’s top 10 MBA programs average 38% international students) and more companies recruit worldwide.

Lesson 4: get the mindset

Languages have regional differences and dialects. The new language of leadership is no exception. Speaking it fluently involves understanding subtleties, nuances and variations, and realizing that standard “diversity training” is no longer sufficient for senior leaders. Rather, our goal should be to develop mindsets and habits for leading inclusively. The work of Mahzarin Banaji, a Harvard University psychology professor and a leading researcher of implicit prejudices, helps lay the foundation for building transformational leadership capabilities. Banaji and her colleague, Anthony Greenwald, are best known for developing the Implicit Association Test (IAT), which reveals biases and attitudes that people may not be consciously aware of and may even contradict in their explicit behavior. The IAT is a flexible task that tests people’s automatic associations between concepts (e.g., math, arts) and attributes (e.g., good or bad, male or female). “The test is unusual in that it provokes a reaction of surprise, even astonishment,” says Banaji. “It is a tool to understand what goes on invisibly in our minds, but it is also a catalyst for insight.”
Increasingly, dynamic leaders are recognizing that insight means understanding differences, not denying their existence. In fact, “cultural blindness” – choosing not to see cultural differences or downplaying their impact – can limit our ability to benefit from diversity, points out organizational psychologist Nancy Adler. Cultural blindness “precludes our ability to minimize the problems caused by cultural diversity and to maximize the potential advantages it offers,” she writes. “To effectively manage cross-culturally, a concentrated effort must be made to recognize cultural diversity without judging it – to see difference where difference exists” (International Dimensions of Organizational Behavior, 5th edition, 2008).

This perception forms the basis for developing a corporate culture based on inclusion and a mindset of encouraging diverse viewpoints. “Behavior needs to change before we can change the results,” says Adam Travis, head of diversity and inclusion at global mobile communications provider Nokia. “How you bridge and approach the subject of diversity needs to be done in a careful way, not a confrontational way. It should be heavily linked to the business agenda.” That agenda includes measuring the effects of diversity: one of the key challenges for organizations is drawing correlations between diversity programs and innovation, productivity and business outcomes. There’s no question that direct cause-and-effect relationships are hard to prove. But the most persuasive argument in favor of diversity is that in practice, it works. Leading global companies have shown that innovative products, services and business models – as well as visible benefits to the bottom line – result from leveraging diverse perspectives. For example:

- Led by its visionary then-CEO Patrick Cescau, in 2005, consumer products company Unilever transformed its historically Anglo-Dutch leadership to foster innovation and growth. Twenty nationalities are now represented among the top 100 managers. In 2008, the company had its fourth successive year of accelerating sales growth.

- PepsiCo attributes one percentage point of its 7.4% revenue growth, or about US$250 million, to new products inspired by diversity efforts.

- At its facilities in India, Google has hired 1,100 employees who come from a spectrum of religious backgrounds and speak several Indian languages in addition to English. This diversity has resulted in Google Finance, Google’s first innovation born in a foreign R&D center.

- Siemens AG has made diversity a key component of its company strategy. The company employs people from more than 140 countries and promotes cross-generational dialogue between experienced and younger employees. Also in place is a network designed to link and leverage talents from emerging markets.

- HP developed its new Latex Printing Technology through teams consisting of 120 engineers working together in four countries. The firm believes that this diversity was critical to the project’s success.

- The Bank of Nova Scotia began an Advancement of Women program in 2003. Managers were made responsible for identifying women with leadership potential; meeting that goal was a factor in compensation. Since the program began, the proportion of women in senior management has jumped from 19% in 2003 to 31% in 2008, and return on equity has risen from 16.6% to 22.1%.

“Behavior needs to change before we can change the results.”

Adam Travis, head of diversity and inclusion, Nokia
Behavior needs to change before we can change the results.”

Adam Travis, head of diversity and inclusion, Nokia
Toward a “third culture”

It’s great to be able to speak Spanish or French, but in a global world, business leaders must learn a new language: intercultural competency. Pierre Hurstel, Global Leader, Diversity and Inclusiveness, Ernst & Young, France, discussed how leaders can develop this competency with Milton Bennett, Ph.D., a leading authority in the field who designs training programs to develop intercultural skills for global corporations in the US, Asia and Europe. Bennett is on the executive training faculty of the Tuck School of Business at Dartmouth (US) and the Stockholm School of Economics, and serves as Director of the Intercultural Development Research Institute.

**Pierre Hurstel:** What does intercultural competency involve?

**Milton Bennett:** In this context, culture means the worldview you acquire when you belong to a certain group. This is distinct from your individual personality, because others in the group share elements of this worldview. Intercultural refers to the interface between individuals from different cultures. Communication is the process of creating shared meaning for people, despite their different ways of seeing the world.

**Pierre Hurstel:** Some executives remain skeptical about the value of diversity in a business context. What’s your response?

**Milton Bennett:** People from different cultures often have trouble communicating in the workplace. This miscommunication has a cost that’s borne by the enterprise; improved intercultural communication can reduce it. Diversity can also lead to new perspectives, and possibly to innovative products and services, and companies definitely want that. Sophisticated companies – those who aren’t just checking a box, or being politically correct – want to improve the performance of their multicultural teams.

**Pierre Hurstel:** This would seem to be particularly relevant to companies involved in cross-border acquisitions.

**Milton Bennett:** Yes. When mergers fail to produce their intended benefits, it’s generally because of cultural reasons: the acquiring organization seeks to subsume the perspective of the target, and as a result they lose it.

**Pierre Hurstel:** Leadership is about action, and your work offers a model of what leaders must do to get the benefits of diversity. What are the steps?

**Milton Bennett:** To gain the value of diversity, you need a program of training and coaching aimed at acquiring the benefits of diversity, rather than avoiding its difficulties. There are three main aspects to this programming:

1. **Dealing with the issues of cultural identity.** Diversity initiatives must help people understand how certain culturally determined worldviews may play out at work. Basically, this allows them to generalize about people who are different from them, without lapsing into stereotypes.

2. **Interaction analysis.** This has to do with predicting misunderstandings that might arise in cross-cultural situations. For example, an American at a meeting might want to start discussing business immediately, while a European would find this too abrupt. This analysis also can help you spot areas where the different sides have complementary skills or talents.
3. Developing competence at intercultural communication. There’s a model of intercultural sensitivity that maps a sequence of stages people move through – from more ethnocentric positions to more “ethno-relative” ones. On the way, people become more sophisticated in their ability to experience cultural difference.

Pierre Hurstel: Some of those ideas seem focused on helping people see their own blind spots.

Milton Bennett: The programming must help people understand some of their own unconscious biases. These can be subtle and well-intentioned. For example, Americans often say, “We should treat everyone as individuals.” It sounds reasonable enough – especially to an American. But in fact it’s a culturally biased approach in that it places special value on individualism. Not all cultures do.

Pierre Hurstel: Are there any unintended consequences or possible negative side effects of diversity initiatives?

Milton Bennett: Yes, they can actually exacerbate a business situation rather than improve it: by leading to stereotyping, for example. The implied promise of an affirmative action program or a recruitment initiative is that I’m being hired because I have a unique perspective, not because my prospective employer has to check off a box on some form. Handled badly, or without adequate support from top leadership, diversity programs can create disaffected workers who don’t consider the company to be “the employer of choice” – and who may not stick around for long.

Pierre Hurstel: Your work talks about forming a third culture. What does this refer to?

Milton Bennett: It’s a kind of virtual space that opens up in any intercultural communication between two or more people, where one is trying to adapt to the other. Members of the non-dominant group usually adapt to the dominant one. But when the dominant group tries to adapt, you get a third culture – one that isn’t a hybrid but a distinct culture in its own right. Groups that develop a third culture are more likely to generate a “third solution” – not the one either would have reached on its own. That’s where you find the true value to the organization, whether it takes the form of innovation, enhanced problem-solving or some other improved outcome. The organization gets this value not just from being in contact with others who are different, but from undergoing a process that makes its people more interculturally competent.

“To gain the value of diversity, you need a program of training and coaching aimed at acquiring the benefits of diversity, rather than avoiding its difficulties.”

Milton Bennett, Ph.D.
The last word: cracking the code
We're conditioned to think of action as a surefire way to succeed at anything. To quickly learn a language, you immerse yourself in it. To run or swim faster, you “just do it,” as the famous Nike slogan goes. But industry watchers warn that diversity is one area where action is not the best place to start. For example, in their book *The Power of Inclusion* (2005), leadership training consultants Michael Hyter and Judith Turnock point out that “many companies launch inclusion and development initiatives with action, never taking the time to understand their real issues and opportunities.” They urge organizations to “begin by assessing the current situation and then move on to defining objectives, identifying improvement opportunities, developing realistic, measurable goals and designing targeted interventions.”

That means stepping back and taking stock of an organization's circumstances. When Schneider Electric began operating in India, it had to implement a broad-based notion of diversity, says local Managing Director Hema Hattangady. “In India, ‘diversity and inclusiveness’ mean so many things because we’re such an eclectic country,” she says. “Gender and educational background are two main components. So is geographic diversity: India has 28 states, and several different religions, all with different dress, food habits and social customs.”

The key to managing such a diverse workforce, she says, is for leaders to keep emphasizing their inclusive mindset and continually articulate the terms of success. “Sometimes people who are not comfortable working with diverse groups swing from being non-inclusive to being patronizing,” she cautions. “Leadership plays a big role in ensuring that the right signals are being sent. Also, if leadership’s enthusiasm fades, people will stop picking up on those signals and they’ll start checking boxes: you know, ‘I’ve got 40% women in my group now, so everything’s fine.’”

Schneider Electric has set KPIs for diversity that every country head must meet as part of the firm’s business objectives. But, Hattangady points out, the transformation must first take place in the mind. “At Schneider India, we try to ‘lead from the front,’ meaning we sit down with senior management and see how comfortable they are with the diversity mandate,” she says. “You can give everyone KPIs, but that by itself may not be enough.
The best leadership style will be both sensitive and willing to sensitize.”

Sensitivity is itself but one step on the road to evolving as an inclusive leader. It must be backed up by a commitment to develop and support a different organizational mindset, willingness to change and the capacity to learn from failure. The new style of leadership also involves meticulously tracking one’s own behavior. “Leaders signal attitudes toward diversity – that is to say, the values of diversity – in a variety of ways,” says psychologist Mahzarin Banaji. “They can embody the values of diversity such that they are expressed in small and consistent ways. It is less about making a speech at an event and more about showing through daily behavior that different perspectives on all topics must be considered. It is about signaling verbally and nonverbally that those who represent less dominant positions within the organization have a voice and will be heard.”
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