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First eBook Edition: November 2010

ISBN: 978-1-4221-3344-6

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Meeting the Challenge of Disruptive Change

by Clayton M. Christensen and Michael Overdorf

THESE ARE SCARY TIMES for managers in big companies. Even before the Internet and globalization, their track record for dealing with major, disruptive change was not good. Out of hundreds of department stores, for example, only one—Dayton Hudson—became a leader in discount retailing. Not one of the minicomputer companies succeeded in the personal computer business. Medical and business schools are struggling—and failing—to change their curricula fast enough to train the types of doctors and managers their markets need. The list could go on.

It's not that managers in big companies can't see disruptive changes coming. Usually they can. Nor do they lack resources to confront them. Most big companies have talented managers and specialists, strong product portfolios, first-rate technological know-how, and deep pockets. What managers lack is a habit of thinking about their organization's capabilities as carefully as they think about individual people's capabilities.

One of the hallmarks of a great manager is the ability to identify the right person for the right job and to train employees to succeed at the jobs they're given. But unfortunately, most managers assume that if each person working on a project is well matched to the job, then the organization in which they work will be, too. Often that is not the case. One could put two sets of identically capable people to work in different organizations, and what they accomplished would be significantly different. That's because organizations themselves—independent of the people and other resources in them—have capabilities. To succeed consistently, good managers need to be skilled not just in assessing people but also in assessing the abilities and disabilities of their organization as a whole.

This article offers managers a framework to help them understand what

their organizations are capable of accomplishing. It will show them how their company's disabilities become more sharply defined even as its core capabilities grow. It will give them a way to recognize different kinds of change and make appropriate organizational responses to the opportunities that arise from each. And it will offer some bottom-line advice that runs counter to much that's assumed in our can-do business culture: if an organization faces major change—a disruptive innovation, perhaps—the worst possible approach may be to make drastic adjustments to the existing organization. In trying to transform an enterprise, managers can destroy the very capabilities that sustain it.

Before rushing into the breach, managers must understand precisely what types of change the existing organization is capable and incapable of handling. To help them do that, we'll first take a systematic look at how to recognize a company's core capabilities on an organizational level and then examine how those capabilities migrate as companies grow and mature.

Where Capabilities Reside

Our research suggests that three factors affect what an organization can and cannot do: its resources, its processes, and its values. When thinking about what sorts of innovations their organization will be able to embrace, managers need to assess how each of these factors might affect their organization's capacity to change.

Idea in Brief

Why do so few established companies innovate successfully? Of hundreds of department stores, for instance, only Dayton Hudson became a discount-retailing leader. And not one minicomputer company succeeded in the personal-computer business.

What's going on? After all, most established firms boast deep pockets and talented people. But when a new venture captures their imagination, they get their people working on it within organizational structures (such as functional teams) designed to surmount *old* challenges—not ones that the new venture is facing.

To avoid this mistake, ask:

- **“Does my organization have the right *resources* to support this innovation?”** Resources supporting business-as-usual—people, technologies, product designs, brands, customer and supplier relationships—rarely match those required for new ventures.
- **“Does my organization have the right *processes* to innovate?”** Processes supporting your established business—decision-making protocols, coordination patterns—may hamstring your new venture.
- **“Does my organization have the right *values* to innovate?”** Consider how you decide whether to commit to a new venture. For example, can you tolerate lower profit margins than your established enterprise demands?
- **“What team and structure will best support our innovation effort?”** Should you use a team dedicated to the project within your company? Create a separate spin-off organization?

By selecting the right team and organizational structure for your innovation—and

infusing it with the right resources, processes, and values—you heighten your chances of innovating successfully.

Idea in Practice

Selecting the Right Structure for Your Innovation			
If your innovation . . .	Select this type of team . . .	To operate . . .	Because . . .
Fits <i>well</i> with your existing values <i>and</i> processes	Functional teams who work sequentially on issues, or lightweight teams —ad hoc cross-functional teams who work simultaneously on multiple issues	Within your existing organization	Owing to the good fit with existing processes and values, no new capabilities or organizational structures are called for.
Fits <i>well</i> with existing values but <i>poorly</i> with existing processes	Heavyweight team dedicated exclusively to the innovation project, with complete responsibility for its success	Within your existing organization	The poor fit with existing processes requires new types of coordination among groups and individuals.
Fits <i>poorly</i> with	Heavyweight team	Within your existing	In-house development

existing values but <i>well</i> with existing processes	dedicated exclusively to the innovation project, with complete responsibility for its success	organization for development, followed by a spin-off for commercialization	capitalizes on existing processes. A spin-off for the commercialization phase facilitates new values—such as a different cost structure with lower profit margins.
Fits <i>poorly</i> with your existing processes <i>and</i> values	Heavyweight team dedicated exclusively to the innovation project, with complete responsibility for its success	In a separate spin-off or acquired organization	A spin-off enables the project to be governed by different values <i>and</i> ensures that new processes emerge.

Resources

When they ask the question, “What can this company do?” the place most managers look for the answer is in its resources—both the tangible ones like people, equipment, technologies, and cash, and the less tangible ones like product designs, information, brands, and relationships with suppliers, distributors, and customers. Without doubt, access to abundant, high-quality resources increases an organization’s chances of coping with change. But resource analysis doesn’t come close to telling the whole story.

Processes

The second factor that affects what a company can and cannot do is its processes. By processes, we mean the patterns of interaction, coordination, communication, and decision making employees use to transform resources into products and services of greater worth. Such examples as the processes that govern product development, manufacturing, and budgeting come immediately to mind. Some processes are formal, in the sense that they are explicitly defined and documented. Others are informal: they are routines or ways of working that evolve over time. The former tend to be more visible, the latter less visible.

One of the dilemmas of management is that processes, by their very nature, are set up so that employees perform tasks in a consistent way, time after time. They are *meant* not to change or, if they must change, to change through tightly controlled procedures. When people use a process to do the task it was designed for, it is likely to perform efficiently. But when the same process is used to tackle a very different task, it is likely to perform sluggishly. Companies focused on developing and winning FDA approval for new drug compounds, for example, often prove inept at developing and winning approval for medical devices because the second task entails very different ways of working. In fact, a process that creates the capability to execute one task concurrently defines disabilities in executing other tasks.¹

The most important capabilities and concurrent disabilities aren't necessarily embodied in the most visible processes, like logistics, development, manufacturing, or customer service. In fact, they are more likely to be in the less visible, background processes that support decisions about where to invest resources—those that define how market research is habitually done, how such analysis is translated into financial projections, how plans and budgets are negotiated internally, and so on. It is in those processes that many organizations' most serious disabilities in coping with change reside.

Values

The third factor that affects what an organization can and cannot do is its values. Sometimes the phrase “corporate values” carries an ethical connotation: one thinks of the principles that ensure patient well-being for Johnson & Johnson or that guide decisions about employee safety at Alcoa. But within our framework, “values” has a broader meaning. We define an organization’s values as the standards by which employees set priorities that enable them to judge whether an order is attractive or unattractive, whether a customer is more important or less important, whether an idea for a new product is attractive or marginal, and so on. Prioritization decisions are made by employees at every level. Among salespeople, they consist of on-the-spot, day-to-day decisions about which products to push with customers and which to de-emphasize. At the executive tiers, they often take the form of decisions to invest, or not, in new products, services, and processes.

The larger and more complex a company becomes, the more important it is for senior managers to train employees throughout the organization to make independent decisions about priorities that are consistent with the strategic direction and the business model of the company. A key metric of good management, in fact, is whether such clear, consistent values have permeated the organization.

But consistent, broadly understood values also define what an organization cannot do. A company’s values reflect its cost structure or its business model because those define the rules its employees must follow for the company to prosper. If, for example, a company’s overhead costs require it to achieve gross profit margins of 40%, then a value or decision rule will have evolved that encourages middle managers to kill ideas that promise gross margins below 40%. Such an organization would be incapable of commercializing projects targeting low-margin markets—such as those in e-commerce—even though another organization’s values, driven by a very different cost structure, might facilitate the success of the same project.

Different companies, of course, embody different values. But we want to focus on two sets of values in particular that tend to evolve in most companies in very predictable ways. The inexorable evolution of these two values is what makes companies progressively less capable of addressing

disruptive change successfully.

As in the previous example, the first value dictates the way the company judges acceptable gross margins. As companies add features and functions to their products and services, trying to capture more attractive customers in premium tiers of their markets, they often add overhead cost. As a result, gross margins that were once attractive become unattractive. For instance, Toyota entered the North American market with the Corona model, which targeted the lower end of the market. As that segment became crowded with look-alike models from Honda, Mazda, and Nissan, competition drove down profit margins. To improve its margins, Toyota then developed more sophisticated cars targeted at higher tiers. The process of developing cars like the Camry and the Lexus added costs to Toyota's operation. It subsequently decided to exit the lower end of the market; the margins had become unacceptable because the company's cost structure, and consequently its values, had changed.

In a departure from that pattern, Toyota recently introduced the Echo model, hoping to rejoin the entry-level tier with a \$10,000 car. It is one thing for Toyota's senior management to decide to launch this new model. It's another for the many people in the Toyota system—including its dealers—to agree that selling more cars at lower margins is a better way to boost profits and equity values than selling more Camrys, Avalons, and Lexuses. Only time will tell whether Toyota can manage this down-market move. To be successful with the Echo, Toyota's management will have to swim against a very strong current—the current of its own corporate values.

The second value relates to how big a business opportunity has to be before it can be interesting. Because a company's stock price represents the discounted present value of its projected earnings stream, most managers feel compelled not just to maintain growth but to maintain a constant rate of growth. For a \$40 million company to grow 25%, for instance, it needs to find \$10 million in new business the next year. But a \$40 billion company needs to find \$10 billion in new business the next year to grow at that same rate. It follows that an opportunity that excites a small company isn't big enough to be interesting to a large company. One of the bittersweet results of success, in fact, is that as companies become large, they lose the ability to enter small, emerging markets. This disability is not caused by a change in the resources within the companies—their resources typically are vast. Rather, it's caused by an evolution in values.

The problem is magnified when companies suddenly become much bigger through mergers or acquisitions. Executives and Wall Street financiers who engineer megamergers between already-huge pharmaceutical companies, for example, need to take this effect into account. Although their merged research organizations might have more resources to throw at new product development, their commercial organizations will probably have lost their appetites for all but the biggest blockbuster drugs. This constitutes a very real disability in managing innovation. The same problem crops up in high-tech industries as well. In many ways, Hewlett-Packard's recent decision to split itself into two companies is rooted in its recognition of this problem.

The Migration of Capabilities

In the start-up stages of an organization, much of what gets done is attributable to resources—people, in particular. The addition or departure of a few key people can profoundly influence its success. Over time, however, the locus of the organization's capabilities shifts toward its processes and values. As people address recurrent tasks, processes become defined. And as the business model takes shape and it becomes clear which types of business need to be accorded highest priority, values coalesce. In fact, one reason that many soaring young companies flame out after an IPO based on a single hot product is that their initial success is grounded in resources—often the founding engineers—and they fail to develop processes that can create a sequence of hot products.

Avid Technology, a producer of digital-editing systems for television, is an apt case in point. Avid's well-received technology removed tedium from the video-editing process. On the back of its star product, Avid's stock rose from \$16 a share at its 1993 IPO to \$49 in mid-1995. However, the strains of being a one-trick pony soon emerged as Avid faced a saturated market, rising inventories and receivables, increased competition, and shareholder lawsuits. Customers loved the product, but Avid's lack of effective processes for consistently developing new products and for controlling quality, delivery, and service ultimately tripped the company and sent its stock back down.

By contrast, at highly successful firms such as McKinsey & Company, the processes and values have become so powerful that it almost doesn't matter which people get assigned to which project teams. Hundreds of MBAs join the firm every year, and almost as many leave. But the company is able to crank out high-quality work year after year because its core capabilities are rooted in its processes and values rather than in its resources.

When a company's processes and values are being formed in its early and middle years, the founder typically has a profound impact. The founder usually has strong opinions about how employees should do their work and what the organization's priorities need to be. If the founder's judgments are flawed, of course, the company will likely fail. But if they're sound, employees will experience for themselves the validity of the founder's

problem-solving and decision-making methods. Thus processes become defined. Likewise, if the company becomes financially successful by allocating resources according to criteria that reflect the founder's priorities, the company's values coalesce around those criteria.

As successful companies mature, employees gradually come to assume that the processes and priorities they've used so successfully so often are the right way to do their work. Once that happens and employees begin to follow processes and decide priorities by assumption rather than by conscious choice, those processes and values come to constitute the organization's culture.² As companies grow from a few employees to hundreds and thousands of them, the challenge of getting all employees to agree on what needs to be done and how can be daunting for even the best managers. Culture is a powerful management tool in those situations. It enables employees to act autonomously but causes them to act consistently.

Digital's Dilemma

A LOT OF BUSINESS THINKERS have analyzed Digital Equipment Corporation's abrupt fall from grace. Most have concluded that Digital simply read the market very badly. But if we look at the company's fate through the lens of our framework, a different picture emerges.

Digital was a spectacularly successful maker of minicomputers from the 1960s through the 1980s. One might have been tempted to assert, when personal computers first appeared in the market around 1980, that Digital's core capability was in building computers. But if that were the case, why did the company stumble?

Clearly, Digital had the resources to succeed in personal computers. Its engineers routinely designed computers that were far more sophisticated than PCs. The company had plenty of cash, a great brand, good technology, and so on. But it did not have the processes to succeed in the personal computer business. Minicomputer companies designed most of the key components of their computers internally and then integrated those components into proprietary configurations. Designing a new product platform took two to three years. Digital manufactured most of its own components and assembled them in a batch mode. It sold directly to corporate engineering organizations. Those processes worked extremely well in the minicomputer business.

PC makers, by contrast, outsourced most components from the best suppliers around the globe. New computer designs, made up of modular components, had to be completed in six to 12 months. The computers were manufactured in high-volume assembly lines and sold through retailers to consumers and businesses. None of these processes existed within Digital. In other words, although the people working at the

company had the ability to design, build, and sell personal computers profitably, they were working in an organization that was incapable of doing so because its processes had been designed and had evolved to do other tasks well.

Similarly, because of its overhead costs, Digital had to adopt a set of values that dictated, “If it generates 50% gross margins or more, it’s good business. If it generates less than 40% margins, it’s not worth doing.” Management had to ensure that all employees gave priority to projects according to these criteria or the company couldn’t make money. Because PCs generated lower margins, they did not fit with Digital’s values. The company’s criteria for setting priorities always placed higher-performance minicomputers ahead of personal computers in the resource-allocation process.

Digital could have created a different organization that would have honed the different processes and values required to succeed in PCs—as IBM did. But Digital’s mainstream organization simply was incapable of succeeding at the job.

Hence, the factors that define an organization’s capabilities and disabilities evolve over time—they start in resources; then move to visible, articulated processes and values; and migrate finally to culture. As long as the organization continues to face the same sorts of problems that its processes and values were designed to address, managing the organization can be straightforward. But because those factors also define what an organization cannot do, they constitute disabilities when the problems facing the company change fundamentally. When the organization’s capabilities reside primarily in its people, changing capabilities to address the new problems is relatively simple. But when the capabilities have come to reside in processes and values, and especially when they have become embedded in culture, change can be extraordinarily difficult. (See the sidebar “Digital’s Dilemma.”)

Sustaining Versus Disruptive Innovation

Successful companies, no matter what the source of their capabilities, are pretty good at responding to evolutionary changes in their markets—what in *The Innovator's Dilemma* (Harvard Business School, 1997), Clayton Christensen referred to as *sustaining innovation*. Where they run into trouble is in handling or initiating revolutionary changes in their markets, or dealing with *disruptive innovation*.

Sustaining technologies are innovations that make a product or service perform better in ways that customers in the mainstream market already value. Compaq's early adoption of Intel's 32-bit 386 microprocessor instead of the 16-bit 286 chip was a sustaining innovation. So was Merrill Lynch's introduction of its Cash Management Account, which allowed customers to write checks against their equity accounts. Those were breakthrough innovations that sustained the best customers of these companies by providing something better than had previously been available.

Disruptive innovations create an entirely new market through the introduction of a new kind of product or service, one that's actually worse, initially, as judged by the performance metrics that mainstream customers value. Charles Schwab's initial entry as a bare-bones discount broker was a disruptive innovation relative to the offerings of full-service brokers like Merrill Lynch. Merrill Lynch's best customers wanted more than Schwab-like services. Early personal computers were a disruptive innovation relative to mainframes and minicomputers. PCs were not powerful enough to run the computing applications that existed at the time they were introduced. These innovations were disruptive in that they didn't address the next-generation needs of leading customers in existing markets. They had other attributes, of course, that enabled new market applications to emerge—and the disruptive innovations improved so rapidly that they ultimately could address the needs of customers in the mainstream of the market as well.

Sustaining innovations are nearly always developed and introduced by established industry leaders. But those same companies never introduce—or cope well with—disruptive innovations. Why? Our resources-processes-values framework holds the answer. Industry leaders are organized to develop

and introduce sustaining technologies. Month after month, year after year, they launch new and improved products to gain an edge over the competition. They do so by developing processes for evaluating the technological potential of sustaining innovations and for assessing their customers' needs for alternatives. Investment in sustaining technology also fits in with the values of leading companies in that they promise higher margins from better products sold to leading-edge customers.

Disruptive innovations occur so intermittently that no company has a routine process for handling them. Furthermore, because disruptive products nearly always promise lower profit margins per unit sold and are not attractive to the company's best customers, they're inconsistent with the established company's values. Merrill Lynch had the resources—the people, money, and technology—required to succeed at the sustaining innovations (Cash Management Account) and the disruptive innovations (bare-bones discount brokering) that it has confronted in recent history. But its processes and values supported only the sustaining innovation: they became disabilities when the company needed to understand and confront the discount and on-line brokerage businesses.

The reason, therefore, that large companies often surrender emerging growth markets is that smaller, disruptive companies are actually more capable of pursuing them. Start-ups lack resources, but that doesn't matter. Their values can embrace small markets, and their cost structures can accommodate low margins. Their market research and resource allocation processes allow managers to proceed intuitively; every decision need not be backed by careful research and analysis. All these advantages add up to the ability to embrace and even initiate disruptive change. But how can a large company develop those capabilities?

Creating Capabilities to Cope with Change

Despite beliefs spawned by popular change-management and reengineering programs, processes are not nearly as flexible or adaptable as resources are—and values are even less so. So whether addressing sustaining or disruptive innovations, when an organization needs new processes and values—because it needs new capabilities—managers must create a new organizational space where those capabilities can be developed. There are three possible ways to do that. Managers can

- create new organizational structures within corporate boundaries in which new processes can be developed,
- spin out an independent organization from the existing organization and develop within it the new processes and values required to solve the new problem,
- acquire a different organization whose processes and values closely match the requirements of the new task.

Creating new capabilities internally

When a company's capabilities reside in its processes, and when new challenges require new processes—that is, when they require different people or groups in a company to interact differently and at a different pace than they habitually have done—managers need to pull the relevant people out of the existing organization and draw a new boundary around a new group. Often, organizational boundaries were first drawn to facilitate the operation of existing processes, and they impede the creation of new processes. New team boundaries facilitate new patterns of working together that ultimately can coalesce as new processes. In *Revolutionizing Product Development* (The Free Press, 1992), Steven Wheelwright and Kim Clark referred to these structures as “heavyweight teams.”

These teams are entirely dedicated to the new challenge, team members are physically located together, and each member is charged with assuming personal responsibility for the success of the entire project. At Chrysler, for example, the boundaries of the groups within its product development organization historically had been defined by components—power train, electrical systems, and so on. But to accelerate auto development, Chrysler needed to focus not on components but on automobile platforms—the minivan, small car, Jeep, and truck, for example—so it created heavyweight teams. Although these organizational units aren't as good at focusing on component design, they facilitated the definition of new processes that were much faster and more efficient in integrating various subsystems into new car designs. Companies as diverse as Medtronic for its cardiac pacemakers, IBM for its disk drives, and Eli Lilly for its new blockbuster drug Zyprexa have used heavyweight teams as vehicles for creating new processes so they could develop better products faster.

Creating capabilities through a spinout organization

When the mainstream organization's values would render it incapable of allocating resources to an innovation project, the company should spin it out as a new venture. Large organizations cannot be expected to allocate the critical financial and human resources needed to build a strong position in small, emerging markets. And it is very difficult for a company whose cost structure is tailored to compete in high-end markets to be profitable in low-end markets as well. Spinouts are very much in vogue among managers in old-line companies struggling with the question of how to address the Internet. But that's not always appropriate. When a disruptive innovation requires a different cost structure in order to be profitable and competitive, or when the current size of the opportunity is insignificant relative to the growth needs of the mainstream organization, then—and only then—is a spinout organization required.

Hewlett-Packard's laser-printer division in Boise, Idaho, was hugely successful, enjoying high margins and a reputation for superior product quality. Unfortunately, its ink-jet project, which represented a disruptive innovation, languished inside the mainstream HP printer business. Although the processes for developing the two types of printers were basically the same, there was a difference in values. To thrive in the ink-jet market, HP needed to be comfortable with lower gross margins and a smaller market than its laser printers commanded, and it needed to be willing to embrace relatively lower performance standards. It was not until HP's managers decided to transfer the unit to a separate division in Vancouver, British Columbia, with the goal of competing head-to-head with its own laser business, that the ink-jet business finally became successful.

How separate does such an effort need to be? A new physical location isn't always necessary. The primary requirement is that the project not be forced to compete for resources with projects in the mainstream organization. As we have seen, projects that are inconsistent with a company's mainstream values will naturally be accorded lowest priority. Whether the independent organization is physically separate is less important than its independence from the normal decision-making criteria in the resource allocation process. The sidebar "Fitting the Tool to the Task" goes into more detail about what

kind of innovation challenge is best met by which organizational structure.

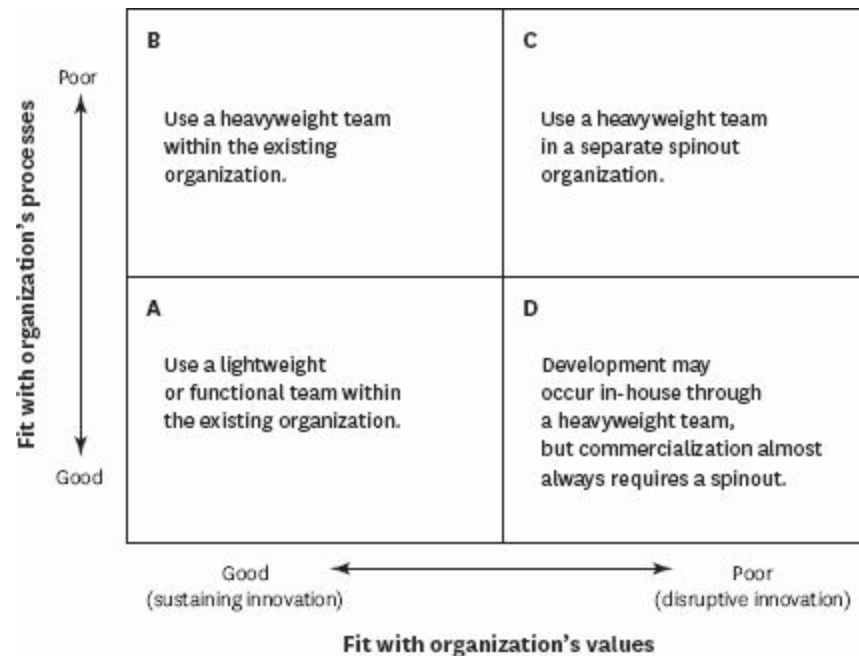
Managers think that developing a new operation necessarily means abandoning the old one, and they're loathe to do that since it works perfectly well for what it was designed to do. But when disruptive change appears on the horizon, managers need to assemble the capabilities to confront that change before it affects the mainstream business. They actually need to run two businesses in tandem—one whose processes are tuned to the existing business model and another that is geared toward the new model. Merrill Lynch, for example, has accomplished an impressive global expansion of its institutional financial services through careful execution of its existing planning, acquisition, and partnership processes. Now, however, faced with the on-line world, the company is required to plan, acquire, and form partnerships more rapidly. Does that mean Merrill Lynch should change the processes that have worked so well in its traditional investment-banking business? Doing so would be disastrous, if we consider the question through the lens of our framework. Instead, Merrill should retain the old processes when working with the existing business (there are probably a few billion dollars still to be made under the old business model!) and create additional processes to deal with the new class of problems.

One word of warning: in our studies of this challenge, we have never seen a company succeed in addressing a change that disrupts its mainstream values without the personal, attentive oversight of the CEO—precisely because of the power of values in shaping the normal resource allocation process. Only the CEO can ensure that the new organization gets the required resources and is free to create processes and values that are appropriate to the new challenge. CEOs who view spinouts as a tool to get disruptive threats off their personal agendas are almost certain to meet with failure. We have seen no exceptions to this rule.

Fitting the Tool to the Task

SUPPOSE THAT AN ORGANIZATION needs to react to or initiate an innovation. The matrix illustrated below can help managers understand what kind of team should work on the project and what organizational structure that team needs to work within. The vertical axis asks the manager to measure the extent to which the organization's existing processes are suited to getting the new job done effectively. The horizontal axis asks managers to assess whether the organization's values will permit the company to allocate the resources the new initiative needs.

In region A, the project is a good fit with the company's processes and values, so no new capabilities are called for. A functional or a lightweight team can tackle the project within the existing organizational structure. A functional team works on function-specific issues, then passes the project on to the next function. A lightweight team is cross-functional, but team members stay under the control of their respective functional managers.



In region B, the project is a good fit with the company's values but not with its processes. It presents the organization with new types of problems and therefore requires new types of interactions and coordination among groups and individuals. The team, like the team in region A, is working on a sustaining rather than a disruptive innovation. In this case, a heavyweight team is a good bet, but the project can be executed within the mainstream company. A heavyweight team—whose members work solely on the project and are expected to behave like general managers, shouldering responsibility for the project's success—is designed so that new processes and new ways of working together can emerge.

In region C, the manager faces a disruptive change that doesn't fit the organization's existing processes or values. To ensure success, the manager should create a spinout organization and commission a heavyweight development team to tackle the challenge. The spinout will allow the project to be governed by different values—a different cost structure, for example, with lower profit margins. The heavyweight team (as in region B) will ensure that new processes can emerge.

Similarly, in region D, when a manager faces a disruptive change that fits the organization's current processes but doesn't fit its values, the key to success almost

always lies in commissioning a heavyweight development team to work in a spinout. Development may occasionally happen successfully in-house, but successful commercialization will require a spinout.

Unfortunately, most companies employ a one-size-fits-all organizing strategy, using lightweight or functional teams for programs of every size and character. But such teams are tools for exploiting established capabilities. And among those few companies that have accepted the heavyweight gospel, many have attempted to organize *all* of their development teams in a heavyweight fashion. Ideally, each company should tailor the team structure and organizational location to the process and values required by each project.

Creating capabilities through acquisitions

Just as innovating managers need to make separate assessments of the capabilities and disabilities that reside in their company's resources, processes, and values, so must they do the same with acquisitions when seeking to buy capabilities. Companies that successfully gain new capabilities through acquisitions are those that know where those capabilities reside in the acquisition and assimilate them accordingly. Acquiring managers begin by asking, "What created the value that I just paid so dearly for? Did I justify the price because of the acquisition's resources? Or was a substantial portion of its worth created by processes and values?"

If the capabilities being purchased are embedded in an acquired company's processes and values, then the last thing the acquiring manager should do is integrate the acquisition into the parent organization. Integration will vaporize the processes and values of the acquired firm. Once the acquisition's managers are forced to adopt the buyer's way of doing business, its capabilities will disappear. A better strategy is to let the business stand alone and to infuse the parent's resources into the acquired company's processes and values. This approach truly constitutes the acquisition of new capabilities.

If, however, the acquired company's resources were the reason for its success and the primary rationale for the acquisition, then integrating it into the parent can make a lot of sense. Essentially, that means plugging the acquired people, products, technology, and customers into the parent's processes as a way of leveraging the parent's existing capabilities.

The perils of the ongoing DaimlerChrysler merger can be better understood in this light. Chrysler had few resources that could be considered unique. Its recent success in the market was rooted in its processes—particularly in its processes for designing products and integrating the efforts of its subsystem suppliers. What is the best way for Daimler to leverage Chrysler's capabilities? Wall Street is pressuring management to consolidate the two organizations to cut costs. But if the two companies are integrated, the very processes that made Chrysler such an attractive acquisition will likely be compromised.

The situation is reminiscent of IBM's 1984 acquisition of the

telecommunications company Rolm. There wasn't anything in Rolm's pool of resources that IBM didn't already have. Rather, it was Rolm's processes for developing and finding new markets for PBX products that mattered. Initially, IBM recognized the value in preserving the informal and unconventional culture of the Rolm organization, which stood in stark contrast to IBM's methodical style. However, in 1987 IBM terminated Rolm's subsidiary status and decided to fully integrate the company into its own corporate structure. IBM's managers soon learned the folly of that decision. When they tried to push Rolm's resources—its products and its customers—through the processes that had been honed in the large-computer business, the Rolm business stumbled badly. And it was impossible for a computer company whose values had been whetted on profit margins of 18% to get excited about products with much lower profit margins. IBM's integration of Rolm destroyed the very source of the deal's original worth. Daimler-Chrysler, bowing to the investment community's drumbeat for efficiency savings, now stands on the edge of the same precipice. Often, it seems, financial analysts have a better intuition about the value of resources than they do about the value of processes.

By contrast, Cisco Systems' acquisitions process has worked well because, we would argue, it has kept resources, processes, and values in the right perspective. Between 1993 and 1997, it primarily acquired small companies that were less than two years old, early-stage organizations whose market value was built primarily upon their resources, particularly their engineers and products. Cisco plugged those resources into its own effective development, logistics, manufacturing, and marketing processes and threw away whatever nascent processes and values came with the acquisitions because those weren't what it had paid for. On a couple of occasions when the company acquired a larger, more mature organization—notably its 1996 acquisition of StrataCom—Cisco did not integrate. Rather, it let StrataCom stand alone and infused Cisco's substantial resources into StrataCom's organization to help it grow more rapidly.³

Managers whose organizations are confronting change must first determine whether they have the resources required to succeed. They then need to ask a separate question: Does the organization have the processes and values it needs to succeed in this new situation? Asking this second question is not as instinctive for most managers because the processes by which work is done and the values by which employees make their decisions have served

them well in the past. What we hope this framework introduces into managers' thinking is the idea that the very capabilities that make their organizations effective also define their disabilities. In that regard, a little time spent soul-searching for honest answers to the following questions will pay off handsomely: Are the processes by which work habitually gets done in the organization appropriate for this new problem? And will the values of the organization cause this initiative to get high priority or to languish?

If the answers to those questions are no, it's okay. Understanding a problem is the most crucial step in solving it. Wishful thinking about these issues can set teams that need to innovate on a course fraught with roadblocks, second-guessing, and frustration. The reason that innovation often seems to be so difficult for established companies is that they employ highly capable people and then set them to work within organizational structures whose processes and values weren't designed for the task at hand. Ensuring that capable people are ensconced in capable organizations is a major responsibility of management in a transformational age such as ours.

Originally published in March 2000. Reprint R00202

Notes

[1.](#) See Dorothy Leonard-Barton, “Core Capabilities and Core Rigidities: A Paradox in Managing New Product Development,” *Strategic Management Journal* (summer, 1992).

[2.](#) Our description of the development of an organization’s culture draws heavily from Edgar Schein’s research, as first laid out in his book *Organizational Culture and Leadership* (Jossey-Bass Publishers, 1985).

[3.](#) See Charles A. Holloway, Stephen C. Wheelwright, and Nicole Tempest, “Cisco Systems, Inc.: Post-Acquisition Manufacturing Integration,” a case published jointly by the Stanford and Harvard business schools, 1998.

Competing on Analytics

by Thomas H. Davenport

WE ALL KNOW THE POWER of the killer app. Over the years, groundbreaking systems from companies such as American Airlines (electronic reservations), Otis Elevator (predictive maintenance), and American Hospital Supply (online ordering) have dramatically boosted their creators' revenues and reputations. These heralded—and coveted—applications amassed and applied data in ways that upended customer expectations and optimized operations to unprecedented degrees. They transformed technology from a supporting tool into a strategic weapon.

Companies questing for killer apps generally focus all their firepower on the one area that promises to create the greatest competitive advantage. But a new breed of company is upping the stakes. Organizations such as Amazon, Harrah's, Capital One, and the Boston Red Sox have dominated their fields by deploying industrial-strength analytics across a wide variety of activities. In essence, they are transforming their organizations into armies of killer apps and crunching their way to victory.

Organizations are competing on analytics not just because they can—business today is awash in data and data crunchers—but also because they should. At a time when firms in many industries offer similar products and use comparable technologies, business processes are among the last remaining points of differentiation. And analytics competitors wring every last drop of value from those processes. So, like other companies, they know what products their customers want, but they also know what prices those customers will pay, how many items each will buy in a lifetime, and what triggers will make people buy more. Like other companies, they know compensation costs and turnover rates, but they can also calculate how much personnel contribute to or detract from the bottom line and how salary levels

relate to individuals' performance. Like other companies, they know when inventories are running low, but they can also predict problems with demand and supply chains, to achieve low rates of inventory and high rates of perfect orders.

And analytics competitors do all those things in a coordinated way, as part of an overarching strategy championed by top leadership and pushed down to decision makers at every level. Employees hired for their expertise with numbers or trained to recognize their importance are armed with the best evidence and the best quantitative tools. As a result, they make the best decisions: big and small, every day, over and over and over.

Although numerous organizations are embracing analytics, only a handful have achieved this level of proficiency. But analytics competitors are the leaders in their varied fields—consumer products, finance, retail, and travel and entertainment among them. Analytics has been instrumental to Capital One, which has exceeded 20% growth in earnings per share every year since it became a public company. It has allowed Amazon to dominate online retailing and turn a profit despite enormous investments in growth and infrastructure. In sports, the real secret weapon isn't steroids, but stats, as dramatic victories by the Boston Red Sox, the New England Patriots, and the Oakland A's attest.

At such organizations, virtuosity with data is often part of the brand. Progressive makes advertising hay from its detailed parsing of individual insurance rates. Amazon customers can watch the company learning about them as its service grows more targeted with frequent purchases. Thanks to Michael Lewis's best-selling book *Moneyball*, which demonstrated the power of statistics in professional baseball, the Oakland A's are almost as famous for their geeky number crunching as they are for their athletic prowess.

Idea in Brief

It's virtually impossible to differentiate yourself from competitors based on products alone. Your rivals sell offerings similar to yours. And thanks to cheap offshore labor, you're hard-pressed to beat overseas competitors on product cost.

How to pull ahead of the pack? Become an **analytics competitor**: Use sophisticated data-collection technology and analysis to wring every last drop of value from all your business processes. With analytics, you discern not only what your customers want but also how much they're willing to pay and what keeps

them loyal. You look beyond compensation costs to calculate your workforce's exact contribution to your bottom line. And you don't just track existing inventories; you also predict and prevent future inventory problems.

Analytics competitors seize the lead in their fields. Capital One's analytics initiative, for example, has spurred at least 20% growth in earnings per share every year since the company went public.

Make analytics part of *your* overarching competitive strategy, and push it down to decision makers at every level. You'll arm your employees with the best evidence and quantitative tools for making the best decisions—big and small, every day.

To identify characteristics shared by analytics competitors, I and two of my colleagues at Babson College's Working Knowledge Research Center studied 32 organizations that have made a commitment to quantitative, fact-based analysis. Eleven of those organizations we classified as full-bore analytics competitors, meaning top management had announced that analytics was key to their strategies; they had multiple initiatives under way involving complex data and statistical analysis, and they managed analytical activity at the enterprise (not departmental) level.

This article lays out the characteristics and practices of these statistical masters and describes some of the very substantial changes other companies must undergo in order to compete on quantitative turf. As one would expect, the transformation requires a significant investment in technology, the accumulation of massive stores of data, and the formulation of companywide strategies for managing the data. But at least as important, it requires executives' vocal, unswerving commitment and willingness to change the way employees think, work, and are treated. As Gary Loveman, CEO of analytics competitor Harrah's, frequently puts it, "Do we think this is true? Or do we know?"

Idea in Practice

To become an analytics competitor:

Champion Analytics from the Top

Acknowledge and endorse the changes in culture, processes, and skills that

analytics competition will mean for much of your workforce. And prepare yourself to lead an analytics-focused organization: You will have to understand the theory behind various quantitative methods so you can recognize their limitations. If you lack background in statistical methods, consult experts who understand your business and know how analytics can be applied to it.

Create a Single Analytics Initiative

Place all data-collection and analysis activities under a common leadership, with common technology and tools. You'll facilitate data sharing and avoid the impediments of inconsistent reporting formats, data definitions, and standards.

Example: Procter & Gamble created a centrally managed “überanalytics” group of 100 analysts drawn from many different functions. It applies this critical mass of expertise to pressing cross-functional issues. For instance, sales and marketing analysts supply data on growth opportunities in existing markets to supply-chain analysts, who can then design more responsive supply networks.

Focus Your Analytics Effort

Channel your resources into analytics initiatives that most directly serve your overarching competitive strategy. Harrah's, for instance, aims much of its analytical activity at improving customer loyalty, customer service, and related areas such as pricing and promotions.

Establish an Analytics Culture

Instill a companywide respect for measuring, testing, and evaluating quantitative evidence. Urge employees to base decisions on hard facts. Gauge and reward performance the same way—applying metrics to compensation and rewards.

Hire the Right People

Pursue and hire analysts who possess top-notch quantitative-analysis skills, can express complex ideas in simple terms, and can interact productively with decision makers. This combination may be difficult to find, so start recruiting well before you need to fill analyst positions.

Use the Right Technology

Prepare to spend significant resources on technology such as customer relationship management (CRM) or enterprise resource planning (ERP) systems. Present data in standard formats, integrate it, store it in a data warehouse, and

make it easily accessible to everyone. And expect to spend years gathering enough data to conduct meaningful analyses.

Example: It took Dell Computer seven years to create a database that includes 1.5 million records of all its print, radio, broadcast TV, and cable ads. Dell couples the database with data on sales for each region in which the ads appeared (before and after their appearance). The information enables Dell to fine-tune its promotions for every medium—in every region.

Anatomy of an Analytics Competitor

One analytics competitor that's at the top of its game is Marriott International. Over the past 20 years, the corporation has honed to a science its system for establishing the optimal price for guest rooms (the key analytics process in hotels, known as revenue management). Today, its ambitions are far grander. Through its Total Hotel Optimization program, Marriott has expanded its quantitative expertise to areas such as conference facilities and catering, and made related tools available over the Internet to property revenue managers and hotel owners. It has developed systems to optimize offerings to frequent customers and assess the likelihood of those customers' defecting to competitors. It has given local revenue managers the power to override the system's recommendations when certain local factors can't be predicted (like the large number of Hurricane Katrina evacuees arriving in Houston). The company has even created a revenue opportunity model, which computes actual revenues as a percentage of the optimal rates that could have been charged. That figure has grown from 83% to 91% as Marriott's revenue-management analytics has taken root throughout the enterprise. The word is out among property owners and franchisees: If you want to squeeze the most revenue from your inventory, Marriott's approach is the ticket.

Clearly, organizations such as Marriott don't behave like traditional companies. Customers notice the difference in every interaction; employees and vendors live the difference every day. Our study found three key attributes among analytics competitors:

Widespread use of modeling and optimization

Any company can generate simple descriptive statistics about aspects of its business—average revenue per employee, for example, or average order size. But analytics competitors look well beyond basic statistics. These companies use predictive modeling to identify the most profitable customers—plus those with the greatest profit potential and the ones most likely to cancel their accounts. They pool data generated in-house and data acquired from outside sources (which they analyze more deeply than do their less statistically savvy competitors) for a comprehensive understanding of their customers. They optimize their supply chains and can thus determine the impact of an unexpected constraint, simulate alternatives, and route shipments around problems. They establish prices in real time to get the highest yield possible from each of their customer transactions. They create complex models of how their operational costs relate to their financial performance.

Leaders in analytics also use sophisticated experiments to measure the overall impact or “lift” of intervention strategies and then apply the results to continuously improve subsequent analyses. Capital One, for example, conducts more than 30,000 experiments a year, with different interest rates, incentives, direct-mail packaging, and other variables. Its goal is to maximize the likelihood both that potential customers will sign up for credit cards and that they will pay back Capital One.

Progressive employs similar experiments using widely available insurance industry data. The company defines narrow groups, or cells, of customers: for example, motorcycle riders ages 30 and above, with college educations, credit scores over a certain level, and no accidents. For each cell, the company performs a regression analysis to identify factors that most closely correlate with the losses that group engenders. It then sets prices for the cells, which should enable the company to earn a profit across a portfolio of customer groups, and uses simulation software to test the financial implications of those hypotheses. With this approach, Progressive can profitably insure customers in traditionally high-risk categories. Other insurers reject high-risk customers out of hand, without bothering to delve more deeply into the data (although even traditional competitors, such as Allstate, are starting to embrace analytics as a strategy).

An enterprise approach

Analytics competitors understand that most business functions—even those, like marketing, that have historically depended on art rather than science—can be improved with sophisticated quantitative techniques. These organizations don't gain advantage from one killer app, but rather from multiple applications supporting many parts of the business—and, in a few cases, being rolled out for use by customers and suppliers.

UPS embodies the evolution from targeted analytics user to comprehensive analytics competitor. Although the company is among the world's most rigorous practitioners of operations research and industrial engineering, its capabilities were, until fairly recently, narrowly focused. Today, UPS is wielding its statistical skill to track the movement of packages and to anticipate and influence the actions of people—assessing the likelihood of customer attrition and identifying sources of problems. The UPS Customer Intelligence Group, for example, is able to accurately predict customer defections by examining usage patterns and complaints. When the data point to a potential defector, a salesperson contacts that customer to review and resolve the problem, dramatically reducing the loss of accounts. UPS still lacks the breadth of initiatives of a full-bore analytics competitor, but it is heading in that direction.

Analytics competitors treat all such activities from all provenances as a single, coherent initiative, often massed under one rubric, such as “information-based strategy” at Capital One or “information-based customer management” at Barclays Bank. These programs operate not just under a common label but also under common leadership and with common technology and tools. In traditional companies, “business intelligence” (the term IT people use for analytics and reporting processes and software) is generally managed by departments; number-crunching functions select their own tools, control their own data warehouses, and train their own people. But that way, chaos lies. For one thing, the proliferation of user-developed spreadsheets and databases inevitably leads to multiple versions of key indicators within an organization. Furthermore, research has shown that between 20% and 40% of spreadsheets contain errors; the more spreadsheets floating around a company, therefore, the more fecund the breeding ground

for mistakes. Analytics competitors, by contrast, field centralized groups to ensure that critical data and other resources are well managed and that different parts of the organization can share data easily, without the impediments of inconsistent formats, definitions, and standards.

Some analytics competitors apply the same enterprise approach to people as to technology. Procter & Gamble, for example, recently created a kind of überanalytics group consisting of more than 100 analysts from such functions as operations, supply chain, sales, consumer research, and marketing. Although most of the analysts are embedded in business operating units, the group is centrally managed. As a result of this consolidation, P&G can apply a critical mass of expertise to its most pressing issues. So, for example, sales and marketing analysts supply data on opportunities for growth in existing markets to analysts who design corporate supply networks. The supply chain analysts, in turn, apply their expertise in certain decision-analysis techniques to such new areas as competitive intelligence.

The group at P&G also raises the visibility of analytical and data-based decision making within the company. Previously, P&G's crack analysts had improved business processes and saved the firm money; but because they were squirreled away in dispersed domains, many executives didn't know what services they offered or how effective they could be. Now those executives are more likely to tap the company's deep pool of expertise for their projects. Meanwhile, masterful number crunching has become part of the story P&G tells to investors, the press, and the public.

Senior executive advocates

A companywide embrace of analytics impels changes in culture, processes, behavior, and skills for many employees. And so, like any major transition, it requires leadership from executives at the very top who have a passion for the quantitative approach. Ideally, the principal advocate is the CEO. Indeed, we found several chief executives who have driven the shift to analytics at their companies over the past few years, including Loveman of Harrah's, Jeff Bezos of Amazon, and Rich Fairbank of Capital One. Before he retired from the Sara Lee Bakery Group, former CEO Barry Beracha kept a sign on his desk that summed up his personal and organizational philosophy: "In God we trust. All others bring data." We did come across some companies in which a single functional or business unit leader was trying to push analytics throughout the organization, and a few were making some progress. But we found that these lower-level people lacked the clout, the perspective, and the cross-functional scope to change the culture in any meaningful way.

CEOs leading the analytics charge require both an appreciation of and a familiarity with the subject. A background in statistics isn't necessary, but those leaders must understand the theory behind various quantitative methods so that they recognize those methods' limitations—which factors are being weighed and which ones aren't. When the CEOs need help grasping quantitative techniques, they turn to experts who understand the business and how analytics can be applied to it. We interviewed several leaders who had retained such advisers, and these executives stressed the need to find someone who can explain things in plain language and be trusted not to spin the numbers. A few CEOs we spoke with had surrounded themselves with very analytical people—professors, consultants, MIT graduates, and the like. But that was a personal preference rather than a necessary practice.

Of course, not all decisions should be grounded in analytics—at least not wholly so. Personnel matters, in particular, are often well and appropriately informed by instinct and anecdote. More organizations are subjecting recruiting and hiring decisions to statistical analysis (see the sidebar "Going to Bat for Stats"). But research shows that human beings can make quick, surprisingly accurate assessments of personality and character based on simple observations. For analytics-minded leaders, then, the challenge boils

down to knowing when to run with the numbers and when to run with their guts.

Going to Bat for Stats

THE ANALYSIS-VERSUS-INSTINCT DEBATE, a favorite of political commentators during the last two U.S. presidential elections, is raging in professional sports, thanks to several popular books and high-profile victories. For now, analysis seems to hold the lead.

Most notably, statistics are a major part of the selection and deployment of players. *Moneyball*, by Michael Lewis, focuses on the use of analytics in player selection for the Oakland A's—a team that wins on a shoestring. The New England Patriots, a team that devotes an enormous amount of attention to statistics, won three of the last four Super Bowls, and their payroll is currently ranked 24th in the league. The Boston Red Sox have embraced “sabermetrics” (the application of analysis to baseball), even going so far as to hire Bill James, the famous baseball statistician who popularized that term. Analytic HR strategies are taking hold in European soccer as well. One leading team, Italy's A.C. Milan, uses predictive models from its Milan Lab research center to prevent injuries by analyzing physiological, orthopedic, and psychological data from a variety of sources. A fast-rising English soccer team, the Bolton Wanderers, is known for its manager's use of extensive data to evaluate players' performance.

Still, sports managers—like business leaders—are rarely fact-or-feeling purists. St. Louis Cardinals manager Tony La Russa, for example, brilliantly combines analytics with intuition to decide when to substitute a charged-up player in the batting lineup or whether to hire a spark-plug personality to improve morale. In his recent book, *Three Nights in August*, Buzz Bissinger describes that balance: “La Russa appreciated the information generated by computers. He studied the rows and the columns. But he also knew they could take you only so far in baseball, maybe even confuse you with a fog of overanalysis. As far as he knew, there was no way to quantify desire. And those numbers told him exactly what he needed to know when added to twenty-four years of managing experience.”

That final sentence is the key. Whether scrutinizing someone's performance record or observing the expression flitting across an employee's face, leaders consult their own experience to understand the “evidence” in all its forms.

Their Sources of Strength

Analytics competitors are more than simple number-crunching factories. Certainly, they apply technology—with a mixture of brute force and finesse—to multiple business problems. But they also direct their energies toward finding the right focus, building the right culture, and hiring the right people to make optimal use of the data they constantly churn. In the end, people and strategy, as much as information technology, give such organizations strength.

The right focus

Although analytics competitors encourage universal fact-based decisions, they must choose where to direct resource-intensive efforts. Generally, they pick several functions or initiatives that together serve an overarching strategy. Harrah's, for example, has aimed much of its analytical activity at increasing customer loyalty, customer service, and related areas like pricing and promotions. UPS has broadened its focus from logistics to customers, in the interest of providing superior service. While such multipronged strategies define analytics competitors, executives we interviewed warned companies against becoming too diffuse in their initiatives or losing clear sight of the business purpose behind each.

Another consideration when allocating resources is how amenable certain functions are to deep analysis. There are at least seven common targets for analytical activity, and specific industries may present their own (see "Things You Can Count On"). Statistical models and algorithms that dangle the possibility of performance breakthroughs make some prospects especially tempting. Marketing, for example, has always been tough to quantify because it is rooted in psychology. But now consumer products companies can hone their market research using multiattribute utility theory—a tool for understanding and predicting consumer behaviors and decisions. Similarly, the advertising industry is adopting econometrics—statistical techniques for measuring the lift provided by different ads and promotions over time.

Things you can count on		
<i>Analytics competitors make expert use of statistics and modeling to improve a wide variety of functions. Here are some common applications:</i>		
Function	Description	Exemplars
Supply chain	Simulate and optimize supply chain flows; reduce inventory and stock-outs.	Dell, Wal-Mart, Amazon
Customer selection, loyalty, and service	Identify customers with the greatest profit potential; increase likelihood that they will want the product or service offering; retain their loyalty.	Harrah's, Capital One, Barclays

Pricing	Identify the price that will maximize yield, or profit.	Progressive, Marriott
Human capital	Select the best employees for particular tasks or jobs, at particular compensation levels.	New England Patriots, Oakland A's, Boston Red Sox
Product and service quality	Detect quality problems early and minimize them.	Honda, Intel
Financial performance	Better understand the drivers of financial performance and the effects of nonfinancial factors.	MCI, Verizon
Research and development	Improve quality, efficacy, and, where applicable, safety of products and services.	Novartis, Amazon, Yahoo

The most proficient analytics practitioners don't just measure their own navels—they also help customers and vendors measure theirs. Wal-Mart, for example, insists that suppliers use its Retail Link system to monitor product movement by store, to plan promotions and layouts within stores, and to reduce stock-outs. E.&J. Gallo provides distributors with data and analysis on retailers' costs and pricing so they can calculate the per-bottle profitability for each of Gallo's 95 wines. The distributors, in turn, use that information to help retailers optimize their mixes while persuading them to add shelf space for Gallo products. Procter & Gamble offers data and analysis to its retail customers, as part of a program called Joint Value Creation, and to its suppliers to help improve responsiveness and reduce costs. Hospital supplier Owens & Minor furnishes similar services, enabling customers and suppliers to access and analyze their buying and selling data, track ordering patterns in search of consolidation opportunities, and move off-contract purchases to group contracts that include products distributed by Owens & Minor and its competitors. For example, Owens & Minor might show a hospital chain's executives how much money they could save by consolidating purchases across multiple locations or help them see the trade-offs between increasing delivery frequency and carrying inventory.

The right culture

Culture is a soft concept; analytics is a hard discipline. Nonetheless, analytics competitors must instill a companywide respect for measuring, testing, and evaluating quantitative evidence. Employees are urged to base decisions on hard facts. And they know that their performance is gauged the same way. Human resource organizations within analytics competitors are rigorous about applying metrics to compensation and rewards. Harrah's, for example, has made a dramatic change from a rewards culture based on paternalism and tenure to one based on such meticulously collected performance measurements as financial and customer service results. Senior executives also set a consistent example with their own behavior, exhibiting a hunger for and confidence in fact and analysis. One exemplar of such leadership was Beracha of the Sara Lee Bakery Group, known to his employees as a "data dog" because he hounded them for data to support any assertion or hypothesis.

Not surprisingly, in an analytics culture, there's sometimes tension between innovative or entrepreneurial impulses and the requirement for evidence. Some companies place less emphasis on blue-sky development, in which designers or engineers chase after a gleam in someone's eye. In these organizations, R&D, like other functions, is rigorously metric-driven. At Yahoo, Progressive, and Capital One, process and product changes are tested on a small scale and implemented as they are validated. That approach, well established within various academic and business disciplines (including engineering, quality management, and psychology), can be applied to most corporate processes—even to not-so-obvious candidates, like human resources and customer service. HR, for example, might create profiles of managers' personality traits and leadership styles and then test those managers in different situations. It could then compare data on individuals' performance with data about personalities to determine what traits are most important to managing a project that is behind schedule, say, or helping a new group to assimilate.

There are, however, instances when a decision to change something or try something new must be made too quickly for extensive analysis, or when it's not possible to gather data beforehand. For example, even though Amazon's

Jeff Bezos greatly prefers to rigorously quantify users' reactions before rolling out new features, he couldn't test the company's search-inside-the-book offering without applying it to a critical mass of books (120,000, to begin with). It was also expensive to develop, and that increased the risk. In this case, Bezos trusted his instincts and took a flier. And the feature did prove popular when introduced.

The right people

Analytical firms hire analytical people—and like all companies that compete on talent, they pursue the best. When Amazon needed a new head for its global supply chain, for example, it recruited Gang Yu, a professor of management science and software entrepreneur who is one of the world's leading authorities on optimization analytics. Amazon's business model requires the company to manage a constant flow of new products, suppliers, customers, and promotions, as well as deliver orders by promised dates. Since his arrival, Yu and his team have been designing and building sophisticated supply chain systems to optimize those processes. And while he tosses around phrases like “nonstationary stochastic processes,” he's also good at explaining the new approaches to Amazon's executives in clear business terms.

Established analytics competitors such as Capital One employ squadrons of analysts to conduct quantitative experiments and, with the results in hand, design credit card and other financial offers. These efforts call for a specialized skill set, as you can see from this job description (typical for a Capital One analyst):

High conceptual problem-solving and quantitative analytical aptitudes . . . Engineering, financial, consulting, and/or other analytical quantitative educational/work background. Ability to quickly learn how to use software applications. Experience with Excel models. Some graduate work preferred but not required (e.g., MBA). Some experience with project management methodology, process improvement tools (Lean, Six Sigma), or statistics preferred.

Other firms hire similar kinds of people, but analytics competitors have them in much greater numbers. Capital One is currently seeking three times as many analysts as operations people—hardly the common practice for a bank. “We are really a company of analysts,” one executive there noted. “It's the primary job in this place.”

Good analysts must also have the ability to express complex ideas in

simple terms and have the relationship skills to interact well with decision makers. One consumer products company with a 30-person analytics group looks for what it calls “PhDs with personality”—people with expertise in math, statistics, and data analysis who can also speak the language of business and help market their work internally and sometimes externally. The head of a customer analytics group at Wachovia Bank describes the rapport with others his group seeks: “We are trying to build our people as part of the business team,” he explains. “We want them sitting at the business table, participating in a discussion of what the key issues are, determining what information needs the businesspeople have, and recommending actions to the business partners. We want this [analytics group] to be not just a general utility, but rather an active and critical part of the business unit’s success.”

Of course, a combination of analytical, business, and relationship skills may be difficult to find. When the software company SAS (a sponsor of this research, along with Intel) knows it will need an expert in state-of-the-art business applications such as predictive modeling or recursive partitioning (a form of decision tree analysis applied to very complex data sets), it begins recruiting up to 18 months before it expects to fill the position.

In fact, analytical talent may be to the early 2000s what programming talent was to the late 1990s. Unfortunately, the U.S. and European labor markets aren’t exactly teeming with analytically sophisticated job candidates. Some organizations cope by contracting work to countries such as India, home to many statistical experts. That strategy may succeed when offshore analysts work on stand-alone problems. But if an iterative discussion with business decision makers is required, the distance can become a major barrier.

The right technology

Competing on analytics means competing on technology. And while the most serious competitors investigate the latest statistical algorithms and decision science approaches, they also constantly monitor and push the IT frontier. The analytics group at one consumer products company went so far as to build its own supercomputer because it felt that commercially available models were inadequate for its demands. Such heroic feats usually aren't necessary, but serious analytics does require the following:

A data strategy. Companies have invested many millions of dollars in systems that snatch data from every conceivable source. Enterprise resource planning, customer relationship management, point-of-sale, and other systems ensure that no transaction or other significant exchange occurs without leaving a mark. But to compete on that information, companies must present it in standard formats, integrate it, store it in a data warehouse, and make it easily accessible to anyone and everyone. And they will need *a lot* of it. For example, a company may spend several years accumulating data on different marketing approaches before it has gathered enough to reliably analyze the effectiveness of an advertising campaign. Dell employed DDB Matrix, a unit of the advertising agency DDB Worldwide, to create (over a period of seven years) a database that includes 1.5 million records on all the computer maker's print, radio, network TV, and cable ads, coupled with data on Dell sales for each region in which the ads appeared (before and after their appearance). That information allows Dell to fine-tune its promotions for every medium in every region.

Business intelligence software. The term "business intelligence," which first popped up in the late 1980s, encompasses a wide array of processes and software used to collect, analyze, and disseminate data, all in the interests of better decision making. Business intelligence tools allow employees to extract, transform, and load (or ETL, as people in the industry would say) data for analysis and then make those analyses available in reports, alerts, and scorecards. The popularity of analytics competition is partly a response to the emergence of integrated packages of these tools.

Computing hardware. The volumes of data required for analytics applications may strain the capacity of low-end computers and servers. Many analytics competitors are converting their hardware to 64-bit processors that churn large amounts of data quickly.

The Long Road Ahead

Most companies in most industries have excellent reasons to pursue strategies shaped by analytics. Virtually all the organizations we identified as aggressive analytics competitors are clear leaders in their fields, and they attribute much of their success to the masterful exploitation of data. Rising global competition intensifies the need for this sort of proficiency. Western companies unable to beat their Indian or Chinese competitors on product cost, for example, can seek the upper hand through optimized business processes.

You Know You Compete on Analytics When . . .

1. You apply sophisticated information systems and rigorous analysis not only to your core capability but also to a range of functions as varied as marketing and human resources.
2. Your senior executive team not only recognizes the importance of analytics capabilities but also makes their development and maintenance a primary focus.
3. You treat fact-based decision making not only as a best practice but also as a part of the culture that's constantly emphasized and communicated by senior executives.
4. You hire not only people with analytical skills but a lot of people with *the very best* analytical skills—and consider them a key to your success.
5. You not only employ analytics in almost every function and department but also consider it so strategically important that you manage it at the enterprise level.
6. You not only are expert at number crunching but also invent proprietary metrics for use in key business processes.
7. You not only use copious data and in-house analysis but also share them with customers and suppliers.
8. You not only avidly consume data but also seize every opportunity to generate information, creating a “test and learn” culture based on numerous small

experiments.

9. You not only have committed to competing on analytics but also have been building your capabilities for several years.
10. You not only emphasize the importance of analytics internally but also make quantitative capabilities part of your company's story, to be shared in the annual report and in discussions with financial analysts.

Companies just now embracing such strategies, however, will find that they take several years to come to fruition. The organizations in our study described a long, sometimes arduous journey. The UK Consumer Cards and Loans business within Barclays Bank, for example, spent five years executing its plan to apply analytics to the marketing of credit cards and other financial products. The company had to make process changes in virtually every aspect of its consumer business: underwriting risk, setting credit limits, servicing accounts, controlling fraud, cross selling, and so on. On the technical side, it had to integrate data on 10 million Barclaycard customers, improve the quality of the data, and build systems to step up data collection and analysis. In addition, the company embarked on a long series of small tests to begin learning how to attract and retain the best customers at the lowest price. And it had to hire new people with top-drawer quantitative skills.

Much of the time—and corresponding expense—that any company takes to become an analytics competitor will be devoted to technological tasks: refining the systems that produce transaction data, making data available in warehouses, selecting and implementing analytic software, and assembling the hardware and communications environment. And because those who don't record history are doomed not to learn from it, companies that have collected little information—or the wrong kind—will need to amass a sufficient body of data to support reliable forecasting. “We’ve been collecting data for six or seven years, but it’s only become usable in the last two or three, because we needed time and experience to validate conclusions based on the data,” remarked a manager of customer data analytics at UPS.

And, of course, new analytics competitors will have to stock their personnel larders with fresh people. (When Gary Loveman became COO, and then CEO, of Harrah's, he brought in a group of statistical experts who could

design and implement quantitatively based marketing campaigns and loyalty programs.) Existing employees, meanwhile, will require extensive training. They need to know what data are available and all the ways the information can be analyzed; and they must learn to recognize such peculiarities and shortcomings as missing data, duplication, and quality problems. An analytics-minded executive at Procter & Gamble suggested to me that firms should begin to keep managers in their jobs for longer periods because of the time required to master quantitative approaches to their businesses.

The German pathologist Rudolph Virchow famously called the task of science “to stake out the limits of the knowable.” Analytics competitors pursue a similar goal, although the universe they seek to know is a more circumscribed one of customer behavior, product movement, employee performance, and financial reactions. Every day, advances in technology and techniques give companies a better and better handle on the critical minutiae of their operations.

The Oakland A’s aren’t the only ones playing moneyball. Companies of every stripe want to be part of the game.

Originally published in January 2006. Reprint R0601H

Managing Oneself

by Peter F. Drucker

HISTORY'S GREAT ACHIEVERS—a Napoléon, a da Vinci, a Mozart—have always managed themselves. That, in large measure, is what makes them great achievers. But they are rare exceptions, so unusual both in their talents and their accomplishments as to be considered outside the boundaries of ordinary human existence. Now, most of us, even those of us with modest endowments, will have to learn to manage ourselves. We will have to learn to develop ourselves. We will have to place ourselves where we can make the greatest contribution. And we will have to stay mentally alert and engaged during a 50-year working life, which means knowing how and when to change the work we do.

What Are My Strengths?

Most people think they know what they are good at. They are usually wrong. More often, people know what they are not good at—and even then more people are wrong than right. And yet, a person can perform only from strength. One cannot build performance on weaknesses, let alone on something one cannot do at all.

Throughout history, people had little need to know their strengths. A person was born into a position and a line of work: The peasant's son would also be a peasant; the artisan's daughter, an artisan's wife; and so on. But now people have choices. We need to know our strengths in order to know where we belong.

The only way to discover your strengths is through feedback analysis. Whenever you make a key decision or take a key action, write down what you expect will happen. Nine or 12 months later, compare the actual results with your expectations. I have been practicing this method for 15 to 20 years now, and every time I do it, I am surprised. The feedback analysis showed me, for instance—and to my great surprise—that I have an intuitive understanding of technical people, whether they are engineers or accountants or market researchers. It also showed me that I don't really resonate with generalists.

Feedback analysis is by no means new. It was invented sometime in the fourteenth century by an otherwise totally obscure German theologian and picked up quite independently, some 150 years later, by John Calvin and Ignatius of Loyola, each of whom incorporated it into the practice of his followers. In fact, the steadfast focus on performance and results that this habit produces explains why the institutions these two men founded, the Calvinist church and the Jesuit order, came to dominate Europe within 30 years.

Practiced consistently, this simple method will show you within a fairly short period of time, maybe two or three years, where your strengths lie—and this is the most important thing to know. The method will show you what you are doing or failing to do that deprives you of the full benefits of your strengths. It will show you where you are not particularly competent. And

finally, it will show you where you have no strengths and cannot perform.

Several implications for action follow from feedback analysis. First and foremost, concentrate on your strengths. Put yourself where your strengths can produce results.

Second, work on improving your strengths. Analysis will rapidly show where you need to improve skills or acquire new ones. It will also show the gaps in your knowledge—and those can usually be filled. Mathematicians are born, but everyone can learn trigonometry.

Third, discover where your intellectual arrogance is causing disabling ignorance and overcome it. Far too many people—especially people with great expertise in one area—are contemptuous of knowledge in other areas or believe that being bright is a substitute for knowledge. First-rate engineers, for instance, tend to take pride in not knowing anything about people. Human beings, they believe, are much too disorderly for the good engineering mind. Human resources professionals, by contrast, often pride themselves on their ignorance of elementary accounting or of quantitative methods altogether. But taking pride in such ignorance is self-defeating. Go to work on acquiring the skills and knowledge you need to fully realize your strengths.

Idea in Brief

We live in an age of unprecedented opportunity: If you've got ambition, drive, and smarts, you can rise to the top of your chosen profession—regardless of where you started out. But with opportunity comes responsibility. Companies today aren't managing their knowledge workers' careers. Rather, we must each be our own chief executive officer.

Simply put, it's up to you to carve out your place in the work world and know when to change course. And it's up to you to keep yourself engaged and productive during a work life that may span some 50 years.

To do all of these things well, you'll need to cultivate a deep understanding of yourself. What are your most valuable strengths and most dangerous weaknesses? Equally important, how do you learn and work with others? What are your most deeply held values? And in what type of work environment can you make the greatest contribution?

The implication is clear: Only when you operate from a combination of your strengths and self-knowledge can you achieve true—and lasting—excellence.

It is equally essential to remedy your bad habits—the things you do or fail to do that inhibit your effectiveness and performance. Such habits will quickly show up in the feedback. For example, a planner may find that his beautiful plans fail because he does not follow through on them. Like so many brilliant people, he believes that ideas move mountains. But bulldozers move mountains; ideas show where the bulldozers should go to work. This planner will have to learn that the work does not stop when the plan is completed. He must find people to carry out the plan and explain it to them. He must adapt and change it as he puts it into action. And finally, he must decide when to stop pushing the plan.

Idea in Practice

To build a life of excellence, begin by asking yourself these questions:

“What are my strengths?”

To accurately identify your strengths, use **feedback analysis**. Every time you make a key decision, write down the outcome you expect. Several months later, compare the actual results with your expected results. Look for patterns in what you're seeing: What results are you skilled at generating? What abilities do you need to enhance in order to get the results you want? What unproductive habits are preventing you from creating the outcomes you desire? In identifying opportunities for improvement, don't waste time cultivating skill areas where you have little competence. Instead, concentrate on—and build on—your strengths.

“How do I work?”

In what ways do you work best? Do you process information most effectively by reading it, or by hearing others discuss it? Do you accomplish the most by working with other people, or by working alone? Do you perform best while making decisions, or while advising others on key matters? Are you in top form when things get stressful, or do you function optimally in a highly predictable environment?

“What are my values?”

What are your ethics? What do you see as your most important responsibilities for living a worthy, ethical life? Do your organization's ethics resonate with your own values? If not, your career will likely be marked by frustration and poor

performance.

“Where do I belong?”

Consider your strengths, preferred work style, and values. Based on these qualities, in what kind of work environment would you fit in best? Find the perfect fit, and you'll transform yourself from a merely acceptable employee into a star performer.

“What can I contribute?”

In earlier eras, companies told businesspeople what their contribution should be. Today, you have choices. To decide how you can best enhance your organization's performance, first ask what the situation requires. Based on your strengths, work style, and values, how might you make the greatest contribution to your organization's efforts?

At the same time, feedback will also reveal when the problem is a lack of manners. Manners are the lubricating oil of an organization. It is a law of nature that two moving bodies in contact with each other create friction. This is as true for human beings as it is for inanimate objects. Manners—simple things like saying “please” and “thank you” and knowing a person's name or asking after her family—enable two people to work together whether they like each other or not. Bright people, especially bright young people, often do not understand this. If analysis shows that someone's brilliant work fails again and again as soon as cooperation from others is required, it probably indicates a lack of courtesy—that is, a lack of manners.

Comparing your expectations with your results also indicates what not to do. We all have a vast number of areas in which we have no talent or skill and little chance of becoming even mediocre. In those areas a person—and especially a knowledge worker—should not take on work, jobs, and assignments. One should waste as little effort as possible on improving areas of low competence. It takes far more energy and work to improve from incompetence to mediocrity than it takes to improve from first-rate performance to excellence. And yet most people—especially most teachers and most organizations—concentrate on making incompetent performers into mediocre ones. Energy, resources, and time should go instead to making a competent person into a star performer.

How Do I Perform?

Amazingly few people know how they get things done. Indeed, most of us do not even know that different people work and perform differently. Too many people work in ways that are not their ways, and that almost guarantees nonperformance. For knowledge workers, How do I perform? may be an even more important question than What are my strengths?

Like one's strengths, how one performs is unique. It is a matter of personality. Whether personality be a matter of nature or nurture, it surely is formed long before a person goes to work. And *how* a person performs is a given, just as *what* a person is good at or not good at is a given. A person's way of performing can be slightly modified, but it is unlikely to be completely changed—and certainly not easily. Just as people achieve results by doing what they are good at, they also achieve results by working in ways that they best perform. A few common personality traits usually determine how a person performs.

Am I a reader or a listener?

The first thing to know is whether you are a reader or a listener. Far too few people even know that there are readers and listeners and that people are rarely both. Even fewer know which of the two they themselves are. But some examples will show how damaging such ignorance can be.

When Dwight Eisenhower was Supreme Commander of the Allied forces in Europe, he was the darling of the press. His press conferences were famous for their style—General Eisenhower showed total command of whatever question he was asked, and he was able to describe a situation and explain a policy in two or three beautifully polished and elegant sentences. Ten years later, the same journalists who had been his admirers held President Eisenhower in open contempt. He never addressed the questions, they complained, but rambled on endlessly about something else. And they constantly ridiculed him for butchering the King's English in incoherent and ungrammatical answers.

Eisenhower apparently did not know that he was a reader, not a listener. When he was Supreme Commander in Europe, his aides made sure that every question from the press was presented in writing at least half an hour before a conference was to begin. And then Eisenhower was in total command. When he became president, he succeeded two listeners, Franklin D. Roosevelt and Harry Truman. Both men knew themselves to be listeners and both enjoyed free-for-all press conferences. Eisenhower may have felt that he had to do what his two predecessors had done. As a result, he never even heard the questions journalists asked. And Eisenhower is not even an extreme case of a nonlistener.

A few years later, Lyndon Johnson destroyed his presidency, in large measure, by not knowing that he was a listener. His predecessor, John Kennedy, was a reader who had assembled a brilliant group of writers as his assistants, making sure that they wrote to him before discussing their memos in person. Johnson kept these people on his staff—and they kept on writing. He never, apparently, understood one word of what they wrote. Yet as a senator, Johnson had been superb; for parliamentarians have to be, above all, listeners.

Few listeners can be made, or can make themselves, into competent

readers—and vice versa. The listener who tries to be a reader will, therefore, suffer the fate of Lyndon Johnson, whereas the reader who tries to be a listener will suffer the fate of Dwight Eisenhower. They will not perform or achieve.

How do I learn?

The second thing to know about how one performs is to know how one learns. Many first-class writers—Winston Churchill is but one example—do poorly in school. They tend to remember their schooling as pure torture. Yet few of their classmates remember it the same way. They may not have enjoyed the school very much, but the worst they suffered was boredom. The explanation is that writers do not, as a rule, learn by listening and reading. They learn by writing. Because schools do not allow them to learn this way, they get poor grades.

Schools everywhere are organized on the assumption that there is only one right way to learn and that it is the same way for everybody. But to be forced to learn the way a school teaches is sheer hell for students who learn differently. Indeed, there are probably half a dozen different ways to learn.

There are people, like Churchill, who learn by writing. Some people learn by taking copious notes. Beethoven, for example, left behind an enormous number of sketchbooks, yet he said he never actually looked at them when he composed. Asked why he kept them, he is reported to have replied, “If I don’t write it down immediately, I forget it right away. If I put it into a sketchbook, I never forget it and I never have to look it up again.” Some people learn by doing. Others learn by hearing themselves talk.

A chief executive I know who converted a small and mediocre family business into the leading company in its industry was one of those people who learn by talking. He was in the habit of calling his entire senior staff into his office once a week and then talking at them for two or three hours. He would raise policy issues and argue three different positions on each one. He rarely asked his associates for comments or questions; he simply needed an audience to hear himself talk. That’s how he learned. And although he is a fairly extreme case, learning through talking is by no means an unusual method. Successful trial lawyers learn the same way, as do many medical diagnosticians (and so do I).

Of all the important pieces of self-knowledge, understanding how you learn is the easiest to acquire. When I ask people, “How do you learn?” most of them know the answer. But when I ask, “Do you act on this knowledge?” few answer yes. And yet, acting on this knowledge is the key to performance;

or rather, *not* acting on this knowledge condemns one to nonperformance.

Am I a reader or a listener? and How do I learn? are the first questions to ask. But they are by no means the only ones. To manage yourself effectively, you also have to ask, Do I work well with people, or am I a loner? And if you do work well with people, you then must ask, In what relationship?

Some people work best as subordinates. General George Patton, the great American military hero of World War II, is a prime example. Patton was America's top troop commander. Yet when he was proposed for an independent command, General George Marshall, the U.S. chief of staff—and probably the most successful picker of men in U.S. history—said, "Patton is the best subordinate the American army has ever produced, but he would be the worst commander."

Some people work best as team members. Others work best alone. Some are exceptionally talented as coaches and mentors; others are simply incompetent as mentors.

Another crucial question is, Do I produce results as a decision maker or as an adviser? A great many people perform best as advisers but cannot take the burden and pressure of making the decision. A good many other people, by contrast, need an adviser to force themselves to think; then they can make decisions and act on them with speed, self-confidence, and courage.

This is a reason, by the way, that the number two person in an organization often fails when promoted to the number one position. The top spot requires a decision maker. Strong decision makers often put somebody they trust into the number two spot as their adviser—and in that position the person is outstanding. But in the number one spot, the same person fails. He or she knows what the decision should be but cannot accept the responsibility of actually making it.

Other important questions to ask include, Do I perform well under stress, or do I need a highly structured and predictable environment? Do I work best in a big organization or a small one? Few people work well in all kinds of environments. Again and again, I have seen people who were very successful in large organizations flounder miserably when they moved into smaller ones. And the reverse is equally true.

The conclusion bears repeating: Do not try to change yourself—you are unlikely to succeed. But work hard to improve the way you perform. And try not to take on work you cannot perform or will only perform poorly.

What Are My Values?

To be able to manage yourself, you finally have to ask, What are my values? This is not a question of ethics. With respect to ethics, the rules are the same for everybody, and the test is a simple one. I call it the “mirror test.”

In the early years of this century, the most highly respected diplomat of all the great powers was the German ambassador in London. He was clearly destined for great things—to become his country’s foreign minister, at least, if not its federal chancellor. Yet in 1906 he abruptly resigned rather than preside over a dinner given by the diplomatic corps for Edward VII. The king was a notorious womanizer and made it clear what kind of dinner he wanted. The ambassador is reported to have said, “I refuse to see a pimp in the mirror in the morning when I shave.”

That is the mirror test. Ethics requires that you ask yourself, What kind of person do I want to see in the mirror in the morning? What is ethical behavior in one kind of organization or situation is ethical behavior in another. But ethics is only part of a value system—especially of an organization’s value system.

To work in an organization whose value system is unacceptable or incompatible with one’s own condemns a person both to frustration and to nonperformance.

Consider the experience of a highly successful human resources executive whose company was acquired by a bigger organization. After the acquisition, she was promoted to do the kind of work she did best, which included selecting people for important positions. The executive deeply believed that a company should hire people for such positions from the outside only after exhausting all the inside possibilities. But her new company believed in first looking outside “to bring in fresh blood.” There is something to be said for both approaches—in my experience, the proper one is to do some of both. They are, however, fundamentally incompatible—not as policies but as values. They bespeak different views of the relationship between organizations and people; different views of the responsibility of an organization to its people and their development; and different views of a person’s most important contribution to an enterprise. After several years of

frustration, the executive quit—at considerable financial loss. Her values and the values of the organization simply were not compatible.

Similarly, whether a pharmaceutical company tries to obtain results by making constant, small improvements or by achieving occasional, highly expensive, and risky “breakthroughs” is not primarily an economic question. The results of either strategy may be pretty much the same. At bottom, there is a conflict between a value system that sees the company’s contribution in terms of helping physicians do better what they already do and a value system that is oriented toward making scientific discoveries.

Whether a business should be run for short-term results or with a focus on the long term is likewise a question of values. Financial analysts believe that businesses can be run for both simultaneously. Successful businesspeople know better. To be sure, every company has to produce short-term results. But in any conflict between short-term results and long-term growth, each company will determine its own priority. This is not primarily a disagreement about economics. It is fundamentally a value conflict regarding the function of a business and the responsibility of management.

Value conflicts are not limited to business organizations. One of the fastest-growing pastoral churches in the United States measures success by the number of new parishioners. Its leadership believes that what matters is how many newcomers join the congregation. The Good Lord will then minister to their spiritual needs or at least to the needs of a sufficient percentage. Another pastoral, evangelical church believes that what matters is people’s spiritual growth. The church eases out newcomers who join but do not enter into its spiritual life.

Again, this is not a matter of numbers. At first glance, it appears that the second church grows more slowly. But it retains a far larger proportion of newcomers than the first one does. Its growth, in other words, is more solid. This is also not a theological problem, or only secondarily so. It is a problem about values. In a public debate, one pastor argued, “Unless you first come to church, you will never find the gate to the Kingdom of Heaven.”

“No,” answered the other. “Until you first look for the gate to the Kingdom of Heaven, you don’t belong in church.”

Organizations, like people, have values. To be effective in an organization, a person’s values must be compatible with the organization’s values. They do not need to be the same, but they must be close enough to coexist. Otherwise, the person will not only be frustrated but also will not

produce results.

A person's strengths and the way that person performs rarely conflict; the two are complementary. But there is sometimes a conflict between a person's values and his or her strengths. What one does well—even very well and successfully—may not fit with one's value system. In that case, the work may not appear to be worth devoting one's life to (or even a substantial portion thereof).

If I may, allow me to interject a personal note. Many years ago, I too had to decide between my values and what I was doing successfully. I was doing very well as a young investment banker in London in the mid-1930s, and the work clearly fit my strengths. Yet I did not see myself making a contribution as an asset manager. People, I realized, were what I valued, and I saw no point in being the richest man in the cemetery. I had no money and no other job prospects. Despite the continuing Depression, I quit—and it was the right thing to do. Values, in other words, are and should be the ultimate test.

Where Do I Belong?

A small number of people know very early where they belong. Mathematicians, musicians, and cooks, for instance, are usually mathematicians, musicians, and cooks by the time they are four or five years old. Physicians usually decide on their careers in their teens, if not earlier. But most people, especially highly gifted people, do not really know where they belong until they are well past their mid-twenties. By that time, however, they should know the answers to the three questions: What are my strengths? How do I perform? and, What are my values? And then they can and should decide where they belong.

Or rather, they should be able to decide where they do *not* belong. The person who has learned that he or she does not perform well in a big organization should have learned to say no to a position in one. The person who has learned that he or she is not a decision maker should have learned to say no to a decision-making assignment. A General Patton (who probably never learned this himself) should have learned to say no to an independent command.

Equally important, knowing the answer to these questions enables a person to say to an opportunity, an offer, or an assignment, “Yes, I will do that. But this is the way I should be doing it. This is the way it should be structured. This is the way the relationships should be. These are the kind of results you should expect from me, and in this time frame, because this is who I am.”

Successful careers are not planned. They develop when people are prepared for opportunities because they know their strengths, their method of work, and their values. Knowing where one belongs can transform an ordinary person—hardworking and competent but otherwise mediocre—into an outstanding performer.

What Should I Contribute?

Throughout history, the great majority of people never had to ask the question, What should I contribute? They were told what to contribute, and their tasks were dictated either by the work itself—as it was for the peasant or artisan—or by a master or a mistress—as it was for domestic servants. And until very recently, it was taken for granted that most people were subordinates who did as they were told. Even in the 1950s and 1960s, the new knowledge workers (the so-called organization men) looked to their company's personnel department to plan their careers.

Then in the late 1960s, no one wanted to be told what to do any longer. Young men and women began to ask, What do *I* want to do? And what they heard was that the way to contribute was to “do your own thing.” But this solution was as wrong as the organization men's had been. Very few of the people who believed that doing one's own thing would lead to contribution, self-fulfillment, and success achieved any of the three.

But still, there is no return to the old answer of doing what you are told or assigned to do. Knowledge workers in particular have to learn to ask a question that has not been asked before: What *should* my contribution be? To answer it, they must address three distinct elements: What does the situation require? Given my strengths, my way of performing, and my values, how can I make the greatest contribution to what needs to be done? And finally, What results have to be achieved to make a difference?

Consider the experience of a newly appointed hospital administrator. The hospital was big and prestigious, but it had been coasting on its reputation for 30 years. The new administrator decided that his contribution should be to establish a standard of excellence in one important area within two years. He chose to focus on the emergency room, which was big, visible, and sloppy. He decided that every patient who came into the ER had to be seen by a qualified nurse within 60 seconds. Within 12 months, the hospital's emergency room had become a model for all hospitals in the United States, and within another two years, the whole hospital had been transformed.

As this example suggests, it is rarely possible—or even particularly fruitful—to look too far ahead. A plan can usually cover no more than 18

months and still be reasonably clear and specific. So the question in most cases should be, Where and how can I achieve results that will make a difference within the next year and a half? The answer must balance several things. First, the results should be hard to achieve—they should require “stretching,” to use the current buzzword. But also, they should be within reach. To aim at results that cannot be achieved—or that can be only under the most unlikely circumstances—is not being ambitious; it is being foolish. Second, the results should be meaningful. They should make a difference. Finally, results should be visible and, if at all possible, measurable. From this will come a course of action: what to do, where and how to start, and what goals and deadlines to set.

Responsibility for Relationships

Very few people work by themselves and achieve results by themselves—a few great artists, a few great scientists, a few great athletes. Most people work with others and are effective with other people. That is true whether they are members of an organization or independently employed. Managing yourself requires taking responsibility for relationships. This has two parts.

The first is to accept the fact that other people are as much individuals as you yourself are. They perversely insist on behaving like human beings. This means that they too have their strengths; they too have their ways of getting things done; they too have their values. To be effective, therefore, you have to know the strengths, the performance modes, and the values of your coworkers.

That sounds obvious, but few people pay attention to it. Typical is the person who was trained to write reports in his or her first assignment because that boss was a reader. Even if the next boss is a listener, the person goes on writing reports that, invariably, produce no results. Invariably the boss will think the employee is stupid, incompetent, and lazy, and he or she will fail. But that could have been avoided if the employee had only looked at the new boss and analyzed how *this* boss performs.

Bosses are neither a title on the organization chart nor a “function.” They are individuals and are entitled to do their work in the way they do it best. It is incumbent on the people who work with them to observe them, to find out how they work, and to adapt themselves to what makes their bosses most effective. This, in fact, is the secret of “managing” the boss.

The same holds true for all your coworkers. Each works his or her way, not your way. And each is entitled to work in his or her way. What matters is whether they perform and what their values are. As for how they perform—each is likely to do it differently. The first secret of effectiveness is to understand the people you work with and depend on so that you can make use of their strengths, their ways of working, and their values. Working relationships are as much based on the people as they are on the work.

The second part of relationship responsibility is taking responsibility for communication. Whenever I, or any other consultant, start to work with an

organization, the first thing I hear about are all the personality conflicts. Most of these arise from the fact that people do not know what other people are doing and how they do their work, or what contribution the other people are concentrating on and what results they expect. And the reason they do not know is that they have not asked and therefore have not been told.

This failure to ask reflects human stupidity less than it reflects human history. Until recently, it was unnecessary to tell any of these things to anybody. In the medieval city, everyone in a district plied the same trade. In the countryside, everyone in a valley planted the same crop as soon as the frost was out of the ground. Even those few people who did things that were not “common” worked alone, so they did not have to tell anyone what they were doing.

Today the great majority of people work with others who have different tasks and responsibilities. The marketing vice president may have come out of sales and know everything about sales, but she knows nothing about the things she has never done—pricing, advertising, packaging, and the like. So the people who do these things must make sure that the marketing vice president understands what they are trying to do, why they are trying to do it, how they are going to do it, and what results to expect.

If the marketing vice president does not understand what these high-grade knowledge specialists are doing, it is primarily their fault, not hers. They have not educated her. Conversely, it is the marketing vice president’s responsibility to make sure that all of her coworkers understand how she looks at marketing: what her goals are, how she works, and what she expects of herself and of each one of them.

Even people who understand the importance of taking responsibility for relationships often do not communicate sufficiently with their associates. They are afraid of being thought presumptuous or inquisitive or stupid. They are wrong. Whenever someone goes to his or her associates and says, “This is what I am good at. This is how I work. These are my values. This is the contribution I plan to concentrate on and the results I should be expected to deliver,” the response is always, “This is most helpful. But why didn’t you tell me earlier?”

And one gets the same reaction—without exception, in my experience—if one continues by asking, “And what do I need to know about your strengths, how you perform, your values, and your proposed contribution?” In fact, knowledge workers should request this of everyone with whom they work,

whether as subordinate, superior, colleague, or team member. And again, whenever this is done, the reaction is always, “Thanks for asking me. But why didn’t you ask me earlier?”

Organizations are no longer built on force but on trust. The existence of trust between people does not necessarily mean that they like one another. It means that they understand one another. Taking responsibility for relationships is therefore an absolute necessity. It is a duty. Whether one is a member of the organization, a consultant to it, a supplier, or a distributor, one owes that responsibility to all one’s coworkers: those whose work one depends on as well as those who depend on one’s own work.

The Second Half of Your Life

When work for most people meant manual labor, there was no need to worry about the second half of your life. You simply kept on doing what you had always done. And if you were lucky enough to survive 40 years of hard work in the mill or on the railroad, you were quite happy to spend the rest of your life doing nothing. Today, however, most work is knowledge work, and knowledge workers are not “finished” after 40 years on the job, they are merely bored.

We hear a great deal of talk about the midlife crisis of the executive. It is mostly boredom. At 45, most executives have reached the peak of their business careers, and they know it. After 20 years of doing very much the same kind of work, they are very good at their jobs. But they are not learning or contributing or deriving challenge and satisfaction from the job. And yet they are still likely to face another 20 if not 25 years of work. That is why managing oneself increasingly leads one to begin a second career.

There are three ways to develop a second career. The first is actually to start one. Often this takes nothing more than moving from one kind of organization to another: the divisional controller in a large corporation, for instance, becomes the controller of a medium-sized hospital. But there are also growing numbers of people who move into different lines of work altogether: the business executive or government official who enters the ministry at 45, for instance; or the midlevel manager who leaves corporate life after 20 years to attend law school and become a small-town attorney.

We will see many more second careers undertaken by people who have achieved modest success in their first jobs. Such people have substantial skills, and they know how to work. They need a community—the house is empty with the children gone—and they need income as well. But above all, they need challenge.

The second way to prepare for the second half of your life is to develop a parallel career. Many people who are very successful in their first careers stay in the work they have been doing, either on a full-time or part-time or consulting basis. But in addition, they create a parallel job, usually in a nonprofit organization, that takes another ten hours of work a week. They

might take over the administration of their church, for instance, or the presidency of the local Girl Scouts council. They might run the battered women's shelter, work as a children's librarian for the local public library, sit on the school board, and so on.

Finally, there are the social entrepreneurs. These are usually people who have been very successful in their first careers. They love their work, but it no longer challenges them. In many cases they keep on doing what they have been doing all along but spend less and less of their time on it. They also start another activity, usually a nonprofit. My friend Bob Buford, for example, built a very successful television company that he still runs. But he has also founded and built a successful nonprofit organization that works with Protestant churches, and he is building another to teach social entrepreneurs how to manage their own nonprofit ventures while still running their original businesses.

People who manage the second half of their lives may always be a minority. The majority may "retire on the job" and count the years until their actual retirement. But it is this minority, the men and women who see a long working-life expectancy as an opportunity both for themselves and for society, who will become leaders and models.

There is one prerequisite for managing the second half of your life: You must begin long before you enter it. When it first became clear 30 years ago that working-life expectancies were lengthening very fast, many observers (including myself) believed that retired people would increasingly become volunteers for nonprofit institutions. That has not happened. If one does not begin to volunteer before one is 40 or so, one will not volunteer once past 60.

Similarly, all the social entrepreneurs I know began to work in their chosen second enterprise long before they reached their peak in their original business. Consider the example of a successful lawyer, the legal counsel to a large corporation, who has started a venture to establish model schools in his state. He began to do volunteer legal work for the schools when he was around 35. He was elected to the school board at age 40. At age 50, when he had amassed a fortune, he started his own enterprise to build and to run model schools. He is, however, still working nearly full-time as the lead counsel in the company he helped found as a young lawyer.

There is another reason to develop a second major interest, and to develop it early. No one can expect to live very long without experiencing a serious setback in his or her life or work. There is the competent engineer who is

passed over for promotion at age 45. There is the competent college professor who realizes at age 42 that she will never get a professorship at a big university, even though she may be fully qualified for it. There are tragedies in one's family life: the breakup of one's marriage or the loss of a child. At such times, a second major interest—not just a hobby—may make all the difference. The engineer, for example, now knows that he has not been very successful in his job. But in his outside activity—as church treasurer, for example—he is a success. One's family may break up, but in that outside activity there is still a community.

In a society in which success has become so terribly important, having options will become increasingly vital. Historically, there was no such thing as “success.” The overwhelming majority of people did not expect anything but to stay in their “proper station,” as an old English prayer has it. The only mobility was downward mobility.

In a knowledge society, however, we expect everyone to be a success. This is clearly an impossibility. For a great many people, there is at best an absence of failure. Wherever there is success, there has to be failure. And then it is vitally important for the individual, and equally for the individual's family, to have an area in which he or she can contribute, make a difference, and be *somebody*. That means finding a second area—whether in a second career, a parallel career, or a social venture—that offers an opportunity for being a leader, for being respected, for being a success.

The challenges of managing oneself may seem obvious, if not elementary. And the answers may seem self-evident to the point of appearing naïve. But managing oneself requires new and unprecedented things from the individual, and especially from the knowledge worker. In effect, managing oneself demands that each knowledge worker think and behave like a chief executive officer. Further, the shift from manual workers who do as they are told to knowledge workers who have to manage themselves profoundly challenges social structure. Every existing society, even the most individualistic one, takes two things for granted, if only subconsciously: that organizations outlive workers, and that most people stay put.

But today the opposite is true. Knowledge workers outlive organizations, and they are mobile. The need to manage oneself is therefore creating a revolution in human affairs.

What Makes a Leader?

by Daniel Goleman

EVERY BUSINESSPERSON KNOWS a story about a highly intelligent, highly skilled executive who was promoted into a leadership position only to fail at the job. And they also know a story about someone with solid—but not extraordinary—intellectual abilities and technical skills who was promoted into a similar position and then soared.

Such anecdotes support the widespread belief that identifying individuals with the “right stuff” to be leaders is more art than science. After all, the personal styles of superb leaders vary: Some leaders are subdued and analytical; others shout their manifestos from the mountaintops. And just as important, different situations call for different types of leadership. Most mergers need a sensitive negotiator at the helm, whereas many turnarounds require a more forceful authority.

I have found, however, that the most effective leaders are alike in one crucial way: They all have a high degree of what has come to be known as *emotional intelligence*. It’s not that IQ and technical skills are irrelevant. They do matter, but mainly as “threshold capabilities”; that is, they are the entry-level requirements for executive positions. But my research, along with other recent studies, clearly shows that emotional intelligence is the sine qua non of leadership. Without it, a person can have the best training in the world, an incisive, analytical mind, and an endless supply of smart ideas, but he still won’t make a great leader.

In the course of the past year, my colleagues and I have focused on how emotional intelligence operates at work. We have examined the relationship between emotional intelligence and effective performance, especially in leaders. And we have observed how emotional intelligence shows itself on the job. How can you tell if someone has high emotional intelligence, for

example, and how can you recognize it in yourself? In the following pages, we'll explore these questions, taking each of the components of emotional intelligence—self-awareness, self-regulation, motivation, empathy, and social skill—in turn.

Evaluating Emotional Intelligence

Most large companies today have employed trained psychologists to develop what are known as “competency models” to aid them in identifying, training, and promoting likely stars in the leadership firmament. The psychologists have also developed such models for lower-level positions. And in recent years, I have analyzed competency models from 188 companies, most of which were large and global and included the likes of Lucent Technologies, British Airways, and Credit Suisse.

In carrying out this work, my objective was to determine which personal capabilities drove outstanding performance within these organizations, and to what degree they did so. I grouped capabilities into three categories: purely technical skills like accounting and business planning; cognitive abilities like analytical reasoning; and competencies demonstrating emotional intelligence, such as the ability to work with others and effectiveness in leading change.

Idea in Brief

What distinguishes great leaders from merely good ones? It isn't IQ or technical skills, says Daniel Goleman. It's **emotional intelligence**: a group of five skills that enable the best leaders to maximize their own *and* their followers' performance. When senior managers at one company had a critical mass of EI capabilities, their divisions outperformed yearly earnings goals by 20%.

The EI skills are:

- *Self-awareness*—knowing one's strengths, weaknesses, drives, values, and impact on others
- *Self-regulation*—controlling or redirecting disruptive impulses and moods
- *Motivation*—relishing achievement for its own sake
- *Empathy*—understanding other people's emotional makeup
- *Social skill*—building rapport with others to move them in desired directions

We're each born with certain levels of EI skills. But we can strengthen these abilities through persistence, practice, and feedback from colleagues or coaches.

To create some of the competency models, psychologists asked senior managers at the companies to identify the capabilities that typified the organization's most outstanding leaders. To create other models, the psychologists used objective criteria, such as a division's profitability, to differentiate the star performers at senior levels within their organizations from the average ones. Those individuals were then extensively interviewed and tested, and their capabilities were compared. This process resulted in the creation of lists of ingredients for highly effective leaders. The lists ranged in length from seven to 15 items and included such ingredients as initiative and strategic vision.

When I analyzed all this data, I found dramatic results. To be sure, intellect was a driver of outstanding performance. Cognitive skills such as big-picture thinking and long-term vision were particularly important. But when I calculated the ratio of technical skills, IQ, and emotional intelligence as ingredients of excellent performance, emotional intelligence proved to be twice as important as the others for jobs at all levels.

Moreover, my analysis showed that emotional intelligence played an increasingly important role at the highest levels of the company, where differences in technical skills are of negligible importance. In other words, the higher the rank of a person considered to be a star performer, the more emotional intelligence capabilities showed up as the reason for his or her effectiveness. When I compared star performers with average ones in senior leadership positions, nearly 90% of the difference in their profiles was attributable to emotional intelligence factors rather than cognitive abilities.

Idea in Practice

Understanding EI'S Components

EI Component	Definition	Hallmarks	Example
Self-	Knowing	• Self-	A manager

awareness	one's emotions, strengths, weaknesses, drives, values, and goals—and their impact on others	confidence • Realistic self-assessment • Self-deprecating sense of humor • Thirst for constructive criticism	knows tight deadlines bring out the worst in him. So he plans his time to get work done well in advance.
Self-regulation	Controlling or redirecting disruptive emotions and impulses	• Trustworthiness • Integrity • Comfort with ambiguity and change	When a team botches a presentation, its leader resists the urge to scream. Instead, she considers possible reasons for the failure, explains the consequences to her team, and explores solutions with them.
Motivation	Being driven to achieve for the sake of achievement	• A passion for the work itself and for new challenges	A portfolio manager at an investment company sees his fund tumble for three

		• Unflagging energy to improve • Optimism in the face of failure	consecutive quarters. Major clients defect. Instead of blaming external circumstances, she decides to learn from the experience—and engineers a turnaround.
Empathy	Considering others' feelings, especially when making decisions	• Expertise in attracting and retaining talent • Ability to develop others • Sensitivity to cross-cultural differences	An American consultant and her team pitch a project to a potential client in Japan. Her team interprets the client's silence as disapproval, and prepares to leave. The consultant reads the client's body language and senses interest. She continues the meeting, and her team gets the job.
Social Skill	Managing relationships	•	A manager wants his

	to move people in desired directions	Effectiveness in leading change • Persuasiveness • Extensive networking • Expertise in building and leading teams	company to adopt a better Internet strategy. He finds kindred spirits and assembles a de facto team to create a prototype Web site. He persuades allies in other divisions to fund the company's participation in a relevant convention. His company forms an Internet division—and puts him in charge of it.

Strengthening Your EI

Use practice and feedback from others to strengthen specific EI skills.

Example: An executive learned from others that she lacked empathy, especially the ability to listen. She wanted to fix the problem, so she asked a coach to tell her when she exhibited poor listening skills. She then role-played incidents to practice giving better responses; for example, not interrupting. She also began observing executives skilled at listening-and imitated their behavior.

The five components of emotional intelligence at work

	Definition	Hallmarks
Self-awareness	The ability to recognize and understand your moods, emotions, and drives, as well as their effect on others	Self-confidence Realistic self-assessment Self-deprecating sense of humor
Self-Regulation	The ability to control or redirect disruptive impulses and moods The propensity to suspend judgment—to think before acting	Trustworthiness and integrity Comfort with ambiguity Openness to change
Motivation	A passion to work for reasons that go beyond money or status A propensity to pursue goals with energy and persistence	Strong drive to achieve Optimism, even in the face of failure Organizational commitment
Empathy	The ability to understand the emotional makeup of other people Skill in treating people according to their emotional reactions	Expertise in building and retaining talent Cross-cultural sensitivity Service to clients and customers
Social Skill	Proficiency in managing relationships and building networks An ability to find common ground and build rapport	Effectiveness in leading change Persuasiveness Expertise in building and leading teams

Other researchers have confirmed that emotional intelligence not only distinguishes outstanding leaders but can also be linked to strong performance. The findings of the late David McClelland, the renowned researcher in human and organizational behavior, are a good example. In a 1996 study of a global food and beverage company, McClelland found that when senior managers had a critical mass of emotional intelligence capabilities, their divisions outperformed yearly earnings goals by 20%. Meanwhile, division leaders without that critical mass underperformed by almost the same amount. McClelland's findings, interestingly, held as true in the company's U.S. divisions as in its divisions in Asia and Europe.

In short, the numbers are beginning to tell us a persuasive story about the link between a company's success and the emotional intelligence of its leaders. And just as important, research is also demonstrating that people can, if they take the right approach, develop their emotional intelligence. (See the sidebar "Can Emotional Intelligence Be Learned?")

Self-Awareness

Self-awareness is the first component of emotional intelligence—which makes sense when one considers that the Delphic oracle gave the advice to “know thyself” thousands of years ago. Self-awareness means having a deep understanding of one’s emotions, strengths, weaknesses, needs, and drives. People with strong self-awareness are neither overly critical nor unrealistically hopeful. Rather, they are honest—with themselves and with others.

People who have a high degree of self-awareness recognize how their feelings affect them, other people, and their job performance. Thus, a self-aware person who knows that tight deadlines bring out the worst in him plans his time carefully and gets his work done well in advance. Another person with high self-awareness will be able to work with a demanding client. She will understand the client’s impact on her moods and the deeper reasons for her frustration. “Their trivial demands take us away from the real work that needs to be done,” she might explain. And she will go one step further and turn her anger into something constructive.

Can Emotional Intelligence Be Learned?

FOR AGES, PEOPLE HAVE DEBATED if leaders are born or made. So too goes the debate about emotional intelligence. Are people born with certain levels of empathy, for example, or do they acquire empathy as a result of life’s experiences? The answer is both. Scientific inquiry strongly suggests that there is a genetic component to emotional intelligence. Psychological and developmental research indicates that nurture plays a role as well. How much of each perhaps will never be known, but research and practice clearly demonstrate that emotional intelligence can be learned.

One thing is certain: Emotional intelligence increases with age. There is an old-fashioned word for the phenomenon: maturity. Yet even with maturity, some people still need training to enhance their emotional intelligence. Unfortunately, far too many training programs that intend to build leadership skills—including emotional intelligence—are a waste of time and money. The problem is simple: They focus on the wrong part of the brain.

Emotional intelligence is born largely in the neurotransmitters of the brain’s limbic

system, which governs feelings, impulses, and drives. Research indicates that the limbic system learns best through motivation, extended practice, and feedback. Compare this with the kind of learning that goes on in the neocortex, which governs analytical and technical ability. The neocortex grasps concepts and logic. It is the part of the brain that figures out how to use a computer or make a sales call by reading a book. Not surprisingly—but mistakenly—it is also the part of the brain targeted by most training programs aimed at enhancing emotional intelligence. When such programs take, in effect, a neocortical approach, my research with the Consortium for Research on Emotional Intelligence in Organizations has shown they can even have a *negative* impact on people's job performance.

To enhance emotional intelligence, organizations must refocus their training to include the limbic system. They must help people break old behavioral habits and establish new ones. That not only takes much more time than conventional training programs, it also requires an individualized approach.

Imagine an executive who is thought to be low on empathy by her colleagues. Part of that deficit shows itself as an inability to listen; she interrupts people and doesn't pay close attention to what they're saying. To fix the problem, the executive needs to be motivated to change, and then she needs practice and feedback from others in the company. A colleague or coach could be tapped to let the executive know when she has been observed failing to listen. She would then have to replay the incident and give a better response; that is, demonstrate her ability to absorb what others are saying. And the executive could be directed to observe certain executives who listen well and to mimic their behavior.

With persistence and practice, such a process can lead to lasting results. I know one Wall Street executive who sought to improve his empathy—specifically his ability to read people's reactions and see their perspectives. Before beginning his quest, the executive's subordinates were terrified of working with him. People even went so far as to hide bad news from him. Naturally, he was shocked when finally confronted with these facts. He went home and told his family—but they only confirmed what he had heard at work. When their opinions on any given subject did not mesh with his, they, too, were frightened of him.

Enlisting the help of a coach, the executive went to work to heighten his empathy through practice and feedback. His first step was to take a vacation to a foreign country where he did not speak the language. While there, he monitored his reactions to the unfamiliar and his openness to people who were different from him. When he returned home, humbled by his week abroad, the executive asked his coach to shadow him for parts of the day, several times a week, to critique how he treated people with new or different perspectives. At the same time, he consciously used on-the-job interactions as opportunities to practice "hearing" ideas that differed from his. Finally, the executive had himself videotaped in meetings and asked those who worked for and with him to critique his ability to acknowledge and understand the feelings of others. It took several months, but the executive's emotional intelligence did ultimately rise, and the improvement was reflected in his overall performance on the job.

It's important to emphasize that building one's emotional intelligence cannot—will not—

happen without sincere desire and concerted effort. A brief seminar won't help; nor can one buy a how-to manual. It is much harder to learn to empathize—to internalize empathy as a natural response to people—than it is to become adept at regression analysis. But it can be done. “Nothing great was ever achieved without enthusiasm,” wrote Ralph Waldo Emerson. If your goal is to become a real leader, these words can serve as a guidepost in your efforts to develop high emotional intelligence.

Self-awareness extends to a person's understanding of his or her values and goals. Someone who is highly self-aware knows where he is headed and why; so, for example, he will be able to be firm in turning down a job offer that is tempting financially but does not fit with his principles or long-term goals. A person who lacks self-awareness is apt to make decisions that bring on inner turmoil by treading on buried values. “The money looked good so I signed on,” someone might say two years into a job, “but the work means so little to me that I'm constantly bored.” The decisions of self-aware people mesh with their values; consequently, they often find work to be energizing.

How can one recognize self-awareness? First and foremost, it shows itself as candor and an ability to assess oneself realistically. People with high self-awareness are able to speak accurately and openly—although not necessarily effusively or confessionally—about their emotions and the impact they have on their work. For instance, one manager I know of was skeptical about a new personal-shopper service that her company, a major department-store chain, was about to introduce. Without prompting from her team or her boss, she offered them an explanation: “It's hard for me to get behind the rollout of this service,” she admitted, “because I really wanted to run the project, but I wasn't selected. Bear with me while I deal with that.” The manager did indeed examine her feelings; a week later, she was supporting the project fully.

Such self-knowledge often shows itself in the hiring process. Ask a candidate to describe a time he got carried away by his feelings and did something he later regretted. Self-aware candidates will be frank in admitting to failure—and will often tell their tales with a smile. One of the hallmarks of self-awareness is a self-deprecating sense of humor.

Self-awareness can also be identified during performance reviews. Self-aware people know—and are comfortable talking about—their limitations and strengths, and they often demonstrate a thirst for constructive criticism. By contrast, people with low self-awareness interpret the message that they need to improve as a threat or a sign of failure.

Self-aware people can also be recognized by their self-confidence. They have a firm grasp of their capabilities and are less likely to set themselves up to fail by, for example, overstretching on assignments. They know, too, when to ask for help. And the risks they take on the job are calculated. They won't ask for a challenge that they know they can't handle alone. They'll play to their strengths.

Consider the actions of a midlevel employee who was invited to sit in on a strategy meeting with her company's top executives. Although she was the most junior person in the room, she did not sit there quietly, listening in awestruck or fearful silence. She knew she had a head for clear logic and the skill to present ideas persuasively, and she offered cogent suggestions about the company's strategy. At the same time, her self-awareness stopped her from wandering into territory where she knew she was weak.

Despite the value of having self-aware people in the workplace, my research indicates that senior executives don't often give self-awareness the credit it deserves when they look for potential leaders. Many executives mistake candor about feelings for "wimpiness" and fail to give due respect to employees who openly acknowledge their shortcomings. Such people are too readily dismissed as "not tough enough" to lead others.

In fact, the opposite is true. In the first place, people generally admire and respect candor. Furthermore, leaders are constantly required to make judgment calls that require a candid assessment of capabilities—their own and those of others. Do we have the management expertise to acquire a competitor? Can we launch a new product within six months? People who assess themselves honestly—that is, self-aware people—are well suited to do the same for the organizations they run.

Self-Regulation

Biological impulses drive our emotions. We cannot do away with them—but we can do much to manage them. Self-regulation, which is like an ongoing inner conversation, is the component of emotional intelligence that frees us from being prisoners of our feelings. People engaged in such a conversation feel bad moods and emotional impulses just as everyone else does, but they find ways to control them and even to channel them in useful ways.

Imagine an executive who has just watched a team of his employees present a botched analysis to the company's board of directors. In the gloom that follows, the executive might find himself tempted to pound on the table in anger or kick over a chair. He could leap up and scream at the group. Or he might maintain a grim silence, glaring at everyone before stalking off.

But if he had a gift for self-regulation, he would choose a different approach. He would pick his words carefully, acknowledging the team's poor performance without rushing to any hasty judgment. He would then step back to consider the reasons for the failure. Are they personal—a lack of effort? Are there any mitigating factors? What was his role in the debacle? After considering these questions, he would call the team together, lay out the incident's consequences, and offer his feelings about it. He would then present his analysis of the problem and a well-considered solution.

Why does self-regulation matter so much for leaders? First of all, people who are in control of their feelings and impulses—that is, people who are reasonable—are able to create an environment of trust and fairness. In such an environment, politics and infighting are sharply reduced and productivity is high. Talented people flock to the organization and aren't tempted to leave. And self-regulation has a trickle-down effect. No one wants to be known as a hothead when the boss is known for her calm approach. Fewer bad moods at the top mean fewer throughout the organization.

Second, self-regulation is important for competitive reasons. Everyone knows that business today is rife with ambiguity and change. Companies merge and break apart regularly. Technology transforms work at a dizzying pace. People who have mastered their emotions are able to roll with the changes. When a new program is announced, they don't panic; instead, they

are able to suspend judgment, seek out information, and listen to the executives as they explain the new program. As the initiative moves forward, these people are able to move with it.

Sometimes they even lead the way. Consider the case of a manager at a large manufacturing company. Like her colleagues, she had used a certain software program for five years. The program drove how she collected and reported data and how she thought about the company's strategy. One day, senior executives announced that a new program was to be installed that would radically change how information was gathered and assessed within the organization. While many people in the company complained bitterly about how disruptive the change would be, the manager mulled over the reasons for the new program and was convinced of its potential to improve performance. She eagerly attended training sessions—some of her colleagues refused to do so—and was eventually promoted to run several divisions, in part because she used the new technology so effectively.

I want to push the importance of self-regulation to leadership even further and make the case that it enhances integrity, which is not only a personal virtue but also an organizational strength. Many of the bad things that happen in companies are a function of impulsive behavior. People rarely plan to exaggerate profits, pad expense accounts, dip into the till, or abuse power for selfish ends. Instead, an opportunity presents itself, and people with low impulse control just say yes.

By contrast, consider the behavior of the senior executive at a large food company. The executive was scrupulously honest in his negotiations with local distributors. He would routinely lay out his cost structure in detail, thereby giving the distributors a realistic understanding of the company's pricing. This approach meant the executive couldn't always drive a hard bargain. Now, on occasion, he felt the urge to increase profits by withholding information about the company's costs. But he challenged that impulse—he saw that it made more sense in the long run to counteract it. His emotional self-regulation paid off in strong, lasting relationships with distributors that benefited the company more than any short-term financial gains would have.

The signs of emotional self-regulation, therefore, are easy to see: a propensity for reflection and thoughtfulness; comfort with ambiguity and change; and integrity—an ability to say no to impulsive urges.

Like self-awareness, self-regulation often does not get its due. People who can master their emotions are sometimes seen as cold fish—their considered

responses are taken as a lack of passion. People with fiery temperaments are frequently thought of as “classic” leaders—their outbursts are considered hallmarks of charisma and power. But when such people make it to the top, their impulsiveness often works against them. In my research, extreme displays of negative emotion have never emerged as a driver of good leadership.

Motivation

If there is one trait that virtually all effective leaders have, it is motivation. They are driven to achieve beyond expectations—their own and everyone else's. The key word here is *achieve*. Plenty of people are motivated by external factors, such as a big salary or the status that comes from having an impressive title or being part of a prestigious company. By contrast, those with leadership potential are motivated by a deeply embedded desire to achieve for the sake of achievement.

If you are looking for leaders, how can you identify people who are motivated by the drive to achieve rather than by external rewards? The first sign is a passion for the work itself—such people seek out creative challenges, love to learn, and take great pride in a job well done. They also display an unflagging energy to do things better. People with such energy often seem restless with the status quo. They are persistent with their questions about why things are done one way rather than another; they are eager to explore new approaches to their work.

A cosmetics company manager, for example, was frustrated that he had to wait two weeks to get sales results from people in the field. He finally tracked down an automated phone system that would beep each of his salespeople at 5 pm every day. An automated message then prompted them to punch in their numbers—how many calls and sales they had made that day. The system shortened the feedback time on sales results from weeks to hours.

That story illustrates two other common traits of people who are driven to achieve. They are forever raising the performance bar, and they like to keep score. Take the performance bar first. During performance reviews, people with high levels of motivation might ask to be “stretched” by their superiors. Of course, an employee who combines self-awareness with internal motivation will recognize her limits—but she won't settle for objectives that seem too easy to fulfill.

And it follows naturally that people who are driven to do better also want a way of tracking progress—their own, their team's, and their company's. Whereas people with low achievement motivation are often fuzzy about results, those with high achievement motivation often keep score by tracking

such hard measures as profitability or market share. I know of a money manager who starts and ends his day on the Internet, gauging the performance of his stock fund against four industry-set benchmarks.

Interestingly, people with high motivation remain optimistic even when the score is against them. In such cases, self-regulation combines with achievement motivation to overcome the frustration and depression that come after a setback or failure. Take the case of another portfolio manager at a large investment company. After several successful years, her fund tumbled for three consecutive quarters, leading three large institutional clients to shift their business elsewhere.

Some executives would have blamed the nosedive on circumstances outside their control; others might have seen the setback as evidence of personal failure. This portfolio manager, however, saw an opportunity to prove she could lead a turnaround. Two years later, when she was promoted to a very senior level in the company, she described the experience as “the best thing that ever happened to me; I learned so much from it.”

Executives trying to recognize high levels of achievement motivation in their people can look for one last piece of evidence: commitment to the organization. When people love their jobs for the work itself, they often feel committed to the organizations that make that work possible. Committed employees are likely to stay with an organization even when they are pursued by headhunters waving money.

It's not difficult to understand how and why a motivation to achieve translates into strong leadership. If you set the performance bar high for yourself, you will do the same for the organization when you are in a position to do so. Likewise, a drive to surpass goals and an interest in keeping score can be contagious. Leaders with these traits can often build a team of managers around them with the same traits. And of course, optimism and organizational commitment are fundamental to leadership—just try to imagine running a company without them.

Empathy

Of all the dimensions of emotional intelligence, empathy is the most easily recognized. We have all felt the empathy of a sensitive teacher or friend; we have all been struck by its absence in an unfeeling coach or boss. But when it comes to business, we rarely hear people praised, let alone rewarded, for their empathy. The very word seems unbusinesslike, out of place amid the tough realities of the marketplace.

But empathy doesn't mean a kind of "I'm OK, you're OK" mushiness. For a leader, that is, it doesn't mean adopting other people's emotions as one's own and trying to please everybody. That would be a nightmare—it would make action impossible. Rather, empathy means thoughtfully considering employees' feelings—along with other factors—in the process of making intelligent decisions.

For an example of empathy in action, consider what happened when two giant brokerage companies merged, creating redundant jobs in all their divisions. One division manager called his people together and gave a gloomy speech that emphasized the number of people who would soon be fired. The manager of another division gave his people a different kind of speech. He was up-front about his own worry and confusion, and he promised to keep people informed and to treat everyone fairly.

The difference between these two managers was empathy. The first manager was too worried about his own fate to consider the feelings of his anxiety-stricken colleagues. The second knew intuitively what his people were feeling, and he acknowledged their fears with his words. Is it any surprise that the first manager saw his division sink as many demoralized people, especially the most talented, departed? By contrast, the second manager continued to be a strong leader, his best people stayed, and his division remained as productive as ever.

Empathy is particularly important today as a component of leadership for at least three reasons: the increasing use of teams; the rapid pace of globalization; and the growing need to retain talent.

Consider the challenge of leading a team. As anyone who has ever been a part of one can attest, teams are cauldrons of bubbling emotions. They are

often charged with reaching a consensus—which is hard enough with two people and much more difficult as the numbers increase. Even in groups with as few as four or five members, alliances form and clashing agendas get set. A team's leader must be able to sense and understand the viewpoints of everyone around the table.

That's exactly what a marketing manager at a large information technology company was able to do when she was appointed to lead a troubled team. The group was in turmoil, overloaded by work and missing deadlines. Tensions were high among the members. Tinkering with procedures was not enough to bring the group together and make it an effective part of the company.

So the manager took several steps. In a series of one-on-one sessions, she took the time to listen to everyone in the group—what was frustrating them, how they rated their colleagues, whether they felt they had been ignored. And then she directed the team in a way that brought it together: She encouraged people to speak more openly about their frustrations, and she helped people raise constructive complaints during meetings. In short, her empathy allowed her to understand her team's emotional makeup. The result was not just heightened collaboration among members but also added business, as the team was called on for help by a wider range of internal clients.

Globalization is another reason for the rising importance of empathy for business leaders. Cross-cultural dialogue can easily lead to miscues and misunderstandings. Empathy is an antidote. People who have it are attuned to subtleties in body language; they can hear the message beneath the words being spoken. Beyond that, they have a deep understanding of both the existence and the importance of cultural and ethnic differences.

Consider the case of an American consultant whose team had just pitched a project to a potential Japanese client. In its dealings with Americans, the team was accustomed to being bombarded with questions after such a proposal, but this time it was greeted with a long silence. Other members of the team, taking the silence as disapproval, were ready to pack and leave. The lead consultant gestured them to stop. Although he was not particularly familiar with Japanese culture, he read the client's face and posture and sensed not rejection but interest—even deep consideration. He was right: When the client finally spoke, it was to give the consulting firm the job.

Finally, empathy plays a key role in the retention of talent, particularly in today's information economy. Leaders have always needed empathy to

develop and keep good people, but today the stakes are higher. When good people leave, they take the company's knowledge with them.

That's where coaching and mentoring come in. It has repeatedly been shown that coaching and mentoring pay off not just in better performance but also in increased job satisfaction and decreased turnover. But what makes coaching and mentoring work best is the nature of the relationship. Outstanding coaches and mentors get inside the heads of the people they are helping. They sense how to give effective feedback. They know when to push for better performance and when to hold back. In the way they motivate their protégés, they demonstrate empathy in action.

In what is probably sounding like a refrain, let me repeat that empathy doesn't get much respect in business. People wonder how leaders can make hard decisions if they are "feeling" for all the people who will be affected. But leaders with empathy do more than sympathize with people around them: They use their knowledge to improve their companies in subtle but important ways.

Social Skill

The first three components of emotional intelligence are self- management skills. The last two, empathy and social skill, concern a person's ability to manage relationships with others. As a component of emotional intelligence, social skill is not as simple as it sounds. It's not just a matter of friendliness, although people with high levels of social skill are rarely mean-spirited. Social skill, rather, is friendliness with a purpose: moving people in the direction you desire, whether that's agreement on a new marketing strategy or enthusiasm about a new product.

Socially skilled people tend to have a wide circle of acquaintances, and they have a knack for finding common ground with people of all kinds—a knack for building rapport. That doesn't mean they socialize continually; it means they work according to the assumption that nothing important gets done alone. Such people have a network in place when the time for action comes.

Social skill is the culmination of the other dimensions of emotional intelligence. People tend to be very effective at managing relationships when they can understand and control their own emotions and can empathize with the feelings of others. Even motivation contributes to social skill. Remember that people who are driven to achieve tend to be optimistic, even in the face of setbacks or failure. When people are upbeat, their “glow” is cast upon conversations and other social encounters. They are popular, and for good reason.

Because it is the outcome of the other dimensions of emotional intelligence, social skill is recognizable on the job in many ways that will by now sound familiar. Socially skilled people, for instance, are adept at managing teams—that's their empathy at work. Likewise, they are expert persuaders—a manifestation of self-awareness, self-regulation, and empathy combined. Given those skills, good persuaders know when to make an emotional plea, for instance, and when an appeal to reason will work better. And motivation, when publicly visible, makes such people excellent collaborators; their passion for the work spreads to others, and they are driven to find solutions.

But sometimes social skill shows itself in ways the other emotional intelligence components do not. For instance, socially skilled people may at times appear not to be working while at work. They seem to be idly schmoozing—chatting in the hallways with colleagues or joking around with people who are not even connected to their “real” jobs. Socially skilled people, however, don’t think it makes sense to arbitrarily limit the scope of their relationships. They build bonds widely because they know that in these fluid times, they may need help someday from people they are just getting to know today.

For example, consider the case of an executive in the strategy department of a global computer manufacturer. By 1993, he was convinced that the company’s future lay with the Internet. Over the course of the next year, he found kindred spirits and used his social skill to stitch together a virtual community that cut across levels, divisions, and nations. He then used this de facto team to put up a corporate Web site, among the first by a major company. And, on his own initiative, with no budget or formal status, he signed up the company to participate in an annual Internet industry convention. Calling on his allies and persuading various divisions to donate funds, he recruited more than 50 people from a dozen different units to represent the company at the convention.

Management took notice: Within a year of the conference, the executive’s team formed the basis for the company’s first Internet division, and he was formally put in charge of it. To get there, the executive had ignored conventional boundaries, forging and maintaining connections with people in every corner of the organization.

Is social skill considered a key leadership capability in most companies? The answer is yes, especially when compared with the other components of emotional intelligence. People seem to know intuitively that leaders need to manage relationships effectively; no leader is an island. After all, the leader’s task is to get work done through other people, and social skill makes that possible. A leader who cannot express her empathy may as well not have it at all. And a leader’s motivation will be useless if he cannot communicate his passion to the organization. Social skill allows leaders to put their emotional intelligence to work.

It would be foolish to assert that good-old-fashioned IQ and technical ability are not important ingredients in strong leadership. But the recipe would not be complete without emotional intelligence. It was once thought

that the components of emotional intelligence were “nice to have” in business leaders. But now we know that, for the sake of performance, these are ingredients that leaders “need to have.”

It is fortunate, then, that emotional intelligence can be learned. The process is not easy. It takes time and, most of all, commitment. But the benefits that come from having a well-developed emotional intelligence, both for the individual and for the organization, make it worth the effort.

Originally published in June 1996. Reprint R0401H

Putting the Balanced Scorecard to Work

by Robert S. Kaplan and David P. Norton

TODAY'S MANAGERS RECOGNIZE the impact that measures have on performance. But they rarely think of measurement as an essential part of their strategy. For example, executives may introduce new strategies and innovative operating processes intended to achieve breakthrough performance, then continue to use the same short-term financial indicators they have used for decades, measures like return-on-investment, sales growth, and operating income. These managers fail not only to introduce new measures to monitor new goals and processes but also to question whether or not their old measures are relevant to the new initiatives.

Effective measurement, however, must be an integral part of the management process. The balanced scorecard, first proposed in the January–February 1992 issue of HBR (“The Balanced Scorecard—Measures that Drive Performance”), provides executives with a comprehensive framework that translates a company’s strategic objectives into a coherent set of performance measures. Much more than a measurement exercise, the balanced scorecard is a management system that can motivate breakthrough improvements in such critical areas as product, process, customer, and market development.

The scorecard presents managers with four different perspectives from which to choose measures. It complements traditional financial indicators with measures of performance for customers, internal processes, and innovation and improvement activities. These measures differ from those traditionally used by companies in a few important ways:

Clearly, many companies already have myriad operational and physical measures for local activities. But these local measures are bottom-up and derived from ad hoc processes. The scorecard’s measures, on the other hand,

are grounded in an organization's strategic objectives and competitive demands. And, by requiring managers to select a limited number of critical indicators within each of the four perspectives, the scorecard helps focus this strategic vision.

In addition, while traditional financial measures report on what happened last period without indicating how managers can improve performance in the next, the scorecard functions as the cornerstone of a company's current *and* future success.

Moreover, unlike conventional metrics, the information from the four perspectives provides balance between external measures like operating income and internal measures like new product development. This balanced set of measures both reveals the trade-offs that managers have already made among performance measures and encourages them to achieve their goals in the future without making trade-offs among key success factors.

Finally, many companies that are now attempting to implement local improvement programs such as process reengineering, total quality, and employee empowerment lack a sense of integration. The balanced scorecard can serve as the focal point for the organization's efforts, defining and communicating priorities to managers, employees, investors, even customers. As a senior executive at one major company said, "Previously, the one-year budget was our primary management planning device. The balanced scorecard is now used as the language, the benchmark against which all new projects and businesses are evaluated."

The balanced scorecard is not a template that can be applied to businesses in general or even industrywide. Different market situations, product strategies, and competitive environments require different scorecards. Business units devise customized scorecards to fit their mission, strategy, technology, and culture. In fact, a critical test of a scorecard's success is its transparency: from the 15 to 20 scorecard measures, an observer should be able to see through to the business unit's competitive strategy. A few examples will illustrate how the scorecard uniquely combines management and measurement in different companies.

Idea in Brief

What makes a balanced scorecard special? Four characteristics stand out:

1. **It is a top-down reflection of the company's mission and strategy.** By contrast, the measures most companies track are bottom-up: deriving from local activities or ad hoc processes, they are often irrelevant to the overall strategy.
2. **It is forward-looking.** It addresses current and future success. Traditional financial measures describe how the company performed during the last reporting period—without indicating how managers can improve performance during the next.
3. **It integrates external and internal measures.** This helps managers see where they have made trade-offs between performance measures in the past and helps ensure that future success on one measure does not come at the expense of another.
4. **It helps you focus.** Many companies track more measures than they can possibly use. But a balanced scorecard requires managers to reach agreement on only those measures that are most critical to the success of the company's strategy. Fifteen to twenty distinct measures are usually enough, each measure custom-designed for the unit to which it applies.

Rockwater: Responding to a Changing Industry

Rockwater, a wholly owned subsidiary of Brown & Root/Halliburton, a global engineering and construction company, is a worldwide leader in underwater engineering and construction. Norman Chambers, hired as CEO in late 1989, knew that the industry's competitive world had changed dramatically. "In the 1970s, we were a bunch of guys in wet suits diving off barges into the North Sea with burning torches," Chambers said. But competition in the subsea contracting business had become keener in the 1980s, and many smaller companies left the industry. In addition, the focus of competition had shifted. Several leading oil companies wanted to develop long-term partnerships with their suppliers rather than choose suppliers based on low-price competition.

Idea in Practice

Linking measurements to strategy is the heart of a successful scorecard development process. The three key questions to ask here:

1. If we succeed with our vision and strategy, how will we look different
 - to our shareholders and customers?
 - in terms of our internal processes?
 - in terms of our ability to innovate and grow?
2. What are the critical success factors in each of the four scorecard perspectives?
3. What are the key measurements that will tell us whether we're addressing those success factors as planned?

The balanced scorecard also brings an organizational focus to the variety of local change programs under way in a company at any given time. As the benchmark against which all new projects are evaluated, the scorecard functions as more than just a measurement system. In the words of FMC Corp. executive Larry Brady, it becomes "the cornerstone of the way you run the business," that is, "the

core of the management system” itself.

Example: Rockwater, an underwater engineering and construction firm, crafted a five-pronged strategy: to provide services that surpassed customers’ expectations and needs; to achieve high levels of customer satisfaction; to make continuous improvements in safety, equipment reliability, responsiveness, and cost effectiveness; to recruit and retain high-quality employees; and to realize shareholder expectations. Using the balanced scorecard, Rockwater’s senior management translated this strategy into tangible goals and actions.

- The financial measures they chose included return-on-capital employed and cash flow, because shareholders had indicated a preference for short-term results.
- Customer measures focused on those clients most interested in a high value-added relationship.
- The company introduced new benchmarks that emphasized the integration of key internal processes. It also added a safety index as a means of controlling indirect costs associated with accidents.
- Learning and growth targets emphasized the percentage of revenue coming from new services and the rate of improvement of safety and rework measures.

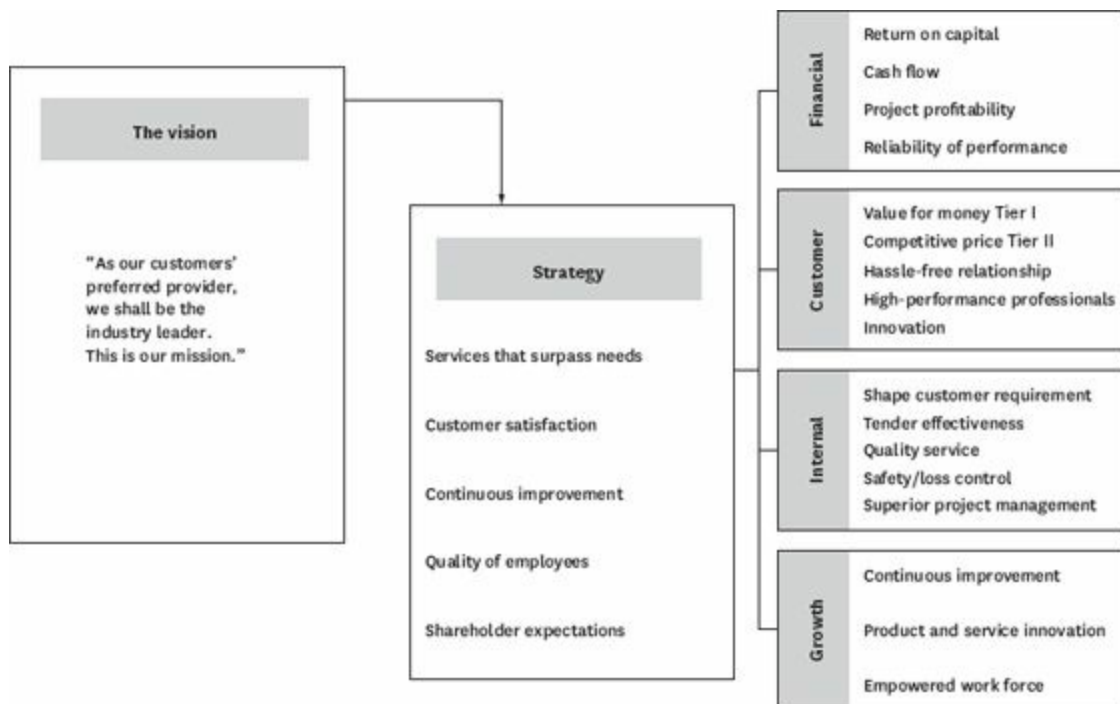
With his senior management team, Chambers developed a vision: “As our customers’ preferred provider, we shall be the industry leader in providing the highest standards of safety and quality to our clients.” He also developed a strategy to implement the vision. The five elements of that strategy were: services that surpass customers’ expectations and needs; high levels of customer satisfaction; continuous improvement of safety, equipment reliability, responsiveness, and cost effectiveness; high-quality employees; and realization of shareholder expectations. Those elements were in turn developed into strategic objectives (see the chart “Rockwater’s Strategic Objectives”). If, however, the strategic objectives were to create value for the company, they had to be translated into tangible goals and actions.

Rockwater’s senior management team transformed its vision and strategy into the balanced scorecard’s four sets of performance measures (see the chart “Rockwater’s Balanced Scorecard”).

Financial measures

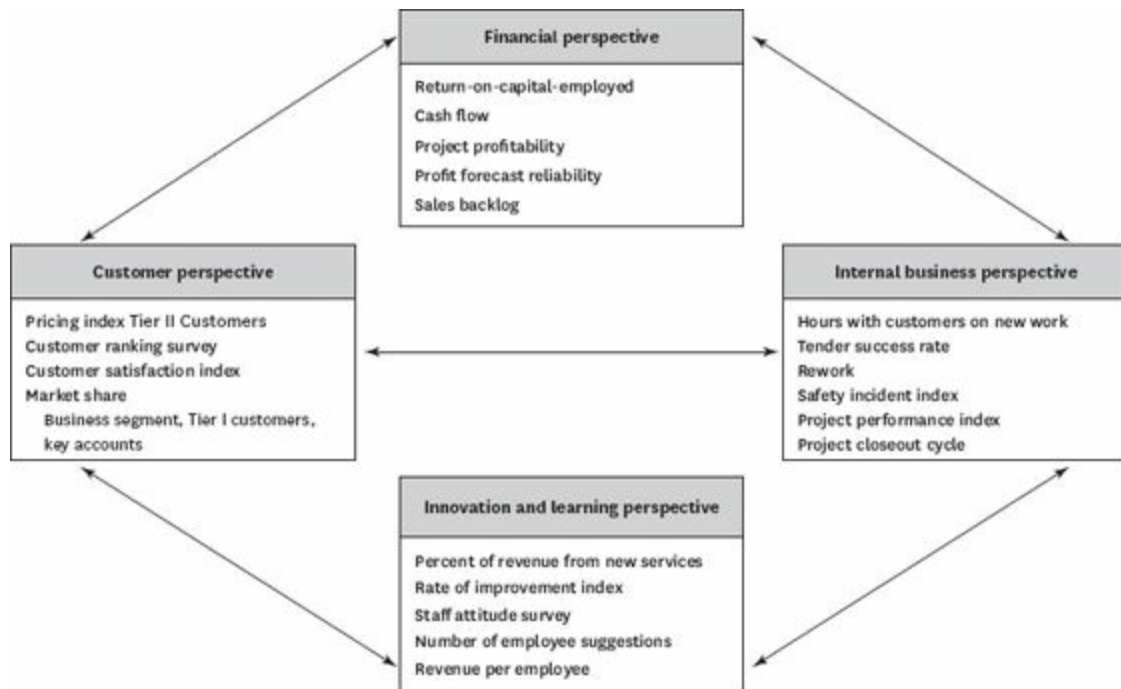
The financial perspective included three measures of importance to the shareholder. Return-on-capital-employed and cash flow reflected preferences for short-term results, while forecast reliability signaled the corporate parent's desire to reduce the historical uncertainty caused by unexpected variations in performance. Rockwater management added two financial measures. Project profitability provided focus on the project as the basic unit for planning and control, and sales backlog helped reduce uncertainty of performance.

Rockwater's strategic objectives



Rockwater's balanced scorecard

Rockwater's strategic objectives



Customer satisfaction

Rockwater wanted to recognize the distinction between its two types of customers: Tier I customers, oil companies that wanted a high value-added relationship, and Tier II customers, those that chose suppliers solely on the basis of price. A price index, incorporating the best available intelligence on competitive position, was included to ensure that Rockwater could still retain Tier II customers' business when required by competitive conditions.

The company's strategy, however, was to emphasize value-based business. An independent organization conducted an annual survey to rank customers' perceptions of Rockwater's services compared to those of its competitors. In addition, Tier I customers were asked to supply monthly satisfaction and performance ratings. Rockwater executives felt that implementing these ratings gave them a direct tie to their customers and a level of market feedback unsurpassed in most industries. Finally, market share by key accounts provided objective evidence that improvements in customer satisfaction were being translated into tangible benefits.

Internal Processes

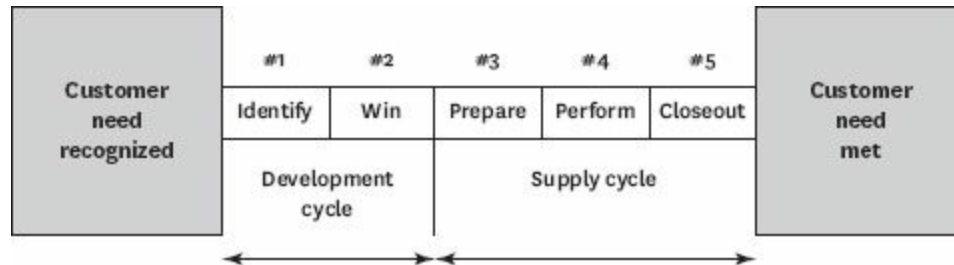
To develop measures of internal processes, Rockwater executives defined the life cycle of a project from launch (when a customer need was recognized) to completion (when the customer need had been satisfied). Measures were formulated for each of the five business-process phases in this project cycle (see the chart “How Rockwater Fulfills Customer Needs”):

- *Identify*: number of hours spent with prospects discussing new work;
- *Win*: tender success rate;
- *Prepare and Deliver*: project performance effectiveness index, safety/loss control, rework;
- *Closeout*: length of project closeout cycle.

The internal business measures emphasized a major shift in Rockwater’s thinking. Formerly, the company stressed performance for each functional department. The new focus emphasized measures that integrated key business processes. The development of a comprehensive and timely index of project performance effectiveness was viewed as a key core competency for the company. Rockwater felt that safety was also a major competitive factor. Internal studies had revealed that the indirect costs from an accident could be 5 to 50 times the direct costs. The scorecard included a safety index, derived from a comprehensive safety measurement system, that could identify and classify all undesired events with the potential for harm to people, property, or process.

The Rockwater team deliberated about the choice of metric for the identification stage. It recognized that hours spent with key prospects discussing new work was an input or process measure rather than an output measure. The management team wanted a metric that would clearly communicate to all members of the organization the importance of building relationships with and satisfying customers. The team believed that spending quality time with key customers was a prerequisite for influencing results.

How Rockwater fulfills customer needs



Innovation and improvement

The innovation and learning objectives are intended to drive improvement in financial, customer, and internal process performance. At Rockwater, such improvements came from product and service innovation that would create new sources of revenue and market expansion, as well as from continuous improvement in internal work processes. The first objective was measured by percent revenue from new services and the second objective by a continuous improvement index that represented the rate of improvement of several key operational measures, such as safety and rework. But in order to drive both product/service innovation and operational improvements, a supportive climate of empowered, motivated employees was believed necessary. A staff attitude survey and a metric for the number of employee suggestions measured whether or not such a climate was being created. Finally, revenue per employee measured the outcomes of employee commitment and training programs.

The balanced scorecard has helped Rockwater's management emphasize a process view of operations, motivate its employees, and incorporate client feedback into its operations. It developed a consensus on the necessity of creating partnerships with key customers, the importance of order-of-magnitude reductions in safety-related incidents, and the need for improved management at every phase of multiyear projects. Chambers sees the scorecard as an invaluable tool to help his company ultimately achieve its mission: to be number one in the industry.

Apple Computer: Adjusting Long-Term Performance

Apple Computer developed a balanced scorecard to focus senior management on a strategy that would expand discussions beyond gross margin, return on equity, and market share. A small steering committee, intimately familiar with the deliberations and strategic thinking of Apple's Executive Management Team, chose to concentrate on measurement categories within each of the four perspectives and to select multiple measurements within each category. For the financial perspective, Apple emphasized shareholder value; for the customer perspective, market share and customer satisfaction; for the internal process perspective, core competencies; and, finally, for the innovation and improvement perspective, employee attitudes. Apple's management stressed these categories in the following order.

Customer satisfaction

Historically, Apple had been a technology- and product-focused company that competed by designing better computers. Customer satisfaction metrics are just being introduced to orient employees toward becoming a customer-driven company. J.D. Power & Associates, a customer-survey company, now works for the computer industry. However, because it recognized that its customer base was not homogeneous, Apple felt that it had to go beyond J.D. Power & Associates and develop its own independent surveys in order to track its key market segments around the world.

Core competencies

Company executives wanted employees to be highly focused on a few key competencies: for example, user-friendly interfaces, powerful software architectures, and effective distribution systems. However, senior executives recognized that measuring performance along these competency dimensions could be difficult. As a result, the company is currently experimenting with obtaining quantitative measures of these hard-to-measure competencies.

Employee commitment and alignment

Apple conducts a comprehensive employee survey in each of its organizations every two years; surveys of randomly selected employees are performed more frequently. The survey questions are concerned with how well employees understand the company's strategy as well as whether or not they are asked to deliver results that are consistent with that strategy. The results of the survey are displayed in terms of both the actual level of employee responses and the overall trend of responses.

Market share

Achieving a critical threshold of market share was important to senior management not only for the obvious sales growth benefits but also to attract and retain software developers to Apple platforms.

Shareholder value

Shareholder value is included as a performance indicator, even though this measure is a result—not a driver—of performance. The measure is included to offset the previous emphasis on gross margin and sales growth, measures that ignored the investments required today to generate growth for tomorrow. In contrast, the shareholder value metric quantifies the impact of proposed investments for business creation and development. The majority of Apple's business is organized on a functional basis—sales, product design, and worldwide manufacturing and operations—so shareholder value can be calculated only for the entire company instead of at a decentralized level. The measure, however, helps senior managers in each major organizational unit assess the impact of their activities on the entire company's valuation and evaluate new business ventures.

While these five performance indicators have only recently been developed, they have helped Apple's senior managers focus their strategy in a number of ways. First of all, the balanced scorecard at Apple serves primarily as a planning device, instead of as a control device. To put it another way, Apple uses the measures to adjust the “long wave” of corporate performance, not to drive operating changes. Moreover, the metrics at Apple, with the exception of shareholder value, can be driven both horizontally and vertically into each functional organization. Considered vertically, each individual measure can be broken down into its component parts in order to evaluate how each part contributes to the functioning of the whole. Thought of horizontally, the measures can identify how, for example, design and manufacturing contribute to an area such as customer satisfaction. In addition, Apple has found that its balanced scorecard has helped develop a language of measurable outputs for how to launch and leverage programs.

The five performance indicators at Apple are benchmarked against best-in-class organizations. Today they are used to build business plans and are incorporated into senior executives' compensation plans.

Advanced Micro Devices: Consolidating Strategic Information

Advanced Micro Devices (AMD), a semiconductor company, executed a quick and easy transition to a balanced scorecard. It already had a clearly defined mission, strategy statement, and shared understanding among senior executives about its competitive niche. It also had many performance measures from many different sources and information systems. The balanced scorecard consolidated and focused these diverse measures into a quarterly briefing book that contained seven sections: financial measures; customer-based measures, such as on-time delivery, lead time, and performance-to-schedule; measures of critical business processes in wafer fabrication, assembly and test, new product development, process technology development (e.g., submicron etching precision); and, finally, measures for corporate quality. In addition, organizational learning was measured by imposing targeted rates of improvements for key operating parameters, such as cycle time and yields by process.

At present, AMD sees its scorecard as a systematic repository for strategic information that facilitates long-term trend analysis for planning and performance evaluation.

Driving the Process of Change

The experiences of these companies and others reveal that the balanced scorecard is most successful when it is used to drive the process of change. Rockwater, for instance, came into existence after the merger of two different organizations. Employees came from different cultures, spoke different languages, and had different operating experiences and backgrounds. The balanced scorecard helped the company focus on what it had to do well in order to become the industry leader.

Building a balanced scorecard

Each organization is unique and so follows its own path for building a balanced scorecard. At Apple and AMD, for instance, a senior finance or business development executive, intimately familiar with the strategic thinking of the top management group, constructed the initial scorecard without extensive deliberations. At Rockwater, however, senior management had yet to define sharply the organization's strategy, much less the key performance levers that drive and measure the strategy's success.

Companies like Rockwater can follow a systematic development plan to create the balanced scorecard and encourage commitment to the scorecard among senior and mid-level managers. What follows is a typical project profile:

1. Preparation

The organization must first define the business unit for which a top-level scorecard is appropriate. In general, a scorecard is appropriate for a business unit that has its own customers, distribution channels, production facilities, and financial performance measures.

2. Interviews: First Round

Each senior manager in the business unit—typically between 6 and 12 executives—receives background material on the balanced scorecard as well as internal documents that describe the company's vision, mission, and strategy.

The balanced scorecard facilitator (either an outside consultant or the company

executive who organizes the effort) conducts interviews of approximately 90 minutes each with the senior managers to obtain their input on the company's strategic objectives and tentative proposals for balanced scorecard measures. The facilitator may also interview some principal shareholders to learn about their expectations for the business unit's financial performance, as well as some key customers to learn about their performance expectations for top-ranked suppliers.

3. Executive Workshop: First Round

The top management team is brought together with the facilitator to undergo the process of developing the scorecard (see the chart "Begin by Linking Measurements to Strategy"). During the workshop, the group debates the proposed mission and strategy statements until a consensus is reached. The group then moves from the mission and strategy statement to answer the question, "If I succeed with my vision and strategy, how will my performance differ for shareholders; for customers; for internal business processes; for my ability to innovate, grow, and improve?"

Videotapes of interviews with shareholder and customer representatives can be shown to provide an external perspective to the deliberations. After defining the key success factors, the group formulates a preliminary balanced scorecard containing operational measures for the strategic objectives. Frequently, the group proposes far more than four or five measures for each perspective. At this time, narrowing the choices is not critical, though straw votes can be taken to see whether or not some of the proposed measures are viewed as low priority by the group.

4. Interviews: Second Round

The facilitator reviews, consolidates, and documents the output from the executive workshop and interviews each senior executive about the tentative balanced scorecard. The facilitator also seeks opinions about issues involved in implementing the scorecard.

5. Executive Workshop: Second Round

A second workshop, involving the senior management team, their direct subordinates, and a larger number of middle managers, debates the organization's vision, strategy statements, and the tentative scorecard. The participants, working in groups, comment on the proposed measures, link the various change programs under way to the measures, and start to develop an implementation plan. At the end of the workshop, participants are asked to formulate stretch objectives for each of the proposed measures, including targeted rates of improvement.

6. Executive Workshop: Third Round

The senior executive team meets to come to a final consensus on the vision, objectives,

and measurements developed in the first two workshops; to develop stretch targets for each measure on the scorecard; and to identify preliminary action programs to achieve the targets. The team must agree on an implementation program, including communicating the scorecard to employees, integrating the scorecard into a management philosophy, and developing an information system to support the scorecard.

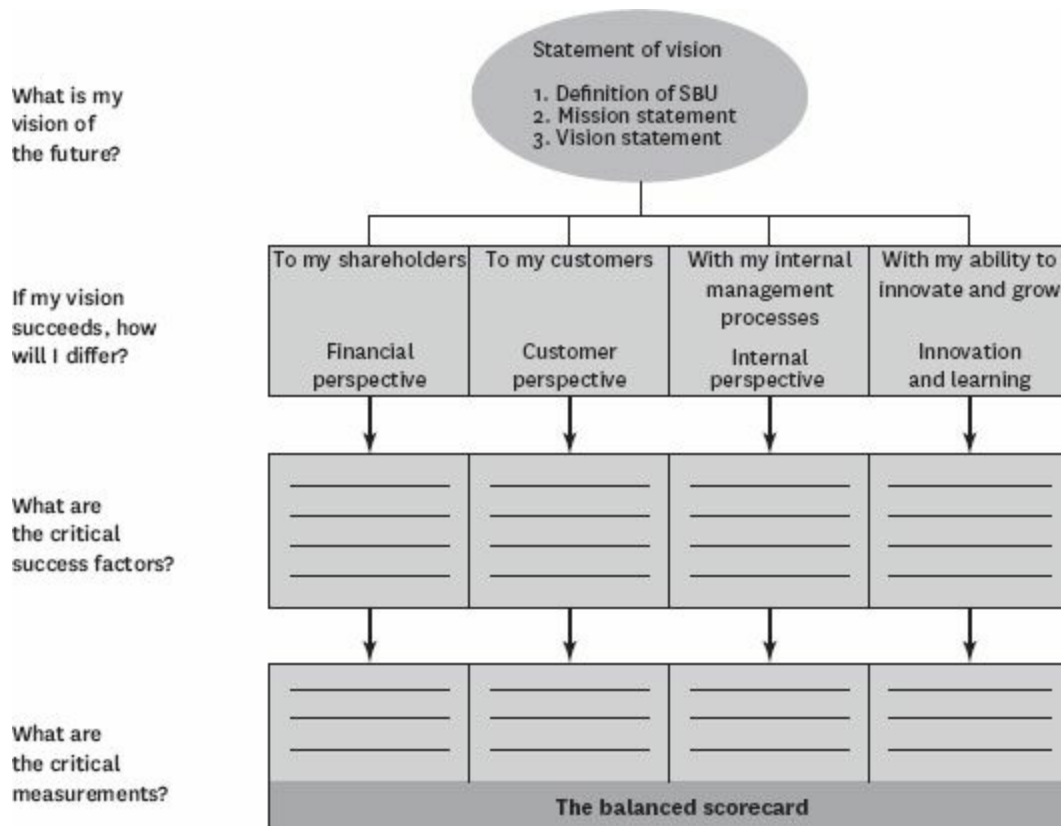
7. Implementation

A newly formed team develops an implementation plan for the scorecard, including linking the measures to databases and information systems, communicating the balanced scorecard throughout the organization, and encouraging and facilitating the development of second-level metrics for decentralized units. As a result of this process, for instance, an entirely new executive information system that links top-level business unit metrics down through shop floor and site-specific operational measures could be developed.

8. Periodic Reviews

Each quarter or month, a blue book of information on the balanced scorecard measures is prepared for both top management review and discussion with managers of decentralized divisions and departments. The balanced scorecard metrics are revisited annually as part of the strategic planning, goal setting, and resource allocation processes.

Begin by linking measurements to strategy



Similarly, Joseph De Feo, chief executive of Service Businesses, one of the three operating divisions of Barclays Bank, had to transform what had been a captive, internal supplier of services into a global competitor. The scorecard highlighted areas where, despite apparent consensus on strategy, there still was considerable disagreement about how to make the strategy operational. With the help of the scorecard, the division eventually achieved consensus concerning the highest priority areas for achievement and improvement and identified additional areas that needed attention, such as quality and productivity. De Feo assessed the impact of the scorecard, saying, “It helped us to drive major change, to become more market oriented, throughout our organization. It provided a shared understanding of our goals and what it took to achieve them.”

Analog Devices, a semiconductor company, served as the prototype for the balanced scorecard and now uses it each year to update the targets and goals for division managers. Jerry Fishman, president of Analog, said, “At

the beginning, the scorecard drove significant and considerable change. It still does when we focus attention on particular areas, such as the gross margins on new products. But its main impact today is to help sustain programs that our people have been working on for years.” Recently, the company has been attempting to integrate the scorecard metrics with *hoshin* planning, a procedure that concentrates an entire company on achieving one or two key objectives each year. Analog’s hoshin objectives have included customer service and new product development, for which measures already exist on the company’s scorecard.

But the scorecard isn’t always the impetus for such dramatic change. For example, AMD’s scorecard has yet to have a significant impact because company management didn’t use it to drive the change process. Before turning to the scorecard, senior managers had already formulated and gained consensus for the company’s mission, strategy, and key performance measures. AMD competes in a single industry segment. The top 12 managers are intimately familiar with the markets, engineering, technology, and other key levers in this segment. The summary and aggregate information in the scorecard were neither new nor surprising to them. And managers of decentralized production units also already had a significant amount of information about their own operations. The scorecard did enable them to see the breadth and totality of company operations, enhancing their ability to become better managers for the entire company. But, on balance, the scorecard could only encapsulate knowledge that managers in general had already learned.

The Scorecard’s Impact on External Reporting

SEVERAL MANAGERS HAVE ASKED whether or not the balanced scorecard is applicable to external reporting. If the scorecard is indeed a driver of long-term performance, shouldn’t this information be relevant to the investment community?

In fact, the scorecard does not translate easily to the investment community. A scorecard makes sense primarily for business units and divisions with a well-defined strategy. Most companies have several divisions, each with its own mission and strategy, whose scorecards cannot be aggregated into an overall corporate scorecard. And if the scorecard does indeed provide a transparent vision into a unit’s strategy, then the information, even the measures being used, might be highly sensitive data that could reveal much of value to competitors. But most important, as a relatively recent innovation, the scorecard would benefit from several years of experimentation within

companies before it becomes a systematic part of reporting to external constituencies.

Even if the scorecard itself were better suited to external reporting, at present the financial community itself shows little interest in making the change from financial to strategic reporting. One company president has found the outside financial community leery of the principles that ground the scorecard: "We use the scorecard more with our customers than with our investors. The financial community is skeptical about long-term indicators and occasionally tells us about some empirical evidence of a negative correlation between stock prices and attention to total quality and internal processes."

However, the investment community has begun to focus on some key metrics of new product performance. Could this be an early sign of a shift to strategic thinking?

AMD's limited success with the balanced scorecard demonstrates that the scorecard has its greatest impact when used to drive a change process. Some companies link compensation of senior executives to achieving stretch targets for the scorecard measures. Most are attempting to translate the scorecard into operational measures that become the focus for improvement activities in local units. The scorecard is not just a measurement system; it is a management system to motivate breakthrough competitive performance.

Implementing the Balanced Scorecard at FMC Corporation: An Interview with Larry D. Brady

FMC Corporation is one of the most diversified companies in the United States, producing more than 300 product lines in 21 divisions organized into 5 business segments: industrial chemicals, performance chemicals, precious metals, defense systems, and machinery and equipment. Based in Chicago, FMC has worldwide revenues in excess of \$4 billion.

Since 1984, the company has realized annual returns-on-investment of greater than 15%. Coupled with a major recapitalization in 1986, these returns resulted in an increasing shareholder value that significantly exceeded industrial averages. In 1992, the company completed a strategic review to determine the best future course to maximize shareholder value. As a result of that review, FMC adopted a growth strategy to complement its strong operating performance. This strategy required a greater external focus and appreciation of operating trade-offs.

To help make the shift, the company decided to use the balanced scorecard. In this interview conducted by Robert S. Kaplan, Larry D. Brady, executive vice president of FMC, talks about the company's experience implementing the scorecard.

Robert S. Kaplan: *What's the status of the balanced scorecard at FMC?*

Larry D. Brady: Although we are just completing the pilot phase of implementation, I think that the balanced scorecard is likely to become the cornerstone of the management system at FMC. It enables us to translate business unit strategies into a measurement system that meshes with our entire system of management.

For instance, one manager reported that while his division had measured many operating variables in the past, now, because of the scorecard, it had chosen 12 parameters as the key to its strategy implementation. Seven of these strategic variables were entirely new measurements for the division.

The manager interpreted this finding as verifying what many other managers were reporting: the scorecard improved the understanding and consistency of strategy implementation. Another manager reported that, unlike monthly financial statements or even his strategic plan, if a rival were to see his scorecard, he would lose his competitive edge.

It's rare to get that much enthusiasm among divisional managers for a corporate initiative. What led you and them to the balanced scorecard?

FMC had a clearly defined mission: to become our customers' most valued supplier. We had initiated many of the popular improvement programs: total quality, managing by objectives, organizational effectiveness, building a high-performance organization. But these efforts had not been effective. Every time we promoted a new program, people in each division would sit back and ask, "How is that supposed to fit in with the six other things we're supposed to be doing?"

Corporate staff groups were perceived by operating managers as pushing their pet programs on divisions. The diversity of initiatives, each with its own slogan, created confusion and mixed signals about where to concentrate and how the various programs interrelated. At the end of the day, with all these new initiatives, we were still asking division managers to deliver consistent short-term financial performance.

What kinds of measures were you using?

The FMC corporate executive team, like most corporate offices, reviews the financial performance of each operating division monthly. As a highly diversified company that redeploys assets from mature cash generators to divisions with significant growth opportunities, the return-on-capital-employed (ROCE) measure was especially important for us. We were one of the few companies to inflation-adjust our internal financial measures so that we could get a more accurate picture of a division's economic profitability.

At year-end, we rewarded division managers who delivered predictable financial performance. We had run the company tightly for the past 20 years and had been successful. But it was becoming less clear where future growth would come from and where the company should look for breakthroughs into new areas. We had become a high return-on-investment company but had less potential for further growth. It was also not at all clear from our financial reports what progress we were making in implementing long-term initiatives. Questions from the corporate office about spending versus budget also reinforced a focus on the short-term and on internal operations.

But the problem went even deeper than that. Think about it. What is the value added of a corporate office that concentrates on making division managers accountable for financial results that can be added up across divisions? We combine a business that's doing well with a business that's doing poorly and have a total business that performs at an average level. Why not split the company up into independent companies and let the market reallocate capital? If we were going to create value by managing a group of diversified companies, we had to understand and provide strategic focus to their operations. We had to be sure that each division had a strategy that would give it sustainable competitive advantage. In addition, we had to be able to assess, through measurement of their operations, whether or not the divisions were meeting their strategic objectives.

If you're going to ask a division or the corporation to change its strategy, you had better change the system of measurement to be consistent with the new strategy.

How did the balanced scorecard emerge as the remedy to the limitations of measuring only short-term financial results?

In early 1992, we assembled a task force to integrate our various corporate initiatives. We wanted to understand what had to be done differently to achieve dramatic improvements in overall organizational effectiveness. We acknowledged that the company may have become too short-term and too internally focused in its business measures. Defining what should replace the financial focus was more difficult. We wanted managers to sustain their search for continuous improvement, but we also wanted them to identify the

opportunities for breakthrough performance.

When divisions missed financial targets, the reasons were generally not internal. Typically, division management had inaccurately estimated market demands or had failed to forecast competitive reactions. A new measurement system was needed to lead operating managers beyond achieving internal goals to searching for competitive breakthroughs in the global marketplace. The system would have to focus on measures of customer service, market position, and new products that could generate long-term value for the business. We used the scorecard as the focal point for the discussion. It forced division managers to answer these questions: How do we become our customers' most valued supplier? How do we become more externally focused? What is my division's competitive advantage? What is its competitive vulnerability?

How did you launch the scorecard effort at FMC?

We decided to try a pilot program. We selected six division managers to develop prototype scorecards for their operations. Each division had to perform a strategic analysis to identify its sources of competitive advantage. The 15 to 20 measures in the balanced scorecard had to be organization-specific and had to communicate clearly what short-term measures of operating performance were consistent with a long-term trajectory of strategic success.

Were the six division managers free to develop their own scorecard?

We definitely wanted the division managers to perform their own strategic analysis and to develop their own measures. That was an essential part of creating a consensus between senior and divisional management on operating objectives. Senior management did, however, place some conditions on the outcomes.

First of all, we wanted the measures to be objective and quantifiable. Division managers were to be just as accountable for improving scorecard

measures as they had been for using monthly financial reviews. Second, we wanted output measures not process-oriented measures. Many of the improvement programs under way were emphasizing time, quality, and cost measurements. Focusing on T-Q-C measurements, however, encourages managers to seek narrow process improvements instead of breakthrough output targets. Focusing on achieving outputs forces division managers to understand their industry and strategy and help them to quantify strategic success through specific output targets.

Could you illustrate the distinction between process measures and output measures?

You have to understand your industry well to develop the connection between process improvements and outputs achieved. Take three divisional examples of cycle-time measurement, a common process measure.

For much of our defense business, no premium is earned for early delivery. And the contracts allow for reimbursement of inventory holding costs. Therefore, attempts to reduce inventory or cycle times in this business produce no benefit for which the customer is willing to pay. The only benefits from cycle time or inventory reduction occur when reduction in factory-floor complexity leads to real reductions in product cost. The output performance targets must be real cash savings, not reduced inventory levels or cycle times.

In contrast, significant lead-time reductions could be achieved for our packaging machinery business. This improvement led to lower inventory and an option to access an additional 35% of the market. In this case, the cycle-time improvements could be tied to specific targets for increased sales and market share. It wasn't linear, but output seemed to improve each time we improved throughput times.

And in one of our agricultural machinery businesses, orders come within a narrow time window each year. The current build cycle is longer than the ordering window, so all units must be built to the sales forecast. This process of building to forecast leads to high inventory—more than twice the levels of our other businesses—and frequent overstocking and obsolescence of equipment. Incremental reductions in lead time do little to change the

economics of this operation. But if the build cycle time could be reduced to less than the six-week ordering time window for part or all of the build schedule, then a breakthrough occurs. The division can shift to a build-to-order schedule and eliminate the excess inventory caused by building to forecasts. In this case, the benefit from cycle-time reductions is a step-function that comes only when the cycle time drops below a critical level.

So here we have three businesses, three different processes, all of which could have elaborate systems for measuring quality, cost, and time but would feel the impact of improvements in radically different ways. With all the diversity in our business units, senior management really can't have a detailed understanding of the relative impact of time and quality improvements on each unit. All of our senior managers, however, understand output targets, particularly when they are displayed with historical trends and future targets.

Benchmarking has become popular with a lot of companies. Does it tie in to the balanced scorecard measurements?

Unfortunately, benchmarking is one of those initially good ideas that has turned into a fad. About 95% of those companies that have tried benchmarking have spent a lot of money and have gotten very little in return. And the difference between benchmarking and the scorecard helps reinforce the difference between process measures and output measures. It's a lot easier to benchmark a process than to benchmark an output. With the scorecard, we ask each division manager to go outside their organization and determine the approaches that will allow achievement of their long-term output targets. Each of our output measures has an associated long-term target. We have been deliberately vague on specifying when the target is to be accomplished. We want to stimulate a thought process about how to do things differently to achieve the target rather than how to do existing things better. The activity of searching externally for how others have accomplished these breakthrough achievements is called target verification not benchmarking.

Were the division managers able to develop such output-oriented measures?

Well, the division managers did encounter some obstacles. Because of the emphasis on output measures and the previous focus on operations and financial measures, the customer and innovation perspectives proved the most difficult. These were also the two areas where the balanced scorecard process was most helpful in refining and understanding our existing strategies.

But the initial problem was that the management teams ran afoul of both conditions: the measures they proposed tended to be nonquantifiable and input- rather than output-oriented. Several divisions wanted to conduct customer surveys and provide an index of the results. We judged a single index to be of little value and opted instead for harder measures such as price premiums over competitors.

We did conclude, however, that the full customer survey was an excellent vehicle for promoting external focus and, therefore, decided to use survey results to kick-off discussion at our annual operating reviews.

Did you encounter any problems as you launched the six pilot projects?

At first, several divisional managers were less than enthusiastic about the additional freedom they were being given from headquarters. They knew that the heightened visibility and transparency of the scorecard took away the internal trade-offs they had gained experience in making. They initially interpreted the increase in visibility of divisional performance as just the latest attempt by corporate staff to meddle in their internal business processes.

To offset this concern, we designed targets around long-term objectives. We still closely examine the monthly and quarterly statistics, but these statistics now relate to progress in achieving long-term objectives and justify the proper balance between short-term and long-term performance.

We also wanted to transfer quickly the focus from a measurement system to achieving performance results. A measurement orientation reinforces

concerns about control and a short-term focus. By emphasizing targets rather than measurements, we could demonstrate our purpose to achieve breakthrough performance.

But the process was not easy. One division manager described his own three-stage implementation process after receiving our directive to build a balanced scorecard: denial—hope it goes away; medicinal—it won't go away, so let's do it quickly and get it over with; ownership—let's do it for ourselves.

In the end, we were successful. We now have six converts who are helping us to spread the message throughout the organization.

I understand that you have started to apply the scorecard not just to operating units but to staff groups as well.

Applying the scorecard approach to staff groups has been even more eye-opening than our initial work with the six operating divisions. We have done very little to define our strategy for corporate staff utilization. I doubt that many companies can respond crisply to the question, "How does staff provide competitive advantage?" Yet we ask that question every day about our line operations. We have just started to ask our staff departments to explain to us whether they are offering low-cost or differentiated services. If they are offering neither, we should probably outsource the function. This area is loaded with real potential for organizational development and improved strategic capability.

My conversations with financial people in organizations reveal some concern about the expanded responsibilities implied by developing and maintaining a balanced scorecard. How does the role of the controller change as a company shifts its primary measurement system from a purely financial one to the balanced scorecard?

Historically, we have had two corporate departments involved in

overseeing business unit performance. Corporate development was in charge of strategy, and the controller's office kept the historical records and budgeted and measured short-term performance. Strategists came up with five- and ten-year plans, controllers one-year budgets and near-term forecasts. Little interplay occurred between the two groups. But the scorecard now bridges the two. The financial perspective builds on the traditional function performed by controllers. The other three perspectives make the division's long-term strategic objectives measurable.

In our old environment, division managers tried to balance short-term profits with long-term growth, while they were receiving different signals depending on whether or not they were reviewing strategic plans or budgets. This structure did not make the balancing of short-term profits and long-term growth an easy trade-off, and, frankly, it let senior management off the hook when it came to sharing responsibility for making the trade-offs.

Perhaps the corporate controller should take responsibility for all measurement and goal setting, including the systems required to implement these processes. The new corporate controller could be an outstanding system administrator, knowledgeable about the various trade-offs and balances, and skillful in reporting and presenting them. This role does not eliminate the need for strategic planning. It just makes the two systems more compatible. The scorecard can serve to motivate and evaluate performance. But I see its primary value as its ability to join together what had been strong but separated capabilities in strategy development and financial control. It's the operating performance bridge that corporations have never had.

How often do you envision reviewing a division's balanced scorecard?

I think we will ask group managers to review a monthly submission from each of their divisions, but the senior corporate team will probably review scorecards quarterly on a rotating basis so that we can review up to seven or eight division scorecards each month.

Isn't it inconsistent to assess a division's strategy on a monthly or quarterly

basis? Doesn't such a review emphasize short-term performance?

I see the scorecard as a strategic measurement system, not a measure of our strategy. And I think that's an important distinction. The monthly or quarterly scorecard measures operations that have been configured to be consistent with our long-term strategy.

Here's an example of the interaction between the short and the long term. We have pushed division managers to choose measures that will require them to create change, for example, penetration of key markets in which we are not currently represented. We can measure that penetration monthly and get valuable short-term information about the ultimate success of our long-term strategy. Of course, some measures, such as annual market share and innovation metrics, don't lend themselves to monthly updates. For the most part, however, the measures are calculated monthly.

Any final thoughts on the scorecard?

I think that it's important for companies not to approach the scorecard as the latest fad. I sense that a number of companies are turning to scorecards in the same way they turned to total quality management, high-performance organization, and so on. You hear about a good idea, several people on corporate staff work on it, probably with some expensive outside consultants, and you put in a system that's a bit different from what existed before. Such systems are only incremental, and you don't gain much additional value from them.

It gets worse if you think of the scorecard as a new measurement system that eventually requires hundreds and thousands of measurements and a big, expensive executive information system. These companies lose sight of the essence of the scorecard: its focus, its simplicity, and its vision. The real benefit comes from making the scorecard the cornerstone of the way you run the business. It should be the core of the management system, not the measurement system. Senior managers alone will determine whether the scorecard becomes a mere record-keeping exercise or the lever to streamline and focus strategy that can lead to breakthrough performance.

Originally published in September 1993. Reprint 93505

Innovation

The Classic Traps. *by Rosabeth Moss Kanter*

INNOVATION IS BACK AT the top of the corporate agenda. Never a fad, but always in or out of fashion, innovation gets rediscovered as a growth enabler every half-dozen years (about the length of a managerial generation). Too often, however, grand declarations about innovation are followed by mediocre execution that produces anemic results, and innovation groups are quietly disbanded in cost-cutting drives. Each generation embarks on the same enthusiastic quest for the next new thing and faces the same challenge of overcoming innovation stifiers. Over the past 25 years, I have conducted research and advised companies during at least four major waves of competitive challenges that led to widespread enthusiasm for innovation.

The first was the dawn of the global information age in the late 1970s and early 1980s, an era that introduced new industries and threatened to topple old ones. Entrepreneurs and foreign competitors imperiled established companies on their own turf. Information technology was beginning to evolve from the clunky mainframe to a consumer and desktop product, and companies such as Apple Computer made Silicon Valley garages the new base for product innovation in the United States. IBM emulated Apple's model by developing its PC in dingy surroundings in Boca Raton, Florida, freed from many corporate constraints. High-quality Japanese products, such as the Sony Walkman and Toyota cars, reflected not just good product design but also innovations in manufacturing processes that forced American giants to create their own programs to generate new ideas faster. "Total quality management" became a passion.

The second wave was the pressure to restructure during the takeover scare of the late 1980s. Buyout groups were attacking traditional companies, seeking to unlock the value of underutilized assets; "shareholder value"

became a rallying cry. In Europe, restructuring was associated with the privatization of state-owned enterprises now exposed to the pressures of capital markets. Software was emerging as a major force behind innovation, and the strategic value of IT was touted, with American Airlines' Sabre reservations system widely cited as an example of a process innovation that succeeded as a separate business. Companies created new-venture departments to make sure they captured the value of their own ideas and inventions, rather than allowing a behemoth like Microsoft to arise outside the firm. Financial innovations were the rage: leveraged and management buyouts, derivatives and other forms of financial engineering, or financial supermarkets combining banks and nearly everything else. The restructuring era also favored products that could be instantly global: After defeating a hostile takeover bid in the late 1980s, Gillette boldly and successfully launched Sensor Excel shaving systems in the early 1990s, in identical form worldwide, with a single advertising message.

Third was the digital mania of the 1990s. The promise (and threat) of the World Wide Web drove many established companies to seek radical new business models. Brick-and-mortar companies were at risk for extinction; many rushed to create stand-alone Web ventures, often unconnected to the core business and sometimes in conflict with it. Eyes were on the capital markets rather than on customers, and companies got rich without profits or revenues. AOL bought Time Warner, put its name first, and proceeded to destroy value rather than create innovation.

The current wave of innovation began in a more sober mood, following the dot-com crash and belt-tightening of the global recession. Having recognized the limits of acquisitions and become skeptical about technology hype, companies refocused on organic growth. Surviving giants such as General Electric and IBM have adopted innovation as a corporate theme. GE, for instance, is committed to double-digit growth from within. For its part, IBM is seeking innovation by tackling difficult social problems that require—and showcase—its technology solutions. A good example is World Community Grid, a nonprofit IBM created that aggregates unused computer power from numerous partners to give AIDS researchers and other scientists the ability to work with unusually large data sets. This wave's central focus is on new products designed to offer users new features and functionality to meet emerging needs. Customers and consumer markets have returned to center stage, after having been temporarily crowded out by other obsessions.

Companies are seeking new categories to enrich their existing businesses rather than grand new ventures that will take them into totally different realms. Signature innovations in this era include Apple's iPod and Procter & Gamble's Swiffer.

Idea in Brief

Most companies fuel growth by creating new products and services. Yet too many firms repeat the same growth-sapping mistakes in their efforts to innovate.

For example, some companies adopt the wrong strategy: investing only in ideas they think will become blockbusters. Result? Small ideas that could have generated big profits get rejected. For years, Time, Inc. didn't develop new publications: managers wanted any start-up to succeed on the same scale as the enormously popular *People* magazine. Only after Time decided to gamble on a large number of new publications did revenues rise.

Other companies err on the side of process-strangling innovations by subjecting them to the strict performance criteria their existing businesses must follow. At AlliedSignal, new Internet-based products and services had to satisfy the same financial metrics as established businesses. Budgets contained no funds for investment—so managers working on innovations had to find their own funding. The consequences? Retrofitted versions of old ideas.

To avoid such traps, Kanter advocates applying lessons from past failures to your innovation efforts. For instance, augment potential “big bets” with promising midrange ideas and incremental innovations. And add flexibility to your innovation planning, budgeting, and reviews.

Your reward? Better odds that the new ideas percolating in your company today will score profitable successes in the market tomorrow.

Idea in Practice

To innovate successfully, replace common mistakes with potent remedies:

Strategy Mistakes

- Rejecting opportunities that at first glance appear too small.

- Assuming that only new products count—not new services or improved processes.
- Launching too many minor product extensions that confuse customers and increase internal complexity.

Remedy: Widen your search and broaden your scope. Support a few big bets at the top that represent clear directions for the future and receive the lion's share of investment. Also create a portfolio of promising midrange ideas. And fund a broad base of early stage ideas or incremental innovations.

Process Mistakes

- Strangling innovation with the same tight planning, budgeting, and reviews applied to existing businesses.
- Rewarding managers for doing only what they committed to do—and discouraging them from making changes as circumstances warrant.

Remedy: Add flexibility to planning and control systems. For instance, reserve special funds for unexpected opportunities.

Example: After executives at the struggling UK television network BBC set aside funds in a corporate account to support innovation proposals, a new recruit used money originally allocated for a new BBC training film to make a pilot for *The Office*. The show became the BBC's biggest hit comedy in decades.

Structure Mistakes

- Isolating fledgling and established enterprises in separate silos.
- Creating two classes of corporate citizens—those who have all the fun (innovators) and those who must make the money (mainstream business managers).

Remedy: Tighten the human connections between innovators and others throughout your organization. Convene frequent conversations between innovators and mainstream business managers to promote mutual learning and integration of new businesses into the organization. Create overlapping relationships—by having representatives from mainstream businesses rotate through innovation groups or innovation advisory boards. Identify people who lead informal networks that span innovation and mainstream groups, and encourage them to strengthen those connections.

Skills Mistakes

- Allowing innovators to rotate out of teams so quickly that team chemistry can't gel.
- Assuming that innovation teams should be led by the best technical people.

Remedy: Select innovation leaders with strong interpersonal skills. They'll keep the innovation team intact, help innovation teams embrace collective goals, leverage one another's different strengths, and share hard-to-document knowledge while innovations are under development.

Example: When Williams-Sonoma launched its ultimately successful e-commerce group, it put a manager in charge who wasn't a technology expert but who could assemble the right team. He chose a mixture of employees from other units who could be ambassadors to their former groups and new hires that brought diverse skills.

Each wave brought new concepts. For example, the rise of biotechnology, characterized by complicated licensing arrangements, helped legitimize the idea that established firms could outsource R&D and learn from entrepreneurial partners or that consumer products companies could turn to external idea shops, as well as their own labs, to invent new products. Approaches to innovation also reflected changing economic conditions and geopolitical events. And, of course, innovation has covered a wide spectrum, including technologies, products, processes, and complete business ventures, each with its own requirements.

Still, despite changes to the environment and differences among types of innovation, each wave of enthusiasm has encountered similar dilemmas. Most of these stem from the tensions between protecting revenue streams from existing businesses critical to current success and supporting new concepts that may be crucial to future success. These tensions are exacerbated by the long-known phenomenon that important innovations often arise from outside an industry and beyond the established players, creating extra pressure for companies to find the next big concept quickly. Consequently, a large body of knowledge about innovation dilemmas has arisen.

Books such as Tom Peters and Bob Waterman's *In Search of Excellence*, my own *The Change Masters*, and Gifford Pinchot's *Intrapreneuring* supported the 1980s innovation wave by pointing to the importance of relieving potential innovators of bureaucratic constraints so they could run with their ideas. This was followed by a body of work documenting the difficulty of exploring the new while exploiting the old, reflected in Michael

Tushman and Charles O'Reilly's call for more ambidextrous organizations in *Winning Through Innovation*; my work on managing the tensions between the powerful organizational mainstream and fragile new streams produced by innovation groups in *When Giants Learn to Dance*; and Clayton Christensen's more recent finding, in *The Innovator's Dilemma*, that listening to current customers can inhibit breakthrough innovation.

Yet despite all the research and literature, I still observe executives exhibiting the same lack of courage or knowledge that undercut previous waves of innovation. They declare that they want more innovation but then ask, "Who else is doing it?" They claim to seek new ideas but shoot down every one brought to them. And, repeatedly, companies make the same mistakes as their predecessors. For example, a 1983 HBR article by Harvard Business School professor Malcolm Salter, et al., "When Corporate Venture Capital Doesn't Work," provided warnings that companies failed to heed about exactly the same dilemmas they face today: With a few notable exceptions, such as Intel and Reuters, companies' venture-capital departments rarely create significant value for the core business.

It's inevitable that historical memory will fade—but not inevitable that we lose the lessons. Here's a chance to collect some of what is known about innovation traps and how to avoid them.

The Lessons of Innovation

Innovation goes in or out of fashion as a strategic driver of corporate growth, but with every wave of enthusiasm, executives make the same mistakes. Most of the time, they stumble in their R&D efforts because they are engaged in a difficult balancing act: They need to protect existing revenue streams while coaxing along new ones. But "corporate entrepreneurship" doesn't have to be an oxymoron. Innovation can flourish if executives heed business lessons from the past.

Strategy Lessons

- Not every innovation idea has to be a blockbuster. Sufficient numbers of small or incremental innovations can lead to big profits.
- Don't just focus on new product development: Transformative ideas can come from any function—for instance, marketing, production, finance, or distribution.
- Successful innovators use an "innovation pyramid," with several big bets at the top that

get most of the investment; a portfolio of promising midrange ideas in test stage; and a broad base of early stage ideas or incremental innovations. Ideas and influence can flow up or down the pyramid.

Process Lessons

- Tight controls strangle innovation. The planning, budgeting, and reviews applied to existing businesses will squeeze the life out of an innovation effort.
- Companies should expect deviations from plan: If employees are rewarded simply for doing what they committed to do, rather than acting as circumstances would suggest, their employers will stifle and drive out innovation.

Structure Lessons

- While loosening formal controls, companies should tighten interpersonal connections between innovation efforts and the rest of the business.
- Game-changing innovations often cut across established channels or combine elements of existing capacity in new ways.
- If companies create two classes of corporate citizens—supplying the innovators with more perks, privileges, and prestige—those in the existing business will make every effort to crush the innovation.

Skills Lessons

- Even the most technical of innovations requires strong leaders with great relationship and communication skills.
- Members of successful innovation teams stick together through the development of an idea, even if the company's approach to career timing requires faster job rotation.
- Because innovations need connectors—people who know how to find partners in the mainstream business or outside world—they flourish in cultures that encourage collaboration.

Strategy Mistakes: Hurdles Too High, Scope Too Narrow

The potential for premium prices and high margins lures executives to seek blockbuster innovations—the next iPod, Viagra, or Toyota Production System. Along the way, they expend enormous resources, though big hits are rare and unpredictable. Meanwhile, in seeking the killer app, managers may reject opportunities that at first glance appear too small, and people who aren't involved in the big projects may feel marginalized.

For years, large consumer products companies typically screened out ideas that couldn't result in revenues of several hundred million dollars within two years. This screen discouraged investments in ideas that couldn't be tested and measured using conventional market research, or that weren't grounded in experience, in favor of ideas that were close to current practice and hardly innovative. In the 1980s and 1990s, Pillsbury, Quaker Oats, and even Procter & Gamble (an innovation powerhouse today) were vulnerable to smaller companies that could quickly roll out new products, thus eroding the giants' market share. P&G, for example, lamented not having introduced a new toilet bowl cleaner before a competitor did, despite P&G labs' having developed similar technology. The rival, of course, gained dominant market share by being a first mover. Likewise, Pillsbury and Quaker lagged the competition in bringing new concepts to market and, as underperformers, were eventually acquired.

Time Incorporated, the magazine wing of Time Warner, for a long time was slow to develop new publications because managers wanted any start-up to have the potential to grow into another *People* or *Sports Illustrated*, two of the company's legendary successes. During the period before Don Logan took the helm in 1992, almost no new magazines were launched. After Logan brought a different innovation strategy to the magazine group, Time developed (or bought) about 100 magazines, which dramatically increased the company's revenues, cash flow, and profits. Not every offering was a blockbuster, but Time had learned what successful innovators know: To get more successes, you have to be willing to risk more failures.

A related mistake is to act as if only products count, even though

transformative new ideas can come from a range of functions, such as production and marketing. For instance, a fabric company that made complicated woven materials had a long-standing problem: yarn breakage during production, which was reflected in the cost of the company's products and represented a competitive disadvantage. But the top team at the fabric maker continued to talk about the company's search for really big product innovations, such as totally new materials. A new executive, who believed in opening the search for innovation to all employees, joined the company. After a meeting discussing the need for change, a veteran factory worker, who had joined as a young immigrant and still spoke with a heavy accent, tentatively approached the new executive with an idea for ending the breakage. The company tried it, and it worked. When asked how long he had had that idea, the worker replied, "Thirty-two years."

Similarly, because managers at Quaker Oats in the 1990s were too busy tweaking product formulas in minor ways, the company missed numerous opportunities in other arenas, such as distribution—for instance, taking advantage of the smaller, health-oriented outlets used by its Snapple beverage acquisition. And in a packaging coup, Ocean Spray, the cranberry juice company, stole a march on America's largest juice purveyors (then including P&G and Coca-Cola) by getting an 18-month exclusive license for the introduction of Tetra Pak's paper bottles to the U.S. market. Ocean Spray boasted a more eclectic innovation strategy than that of its rivals, including idea forums to explore innovations in any domain and open to any employee. Paper bottles were an instant hit with children (and parents packing their lunches), and Ocean Spray's market share shot way up.

Early in its history, the U.S. auto industry gained a breakthrough innovation from its financial function: Consumer financing opened mass markets for products that previously only the affluent could afford. One Intel breakthrough was in marketing: It treated computer chips like potato chips. As a technology company, Intel could have left innovation to its R&D folks. But by marketing a component directly to consumers, Intel gained enormous power with computer manufacturers, which had little choice but to put an Intel Inside label on every machine.

Similarly, Cemex, the global cement company based in Mexico, has used widespread brainstorming to generate innovations that create other sources of value for a product that could easily become a commodity. Those innovations include branded, bagged cement and technology-enabled delivery methods to

get cement to customers as fast as if it were a pizza. And while P&G is getting attention for its product innovations, such as the Swiffer and Crest Whitestrips, its innovations in new media, such as interactive Web sites for the soap operas it sponsors, may prove even more valuable for the company's future.

When a company is both too product centric and too revenue impatient, an additional problem can arise. The organization's innovation energy can dissipate across a raft of tiny me-too projects chasing immediate revenue. Perversely, such projects may raise costs in the long run. While a failure to encourage small wins can mean missed opportunities, too many trivial projects are like seeds sown on stony ground—they might sprout, but they do not take root and grow into anything useful. If new ideas take the form not of distinctive innovations but of modest product variations, the resulting proliferation can dilute the brand, confuse customers, and increase internal complexity—such as offering a dozen sizes and flavors of crackers rather than a new and different snack food, a problem Kraft currently faces.

Process Mistakes: Controls Too Tight

A second set of classic mistakes lies in process; specifically, the impulse to strangle innovation with tight controls—the same planning, budgeting, and reviews applied to existing businesses. The inherent uncertainty of the innovation process makes sidetracks or unexpected turns inevitable. The reason upstart Ocean Spray could grab the paper-bottle opportunity from large U.S. juice makers is that the big companies' funds had already been allocated for the year, and they wanted committees to study the packaging option before making commitments that would deviate from their plans.

AlliedSignal (now Honeywell) in 2000 sought new Internet-based products and services using established strategic-planning and budgeting processes through existing business units. The CEO asked the divisions to bring their best ideas for Internet-related innovations to the quarterly budget reviews. Although designated as a priority, these innovation projects were subjected to the same financial metrics the established businesses were. Budgets contained no additional funds for investment; managers working on innovations had to find their own sources of funding through savings or internal transfers. What emerged were often retrofitted versions of ideas that had been in the pipeline anyway.

Performance reviews, and their associated metrics, are another danger zone for innovations. Established companies don't just want plans; they want managers to stick to those plans. They often reward people for doing what they committed to do and discourage them from making changes as circumstances warrant. At a large defense contractor, for instance, people got low marks for not delivering exactly what they had promised, even if they delivered something better—which led people to underpromise, eventually reducing employees' aspirations and driving out innovation.

In the early 1990s, Bank of Boston (now part of Bank of America) set up an innovative unit called First Community Bank (FCB), the first comprehensive banking initiative to focus on inner-city markets. FCB struggled to convince mainstream managers in Bank of Boston's retail-banking group that the usual performance metrics, such as transaction time and profitability per customer, were not appropriate for this market—which

required customer education, among other things—or for a new venture that still needed investment. Mainstream managers argued that “underperforming” branches should be closed. In order to save the innovation, FCB leaders had to invent their own metrics, based on customer satisfaction and loyalty, and find creative ways to show results by clusters of branches. The venture later proved both profitable and important to the parent bank as it embarked on a series of acquisitions.

Structure Mistakes: Connections Too Loose, Separations Too Sharp

While holding fledgling enterprises to the same processes as established businesses is dangerous, companies must be careful how they structure the two entities to avoid a clash of cultures or conflicting agendas.

The more dramatic approach is to create a unit apart from the mainstream business, which must still serve its embedded base. This was the logic behind the launch of Saturn as an autonomous subsidiary of General Motors. GM's rules were suspended, and the Saturn team was encouraged to innovate in every aspect of vehicle design, production, marketing, sales, and customer service. The hope was that the best ideas would be incorporated back at the parent company, but instead, after a successful launch, Saturn was reintegrated into GM, and many of its innovations disappeared.

In the time it took for Saturn to hit its stride, Toyota—which favored continuous improvement over blockbusters or greenfield initiatives like Saturn—was still ahead of GM in quality, customer satisfaction, and market share growth. Similarly, U.S. charter schools were freed from the rules of public school systems so they could innovate and thus serve as models for improved education. They've employed many innovative practices, including longer school days and focused curricula, but there is little evidence that charter schools have influenced changes in the rest of their school districts.

The problem in both cases can be attributed to poor connections between the greenfield and the mainstream. Indeed, when people operate in silos, companies may miss innovation opportunities altogether. Game-changing innovations often cut across established channels or combine elements of existing capacity in new ways. CBS was once the world's largest broadcaster and owned the world's largest record company, yet it failed to invent music video, losing this opportunity to MTV. In the late 1990s, Gillette had a toothbrush unit (Oral B), an appliance unit (Braun), and a battery unit (Duracell), but lagged in introducing a battery-powered toothbrush.

The likelihood that companies will miss or stifle innovations increases when the potential innovations involve expertise from different industries or knowledge of different technologies. Managers at established organizations

may both fail to understand the nature of a new idea and feel threatened by it.

AT&T Worldnet, the Internet access venture of the venerable long-distance telephone company, faced this lethal mix in the mid-1990s. Managers in the traditional consumer services and business services units participated in a series of debates over whether to manage Worldnet as a distinct business unit, with its own P&L, or to include it in the existing business units focused primarily on the consumer sector. While consumer services managers were reluctant to let go of anything, they eventually agreed to a carve-out intended to protect the embryonic venture from being crushed by the bureaucracy and to keep it from being measured against more-mature businesses that were generating significant cash flow rather than requiring investment. They weren't all that concerned, because they believed an Internet service provider would never generate significant revenue and profitability.

But as Worldnet gained momentum, it attracted more attention. The people in consumer services began to view the innovation's possible expansion to provide voice over Internet protocol (VoIP) services as a threat that could cannibalize existing business. Consumer services managers grabbed control of Worldnet and proceeded to starve it. They used it as a platform to sell core land-based long-distance services and started applying the same metrics to the Internet business that were used for consumer long-distance. Pricing was an immediate problem. Worldnet's services had been priced low to fuel growth, to get the scale and network effects of a large group of subscribers, but the mainstream unit did not want to incur losses on any line of business. So it raised prices, and Worldnet's growth stalled. Consumer services managers could then treat Worldnet as a trivial, slow-growing business, not worthy of large investment. They did not allocate sufficient resources to develop Internet access and VoIP technology, restraining important telecom innovations in which AT&T could have been the pioneer.

Cultural clashes exacerbated tensions at AT&T. Mainstream managers had long tenures in the Bell system. The Internet group, however, hired external tech professionals who spoke the language of computers, not telephony.

Even when a new venture is launched within an existing business, culture clashes become class warfare if there are two classes of corporate citizens—those who have all the fun and those who make all the money. The

designated innovators, whether an R&D group or a new-venture unit, are identified as creators of the future. They are free of rules or revenue demands and are allowed to play with ideas that don't yet work. Their colleagues are expected to follow rules, meet demands, and make money while feeling like grinds and sometimes being told they are dinosaurs whose business models will soon be obsolete.

In the early 2000s, Arrow Electronics' attempt at an Internet venture, Arrow.com, was given space in the same facility as the traditional sales force. The similarities stopped there. The Internet group was composed of new hires, often young, from a different background, who dressed in a completely different style. It spent money on cushy furniture, including a big expenditure on a new kitchen—justified, it was said, because the Arrow.com team worked 24/7. The traditional sales force, already anxious about the threat Internet-enabled sales posed to its commissions and now aware of its dingier offices, became overtly angry. Relations between the groups grew so acrimonious that a brick wall was erected to separate the two sides of the building. Both teams wasted time battling, endangering customer relationships when the two groups fought over the same customers—after all, Arrow.com was just another distribution channel. The CEO had to intervene and find structures to connect them.

Skills Mistakes: Leadership Too Weak, Communication Too Poor

Undervaluing and underinvesting in the human side of innovation is another common mistake. Top managers frequently put the best technical people in charge, not the best leaders. These technically oriented managers, in turn, mistakenly assume that ideas will speak for themselves if they are any good, so they neglect external communication. Or they emphasize tasks over relationships, missing opportunities to enhance the team chemistry necessary to turn undeveloped concepts into useful innovations.

Groups that are convened without attention to interpersonal skills find it difficult to embrace collective goals, take advantage of the different strengths various members bring, or communicate well enough to share the tacit knowledge that is still unformed and hard to document while an innovation is under development. It takes time to build the trust and interplay among team members that will spark great ideas. MIT researchers have found that for R&D team members to be truly productive, they have to have been on board for at least two years. At one point, Pillsbury realized that the average length of time the company took to go from new product idea to successful commercialization was 24 to 26 months, but the average length of time people spent on product teams was 18 months. No wonder the company was falling behind in innovation.

Changes in team composition that result from companies' preferences for the frequency with which individuals make career moves can make it hard for new ventures to deal with difficult challenges, prompting them to settle for quick, easy, conventional solutions. At Honeywell in the 1980s, leaders of new-venture teams were often promoted out of them before the work had been completed. Because promotions were take-it-or-leave-it offers and pay was tied to size of assets controlled (small by definition in new ventures) rather than difficulty of task, even dedicated innovators saw the virtues of leaving their projects midstream. Honeywell was undermining its own innovation efforts. An executive review of why new ventures failed uncovered this problem, but a technology bias made it hard for old-school managers of that era to increase their appreciation for the value of team

bonding and continuity.

Innovation efforts also bog down when communication and relationship building outside the team are neglected. When Gap Incorporated was struggling in the late 1990s, the company mounted several cross-unit projects to find innovations in products, retail concepts, and operations. Some of the project teams quickly became closed environments, and members cut themselves off from their former peers. By failing to tap others' ideas, they produced lackluster recommendations; and by failing to keep peers informed, they missed getting buy-in for even their weak proposals.

Innovators cannot work in isolation if they want their concepts to catch on. They must build coalitions of supporters who will provide air cover for the project, speak up for them in meetings they don't attend, or sponsor the embryonic innovation as it moves into the next stages of diffusion and use. To establish the foundation for successful reception of an innovation, groups must be able to present the radical so it can be understood in familiar terms and to cushion disruptive innovations with assurances that the disruption will be manageable. When technical experts mystify their audiences rather than enlighten them, they lose support—and “no” is always an easier answer than “yes.” Groups that work in secret and then present their ideas full-blown at the end face unexpected objections that sometimes kill the project.

Such inattention to relationships and communication with mainstream business managers doomed the launch of Timberland's promising TravelGear line. Developed by an R&D group called the Invention Factory, which was independent of the company's mainstream businesses, TravelGear allowed a user to travel with a single pair of shoes, adding or subtracting components suitable for a range of outdoor activities. The concept won a design award from *BusinessWeek* in 2005. But some existing business teams had not been included in the Invention Factory's developments, and the traditional sales force refused to sell TravelGear products.

By contrast, Dr. Craig Feied's success in developing a state-of-the-art digital network for Washington Hospital Center and its parent, MedStar Health, was a testimony to investment in the human dimension. A small group of programmers designed a user-friendly information system in the emergency department, not the IT department, so they were already close to users. Dr. Feied and his partner, Dr. Mark Smith, made a point of sitting on numerous hospital committees so they would have a wide base of relationships. Their investment in people and their contributions toward

shared hospital goals had a positive effect: Feied and Smith's actions helped create good word of mouth and support among other departments for their information system (now called Azyxxi), which resulted in saved time and lives.

The climate for relationships within an innovation group is shaped by the climate outside it. Having a negative instead of a positive culture can cost a company real money. During Seagate Technology's troubled period in the mid-to-late 1990s, the company, a large manufacturer of disk drives for personal computers, had seven different design centers working on innovation, yet it had the lowest R&D productivity in the industry because the centers competed rather than cooperated. Attempts to bring them together merely led people to advocate for their own groups rather than find common ground. Not only did Seagate's engineers and managers lack positive norms for group interaction, but they had the opposite in place: People who yelled in executive meetings received "Dog's Head" awards for the worst conduct. Lack of product and process innovation was reflected in loss of market share, disgruntled customers, and declining sales. Seagate, with its dwindling PC sales and fading customer base, was threatening to become a commodity producer in a changing technology environment.

Under a new CEO and COO, Steve Luczo and Bill Watkins, who operated as partners, Seagate developed new norms for how people should treat one another, starting with the executive group. Their raised consciousness led to a systemic process for forming and running "core teams" (cross-functional innovation groups), and Seagate employees were trained in common methodologies for team building, both in conventional training programs and through participation in difficult outdoor activities in New Zealand and other remote locations. To lead core teams, Seagate promoted people who were known for strong relationship skills above others with greater technical skills. Unlike the antagonistic committees convened during the years of decline, the core teams created dramatic process and product innovations that brought the company back to market leadership. The new Seagate was able to create innovations embedded in a wide range of new electronic devices, such as iPods and cell phones.

Innovation Remedies

The quest for breakthrough ideas, products, and services can get derailed in any or all of the ways described earlier. Fortunately, however, history also shows how innovation succeeds. “Corporate entrepreneurship” need not be an oxymoron. Here are four ways to win.

Strategy remedy: widen the search, broaden the scope

Companies can develop an innovation strategy that works at the three levels of what I call the “innovation pyramid”: a few big bets at the top that represent clear directions for the future and receive the lion’s share of investment; a portfolio of promising midrange ideas pursued by designated teams that develop and test them; and a broad base of early-stage ideas or incremental innovations permitting continuous improvement. Influence flows down the pyramid, as the big bets encourage small wins heading in the same direction, but it also can flow up, because big innovations sometimes begin life as small bits of tinkering—as in the famously accidental development of 3M’s Post-it Notes.

Thinking of innovation in terms of this pyramid gives senior managers a tool for assessing current efforts, making adjustments as ideas prove their value and require further support, and ensuring that there is activity at all levels. A culture of innovation grows because everyone can play. While dedicated groups pursue the big projects and temporary teams develop midrange ideas, everyone else in the company can be invited to contribute ideas. Every employee can be a potential idea scout and project initiator, as IBM is demonstrating. This past July, the company held a three-day InnovationJam on the Web, during which about 140,000 employees and clients—representing 104 countries—contributed about 37,000 ideas and ranked them, giving the company an enormous pool of raw ideas, some of them big, most of them small. Indeed, an organization is more likely to get bigger ideas if it has a wide funnel into which numerous small ideas can be poured. One of the secrets of success for companies that demonstrate high rates of innovation is that they simply try more things.

Gillette adopted the pyramid model as part of its push to accelerate

innovation in 2003 and 2004. The result was a stream of innovations in every function and business unit that raised revenues and profits. They included new products such as a battery-powered toothbrush; new concepts in the R&D pipeline, such as the 2006 five-blade, battery-powered Fusion shaving system; innovative marketing campaigns that neutralized the competition, such as the campaign for the Mach3Turbo, which outshone Schick's introduction of its Quattro razor; and new technology in HR. At the first Gillette innovation fair in March 2004, every unit showcased its best ideas of the year in a creative way. The legal department promoted its novel online ethics course with a joke: distributing "get out of jail free" cards like those in *Monopoly*. Having the legal department embrace innovation was a plus for a company in which innovators needed speedy service to file patent applications or help to clear regulatory hurdles.

An innovation strategy that includes incremental innovations and continuous improvement can help to liberate minds throughout the company, making people more receptive to change when big breakthroughs occur.

Process remedy: add flexibility to planning and control systems

One way to encourage innovation to flourish outside the normal planning cycles is to reserve pools of special funds for unexpected opportunities. That way, promising ideas do not have to wait for the next budget cycle, and innovators do not have to beg for funds from mainstream managers who are measured on current revenues and profits. In the mid-to-late 1990s, autocratic management and rigid controls caused the BBC to slip in program innovation and, consequently, audience share. Budgets were tight, and, once they were set, expenditures were confined to predetermined categories. In 2000, a new CEO and his CFO relaxed the rules and began setting aside funds in a corporate account to support proposals for innovation, making it clear that bureaucratic rules should not stand in the way of creative ideas. The BBC's biggest hit comedy in decades, *The Office*, was an accident, made possible when a new recruit took the initiative to use money originally allocated for a BBC training film to make the pilot.

IBM is building such flexibility directly into its infrastructure. The company established a \$100 million innovation fund to support the best ideas arising from its InnovationJam, independent of the normal planning and budgeting processes, to allow bottom-up ideas to flourish. "No one has ever

before brought together such a global and diverse set of business thought leaders on this scale to discuss the most pressing issues and opportunities of our age,” says Nick Donofrio, IBM’s executive vice president of innovation and technology. “We have companies literally knocking at the door and saying, ‘Give us your best and brightest ideas, and let’s work together to make them a reality.’ It’s a golden opportunity to create entirely new markets and partnerships.”

Besides needing different funding models and development partnerships, the innovation process requires exemption from some corporate requirements; after all, there are numerous differences between established businesses and new ventures. For example, the knowledge that innovations could move forward through rapid prototyping—learning from a series of fast trials—might mean that certain milestones triggering review and additional funding would occur faster than they would for established businesses, following the rhythm of the project rather than a fixed quarterly or annual calendar. For other kinds of projects, greater patience might be required—for instance, when an innovation group encounters unexpected obstacles and needs to rethink its model. The key is flexible, customized treatment.

Structure remedy: facilitate close connections between innovators and mainstream businesses

While loosening the formal controls that would otherwise stifle innovations, companies should tighten the human connections between those pursuing innovation efforts and others throughout the rest of the business. Productive conversations should take place regularly between innovators and mainstream business managers. Innovation teams should be charged with external communication as part of their responsibility, but senior leaders should also convene discussions to encourage mutual respect rather than tensions and antagonism. Such conversations should be aimed at mutual learning, to minimize cannibalization and to maximize effective reintegration of innovations that become new businesses. In addition to formal meetings, companies can facilitate informal conversations—as Steelcase did by building a design center that would force people to bump into one another—or identify the people who lead informal cross-unit networks and encourage their efforts at making connections.

Innovation groups can be told at the outset that they have a responsibility

to serve the mainstream while also seeking bigger innovations to start new businesses. This can be built into their charters and reinforced by overlapping relationships—whether it involves representatives from mainstream businesses rotating through innovation groups or advisory boards overseeing innovation efforts. After its first great idea flopped, Timberland’s Invention Factory learned to work closely with mainstream teams to meet their needs for immediate innovations, such as recreational shoes lined with SmartWool, and to seek game-changing breakthroughs. Turner Broadcasting’s new-products group mixes project types: stand-alone developments, enhancements for current channels, external partnerships, and venture capital investments. PNC Financial Services Group recently established a new-products group to oversee mainstream developments, such as pricing and product enhancements, as well as growth engines in new capabilities, such as technology-enabled services and back-office services for investment funds. The company’s sales of emerging products were up 21% in 2005, accounting for 46% of all sales.

Flexible organizational structures, in which teams across functions or disciplines organize around solutions, can facilitate good connections. Media conglomerate Publicis has “holistic communication” teams, which combine people across its ad agencies (Saatchi & Saatchi, Leo Burnett, Publicis Worldwide, and so on) and technology groups to focus on customers and brands. Novartis has organized around diseases, with R&D more closely connected to markets and customers; this has helped the company introduce pathbreaking innovations faster, such as its cancer drug Gleevec. The success of Seagate’s companywide Factory of the Future team at introducing seemingly miraculous process innovations led to widespread use of its core-teams model.

Would-be innovators at AlliedSignal discovered that tackling promising opportunities required outreach across silos. For example, the aerospace division was organized into groups that were dedicated to large commercial airlines, small commercial airlines, and general aviation (private and charter planes), but the best new idea involved differentiating customers by whether they performed their own maintenance or contracted it to others. The division needed to create new connections across previously divided territories in order to begin the innovation process.

The success of Williams-Sonoma as a multichannel retailer innovating in e-commerce can be attributed to the ways its Web pioneers connected their

developments to the rest of the company. From the very beginning, CEO Howard Lester refused to consider Internet ventures that were independent of other company operations. The first main Web development was a bridal registry to create new functionality for the mainstream business. When this pilot project proved its value, an e-commerce department was launched and housed in its own building. But rather than standing apart and pursuing its own direction, that department sought to enhance existing channels, not compete with them. It measured its success not only according to e-commerce sales but also according to incremental sales through other channels that the Web had facilitated. To further its close connections with the mainstream business, the department offered free training to the rest of the company.

Skills remedy: select for leadership and interpersonal skills, and surround innovators with a supportive culture of collaboration

Companies that cultivate leadership skills are more likely to net successful innovations. One reason Williams-Sonoma could succeed in e-commerce quickly and profitably was its careful attention to the human dimension. Shelley Nandkeolyar, the first manager of Williams-Sonoma's e-commerce group, was not the most knowledgeable about the technology, but he was a leader who could assemble the right team. He valued relationships, so he chose a mixture of current employees from other units, who could be ambassadors to their former groups, and new hires that brought new skills. He added cross-company teams to advise and link to the e-commerce team. He invented an integrator role to better connect operations groups and chose Patricia Skerritt, known for being relationship oriented, to fill it.

Similarly, Gail Snowden was able to steer Bank of Boston's First Community Bank through the minefields of middle-manager antagonism toward a successful innovation that produced other innovations (new products and services) because of her leadership skills, not her banking skills. She built a close-knit team of talented people who bonded with one another and felt passion for the mission. Soon her group became one of the parent bank's most desirable places to work. She developed strong relationships with senior executives who helped her deal with tensions in the middle, and she communicated well and often about why her unit needed to be different. Her creativity, vision, teamwork, and persistence helped this group succeed

and become a national role model, while other banks' efforts faltered.

IBM's big innovations, such as demonstrating grid computing through World Community Grid, are possible only because the company's culture encourages people to collaborate. CEO Sam Palmisano has engaged hundreds of thousands of IBMers in a Web-based discussion of company values, and Nick Donofrio, IBM's executive vice president for innovation and technology, works to make 90,000 technical people around the world feel part of one innovation-seeking community. The corporate champion of World Community Grid, IBM vice president Stanley Litow, sought out partners in its business units and geographies to move the innovation forward.

Established companies can avoid falling into the classic traps that stifle innovation by widening the search for new ideas, loosening overly tight controls and rigid structures, forging better connections between innovators and mainstream operations, and cultivating communication and collaboration skills.

Innovation involves ideas that create the future. But the quest for innovation is doomed unless the managers who seek it take time to learn from the past. Getting the balance right between exploiting (getting the highest returns from current activities) and exploring (seeking the new) requires organizational flexibility and a great deal of attention to relationships. It always has, and it always will.

Originally published in November 2006. Reprint R0611C

Leading Change

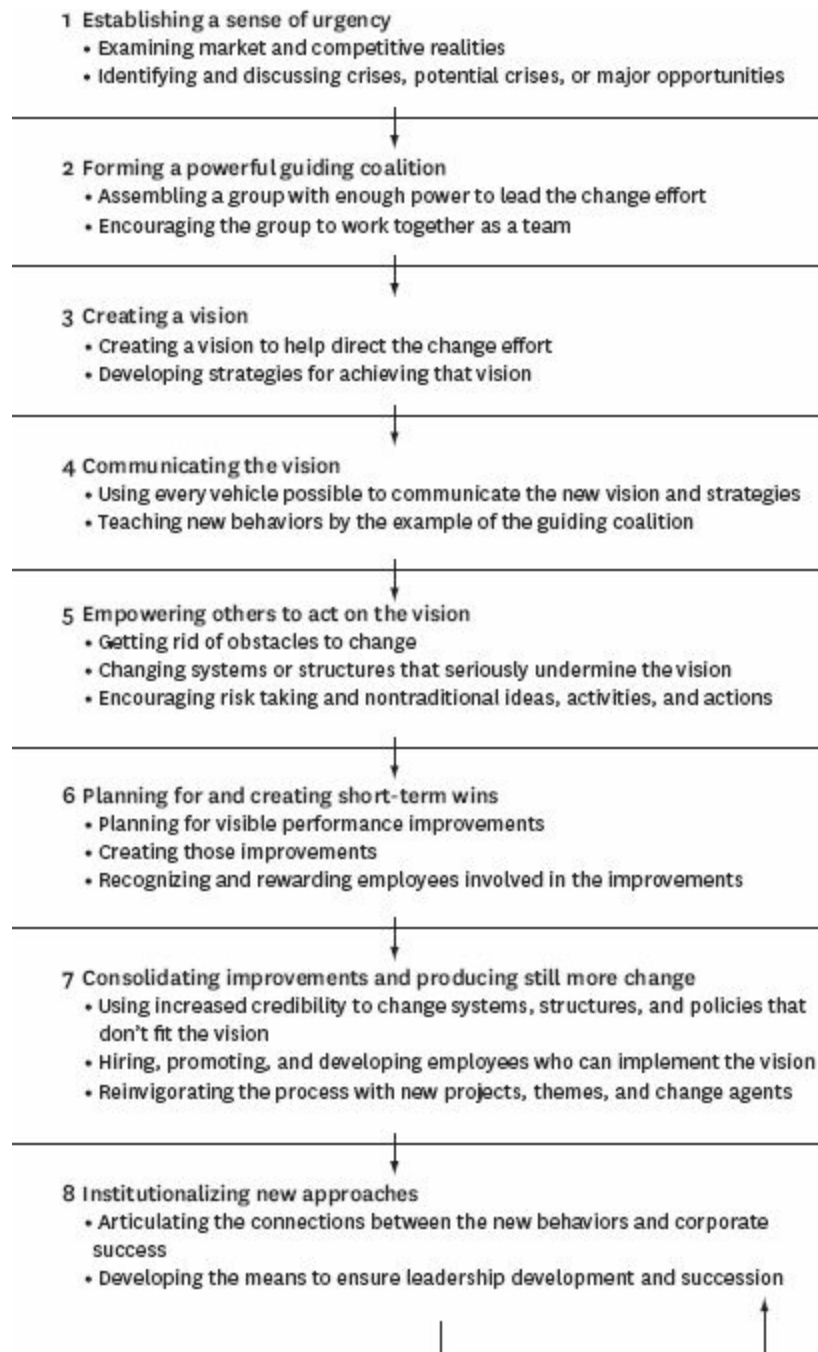
Why Transformation Efforts Fail. *by John P. Kotter*

OVER THE PAST DECADE, I have watched more than 100 companies try to remake themselves into significantly better competitors. They have included large organizations (Ford) and small ones (Landmark Communications), companies based in the United States (General Motors) and elsewhere (British Airways), corporations that were on their knees (Eastern Airlines), and companies that were earning good money (Bristol-Myers Squibb). These efforts have gone under many banners: total quality management, reengineering, rightsizing, restructuring, cultural change, and turnaround. But, in almost every case, the basic goal has been the same: to make fundamental changes in how business is conducted in order to help cope with a new, more challenging market environment.

A few of these corporate change efforts have been very successful. A few have been utter failures. Most fall somewhere in between, with a distinct tilt toward the lower end of the scale. The lessons that can be drawn are interesting and will probably be relevant to even more organizations in the increasingly competitive business environment of the coming decade.

The most general lesson to be learned from the more successful cases is that the change process goes through a series of phases that, in total, usually require a considerable length of time. Skipping steps creates only the illusion of speed and never produces a satisfying result. A second very general lesson is that critical mistakes in any of the phases can have a devastating impact, slowing momentum and negating hard-won gains. Perhaps because we have relatively little experience in renewing organizations, even very capable people often make at least one big error.

Eight steps to transforming your organization



Idea in Brief

Most major change initiatives—whether intended to boost quality, improve culture, or reverse a corporate death spiral—generate only lukewarm results. Many fail miserably.

Why? Kotter maintains that too many managers don't realize transformation is a *process*, not an event. It advances through stages that build on each other. And it takes years. Pressured to accelerate the process, managers skip stages. But shortcuts never work.

Equally troubling, even highly capable managers make critical mistakes—such as declaring victory too soon. Result? Loss of momentum, reversal of hard-won gains, and devastation of the entire transformation effort.

By understanding the stages of change—and the pitfalls unique to each stage—you boost your chances of a successful transformation. The payoff? Your organization flexes with tectonic shifts in competitors, markets, and technologies—leaving rivals far behind.

Error 1: Not Establishing a Great Enough Sense of Urgency

Most successful change efforts begin when some individuals or some groups start to look hard at a company's competitive situation, market position, technological trends, and financial performance. They focus on the potential revenue drop when an important patent expires, the five-year trend in declining margins in a core business, or an emerging market that everyone seems to be ignoring. They then find ways to communicate this information broadly and dramatically, especially with respect to crises, potential crises, or great opportunities that are very timely. This first step is essential because just getting a transformation program started requires the aggressive cooperation of many individuals. Without motivation, people won't help, and the effort goes nowhere.

Compared with other steps in the change process, phase one can sound easy. It is not. Well over 50% of the companies I have watched fail in this first phase. What are the reasons for that failure? Sometimes executives underestimate how hard it can be to drive people out of their comfort zones. Sometimes they grossly overestimate how successful they have already been in increasing urgency. Sometimes they lack patience: "Enough with the preliminaries; let's get on with it." In many cases, executives become paralyzed by the downside possibilities. They worry that employees with seniority will become defensive, that morale will drop, that events will spin out of control, that short-term business results will be jeopardized, that the stock will sink, and that they will be blamed for creating a crisis.

Idea in Practice

To give your transformation effort the best chance of succeeding, take the right actions at each stage—and avoid common pitfalls

Stage	Actions needed	Pitfalls
Establish a		

sense of urgency	• Examine market and competitive realities for potential crises and untapped opportunities. • Convince at least 75% of your managers that the status quo is more dangerous than the unknown.	• Underestimating the difficulty of driving people from their comfort zones • Becoming paralyzed by risks
Form a powerful guiding coalition	• Assemble a group with shared commitment and enough power to lead the change effort. • Encourage them to work	• No prior experience in teamwork at the top • Relegating team leadership to an HR, quality, or strategic-planning executive rather than a senior line manager

	as a team outside the normal hierarchy.	
Create a vision	• Create a vision to direct the change effort. • Develop strategies for realizing that vision.	• Presenting a vision that's too complicated or vague to be communicated in five minutes
Communicate the vision	• Use every vehicle possible to communicate the new vision and strategies for achieving it. • Teach new behaviors by the example of the guiding coalition.	• Undercommunicating the vision • Behaving in ways antithetical to the vision
Empower others to act on the vision	• Remove or alter systems	• Failing to remove powerful individuals

	or structures who resist the undermining change effort the vision. • Encourage risk taking and nontraditional ideas, activities, and actions.	
Plan for and create short-term wins	• Define and engineer visible performance improvements. • Recognize and reward employees contributing to those improvements.	• Leaving short-term successes up to chance • Failing to score successes early enough (12-24 months into the change effort)
Consolidate improvements and produce more change	• Use increased credibility from early wins to change systems,	• Declaring victory too soon—with the first performance improvement • Allowing resistors to convince “troops”

	structures, and policies undermining the vision. • Hire, promote, and develop employees who can implement the vision. • Reinvigorate the change process with new projects and change agents.	that the war has been won
Institutionalize new approaches	• Articulate connections between new behaviors and corporate success. • Create leadership development	• Not creating new social norms and shared values consistent with changes • Promoting people into leadership positions who don't personify the new

	and succession plans consistent with the new approach.	approach

A paralyzed senior management often comes from having too many managers and not enough leaders. Management's mandate is to minimize risk and to keep the current system operating. Change, by definition, requires creating a new system, which in turn always demands leadership. Phase one in a renewal process typically goes nowhere until enough real leaders are promoted or hired into senior-level jobs.

Transformations often begin, and begin well, when an organization has a new head who is a good leader and who sees the need for a major change. If the renewal target is the entire company, the CEO is key. If change is needed in a division, the division general manager is key. When these individuals are not new leaders, great leaders, or change champions, phase one can be a huge challenge.

Bad business results are both a blessing and a curse in the first phase. On the positive side, losing money does catch people's attention. But it also gives less maneuvering room. With good business results, the opposite is true: Convincing people of the need for change is much harder, but you have more resources to help make changes.

But whether the starting point is good performance or bad, in the more successful cases I have witnessed, an individual or a group always facilitates a frank discussion of potentially unpleasant facts about new competition, shrinking margins, decreasing market share, flat earnings, a lack of revenue growth, or other relevant indices of a declining competitive position. Because there seems to be an almost universal human tendency to shoot the bearer of bad news, especially if the head of the organization is not a change champion, executives in these companies often rely on outsiders to bring unwanted information. Wall Street analysts, customers, and consultants can all be

helpful in this regard. The purpose of all this activity, in the words of one former CEO of a large European company, is “to make the status quo seem more dangerous than launching into the unknown.”

In a few of the most successful cases, a group has manufactured a crisis. One CEO deliberately engineered the largest accounting loss in the company’s history, creating huge pressures from Wall Street in the process. One division president commissioned first-ever customer satisfaction surveys, knowing full well that the results would be terrible. He then made these findings public. On the surface, such moves can look unduly risky. But there is also risk in playing it too safe: When the urgency rate is not pumped up enough, the transformation process cannot succeed, and the long-term future of the organization is put in jeopardy.

When is the urgency rate high enough? From what I have seen, the answer is when about 75% of a company’s management is honestly convinced that business as usual is totally unacceptable. Anything less can produce very serious problems later on in the process.

Error 2: Not Creating a Powerful Enough Guiding Coalition

Major renewal programs often start with just one or two people. In cases of successful transformation efforts, the leadership coalition grows and grows over time. But whenever some minimum mass is not achieved early in the effort, nothing much worthwhile happens.

It is often said that major change is impossible unless the head of the organization is an active supporter. What I am talking about goes far beyond that. In successful transformations, the chairman or president or division general manager, plus another five or 15 or 50 people, come together and develop a shared commitment to excellent performance through renewal. In my experience, this group never includes all of the company's most senior executives because some people just won't buy in, at least not at first. But in the most successful cases, the coalition is always pretty powerful—in terms of titles, information and expertise, reputations, and relationships.

In both small and large organizations, a successful guiding team may consist of only three to five people during the first year of a renewal effort. But in big companies, the coalition needs to grow to the 20 to 50 range before much progress can be made in phase three and beyond. Senior managers always form the core of the group. But sometimes you find board members, a representative from a key customer, or even a powerful union leader.

Because the guiding coalition includes members who are not part of senior management, it tends to operate outside of the normal hierarchy by definition. This can be awkward, but it is clearly necessary. If the existing hierarchy were working well, there would be no need for a major transformation. But since the current system is not working, reform generally demands activity outside of formal boundaries, expectations, and protocol.

A high sense of urgency within the managerial ranks helps enormously in putting a guiding coalition together. But more is usually required. Someone needs to get these people together, help them develop a shared assessment of their company's problems and opportunities, and create a minimum level of trust and communication. Off-site retreats, for two or three days, are one popular vehicle for accomplishing this task. I have seen many groups of five

to 35 executives attend a series of these retreats over a period of months.

Companies that fail in phase two usually underestimate the difficulties of producing change and thus the importance of a powerful guiding coalition. Sometimes they have no history of teamwork at the top and therefore undervalue the importance of this type of coalition. Sometimes they expect the team to be led by a staff executive from human resources, quality, or strategic planning instead of a key line manager. No matter how capable or dedicated the staff head, groups without strong line leadership never achieve the power that is required.

Efforts that don't have a powerful enough guiding coalition can make apparent progress for a while. But, sooner or later, the opposition gathers itself together and stops the change.

Error 3: Lacking a Vision

In every successful transformation effort that I have seen, the guiding coalition develops a picture of the future that is relatively easy to communicate and appeals to customers, stockholders, and employees. A vision always goes beyond the numbers that are typically found in five-year plans. A vision says something that helps clarify the direction in which an organization needs to move. Sometimes the first draft comes mostly from a single individual. It is usually a bit blurry, at least initially. But after the coalition works at it for three or five or even 12 months, something much better emerges through their tough analytical thinking and a little dreaming. Eventually, a strategy for achieving that vision is also developed.

In one midsize European company, the first pass at a vision contained two-thirds of the basic ideas that were in the final product. The concept of global reach was in the initial version from the beginning. So was the idea of becoming preeminent in certain businesses. But one central idea in the final version—getting out of low value-added activities—came only after a series of discussions over a period of several months.

Without a sensible vision, a transformation effort can easily dissolve into a list of confusing and incompatible projects that can take the organization in the wrong direction or nowhere at all. Without a sound vision, the reengineering project in the accounting department, the new 360-degree performance appraisal from the human resources department, the plant's quality program, the cultural change project in the sales force will not add up in a meaningful way.

In failed transformations, you often find plenty of plans, directives, and programs but no vision. In one case, a company gave out four-inch-thick notebooks describing its change effort. In mind-numbing detail, the books spelled out procedures, goals, methods, and deadlines. But nowhere was there a clear and compelling statement of where all this was leading. Not surprisingly, most of the employees with whom I talked were either confused or alienated. The big, thick books did not rally them together or inspire change. In fact, they probably had just the opposite effect.

In a few of the less successful cases that I have seen, management had a

sense of direction, but it was too complicated or blurry to be useful. Recently, I asked an executive in a midsize company to describe his vision and received in return a barely comprehensible 30-minute lecture. Buried in his answer were the basic elements of a sound vision. But they were buried—deeply.

A useful rule of thumb: If you can't communicate the vision to someone in five minutes or less and get a reaction that signifies both understanding and interest, you are not yet done with this phase of the transformation process.

Error 4: Undercommunicating the Vision by a Factor of Ten

I've seen three patterns with respect to communication, all very common. In the first, a group actually does develop a pretty good transformation vision and then proceeds to communicate it by holding a single meeting or sending out a single communication. Having used about 0.0001% of the yearly intracompany communication, the group is startled when few people seem to understand the new approach. In the second pattern, the head of the organization spends a considerable amount of time making speeches to employee groups, but most people still don't get it (not surprising, since vision captures only 0.0005% of the total yearly communication). In the third pattern, much more effort goes into newsletters and speeches, but some very visible senior executives still behave in ways that are antithetical to the vision. The net result is that cynicism among the troops goes up, while belief in the communication goes down.

Transformation is impossible unless hundreds or thousands of people are willing to help, often to the point of making short-term sacrifices. Employees will not make sacrifices, even if they are unhappy with the status quo, unless they believe that useful change is possible. Without credible communication, and a lot of it, the hearts and minds of the troops are never captured.

This fourth phase is particularly challenging if the short-term sacrifices include job losses. Gaining understanding and support is tough when downsizing is a part of the vision. For this reason, successful visions usually include new growth possibilities and the commitment to treat fairly anyone who is laid off.

Executives who communicate well incorporate messages into their hour-by-hour activities. In a routine discussion about a business problem, they talk about how proposed solutions fit (or don't fit) into the bigger picture. In a regular performance appraisal, they talk about how the employee's behavior helps or undermines the vision. In a review of a division's quarterly performance, they talk not only about the numbers but also about how the division's executives are contributing to the transformation. In a routine Q&A with employees at a company facility, they tie their answers back to

renewal goals.

In more successful transformation efforts, executives use all existing communication channels to broadcast the vision. They turn boring, unread company newsletters into lively articles about the vision. They take ritualistic, tedious quarterly management meetings and turn them into exciting discussions of the transformation. They throw out much of the company's generic management education and replace it with courses that focus on business problems and the new vision. The guiding principle is simple: Use every possible channel, especially those that are being wasted on nonessential information.

Perhaps even more important, most of the executives I have known in successful cases of major change learn to "walk the talk." They consciously attempt to become a living symbol of the new corporate culture. This is often not easy. A 60-year-old plant manager who has spent precious little time over 40 years thinking about customers will not suddenly behave in a customer-oriented way. But I have witnessed just such a person change, and change a great deal. In that case, a high level of urgency helped. The fact that the man was a part of the guiding coalition and the vision-creation team also helped. So did all the communication, which kept reminding him of the desired behavior, and all the feedback from his peers and subordinates, which helped him see when he was not engaging in that behavior.

Communication comes in both words and deeds, and the latter are often the most powerful form. Nothing undermines change more than behavior by important individuals that is inconsistent with their words.

Error 5: Not Removing Obstacles to the New Vision

Successful transformations begin to involve large numbers of people as the process progresses. Employees are emboldened to try new approaches, to develop new ideas, and to provide leadership. The only constraint is that the actions fit within the broad parameters of the overall vision. The more people involved, the better the outcome.

To some degree, a guiding coalition empowers others to take action simply by successfully communicating the new direction. But communication is never sufficient by itself. Renewal also requires the removal of obstacles. Too often, an employee understands the new vision and wants to help make it happen, but an elephant appears to be blocking the path. In some cases, the elephant is in the person's head, and the challenge is to convince the individual that no external obstacle exists. But in most cases, the blockers are very real.

Sometimes the obstacle is the organizational structure: Narrow job categories can seriously undermine efforts to increase productivity or make it very difficult even to think about customers. Sometimes compensation or performance-appraisal systems make people choose between the new vision and their own self-interest. Perhaps worst of all are bosses who refuse to change and who make demands that are inconsistent with the overall effort.

One company began its transformation process with much publicity and actually made good progress through the fourth phase. Then the change effort ground to a halt because the officer in charge of the company's largest division was allowed to undermine most of the new initiatives. He paid lip service to the process but did not change his behavior or encourage his managers to change. He did not reward the unconventional ideas called for in the vision. He allowed human resource systems to remain intact even when they were clearly inconsistent with the new ideals. I think the officer's motives were complex. To some degree, he did not believe the company needed major change. To some degree, he felt personally threatened by all the change. To some degree, he was afraid that he could not produce both change and the expected operating profit. But despite the fact that they backed the renewal effort, the other officers did virtually nothing to stop the one blocker.

Again, the reasons were complex. The company had no history of confronting problems like this. Some people were afraid of the officer. The CEO was concerned that he might lose a talented executive. The net result was disastrous. Lower-level managers concluded that senior management had lied to them about their commitment to renewal, cynicism grew, and the whole effort collapsed.

In the first half of a transformation, no organization has the momentum, power, or time to get rid of all obstacles. But the big ones must be confronted and removed. If the blocker is a person, it is important that he or she be treated fairly and in a way that is consistent with the new vision. Action is essential, both to empower others and to maintain the credibility of the change effort as a whole.

Error 6: Not Systematically Planning for, and Creating, Short-Term Wins

Real transformation takes time, and a renewal effort risks losing momentum if there are no short-term goals to meet and celebrate. Most people won't go on the long march unless they see compelling evidence in 12 to 24 months that the journey is producing expected results. Without short-term wins, too many people give up or actively join the ranks of those people who have been resisting change.

One to two years into a successful transformation effort, you find quality beginning to go up on certain indices or the decline in net income stopping. You find some successful new product introductions or an upward shift in market share. You find an impressive productivity improvement or a statistically higher customer satisfaction rating. But whatever the case, the win is unambiguous. The result is not just a judgment call that can be discounted by those opposing change.

Creating short-term wins is different from hoping for short-term wins. The latter is passive, the former active. In a successful transformation, managers actively look for ways to obtain clear performance improvements, establish goals in the yearly planning system, achieve the objectives, and reward the people involved with recognition, promotions, and even money. For example, the guiding coalition at a U.S. manufacturing company produced a highly visible and successful new product introduction about 20 months after the start of its renewal effort. The new product was selected about six months into the effort because it met multiple criteria: It could be designed and launched in a relatively short period, it could be handled by a small team of people who were devoted to the new vision, it had upside potential, and the new product-development team could operate outside the established departmental structure without practical problems. Little was left to chance, and the win boosted the credibility of the renewal process.

Managers often complain about being forced to produce short-term wins, but I've found that pressure can be a useful element in a change effort. When it becomes clear to people that major change will take a long time, urgency levels can drop. Commitments to produce short-term wins help keep the

urgency level up and force detailed analytical thinking that can clarify or revise visions.

Error 7: Declaring Victory Too Soon

After a few years of hard work, managers may be tempted to declare victory with the first clear performance improvement. While celebrating a win is fine, declaring the war won can be catastrophic. Until changes sink deeply into a company's culture, a process that can take five to ten years, new approaches are fragile and subject to regression.

In the recent past, I have watched a dozen change efforts operate under the reengineering theme. In all but two cases, victory was declared and the expensive consultants were paid and thanked when the first major project was completed after two to three years. Within two more years, the useful changes that had been introduced slowly disappeared. In two of the ten cases, it's hard to find any trace of the reengineering work today.

Over the past 20 years, I've seen the same sort of thing happen to huge quality projects, organizational development efforts, and more. Typically, the problems start early in the process: The urgency level is not intense enough, the guiding coalition is not powerful enough, and the vision is not clear enough. But it is the premature victory celebration that kills momentum. And then the powerful forces associated with tradition take over.

Ironically, it is often a combination of change initiators and change resisters that creates the premature victory celebration. In their enthusiasm over a clear sign of progress, the initiators go overboard. They are then joined by resisters, who are quick to spot any opportunity to stop change. After the celebration is over, the resisters point to the victory as a sign that the war has been won and the troops should be sent home. Weary troops allow themselves to be convinced that they won. Once home, the foot soldiers are reluctant to climb back on the ships. Soon thereafter, change comes to a halt, and tradition creeps back in.

Instead of declaring victory, leaders of successful efforts use the credibility afforded by short-term wins to tackle even bigger problems. They go after systems and structures that are not consistent with the transformation vision and have not been confronted before. They pay great attention to who is promoted, who is hired, and how people are developed. They include new reengineering projects that are even bigger in scope than the initial ones.

They understand that renewal efforts take not months but years. In fact, in one of the most successful transformations that I have ever seen, we quantified the amount of change that occurred each year over a seven-year period. On a scale of one (low) to ten (high), year one received a two, year two a four, year three a three, year four a seven, year five an eight, year six a four, and year seven a two. The peak came in year five, fully 36 months after the first set of visible wins.

Error 8: Not Anchoring Changes in the Corporation's Culture

In the final analysis, change sticks when it becomes “the way we do things around here,” when it seeps into the bloodstream of the corporate body. Until new behaviors are rooted in social norms and shared values, they are subject to degradation as soon as the pressure for change is removed.

Two factors are particularly important in institutionalizing change in corporate culture. The first is a conscious attempt to show people how the new approaches, behaviors, and attitudes have helped improve performance. When people are left on their own to make the connections, they sometimes create very inaccurate links. For example, because results improved while charismatic Harry was boss, the troops link his mostly idiosyncratic style with those results instead of seeing how their own improved customer service and productivity were instrumental. Helping people see the right connections requires communication. Indeed, one company was relentless, and it paid off enormously. Time was spent at every major management meeting to discuss why performance was increasing. The company newspaper ran article after article showing how changes had boosted earnings.

The second factor is taking sufficient time to make sure that the next generation of top management really does personify the new approach. If the requirements for promotion don't change, renewal rarely lasts. One bad succession decision at the top of an organization can undermine a decade of hard work. Poor succession decisions are possible when boards of directors are not an integral part of the renewal effort. In at least three instances I have seen, the champion for change was the retiring executive, and although his successor was not a resistor, he was not a change champion. Because the boards did not understand the transformations in any detail, they could not see that their choices were not good fits. The retiring executive in one case tried unsuccessfully to talk his board into a less seasoned candidate who better personified the transformation. In the other two cases, the CEOs did not resist the boards' choices, because they felt the transformation could not be undone by their successors. They were wrong. Within two years, signs of renewal began to disappear at both companies.

There are still more mistakes that people make, but these eight are the big ones. I realize that in a short article everything is made to sound a bit too simplistic. In reality, even successful change efforts are messy and full of surprises. But just as a relatively simple vision is needed to guide people through a major change, so a vision of the change process can reduce the error rate. And fewer errors can spell the difference between success and failure.

Originally published March 1995. Reprint R0701J

Marketing Myopia

by Theodore Levitt

EVERY MAJOR INDUSTRY WAS once a growth industry. But some that are now riding a wave of growth enthusiasm are very much in the shadow of decline. Others that are thought of as seasoned growth industries have actually stopped growing. In every case, the reason growth is threatened, slowed, or stopped is *not* because the market is saturated. It is because there has been a failure of management.

Fateful Purposes

The failure is at the top. The executives responsible for it, in the last analysis, are those who deal with broad aims and policies. Thus:

- The railroads did not stop growing because the need for passenger and freight transportation declined. That grew. The railroads are in trouble today not because that need was filled by others (cars, trucks, airplanes, and even telephones) but because it was *not* filled by the railroads themselves. They let others take customers away from them because they assumed themselves to be in the railroad business rather than in the transportation business. The reason they defined their industry incorrectly was that they were railroad oriented instead of transportation oriented; they were product oriented instead of customer oriented.
- Hollywood barely escaped being totally ravished by television. Actually, all the established film companies went through drastic reorganizations. Some simply disappeared. All of them got into trouble not because of TV's inroads but because of their own myopia. As with the railroads, Hollywood defined its business incorrectly. It thought it was in the movie business when it was actually in the entertainment business. "Movies" implied a specific, limited product. This produced a fatuous contentment that from the beginning led producers to view TV as a threat. Hollywood scorned and rejected TV when it should have welcomed it as an opportunity—an opportunity to expand the entertainment business.

Today, TV is a bigger business than the old narrowly defined movie business ever was. Had Hollywood been customer oriented (providing entertainment) rather than product oriented (making movies), would it have gone through the fiscal purgatory that it did? I doubt it. What ultimately

saved Hollywood and accounted for its resurgence was the wave of new young writers, producers, and directors whose previous successes in television had decimated the old movie companies and toppled the big movie moguls.

There are other, less obvious examples of industries that have been and are now endangering their futures by improperly defining their purposes. I shall discuss some of them in detail later and analyze the kind of policies that lead to trouble. Right now, it may help to show what a thoroughly customer-oriented management can do to keep a growth industry growing, even after the obvious opportunities have been exhausted, and here there are two examples that have been around for a long time. They are nylon and glass—specifically, E.I. du Pont de Nemours and Company and Corning Glass Works.

Both companies have great technical competence. Their product orientation is unquestioned. But this alone does not explain their success. After all, who was more pridefully product oriented and product conscious than the erstwhile New England textile companies that have been so thoroughly massacred? The DuPonts and the Cornings have succeeded not primarily because of their product or research orientation but because they have been thoroughly customer oriented also. It is constant watchfulness for opportunities to apply their technical know-how to the creation of customer-satisfying uses that accounts for their prodigious output of successful new products. Without a very sophisticated eye on the customer, most of their new products might have been wrong, their sales methods useless.

Idea in Brief

What business are you *really* in? A seemingly obvious question—but one we should all ask *before* demand for our companies' products or services dwindles.

The railroads failed to ask this same question—and stopped growing. Why? Not because people no longer needed transportation. And not because other innovations (cars, airplanes) filled transportation needs. Rather, railroads stopped growing because *railroads* didn't move to fill those needs. Their executives incorrectly thought that they were in the railroad business, not the transportation business. They viewed themselves as providing a product instead of serving customers. Too many other industries make the same mistake—putting themselves at risk of obsolescence.

How to ensure continued growth for your company? Concentrate on meeting customers' needs rather than selling products. Chemical powerhouse DuPont kept a close eye on its customers' most pressing concerns—and deployed its technical know-how to create an ever-expanding array of products that appealed to customers and continuously enlarged its market. If DuPont had merely found more uses for its flagship invention, nylon, it might not be around today.

Aluminum has also continued to be a growth industry, thanks to the efforts of two wartime-created companies that deliberately set about inventing new customer-satisfying uses. Without Kaiser Aluminum & Chemical Corporation and Reynolds Metals Company, the total demand for aluminum today would be vastly less.

Error of analysis

Some may argue that it is foolish to set the railroads off against aluminum or the movies off against glass. Are not aluminum and glass naturally so versatile that the industries are bound to have more growth opportunities than the railroads and the movies? This view commits precisely the error I have been talking about. It defines an industry or a product or a cluster of know-how so narrowly as to guarantee its premature senescence. When we mention “railroads,” we should make sure we mean “transportation.” As transporters, the railroads still have a good chance for very considerable growth. They are not limited to the railroad business as such (though in my opinion, rail transportation is potentially a much stronger transportation medium than is generally believed).

Idea in Practice

We put our businesses at risk of obsolescence when we accept any of the following myths:

Myth 1: An ever-expanding and more affluent population will ensure our growth. When markets are expanding, we often assume we don't have to think imaginatively about our businesses. Instead, we seek to outdo rivals simply by improving on what we're already doing. The consequence: We increase the efficiency of *making* our products, rather than boosting the value those products deliver to customers.

Myth 2: There is no competitive substitute for our industry's major product. Believing that our products have no rivals makes our companies vulnerable to dramatic innovations from outside our industries—often by smaller, newer companies that are focusing on customer needs rather than the products themselves.

Myth 3: We can protect ourselves through mass production. Few of us can resist the prospect of the increased profits that come with steeply declining unit costs. But focusing on mass production emphasizes our *company's* needs—when we should be emphasizing our *customers'*.

Myth 4: Technical research and development will ensure our growth. When R&D produces breakthrough products, we may be tempted to organize our companies around the technology rather than the consumer. Instead, we should

remain focused on satisfying customer needs.

What the railroads lack is not opportunity but some of the managerial imaginativeness and audacity that made them great. Even an amateur like Jacques Barzun can see what is lacking when he says, “I grieve to see the most advanced physical and social organization of the last century go down in shabby disgrace for lack of the same comprehensive imagination that built it up. [What is lacking is] the will of the companies to survive and to satisfy the public by inventiveness and skill.”^{[1](#)}

Shadow of Obsolescence

It is impossible to mention a single major industry that did not at one time qualify for the magic appellation of “growth industry.” In each case, the industry’s assumed strength lay in the apparently unchallenged superiority of its product. There appeared to be no effective substitute for it. It was itself a runaway substitute for the product it so triumphantly replaced. Yet one after another of these celebrated industries has come under a shadow. Let us look briefly at a few more of them, this time taking examples that have so far received a little less attention.

Dry cleaning

This was once a growth industry with lavish prospects. In an age of wool garments, imagine being finally able to get them clean safely and easily. The boom was on. Yet here we are 30 years after the boom started, and the industry is in trouble. Where has the competition come from? From a better way of cleaning? No. It has come from synthetic fibers and chemical additives that have cut the need for dry cleaning. But this is only the beginning. Lurking in the wings and ready to make chemical dry cleaning totally obsolete is that powerful magician, ultrasonics.

Electric utilities

This is another one of those supposedly “no substitute” products that has been enthroned on a pedestal of invincible growth. When the incandescent lamp came along, kerosene lights were finished. Later, the waterwheel and the steam engine were cut to ribbons by the flexibility, reliability, simplicity, and just plain easy availability of electric motors. The prosperity of electric utilities continues to wax extravagant as the home is converted into a museum of electric gadgetry. How can anybody miss by investing in utilities, with no competition, nothing but growth ahead?

But a second look is not quite so comforting. A score of nonutility companies are well advanced toward developing a powerful chemical fuel cell, which could sit in some hidden closet of every home silently ticking off electric power. The electric lines that vulgarize so many neighborhoods would be eliminated. So would the endless demolition of streets and service interruptions during storms. Also on the horizon is solar energy, again pioneered by nonutility companies.

Who says that the utilities have no competition? They may be natural monopolies now, but tomorrow they may be natural deaths. To avoid this prospect, they too will have to develop fuel cells, solar energy, and other power sources. To survive, they themselves will have to plot the obsolescence of what now produces their livelihood.

Grocery stores

Many people find it hard to realize that there ever was a thriving establishment known as the “corner store.” The supermarket took over with a powerful effectiveness. Yet the big food chains of the 1930s narrowly escaped being completely wiped out by the aggressive expansion of independent supermarkets. The first genuine supermarket was opened in 1930, in Jamaica, Long Island. By 1933, supermarkets were thriving in California, Ohio, Pennsylvania, and elsewhere. Yet the established chains pompously ignored them. When they chose to notice them, it was with such derisive descriptions as “cheapy,” “horse-and-buggy,” “cracker-barrel storekeeping,” and “unethical opportunists.”

The executive of one big chain announced at the time that he found it “hard to believe that people will drive for miles to shop for foods and sacrifice the personal service chains have perfected and to which [the consumer] is accustomed.”² As late as 1936, the National Wholesale Grocers convention and the New Jersey Retail Grocers Association said there was nothing to fear. They said that the supers’ narrow appeal to the price buyer limited the size of their market. They had to draw from miles around. When imitators came, there would be wholesale liquidations as volume fell. The high sales of the supers were said to be partly due to their novelty. People wanted convenient neighborhood grocers. If the neighborhood stores would “cooperate with their suppliers, pay attention to their costs, and improve their service,” they would be able to weather the competition until it blew over.³

It never blew over. The chains discovered that survival required going into the supermarket business. This meant the wholesale destruction of their huge investments in corner store sites and in established distribution and merchandising methods. The companies with “the courage of their convictions” resolutely stuck to the corner store philosophy. They kept their pride but lost their shirts.

A self-deceiving cycle

But memories are short. For example, it is hard for people who today confidently hail the twin messiahs of electronics and chemicals to see how things could possibly go wrong with these galloping industries. They probably also cannot see how a reasonably sensible businessperson could have been as myopic as the famous Boston millionaire who early in the twentieth century unintentionally sentenced his heirs to poverty by stipulating that his entire estate be forever invested exclusively in electric streetcar securities. His posthumous declaration, “There will always be a big demand for efficient urban transportation,” is no consolation to his heirs, who sustain life by pumping gasoline at automobile filling stations.

Yet, in a casual survey I took among a group of intelligent business executives, nearly half agreed that it would be hard to hurt their heirs by tying their estates forever to the electronics industry. When I then confronted them with the Boston streetcar example, they chorused unanimously, “That’s different!” But is it? Is not the basic situation identical?

In truth, *there is no such thing as a growth industry*, I believe. There are only companies organized and operated to create and capitalize on growth opportunities. Industries that assume themselves to be riding some automatic growth escalator invariably descend into stagnation. The history of every dead and dying “growth” industry shows a self-deceiving cycle of bountiful expansion and undetected decay. There are four conditions that usually guarantee this cycle:

1. The belief that growth is assured by an expanding and more affluent population;
2. The belief that there is no competitive substitute for the industry’s major product;
3. Too much faith in mass production and in the advantages of rapidly declining unit costs as output rises;

4. Preoccupation with a product that lends itself to carefully controlled scientific experimentation, improvement, and manufacturing cost reduction.

I should like now to examine each of these conditions in some detail. To build my case as boldly as possible, I shall illustrate the points with reference to three industries: petroleum, automobiles, and electronics. I'll focus on petroleum in particular, because it spans more years and more vicissitudes. Not only do these three industries have excellent reputations with the general public and also enjoy the confidence of sophisticated investors, but their managements have become known for progressive thinking in areas like financial control, product research, and management training. If obsolescence can cripple even these industries, it can happen anywhere.

Population Myth

The belief that profits are assured by an expanding and more affluent population is dear to the heart of every industry. It takes the edge off the apprehensions everybody understandably feels about the future. If consumers are multiplying and also buying more of your product or service, you can face the future with considerably more comfort than if the market were shrinking. An expanding market keeps the manufacturer from having to think very hard or imaginatively. If thinking is an intellectual response to a problem, then the absence of a problem leads to the absence of thinking. If your product has an automatically expanding market, then you will not give much thought to how to expand it.

One of the most interesting examples of this is provided by the petroleum industry. Probably our oldest growth industry, it has an enviable record. While there are some current concerns about its growth rate, the industry itself tends to be optimistic.

But I believe it can be demonstrated that it is undergoing a fundamental yet typical change. It is not only ceasing to be a growth industry but may actually be a declining one, relative to other businesses. Although there is widespread unawareness of this fact, it is conceivable that in time, the oil industry may find itself in much the same position of retrospective glory that the railroads are now in. Despite its pioneering work in developing and applying the present-value method of investment evaluation, in employee relations, and in working with developing countries, the petroleum business is a distressing example of how complacency and wrongheadedness can stubbornly convert opportunity into near disaster.

One of the characteristics of this and other industries that have believed very strongly in the beneficial consequences of an expanding population, while at the same time having a generic product for which there has appeared to be no competitive substitute, is that the individual companies have sought to outdo their competitors by improving on what they are already doing. This makes sense, of course, if one assumes that sales are tied to the country's population strings, because the customer can compare products only on a feature-by-feature basis. I believe it is significant, for example, that not since

John D. Rockefeller sent free kerosene lamps to China has the oil industry done anything really outstanding to create a demand for its product. Not even in product improvement has it showered itself with eminence. The greatest single improvement—the development of tetraethyl lead—came from outside the industry, specifically from General Motors and DuPont. The big contributions made by the industry itself are confined to the technology of oil exploration, oil production, and oil refining.

Asking for trouble

In other words, the petroleum industry's efforts have focused on improving the *efficiency* of getting and making its product, not really on improving the generic product or its marketing. Moreover, its chief product has continually been defined in the narrowest possible terms—namely, gasoline, not energy, fuel, or transportation. This attitude has helped assure that:

- Major improvements in gasoline quality tend not to originate in the oil industry. The development of superior alternative fuels also comes from outside the oil industry, as will be shown later.
- Major innovations in automobile fuel marketing come from small, new oil companies that are not primarily preoccupied with production or refining. These are the companies that have been responsible for the rapidly expanding multipump gasoline stations, with their successful emphasis on large and clean layouts, rapid and efficient driveway service, and quality gasoline at low prices.

Thus, the oil industry is asking for trouble from outsiders. Sooner or later, in this land of hungry investors and entrepreneurs, a threat is sure to come. The possibility of this will become more apparent when we turn to the next dangerous belief of many managements. For the sake of continuity, because this second belief is tied closely to the first, I shall continue with the same example.

The idea of indispensability

The petroleum industry is pretty much convinced that there is no competitive substitute for its major product, gasoline—or, if there is, that it will continue to be a derivative of crude oil, such as diesel fuel or kerosene jet fuel.

There is a lot of automatic wishful thinking in this assumption. The trouble is that most refining companies own huge amounts of crude oil reserves. These have value only if there is a market for products into which oil can be converted. Hence the tenacious belief in the continuing competitive superiority of automobile fuels made from crude oil.

This idea persists despite all historic evidence against it. The evidence not only shows that oil has never been a superior product for any purpose for very long but also that the oil industry has never really been a growth industry. Rather, it has been a succession of different businesses that have gone through the usual historic cycles of growth, maturity, and decay. The industry's overall survival is owed to a series of miraculous escapes from total obsolescence, of last-minute and unexpected reprieves from total disaster reminiscent of the perils of Pauline.

The perils of petroleum

To illustrate, I shall sketch in only the main episodes. First, crude oil was largely a patent medicine. But even before that fad ran out, demand was greatly expanded by the use of oil in kerosene lamps. The prospect of lighting the world's lamps gave rise to an extravagant promise of growth. The prospects were similar to those the industry now holds for gasoline in other parts of the world. It can hardly wait for the underdeveloped nations to get a car in every garage.

In the days of the kerosene lamp, the oil companies competed with each other and against gaslight by trying to improve the illuminating characteristics of kerosene. Then suddenly the impossible happened. Edison invented a light that was totally nondependent on crude oil. Had it not been for the growing use of kerosene in space heaters, the incandescent lamp would have completely finished oil as a growth industry at that time. Oil would have been good for little else than axle grease.

Then disaster and reprieve struck again. Two great innovations occurred, neither originating in the oil industry. First, the successful development of coal-burning domestic central-heating systems made the space heater obsolete. While the industry reeled, along came its most magnificent boost yet: the internal combustion engine, also invented by outsiders. Then, when the prodigious expansion for gasoline finally began to level off in the 1920s, along came the miraculous escape of the central oil heater. Once again, the escape was provided by an outsider's invention and development. And when that market weakened, wartime demand for aviation fuel came to the rescue. After the war, the expansion of civilian aviation, the dieselization of railroads, and the explosive demand for cars and trucks kept the industry's growth in high gear.

Meanwhile, centralized oil heating—whose boom potential had only recently been proclaimed—ran into severe competition from natural gas. While the oil companies themselves owned the gas that now competed with their oil, the industry did not originate the natural gas revolution, nor has it to this day greatly profited from its gas ownership. The gas revolution was made by newly formed transmission companies that marketed the product with an aggressive ardor. They started a magnificent new industry, first against the

advice and then against the resistance of the oil companies.

By all the logic of the situation, the oil companies themselves should have made the gas revolution. They not only owned the gas, they also were the only people experienced in handling, scrubbing, and using it and the only people experienced in pipeline technology and transmission. They also understood heating problems. But, partly because they knew that natural gas would compete with their own sale of heating oil, the oil companies pooched the potential of gas. The revolution was finally started by oil pipeline executives who, unable to persuade their own companies to go into gas, quit and organized the spectacularly successful gas transmission companies. Even after their success became painfully evident to the oil companies, the latter did not go into gas transmission. The multibillion-dollar business that should have been theirs went to others. As in the past, the industry was blinded by its narrow preoccupation with a specific product and the value of its reserves. It paid little or no attention to its customers' basic needs and preferences.

The postwar years have not witnessed any change. Immediately after World War II, the oil industry was greatly encouraged about its future by the rapid increase in demand for its traditional line of products. In 1950, most companies projected annual rates of domestic expansion of around 6% through at least 1975. Though the ratio of crude oil reserves to demand in the free world was about 20 to 1, with 10 to 1 being usually considered a reasonable working ratio in the United States, booming demand sent oil explorers searching for more without sufficient regard to what the future really promised. In 1952, they "hit" in the Middle East; the ratio skyrocketed to 42 to 1. If gross additions to reserves continue at the average rate of the past five years (37 billion barrels annually), then by 1970, the reserve ratio will be up to 45 to 1. This abundance of oil has weakened crude and product prices all over the world.

An uncertain future

Management cannot find much consolation today in the rapidly expanding petrochemical industry, another oil-using idea that did not originate in the leading firms. The total U.S. production of petrochemicals is equivalent to about 2% (by volume) of the demand for all petroleum products. Although the petrochemical industry is now expected to grow by about 10% per year, this will not offset other drains on the growth of crude oil consumption. Furthermore, while petrochemical products are many and growing, it is important to remember that there are nonpetroleum sources of the basic raw material, such as coal. Besides, a lot of plastics can be produced with relatively little oil. A 50,000-barrel-per-day oil refinery is now considered the absolute minimum size for efficiency. But a 5,000-barrel-per-day chemical plant is a giant operation.

Oil has never been a continuously strong growth industry. It has grown by fits and starts, always miraculously saved by innovations and developments not of its own making. The reason it has not grown in a smooth progression is that each time it thought it had a superior product safe from the possibility of competitive substitutes, the product turned out to be inferior and notoriously subject to obsolescence. Until now, gasoline (for motor fuel, anyhow) has escaped this fate. But, as we shall see later, it too may be on its last legs.

The point of all this is that there is no guarantee against product obsolescence. If a company's own research does not make a product obsolete, another's will. Unless an industry is especially lucky, as oil has been until now, it can easily go down in a sea of red figures—just as the railroads have, as the buggy whip manufacturers have, as the corner grocery chains have, as most of the big movie companies have, and, indeed, as many other industries have.

The best way for a firm to be lucky is to make its own luck. That requires knowing what makes a business successful. One of the greatest enemies of this knowledge is mass production.

Production Pressures

Mass production industries are impelled by a great drive to produce all they can. The prospect of steeply declining unit costs as output rises is more than most companies can usually resist. The profit possibilities look spectacular. All effort focuses on production. The result is that marketing gets neglected.

John Kenneth Galbraith contends that just the opposite occurs.⁴ Output is so prodigious that all effort concentrates on trying to get rid of it. He says this accounts for singing commercials, the desecration of the countryside with advertising signs, and other wasteful and vulgar practices. Galbraith has a finger on something real, but he misses the strategic point. Mass production does indeed generate great pressure to “move” the product. But what usually gets emphasized is selling, not marketing. Marketing, a more sophisticated and complex process, gets ignored.

The difference between marketing and selling is more than semantic. Selling focuses on the needs of the seller, marketing on the needs of the buyer. Selling is preoccupied with the seller’s need to convert the product into cash, marketing with the idea of satisfying the needs of the customer by means of the product and the whole cluster of things associated with creating, delivering, and, finally, consuming it.

In some industries, the enticements of full mass production have been so powerful that top management in effect has told the sales department, “You get rid of it; we’ll worry about profits.” By contrast, a truly marketing-minded firm tries to create value-satisfying goods and services that consumers will want to buy. What it offers for sale includes not only the generic product or service but also how it is made available to the customer, in what form, when, under what conditions, and at what terms of trade. Most important, what it offers for sale is determined not by the seller but by the buyer. The seller takes cues from the buyer in such a way that the product becomes a consequence of the marketing effort, not vice versa.

A lag in Detroit

This may sound like an elementary rule of business, but that does not keep it from being violated wholesale. It is certainly more violated than honored. Take the automobile industry.

Here mass production is most famous, most honored, and has the greatest impact on the entire society. The industry has hitched its fortune to the relentless requirements of the annual model change, a policy that makes customer orientation an especially urgent necessity. Consequently, the auto companies annually spend millions of dollars on consumer research. But the fact that the new compact cars are selling so well in their first year indicates that Detroit's vast researches have for a long time failed to reveal what customers really wanted. Detroit was not convinced that people wanted anything different from what they had been getting until it lost millions of customers to other small-car manufacturers.

How could this unbelievable lag behind consumer wants have been perpetuated for so long? Why did not research reveal consumer preferences before consumers' buying decisions themselves revealed the facts? Is that not what consumer research is for—to find out before the fact what is going to happen? The answer is that Detroit never really researched customers' wants. It only researched their preferences between the kinds of things it had already decided to offer them. For Detroit is mainly product oriented, not customer oriented. To the extent that the customer is recognized as having needs that the manufacturer should try to satisfy, Detroit usually acts as if the job can be done entirely by product changes. Occasionally, attention gets paid to financing, too, but that is done more in order to sell than to enable the customer to buy.

As for taking care of other customer needs, there is not enough being done to write about. The areas of the greatest unsatisfied needs are ignored or, at best, get stepchild attention. These are at the point of sale and on the matter of automotive repair and maintenance. Detroit views these problem areas as being of secondary importance. That is underscored by the fact that the retailing and servicing ends of this industry are neither owned and operated nor controlled by the manufacturers. Once the car is produced, things are pretty much in the dealer's inadequate hands. Illustrative of Detroit's arms-

length attitude is the fact that, while servicing holds enormous sales-stimulating, profit-building opportunities, only 57 of Chevrolet's 7,000 dealers provide night maintenance service.

Motorists repeatedly express their dissatisfaction with servicing and their apprehensions about buying cars under the present selling setup. The anxieties and problems they encounter during the auto buying and maintenance processes are probably more intense and widespread today than many years ago. Yet the automobile companies do not seem to listen to or take their cues from the anguished consumer. If they do listen, it must be through the filter of their own preoccupation with production. The marketing effort is still viewed as a necessary consequence of the product—not vice versa, as it should be. That is the legacy of mass production, with its parochial view that profit resides essentially in low-cost full production.

What Ford put first

The profit lure of mass production obviously has a place in the plans and strategy of business management, but it must always *follow* hard thinking about the customer. This is one of the most important lessons we can learn from the contradictory behavior of Henry Ford. In a sense, Ford was both the most brilliant and the most senseless marketer in American history. He was senseless because he refused to give the customer anything but a black car. He was brilliant because he fashioned a production system designed to fit market needs. We habitually celebrate him for the wrong reason: for his production genius. His real genius was marketing. We think he was able to cut his selling price and therefore sell millions of \$500 cars because his invention of the assembly line had reduced the costs. Actually, he invented the assembly line because he had concluded that at \$500 he could sell millions of cars. Mass production was the *result*, not the cause, of his low prices.

Ford emphasized this point repeatedly, but a nation of production-oriented business managers refuses to hear the great lesson he taught. Here is his operating philosophy as he expressed it succinctly:

Our policy is to reduce the price, extend the operations, and improve the article. You will notice that the reduction of price comes first. We have never considered any costs as fixed. Therefore we first reduce the price to the point where we believe more sales will result. Then we go ahead and try to make the prices. We do not bother about the costs. The new price forces the costs down. The more usual way is to take the costs and then determine the price; and although that method may be scientific in the narrow sense, it is not scientific in the broad sense, because what earthly use is it to know the cost if it tells you that you cannot manufacture at a price at which the article can be sold? But more to the point is the fact that, although one may calculate what a cost is, and of course all of our costs are carefully calculated, no one knows what a cost ought to be. One of the ways of discovering . . . is to name a price so low as to force everybody in the place to the highest point of efficiency.

The low price makes everybody dig for profits. We make more discoveries concerning manufacturing and selling under this forced method than by any method of leisurely investigation.⁵

Product provincialism

The tantalizing profit possibilities of low unit production costs may be the most seriously self-deceiving attitude that can afflict a company, particularly a “growth” company, where an apparently assured expansion of demand already tends to undermine a proper concern for the importance of marketing and the customer.

The usual result of this narrow preoccupation with so-called concrete matters is that instead of growing, the industry declines. It usually means that the product fails to adapt to the constantly changing patterns of consumer needs and tastes, to new and modified marketing institutions and practices, or to product developments in competing or complementary industries. The industry has its eyes so firmly on its own specific product that it does not see how it is being made obsolete.

The classic example of this is the buggy whip industry. No amount of product improvement could stave off its death sentence. But had the industry defined itself as being in the transportation business rather than in the buggy whip business, it might have survived. It would have done what survival always entails—that is, change. Even if it had only defined its business as providing a stimulant or catalyst to an energy source, it might have survived by becoming a manufacturer of, say, fan belts or air cleaners.

What may someday be a still more classic example is, again, the oil industry. Having let others steal marvelous opportunities from it (including natural gas, as already mentioned; missile fuels; and jet engine lubricants), one would expect it to have taken steps never to let that happen again. But this is not the case. We are now seeing extraordinary new developments in fuel systems specifically designed to power automobiles. Not only are these developments concentrated in firms outside the petroleum industry, but petroleum is almost systematically ignoring them, securely content in its wedded bliss to oil. It is the story of the kerosene lamp versus the incandescent lamp all over again. Oil is trying to improve hydrocarbon fuels rather than develop *any* fuels best suited to the needs of their users, whether or not made in different ways and with different raw materials from oil.

Here are some things that nonpetroleum companies are working on. More than a dozen such firms now have advanced working models of energy

systems which, when perfected, will replace the internal combustion engine and eliminate the demand for gasoline. The superior merit of each of these systems is their elimination of frequent, time-consuming, and irritating refueling stops. Most of these systems are fuel cells designed to create electrical energy directly from chemicals without combustion. Most of them use chemicals that are not derived from oil—generally, hydrogen and oxygen.

Several other companies have advanced models of electric storage batteries designed to power automobiles. One of these is an aircraft producer that is working jointly with several electric utility companies. The latter hope to use off-peak generating capacity to supply overnight plug-in battery regeneration. Another company, also using the battery approach, is a medium-sized electronics firm with extensive small-battery experience that it developed in connection with its work on hearing aids. It is collaborating with an automobile manufacturer. Recent improvements arising from the need for high-powered miniature power storage plants in rockets have put us within reach of a relatively small battery capable of withstanding great overloads or surges of power. Germanium diode applications and batteries using sintered plate and nickel cadmium techniques promise to make a revolution in our energy sources.

Solar energy conversion systems are also getting increasing attention. One usually cautious Detroit auto executive recently ventured that solar-powered cars might be common by 1980.

As for the oil companies, they are more or less “watching developments,” as one research director put it to me. A few are doing a bit of research on fuel cells, but this research is almost always confined to developing cells powered by hydrocarbon chemicals. None of them is enthusiastically researching fuel cells, batteries, or solar power plants. None of them is spending a fraction as much on research in these profoundly important areas as it is on the usual run-of-the-mill things like reducing combustion chamber deposits in gasoline engines. One major integrated petroleum company recently took a tentative look at the fuel cell and concluded that although “the companies actively working on it indicate a belief in ultimate success...the timing and magnitude of its impact are too remote to warrant recognition in our forecasts.”

One might, of course, ask, Why should the oil companies do anything different? Would not chemical fuel cells, batteries, or solar energy kill the present product lines? The answer is that they would indeed, and that is

precisely the reason for the oil firms' having to develop these power units before their competitors do, so they will not be companies without an industry.

Management might be more likely to do what is needed for its own preservation if it thought of itself as being in the energy business. But even that will not be enough if it persists in imprisoning itself in the narrow grip of its tight product orientation. It has to think of itself as taking care of customer needs, not finding, refining, or even selling oil. Once it genuinely thinks of its business as taking care of people's transportation needs, nothing can stop it from creating its own extravagantly profitable growth.

Creative destruction

Since words are cheap and deeds are dear, it may be appropriate to indicate what this kind of thinking involves and leads to. Let us start at the beginning: the customer. It can be shown that motorists strongly dislike the bother, delay, and experience of buying gasoline. People actually do not buy gasoline. They cannot see it, taste it, feel it, appreciate it, or really test it. What they buy is the right to continue driving their cars. The gas station is like a tax collector to whom people are compelled to pay a periodic toll as the price of using their cars. This makes the gas station a basically unpopular institution. It can never be made popular or pleasant, only less unpopular, less unpleasant.

Reducing its unpopularity completely means eliminating it. Nobody likes a tax collector, not even a pleasantly cheerful one. Nobody likes to interrupt a trip to buy a phantom product, not even from a handsome Adonis or a seductive Venus. Hence, companies that are working on exotic fuel substitutes that will eliminate the need for frequent refueling are heading directly into the outstretched arms of the irritated motorist. They are riding a wave of inevitability, not because they are creating something that is technologically superior or more sophisticated but because they are satisfying a powerful customer need. They are also eliminating noxious odors and air pollution.

Once the petroleum companies recognize the customer-satisfying logic of what another power system can do, they will see that they have no more choice about working on an efficient, long-lasting fuel (or some way of delivering present fuels without bothering the motorist) than the big food chains had a choice about going into the supermarket business or the vacuum tube companies had a choice about making semiconductors. For their own good, the oil firms will have to destroy their own highly profitable assets. No amount of wishful thinking can save them from the necessity of engaging in this form of “creative destruction.”

I phrase the need as strongly as this because I think management must make quite an effort to break itself loose from conventional ways. It is all too easy in this day and age for a company or industry to let its sense of purpose become dominated by the economies of full production and to develop a

dangerously lopsided product orientation. In short, if management lets itself drift, it invariably drifts in the direction of thinking of itself as producing goods and services, not customer satisfactions. While it probably will not descend to the depths of telling its salespeople, “You get rid of it; we’ll worry about profits,” it can, without knowing it, be practicing precisely that formula for withering decay. The historic fate of one growth industry after another has been its suicidal product provincialism.

Dangers of R&D

Another big danger to a firm's continued growth arises when top management is wholly transfixed by the profit possibilities of technical research and development. To illustrate, I shall turn first to a new industry—electronics—and then return once more to the oil companies. By comparing a fresh example with a familiar one, I hope to emphasize the prevalence and insidiousness of a hazardous way of thinking.

Marketing shortchanged

In the case of electronics, the greatest danger that faces the glamorous new companies in this field is not that they do not pay enough attention to research and development but that they pay too much attention to it. And the fact that the fastest-growing electronics firms owe their eminence to their heavy emphasis on technical research is completely beside the point. They have vaulted to affluence on a sudden crest of unusually strong general receptiveness to new technical ideas. Also, their success has been shaped in the virtually guaranteed market of military subsidies and by military orders that in many cases actually preceded the existence of facilities to make the products. Their expansion has, in other words, been almost totally devoid of marketing effort.

Thus, they are growing up under conditions that come dangerously close to creating the illusion that a superior product will sell itself. It is not surprising that, having created a successful company by making a superior product, management continues to be oriented toward the product rather than the people who consume it. It develops the philosophy that continued growth is a matter of continued product innovation and improvement.

A number of other factors tend to strengthen and sustain this belief:

1. Because electronic products are highly complex and sophisticated, managements become top-heavy with engineers and scientists. This creates a selective bias in favor of research and production at the expense of marketing. The organization tends to view itself as making things rather than as satisfying customer needs. Marketing gets treated as a residual activity, “something else” that must be done once the vital job of product creation and production is completed.
2. To this bias in favor of product research, development, and production is added the bias in favor of dealing with controllable variables. Engineers and scientists are at home in the world of concrete things like machines, test tubes, production lines, and even balance sheets. The abstractions to which they feel kindly are those

that are testable or manipulatable in the laboratory or, if not testable, then functional, such as Euclid's axioms. In short, the managements of the new glamour-growth companies tend to favor business activities that lend themselves to careful study, experimentation, and control—the hard, practical realities of the lab, the shop, and the books.

What gets shortchanged are the realities of the *market*. Consumers are unpredictable, varied, fickle, stupid, shortsighted, stubborn, and generally bothersome. This is not what the engineer managers say, but deep down in their consciousness, it is what they believe. And this accounts for their concentration on what they know and what they can control—namely, product research, engineering, and production. The emphasis on production becomes particularly attractive when the product can be made at declining unit costs. There is no more inviting way of making money than by running the plant full blast.

The top-heavy science-engineering-production orientation of so many electronics companies works reasonably well today because they are pushing into new frontiers in which the armed services have pioneered virtually assured markets. The companies are in the felicitous position of having to fill, not find, markets, of not having to discover what the customer needs and wants but of having the customer voluntarily come forward with specific new product demands. If a team of consultants had been assigned specifically to design a business situation calculated to prevent the emergence and development of a customer-oriented marketing viewpoint, it could not have produced anything better than the conditions just described.

Stepchild treatment

The oil industry is a stunning example of how science, technology, and mass production can divert an entire group of companies from their main task. To the extent the consumer is studied at all (which is not much), the focus is forever on getting information that is designed to help the oil companies improve what they are now doing. They try to discover more convincing advertising themes, more effective sales promotional drives, what the market shares of the various companies are, what people like or dislike about service station dealers and oil companies, and so forth. Nobody seems as interested in probing deeply into the basic human needs that the industry might be trying to satisfy as in probing into the basic properties of the raw material that the companies work with in trying to deliver customer satisfactions.

Basic questions about customers and markets seldom get asked. The latter occupy a stepchild status. They are recognized as existing, as having to be taken care of, but not worth very much real thought or dedicated attention. No oil company gets as excited about the customers in its own backyard as about the oil in the Sahara Desert. Nothing illustrates better the neglect of marketing than its treatment in the industry press.

The centennial issue of the *American Petroleum Institute Quarterly*, published in 1959 to celebrate the discovery of oil in Titusville, Pennsylvania, contained 21 feature articles proclaiming the industry's greatness. Only one of these talked about its achievements in marketing, and that was only a pictorial record of how service station architecture has changed. The issue also contained a special section on "New Horizons," which was devoted to showing the magnificent role oil would play in America's future. Every reference was ebulliently optimistic, never implying once that oil might have some hard competition. Even the reference to atomic energy was a cheerful catalog of how oil would help make atomic energy a success. There was not a single apprehension that the oil industry's affluence might be threatened or a suggestion that one "new horizon" might include new and better ways of serving oil's present customers.

But the most revealing example of the stepchild treatment that marketing gets is still another special series of short articles on "The Revolutionary Potential of Electronics." Under that heading, this list of articles appeared in

the table of contents:

- “In the Search for Oil”
- “In Production Operations”
- “In Refinery Processes”
- “In Pipeline Operations”

Significantly, every one of the industry’s major functional areas is listed, *except* marketing. Why? Either it is believed that electronics holds no revolutionary potential for petroleum marketing (which is palpably wrong), or the editors forgot to discuss marketing (which is more likely and illustrates its stepchild status).

The order in which the four functional areas are listed also betrays the alienation of the oil industry from the consumer. The industry is implicitly defined as beginning with the search for oil and ending with its distribution from the refinery. But the truth is, it seems to me, that the industry begins with the needs of the customer for its products. From that primal position its definition moves steadily back stream to areas of progressively lesser importance until it finally comes to rest at the search for oil.

The beginning and end

The view that an industry is a customer-satisfying process, not a goods-producing process, is vital for all businesspeople to understand. An industry begins with the customer and his or her needs, not with a patent, a raw material, or a selling skill. Given the customer's needs, the industry develops backwards, first concerning itself with the physical *delivery* of customer satisfactions. Then it moves back further to *creating* the things by which these satisfactions are in part achieved. How these materials are created is a matter of indifference to the customer, hence the particular form of manufacturing, processing, or what have you cannot be considered as a vital aspect of the industry. Finally, the industry moves back still further to *finding* the raw materials necessary for making its products.

The irony of some industries oriented toward technical research and development is that the scientists who occupy the high executive positions are totally unscientific when it comes to defining their companies' overall needs and purposes. They violate the first two rules of the scientific method: being aware of and defining their companies' problems and then developing testable hypotheses about solving them. They are scientific only about the convenient things, such as laboratory and product experiments.

The customer (and the satisfaction of his or her deepest needs) is not considered to be "the problem"—not because there is any certain belief that no such problem exists but because an organizational lifetime has conditioned management to look in the opposite direction. Marketing is a stepchild.

I do not mean that selling is ignored. Far from it. But selling, again, is not marketing. As already pointed out, selling concerns itself with the tricks and techniques of getting people to exchange their cash for your product. It is not concerned with the values that the exchange is all about. And it does not, as marketing invariably does, view the entire business process as consisting of a tightly integrated effort to discover, create, arouse, and satisfy customer needs. The customer is somebody "out there" who, with proper cunning, can be separated from his or her loose change.

Actually, not even selling gets much attention in some technologically minded firms. Because there is a virtually guaranteed market for the abundant

flow of their new products, they do not actually know what a real market is. It is as if they lived in a planned economy, moving their products routinely from factory to retail outlet. Their successful concentration on products tends to convince them of the soundness of what they have been doing, and they fail to see the gathering clouds over the market.

Less than 75 years ago, American railroads enjoyed a fierce loyalty among astute Wall Streeters. European monarchs invested in them heavily. Eternal wealth was thought to be the benediction for anybody who could scrape together a few thousand dollars to put into rail stocks. No other form of transportation could compete with the railroads in speed, flexibility, durability, economy, and growth potentials.

As Jacques Barzun put it, “By the turn of the century it was an institution, an image of man, a tradition, a code of honor, a source of poetry, a nursery of boyhood desires, a sublimest of toys, and the most solemn machine—next to the funeral hearse—that marks the epochs in man’s life.”⁶

Even after the advent of automobiles, trucks, and airplanes, the railroad tycoons remained imperturbably self-confident. If you had told them 60 years ago that in 30 years they would be flat on their backs, broke, and pleading for government subsidies, they would have thought you totally demented. Such a future was simply not considered possible. It was not even a discussable subject, or an askable question, or a matter that any sane person would consider worth speculating about. Yet a lot of “insane” notions now have matter-of-fact acceptance—for example, the idea of 100-ton tubes of metal moving smoothly through the air 20,000 feet above the earth, loaded with 100 sane and solid citizens casually drinking martinis—and they have dealt cruel blows to the railroads.

What specifically must other companies do to avoid this fate? What does customer orientation involve? These questions have in part been answered by the preceding examples and analysis. It would take another article to show in detail what is required for specific industries. In any case, it should be obvious that building an effective customer-oriented company involves far

more than good intentions or promotional tricks; it involves profound matters of human organization and leadership. For the present, let me merely suggest what appear to be some general requirements.

The visceral feel of greatness

Obviously, the company has to do what survival demands. It has to adapt to the requirements of the market, and it has to do it sooner rather than later. But mere survival is a so-so aspiration. Anybody can survive in some way or other, even the skid row bum. The trick is to survive gallantly, to feel the surging impulse of commercial mastery: not just to experience the sweet smell of success but to have the visceral feel of entrepreneurial greatness.

No organization can achieve greatness without a vigorous leader who is driven onward by a pulsating *will to succeed*. A leader has to have a vision of grandeur, a vision that can produce eager followers in vast numbers. In business, the followers are the customers.

In order to produce these customers, the entire corporation must be viewed as a customer-creating and customer-satisfying organism. Management must think of itself not as producing products but as providing customer-creating value satisfactions. It must push this idea (and everything it means and requires) into every nook and cranny of the organization. It has to do this continuously and with the kind of flair that excites and stimulates the people in it. Otherwise, the company will be merely a series of pigeonholed parts, with no consolidating sense of purpose or direction.

In short, the organization must learn to think of itself not as producing goods or services but as *buying customers*, as doing the things that will make people *want* to do business with it. And the chief executive has the inescapable responsibility for creating this environment, this viewpoint, this attitude, this aspiration. The chief executive must set the company's style, its direction, and its goals. This means knowing precisely where he or she wants to go and making sure the whole organization is enthusiastically aware of where that is. This is a first requisite of leadership, for *unless a leader knows where he is going, any road will take him there*.

If any road is okay, the chief executive might as well pack his attaché case and go fishing. If an organization does not know or care where it is going, it does not need to advertise that fact with a ceremonial figurehead. Everybody will notice it soon enough.

Notes

- [1.](#) Jacques Barzun, “Trains and the Mind of Man,” *Holiday*, February 1960.
- [2.](#) For more details, see M.M. Zimmerman, *The Super Market: A Revolution in Distribution* (McGraw-Hill, 1955).
- [3.](#) Ibid., pp. 45–47.
- [4.](#) John Kenneth Galbraith, *The Affluent Society* (Houghton Mifflin, 1958).
- [5.](#) Henry Ford, *My Life and Work* (Doubleday, 1923).
- [6.](#) Barzun, “Trains and the Mind of Man.”

What Is Strategy?

by Michael E. Porter

I. Operational Effectiveness Is Not Strategy

For almost two decades, managers have been learning to play by a new set of rules. Companies must be flexible to respond rapidly to competitive and market changes. They must benchmark continuously to achieve best practice. They must outsource aggressively to gain efficiencies. And they must nurture a few core competencies in race to stay ahead of rivals.

Positioning—once the heart of strategy—is rejected as too static for today’s dynamic markets and changing technologies. According to the new dogma, rivals can quickly copy any market position, and competitive advantage is, at best, temporary.

But those beliefs are dangerous half-truths, and they are leading more and more companies down the path of mutually destructive competition. True, some barriers to competition are falling as regulation eases and markets become global. True, companies have properly invested energy in becoming leaner and more nimble. In many industries, however, what some call *hypercompetition* is a self-inflicted wound, not the inevitable outcome of a changing paradigm of competition.

The root of the problem is the failure to distinguish between operational effectiveness and strategy. The quest for productivity, quality, and speed has spawned a remarkable number of management tools and techniques: total quality management, benchmarking, time-based competition, outsourcing, partnering, reengineering, change management. Although the resulting operational improvements have often been dramatic, many companies have been frustrated by their inability to translate those gains into sustainable profitability. And bit by bit, almost imperceptibly, management tools have taken the place of strategy. As managers push to improve on all fronts, they move farther away from viable competitive positions.

Operational effectiveness: necessary but not sufficient

Operational effectiveness and strategy are both essential to superior performance, which, after all, is the primary goal of any enterprise. But they work in very different ways.

A company can outperform rivals only if it can establish a difference that it can preserve. It must deliver greater value to customers or create comparable value at a lower cost, or do both. The arithmetic of superior profitability then follows: delivering greater value allows a company to charge higher average unit prices; greater efficiency results in lower average unit costs.

Ultimately, all differences between companies in cost or price derive from the hundreds of activities required to create, produce, sell, and deliver their products or services, such as calling on customers, assembling final products, and training employees. Cost is generated by performing activities, and cost advantage arises from performing particular activities more efficiently than competitors. Similarly, differentiation arises from both the choice of activities and how they are performed. Activities, then, are the basic units of competitive advantage. Overall advantage or disadvantage results from all a company's activities, not only a few.¹

Operational effectiveness (OE) means performing similar activities *better* than rivals perform them. Operational effectiveness includes but is not limited to efficiency. It refers to any number of practices that allow a company to better utilize its inputs by, for example, reducing defects in products or developing better products faster. In contrast, strategic positioning means performing *different* activities from rivals' or performing similar activities in *different* ways.

Differences in operational effectiveness among companies are pervasive. Some companies are able to get more out of their inputs than others because they eliminate wasted effort, employ more advanced technology, motivate employees better, or have greater insight into managing particular activities or sets of activities. Such differences in operational effectiveness are an important source of differences in profitability among competitors because they directly affect relative cost positions and levels of differentiation.

Idea in Brief

The myriad activities that go into creating, producing, selling, and delivering a product or service are the basic units of competitive advantage. **Operational effectiveness** means performing these activities better—that is, faster, or with fewer inputs and defects—than rivals. Companies can reap enormous advantages from operational effectiveness, as Japanese firms demonstrated in the 1970s and 1980s with such practices as total quality management and continuous improvement. But from a competitive standpoint, the problem with operational effectiveness is that best practices are easily emulated. As all competitors in an industry adopt them, the **productivity frontier**—the maximum value a company can deliver at a given cost, given the best available technology, skills, and management techniques—shifts outward, lowering costs and improving value at the same time. Such competition produces absolute improvement in operational effectiveness, but relative improvement for no one. And the more benchmarking that companies do, the more **competitive convergence** you have—that is, the more indistinguishable companies are from one another.

Strategic positioning attempts to achieve sustainable competitive advantage by preserving what is distinctive about a company. It means performing *different* activities from rivals, or performing *similar* activities in different ways.

Differences in operational effectiveness were at the heart of the Japanese challenge to Western companies in the 1980s. The Japanese were so far ahead of rivals in operational effectiveness that they could offer lower cost and superior quality at the same time. It is worth dwelling on this point, because so much recent thinking about competition depends on it. Imagine for a moment a *productivity frontier* that constitutes the sum of all existing best practices at any given time. Think of it as the maximum value that a company delivering a particular product or service can create at a given cost, using the best available technologies, skills, management techniques, and purchased inputs. The productivity frontier can apply to individual activities, to groups of linked activities such as order processing and manufacturing, and to an entire company's activities. When a company improves its operational effectiveness, it moves toward the frontier. Doing so may require capital investment, different personnel, or simply new ways of managing.

Idea in Practice

Three key principles underlie strategic positioning.

1. **Strategy is the creation of a unique and valuable position, involving a different set of activities.** Strategic position emerges from three distinct sources:

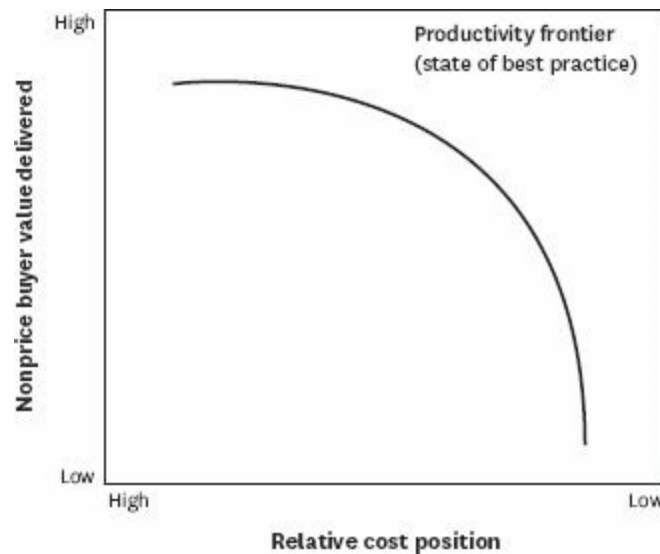
- serving few needs of many customers (Jiffy Lube provides only auto lubricants)
- serving broad needs of few customers (Bessemer Trust targets only very high-wealth clients)
- serving broad needs of many customers in a narrow market (Carmike Cinemas operates only in cities with a population under 200,000)

2. **Strategy requires you to make trade-offs in competing—to choose what *not* to do.** Some competitive activities are incompatible; thus, gains in one area can be achieved only at the expense of another area. For example, Neutrogena soap is positioned more as a medicinal product than as a cleansing agent. The company says “no” to sales based on deodorizing, gives up large volume, and sacrifices manufacturing efficiencies. By contrast, Maytag’s decision to extend its product line and acquire other brands represented a failure to make difficult trade-offs: the boost in revenues came at the expense of return on sales.

3. **Strategy involves creating “fit” among a company’s activities.** Fit has to do with the ways a company’s activities interact and reinforce one another. For example, Vanguard Group aligns all of its activities with a low-cost strategy; it distributes funds directly to consumers and minimizes portfolio turnover. Fit drives both competitive advantage and sustainability: when activities mutually reinforce each other, competitors can’t easily imitate them. When Continental Lite tried to match a few of Southwest Airlines’ activities, but not the whole interlocking system, the results were disastrous.

Employees need guidance about how to deepen a strategic position rather than broaden or compromise it. About how to extend the company’s uniqueness while strengthening the fit among its activities. This work of deciding which target group of customers and needs to serve requires discipline, the ability to set limits, and forthright communication. Clearly, strategy and leadership are inextricably linked.

Operational effectiveness versus strategic positioning



The productivity frontier is constantly shifting outward as new technologies and management approaches are developed and as new inputs become available. Laptop computers, mobile communications, the Internet, and software such as Lotus Notes, for example, have redefined the productivity frontier for sales-force operations and created rich possibilities for linking sales with such activities as order processing and after-sales support. Similarly, lean production, which involves a family of activities, has allowed substantial improvements in manufacturing productivity and asset utilization.

For at least the past decade, managers have been preoccupied with improving operational effectiveness. Through programs such as TQM, time-based competition, and benchmarking, they have changed how they perform activities in order to eliminate inefficiencies, improve customer satisfaction, and achieve best practice. Hoping to keep up with shifts in the productivity frontier, managers have embraced continuous improvement, empowerment, change management, and the so-called learning organization. The popularity of outsourcing and the virtual corporation reflect the growing recognition that it is difficult to perform all activities as productively as specialists.

As companies move to the frontier, they can often improve on multiple dimensions of performance at the same time. For example, manufacturers that adopted the Japanese practice of rapid changeovers in the 1980s were able to lower cost and improve differentiation simultaneously. What were once believed to be real trade-offs—between defects and costs, for example—

turned out to be illusions created by poor operational effectiveness. Managers have learned to reject such false trade-offs.

Constant improvement in operational effectiveness is necessary to achieve superior profitability. However, it is not usually sufficient. Few companies have competed successfully on the basis of operational effectiveness over an extended period, and staying ahead of rivals gets harder every day. The most obvious reason for that is the rapid diffusion of best practices. Competitors can quickly imitate management techniques, new technologies, input improvements, and superior ways of meeting customers' needs. The most generic solutions—those that can be used in multiple settings—diffuse the fastest. Witness the proliferation of OE techniques accelerated by support from consultants.

OE competition shifts the productivity frontier outward, effectively raising the bar for everyone. But although such competition produces absolute improvement in operational effectiveness, it leads to relative improvement for no one. Consider the \$5 billion-plus U.S. commercial-printing industry. The major players—R.R. Donnelley & Sons Company, Quebecor, World Color Press, and Big Flower Press—are competing head to head, serving all types of customers, offering the same array of printing technologies (gravure and web offset), investing heavily in the same new equipment, running their presses faster, and reducing crew sizes. But the resulting major productivity gains are being captured by customers and equipment suppliers, not retained in superior profitability. Even industry-leader Donnelley's profit margin, consistently higher than 7% in the 1980s, fell to less than 4.6% in 1995. This pattern is playing itself out in industry after industry. Even the Japanese, pioneers of the new competition, suffer from persistently low profits. (See the sidebar "Japanese Companies Rarely Have Strategies.")

Japanese Companies Rarely Have Strategies

The Japanese triggered a global revolution in operational effectiveness in the 1970s and 1980s, pioneering practices such as total quality management and continuous improvement. As a result, Japanese manufacturers enjoyed substantial cost and quality advantages for many years.

But Japanese companies rarely developed distinct strategic positions of the kind discussed in this article. Those that did—Sony, Canon, and Sega, for example—were

the exception rather than the rule. Most Japanese companies imitate and emulate one another. All rivals offer most if not all product varieties, features, and services; they employ all channels and match one another's plant configurations.

The dangers of Japanese-style competition are now becoming easier to recognize. In the 1980s, with rivals operating far from the productivity frontier, it seemed possible to win on both cost and quality indefinitely. Japanese companies were all able to grow in an expanding domestic economy and by penetrating global markets. They appeared unstoppable. But as the gap in operational effectiveness narrows, Japanese companies are increasingly caught in a trap of their own making. If they are to escape the mutually destructive battles now ravaging their performance, Japanese companies will have to learn strategy.

To do so, they may have to overcome strong cultural barriers. Japan is notoriously consensus oriented, and companies have a strong tendency to mediate differences among individuals rather than accentuate them. Strategy, on the other hand, requires hard choices. The Japanese also have a deeply ingrained service tradition that predisposes them to go to great lengths to satisfy any need a customer expresses. Companies that compete in that way end up blurring their distinct positioning, becoming all things to all customers.

This discussion of Japan is drawn from the author's research with Hirotaka Takeuchi, with help from Mariko Sakakibara.

The second reason that improved operational effectiveness is insufficient—competitive convergence—is more subtle and insidious. The more benchmarking companies do, the more they look alike. The more that rivals outsource activities to efficient third parties, often the same ones, the more generic those activities become. As rivals imitate one another's improvements in quality, cycle times, or supplier partnerships, strategies converge and competition becomes a series of races down identical paths that no one can win. Competition based on operational effectiveness alone is mutually destructive, leading to wars of attrition that can be arrested only by limiting competition.

The recent wave of industry consolidation through mergers makes sense in the context of OE competition. Driven by performance pressures but lacking strategic vision, company after company has had no better idea than to buy up its rivals. The competitors left standing are often those that outlasted others, not companies with real advantage.

After a decade of impressive gains in operational effectiveness, many companies are facing diminishing returns. Continuous improvement has been etched on managers' brains. But its tools unwittingly draw companies toward

imitation and homogeneity. Gradually, managers have let operational effectiveness supplant strategy. The result is zero-sum competition, static or declining prices, and pressures on costs that compromise companies' ability to invest in the business for the long term.

II. Strategy Rests on Unique Activities

Competitive strategy is about being different. It means deliberately choosing a different set of activities to deliver a unique mix of value.

Southwest Airlines Company, for example, offers short-haul, low-cost, point-to-point service between midsize cities and secondary airports in large cities. Southwest avoids large airports and does not fly great distances. Its customers include business travelers, families, and students. Southwest's frequent departures and low fares attract price-sensitive customers who otherwise would travel by bus or car, and convenience-oriented travelers who would choose a full-service airline on other routes.

Most managers describe strategic positioning in terms of their customers: "Southwest Airlines serves price- and convenience-sensitive travelers," for example. But the essence of strategy is in the activities—choosing to perform activities differently or to perform different activities than rivals. Otherwise, a strategy is nothing more than a marketing slogan that will not withstand competition.

A full-service airline is configured to get passengers from almost any point A to any point B. To reach a large number of destinations and serve passengers with connecting flights, full-service airlines employ a hub-and-spoke system centered on major airports. To attract passengers who desire more comfort, they offer first-class or business-class service. To accommodate passengers who must change planes, they coordinate schedules and check and transfer baggage. Because some passengers will be traveling for many hours, full-service airlines serve meals.

Southwest, in contrast, tailors all its activities to deliver low-cost, convenient service on its particular type of route. Through fast turnarounds at the gate of only 15 minutes, Southwest is able to keep planes flying longer hours than rivals and provide frequent departures with fewer aircraft. Southwest does not offer meals, assigned seats, interline baggage checking, or premium classes of service. Automated ticketing at the gate encourages customers to bypass travel agents, allowing Southwest to avoid their commissions. A standardized fleet of 737 aircraft boosts the efficiency of maintenance.

Southwest has staked out a unique and valuable strategic position based on a tailored set of activities. On the routes served by Southwest, a full-service airline could never be as convenient or as low cost.

Ikea, the global furniture retailer based in Sweden, also has a clear strategic positioning. Ikea targets young furniture buyers who want style at low cost. What turns this marketing concept into a strategic positioning is the tailored set of activities that make it work. Like Southwest, Ikea has chosen to perform activities differently from its rivals.

Consider the typical furniture store. Showrooms display samples of the merchandise. One area might contain 25 sofas; another will display five dining tables. But those items represent only a fraction of the choices available to customers. Dozens of books displaying fabric swatches or wood samples or alternate styles offer customers thousands of product varieties to choose from. Salespeople often escort customers through the store, answering questions and helping them navigate this maze of choices. Once a customer makes a selection, the order is relayed to a third-party manufacturer. With luck, the furniture will be delivered to the customer's home within six to eight weeks. This is a value chain that maximizes customization and service but does so at high cost.

In contrast, Ikea serves customers who are happy to trade off service for cost. Instead of having a sales associate trail customers around the store, Ikea uses a self-service model based on clear, in-store displays. Rather than rely solely on third-party manufacturers, Ikea designs its own low-cost, modular, ready-to-assemble furniture to fit its positioning. In huge stores, Ikea displays every product it sells in room-like settings, so customers don't need a decorator to help them imagine how to put the pieces together. Adjacent to the furnished showrooms is a warehouse section with the products in boxes on pallets. Customers are expected to do their own pickup and delivery, and Ikea will even sell you a roof rack for your car that you can return for a refund on your next visit.

Finding New Positions: The Entrepreneurial Edge

Strategic competition can be thought of as the process of perceiving new positions that woo customers from established positions or draw new customers into the market. For example, superstores offering depth of merchandise in a single product category take market share from broad-line department stores offering a more limited selection in

many categories. Mail-order catalogs pick off customers who crave convenience. In principle, incumbents and entrepreneurs face the same challenges in finding new strategic positions. In practice, new entrants often have the edge.

Strategic positionings are often not obvious, and finding them requires creativity and insight. New entrants often discover unique positions that have been available but simply overlooked by established competitors. Ikea, for example, recognized a customer group that had been ignored or served poorly. Circuit City Stores' entry into used cars, CarMax, is based on a new way of performing activities—extensive refurbishing of cars, product guarantees, no-haggle pricing, sophisticated use of in-house customer financing—that has long been open to incumbents.

New entrants can prosper by occupying a position that a competitor once held but has ceded through years of imitation and straddling. And entrants coming from other industries can create new positions because of distinctive activities drawn from their other businesses. CarMax borrows heavily from Circuit City's expertise in inventory management, credit, and other activities in consumer electronics retailing.

Most commonly, however, new positions open up because of change. New customer groups or purchase occasions arise; new needs emerge as societies evolve; new distribution channels appear; new technologies are developed; new machinery or information systems become available. When such changes happen, new entrants, unencumbered by a long history in the industry, can often more easily perceive the potential for a new way of competing. Unlike incumbents, newcomers can be more flexible because they face no trade-offs with their existing activities.

Although much of its low-cost position comes from having customers “do it themselves,” Ikea offers a number of extra services that its competitors do not. In-store child care is one. Extended hours are another. Those services are uniquely aligned with the needs of its customers, who are young, not wealthy, likely to have children (but no nanny), and, because they work for a living, have a need to shop at odd hours.

The origins of strategic positions

Strategic positions emerge from three distinct sources, which are not mutually exclusive and often overlap. First, positioning can be based on producing a subset of an industry's products or services. I call this *variety-based positioning* because it is based on the choice of product or service varieties rather than customer segments. Variety-based positioning makes economic sense when a company can best produce particular products or services using distinctive sets of activities.

Jiffy Lube International, for instance, specializes in automotive lubricants and does not offer other car repair or maintenance services. Its value chain produces faster service at a lower cost than broader line repair shops, a combination so attractive that many customers subdivide their purchases, buying oil changes from the focused competitor, Jiffy Lube, and going to rivals for other services.

The Vanguard Group, a leader in the mutual fund industry, is another example of variety-based positioning. Vanguard provides an array of common stock, bond, and money market funds that offer predictable performance and rock-bottom expenses. The company's investment approach deliberately sacrifices the possibility of extraordinary performance in any one year for good relative performance in every year. Vanguard is known, for example, for its index funds. It avoids making bets on interest rates and steers clear of narrow stock groups. Fund managers keep trading levels low, which holds expenses down; in addition, the company discourages customers from rapid buying and selling because doing so drives up costs and can force a fund manager to trade in order to deploy new capital and raise cash for redemptions. Vanguard also takes a consistent low-cost approach to managing distribution, customer service, and marketing. Many investors include one or more Vanguard funds in their portfolio, while buying aggressively managed or specialized funds from competitors.

The people who use Vanguard or Jiffy Lube are responding to a superior value chain for a particular type of service. A variety-based positioning can serve a wide array of customers, but for most it will meet only a subset of their needs.

A second basis for positioning is that of serving most or all the needs of a

particular group of customers. I call this *needs-based positioning*, which comes closer to traditional thinking about targeting a segment of customers. It arises when there are groups of customers with differing needs, and when a tailored set of activities can serve those needs best. Some groups of customers are more price sensitive than others, demand different product features, and need varying amounts of information, support, and services. Ikea's customers are a good example of such a group. Ikea seeks to meet all the home furnishing needs of its target customers, not just a subset of them.

A variant of needs-based positioning arises when the same customer has different needs on different occasions or for different types of transactions. The same person, for example, may have different needs when traveling on business than when traveling for pleasure with the family. Buyers of cans—beverage companies, for example—will likely have different needs from their primary supplier than from their secondary source.

It is intuitive for most managers to conceive of their business in terms of the customers' needs they are meeting. But a critical element of needs-based positioning is not at all intuitive and is often overlooked. Differences in needs will not translate into meaningful positions unless the best set of activities to satisfy them *also* differs. If that were not the case, every competitor could meet those same needs, and there would be nothing unique or valuable about the positioning.

In private banking, for example, Bessemer Trust Company targets families with a minimum of \$5 million in investable assets who want capital preservation combined with wealth accumulation. By assigning one sophisticated account officer for every 14 families, Bessemer has configured its activities for personalized service. Meetings, for example, are more likely to be held at a client's ranch or yacht than in the office. Bessemer offers a wide array of customized services, including investment management and estate administration, oversight of oil and gas investments, and accounting for racehorses and aircraft. Loans, a staple of most private banks, are rarely needed by Bessemer's clients and make up a tiny fraction of its client balances and income. Despite the most generous compensation of account officers and the highest personnel cost as a percentage of operating expenses, Bessemer's differentiation with its target families produces a return on equity estimated to be the highest of any private banking competitor.

The Connection with Generic Strategies

In *Competitive Strategy* (The Free Press, 1985), I introduced the concept of generic strategies—cost leadership, differentiation, and focus—to represent the alternative strategic positions in an industry. The generic strategies remain useful to characterize strategic positions at the simplest and broadest level. Vanguard, for instance, is an example of a cost leadership strategy, whereas Ikea, with its narrow customer group, is an example of cost-based focus. Neutrogena is a focused differentiator. The bases for positioning—varieties, needs, and access—carry the understanding of those generic strategies to a greater level of specificity. Ikea and Southwest are both cost-based focusers, for example, but Ikea's focus is based on the needs of a customer group, and Southwest's is based on offering a particular service variety.

The generic strategies framework introduced the need to choose in order to avoid becoming caught between what I then described as the inherent contradictions of different strategies. Trade-offs between the activities of incompatible positions explain those contradictions. Witness Continental Lite, which tried and failed to compete in two ways at once.

Citibank's private bank, on the other hand, serves clients with minimum assets of about \$250,000 who, in contrast to Bessemer's clients, want convenient access to loans—from jumbo mortgages to deal financing. Citibank's account managers are primarily lenders. When clients need other services, their account manager refers them to other Citibank specialists, each of whom handles prepackaged products. Citibank's system is less customized than Bessemer's and allows it to have a lower manager-to-client ratio of 1:125. Biannual office meetings are offered only for the largest clients. Both Bessemer and Citibank have tailored their activities to meet the needs of a different group of private banking customers. The same value chain cannot profitably meet the needs of both groups.

The third basis for positioning is that of segmenting customers who are accessible in different ways. Although their needs are similar to those of other customers, the best configuration of activities to reach them is different. I call this *access-based positioning*. Access can be a function of customer geography or customer scale—or of anything that requires a different set of activities to reach customers in the best way.

Segmenting by access is less common and less well understood than the other two bases. Carmike Cinemas, for example, operates movie theaters exclusively in cities and towns with populations under 200,000. How does Carmike make money in markets that are not only small but also won't

support big-city ticket prices? It does so through a set of activities that result in a lean cost structure. Carmike's small-town customers can be served through standardized, low-cost theater complexes requiring fewer screens and less sophisticated projection technology than big-city theaters. The company's proprietary information system and management process eliminate the need for local administrative staff beyond a single theater manager. Carmike also reaps advantages from centralized purchasing, lower rent and payroll costs (because of its locations), and rock-bottom corporate overhead of 2% (the industry average is 5%). Operating in small communities also allows Carmike to practice a highly personal form of marketing in which the theater manager knows patrons and promotes attendance through personal contacts. By being the dominant if not the only theater in its markets—the main competition is often the high school football team—Carmike is also able to get its pick of films and negotiate better terms with distributors.

Rural versus urban-based customers are one example of access driving differences in activities. Serving small rather than large customers or densely rather than sparsely situated customers are other examples in which the best way to configure marketing, order processing, logistics, and after-sale service activities to meet the similar needs of distinct groups will often differ.

Positioning is not only about carving out a niche. A position emerging from any of the sources can be broad or narrow. A focused competitor, such as Ikea, targets the special needs of a subset of customers and designs its activities accordingly. Focused competitors thrive on groups of customers who are overserved (and hence overpriced) by more broadly targeted competitors, or underserved (and hence underpriced). A broadly targeted competitor—for example, Vanguard or Delta Air Lines—serves a wide array of customers, performing a set of activities designed to meet their common needs. It ignores or meets only partially the more idiosyncratic needs of particular customer groups.

Whatever the basis—variety, needs, access, or some combination of the three—positioning requires a tailored set of activities because it is always a function of differences on the supply side; that is, of differences in activities. However, positioning is not always a function of differences on the demand, or customer, side. Variety and access positionings, in particular, do not rely on *any* customer differences. In practice, however, variety or access differences often accompany needs differences. The tastes—that is, the needs

—of Carmike’s small-town customers, for instance, run more toward comedies, Westerns, action films, and family entertainment. Carmike does not run any films rated NC-17.

Having defined positioning, we can now begin to answer the question, “What is strategy?” Strategy is the creation of a unique and valuable position, involving a different set of activities. If there were only one ideal position, there would be no need for strategy. Companies would face a simple imperative—win the race to discover and preempt it. The essence of strategic positioning is to choose activities that are different from rivals’. If the same set of activities were best to produce all varieties, meet all needs, and access all customers, companies could easily shift among them and operational effectiveness would determine performance.

III. A Sustainable Strategic Position Requires Trade-offs

Choosing a unique position, however, is not enough to guarantee a sustainable advantage. A valuable position will attract imitation by incumbents, who are likely to copy it in one of two ways.

First, a competitor can reposition itself to match the superior performer. J.C. Penney, for instance, has been repositioning itself from a Sears clone to a more upscale, fashion-oriented, soft-goods retailer. A second and far more common type of imitation is straddling. The straddler seeks to match the benefits of a successful position while maintaining its existing position. It grafts new features, services, or technologies onto the activities it already performs.

For those who argue that competitors can copy any market position, the airline industry is a perfect test case. It would seem that nearly any competitor could imitate any other airline's activities. Any airline can buy the same planes, lease the gates, and match the menus and ticketing and baggage handling services offered by other airlines.

Continental Airlines saw how well Southwest was doing and decided to straddle. While maintaining its position as a full-service airline, Continental also set out to match Southwest on a number of point-to-point routes. The airline dubbed the new service Continental Lite. It eliminated meals and first-class service, increased departure frequency, lowered fares, and shortened turnaround time at the gate. Because Continental remained a full-service airline on other routes, it continued to use travel agents and its mixed fleet of planes and to provide baggage checking and seat assignments.

But a strategic position is not sustainable unless there are trade-offs with other positions. Trade-offs occur when activities are incompatible. Simply put, a trade-off means that more of one thing necessitates less of another. An airline can choose to serve meals—adding cost and slowing turnaround time at the gate—or it can choose not to, but it cannot do both without bearing major inefficiencies.

Trade-offs create the need for choice and protect against repositioners and straddlers. Consider Neutrogena soap. Neutrogena Corporation's variety-

based positioning is built on a “kind to the skin,” residue-free soap formulated for pH balance. With a large detail force calling on dermatologists, Neutrogena’s marketing strategy looks more like a drug company’s than a soap maker’s. It advertises in medical journals, sends direct mail to doctors, attends medical conferences, and performs research at its own Skincare Institute. To reinforce its positioning, Neutrogena originally focused its distribution on drugstores and avoided price promotions. Neutrogena uses a slow, more expensive manufacturing process to mold its fragile soap.

In choosing this position, Neutrogena said no to the deodorants and skin softeners that many customers desire in their soap. It gave up the large-volume potential of selling through supermarkets and using price promotions. It sacrificed manufacturing efficiencies to achieve the soap’s desired attributes. In its original positioning, Neutrogena made a whole raft of trade-offs like those, trade-offs that protected the company from imitators.

Trade-offs arise for three reasons. The first is inconsistencies in image or reputation. A company known for delivering one kind of value may lack credibility and confuse customers—or even undermine its reputation—if it delivers another kind of value or attempts to deliver two inconsistent things at the same time. For example, Ivory soap, with its position as a basic, inexpensive everyday soap, would have a hard time reshaping its image to match Neutrogena’s premium “medical” reputation. Efforts to create a new image typically cost tens or even hundreds of millions of dollars in a major industry—a powerful barrier to imitation.

Second, and more important, trade-offs arise from activities themselves. Different positions (with their tailored activities) require different product configurations, different equipment, different employee behavior, different skills, and different management systems. Many trade-offs reflect inflexibilities in machinery, people, or systems. The more Ikea has configured its activities to lower costs by having its customers do their own assembly and delivery, the less able it is to satisfy customers who require higher levels of service.

However, trade-offs can be even more basic. In general, value is destroyed if an activity is overdesigned or underdesigned for its use. For example, even if a given salesperson were capable of providing a high level of assistance to one customer and none to another, the salesperson’s talent (and some of his or her cost) would be wasted on the second customer.

Moreover, productivity can improve when variation of an activity is limited. By providing a high level of assistance all the time, the salesperson and the entire sales activity can often achieve efficiencies of learning and scale.

Finally, trade-offs arise from limits on internal coordination and control. By clearly choosing to compete in one way and not another, senior management makes organizational priorities clear. Companies that try to be all things to all customers, in contrast, risk confusion in the trenches as employees attempt to make day-to-day operating decisions without a clear framework.

Positioning trade-offs are pervasive in competition and essential to strategy. They create the need for choice and purposefully limit what a company offers. They deter straddling or repositioning, because competitors that engage in those approaches undermine their strategies and degrade the value of their existing activities.

Trade-offs ultimately grounded Continental Lite. The airline lost hundreds of millions of dollars, and the CEO lost his job. Its planes were delayed leaving congested hub cities or slowed at the gate by baggage transfers. Late flights and cancellations generated a thousand complaints a day. Continental Lite could not afford to compete on price and still pay standard travel-agent commissions, but neither could it do without agents for its full-service business. The airline compromised by cutting commissions for all Continental flights across the board. Similarly, it could not afford to offer the same frequent-flier benefits to travelers paying the much lower ticket prices for Lite service. It compromised again by lowering the rewards of Continental's entire frequent-flier program. The results: angry travel agents and full-service customers.

Continental tried to compete in two ways at once. In trying to be low cost on some routes and full service on others, Continental paid an enormous straddling penalty. If there were no trade-offs between the two positions, Continental could have succeeded. But the absence of trade-offs is a dangerous half-truth that managers must unlearn. Quality is not always free. Southwest's convenience, one kind of high quality, happens to be consistent with low costs because its frequent departures are facilitated by a number of low-cost practices—fast gate turnarounds and automated ticketing, for example. However, other dimensions of airline quality—an assigned seat, a meal, or baggage transfer—require costs to provide.

In general, false trade-offs between cost and quality occur primarily when

there is redundant or wasted effort, poor control or accuracy, or weak coordination. Simultaneous improvement of cost and differentiation is possible only when a company begins far behind the productivity frontier or when the frontier shifts outward. At the frontier, where companies have achieved current best practice, the trade-off between cost and differentiation is very real indeed.

After a decade of enjoying productivity advantages, Honda Motor Company and Toyota Motor Corporation recently bumped up against the frontier. In 1995, faced with increasing customer resistance to higher automobile prices, Honda found that the only way to produce a less-expensive car was to skimp on features. In the United States, it replaced the rear disk brakes on the Civic with lower-cost drum brakes and used cheaper fabric for the back seat, hoping customers would not notice. Toyota tried to sell a version of its best-selling Corolla in Japan with unpainted bumpers and cheaper seats. In Toyota's case, customers rebelled, and the company quickly dropped the new model.

For the past decade, as managers have improved operational effectiveness greatly, they have internalized the idea that eliminating trade-offs is a good thing. But if there are no trade-offs companies will never achieve a sustainable advantage. They will have to run faster and faster just to stay in place.

As we return to the question, What is strategy? we see that trade-offs add a new dimension to the answer. Strategy is making trade-offs in competing. The essence of strategy is choosing what *not* to do. Without trade-offs, there would be no need for choice and thus no need for strategy. Any good idea could and would be quickly imitated. Again, performance would once again depend wholly on operational effectiveness.

IV. Fit Drives Both Competitive Advantage and Sustainability

Positioning choices determine not only which activities a company will perform and how it will configure individual activities but also how activities relate to one another. While operational effectiveness is about achieving excellence in individual activities, or functions, strategy is about *combining* activities.

Southwest's rapid gate turnaround, which allows frequent departures and greater use of aircraft, is essential to its high-convenience, low-cost positioning. But how does Southwest achieve it? Part of the answer lies in the company's well-paid gate and ground crews, whose productivity in turnarounds is enhanced by flexible union rules. But the bigger part of the answer lies in how Southwest performs other activities. With no meals, no seat assignment, and no interline baggage transfers, Southwest avoids having to perform activities that slow down other airlines. It selects airports and routes to avoid congestion that introduces delays. Southwest's strict limits on the type and length of routes make standardized aircraft possible: every aircraft Southwest turns is a Boeing 737.

What is Southwest's core competence? Its key success factors? The correct answer is that everything matters. Southwest's strategy involves a whole system of activities, not a collection of parts. Its competitive advantage comes from the way its activities fit and reinforce one another.

Fit locks out imitators by creating a chain that is as strong as its *strongest* link. As in most companies with good strategies, Southwest's activities complement one another in ways that create real economic value. One activity's cost, for example, is lowered because of the way other activities are performed. Similarly, one activity's value to customers can be enhanced by a company's other activities. That is the way strategic fit creates competitive advantage and superior profitability.

Types of fit

The importance of fit among functional policies is one of the oldest ideas in strategy. Gradually, however, it has been supplanted on the management agenda. Rather than seeing the company as a whole, managers have turned to “core” competencies, “critical” resources, and “key” success factors. In fact, fit is a far more central component of competitive advantage than most realize.

Fit is important because discrete activities often affect one another. A sophisticated sales force, for example, confers a greater advantage when the company’s product embodies premium technology and its marketing approach emphasizes customer assistance and support. A production line with high levels of model variety is more valuable when combined with an inventory and order processing system that minimizes the need for stocking finished goods, a sales process equipped to explain and encourage customization, and an advertising theme that stresses the benefits of product variations that meet a customer’s special needs. Such complementarities are pervasive in strategy. Although some fit among activities is generic and applies to many companies, the most valuable fit is strategy-specific because it enhances a position’s uniqueness and amplifies trade-offs.²

There are three types of fit, although they are not mutually exclusive. First-order fit is *simple consistency* between each activity (function) and the overall strategy. Vanguard, for example, aligns all activities with its low-cost strategy. It minimizes portfolio turnover and does not need highly compensated money managers. The company distributes its funds directly, avoiding commissions to brokers. It also limits advertising, relying instead on public relations and word-of-mouth recommendations. Vanguard ties its employees’ bonuses to cost savings.

Consistency ensures that the competitive advantages of activities cumulate and do not erode or cancel themselves out. It makes the strategy easier to communicate to customers, employees, and shareholders, and improves implementation through single-mindedness in the corporation.

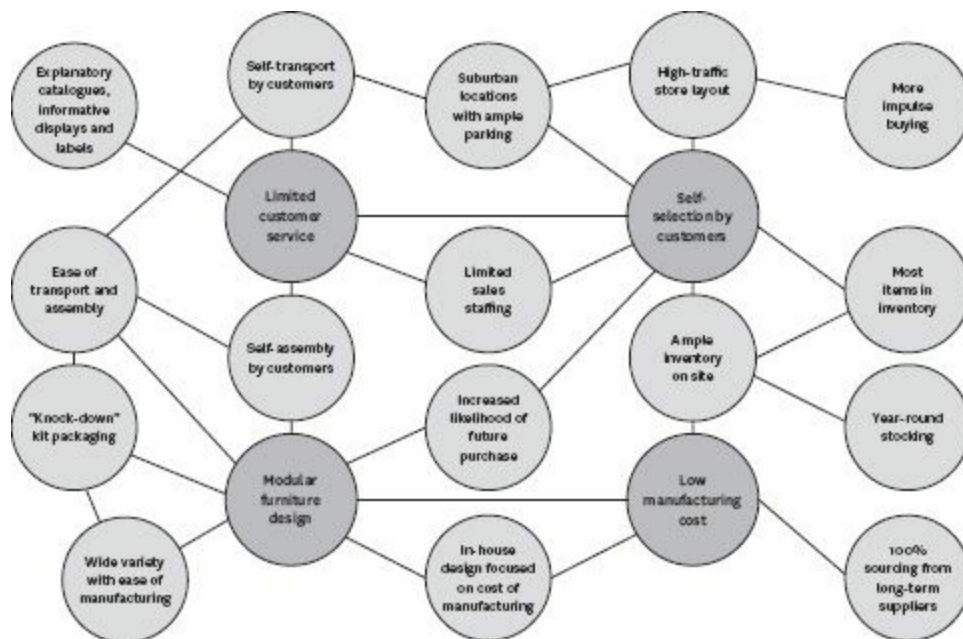
Second-order fit occurs when *activities are reinforcing*. Neutrogena, for example, markets to upscale hotels eager to offer their guests a soap recommended by dermatologists. Hotels grant Neutrogena the privilege of

using its customary packaging while requiring other soaps to feature the hotel's name. Once guests have tried Neutrogena in a luxury hotel, they are more likely to purchase it at the drugstore or ask their doctor about it. Thus Neutrogena's medical and hotel marketing activities reinforce one another, lowering total marketing costs.

In another example, Bic Corporation sells a narrow line of standard, low-priced pens to virtually all major customer markets (retail, commercial, promotional, and giveaway) through virtually all available channels. As with any variety-based positioning serving a broad group of customers, Bic emphasizes a common need (low price for an acceptable pen) and uses marketing approaches with a broad reach (a large sales force and heavy television advertising). Bic gains the benefits of consistency across nearly all activities, including product design that emphasizes ease of manufacturing, plants configured for low cost, aggressive purchasing to minimize material costs, and in-house parts production whenever the economics dictate.

Mapping activity systems

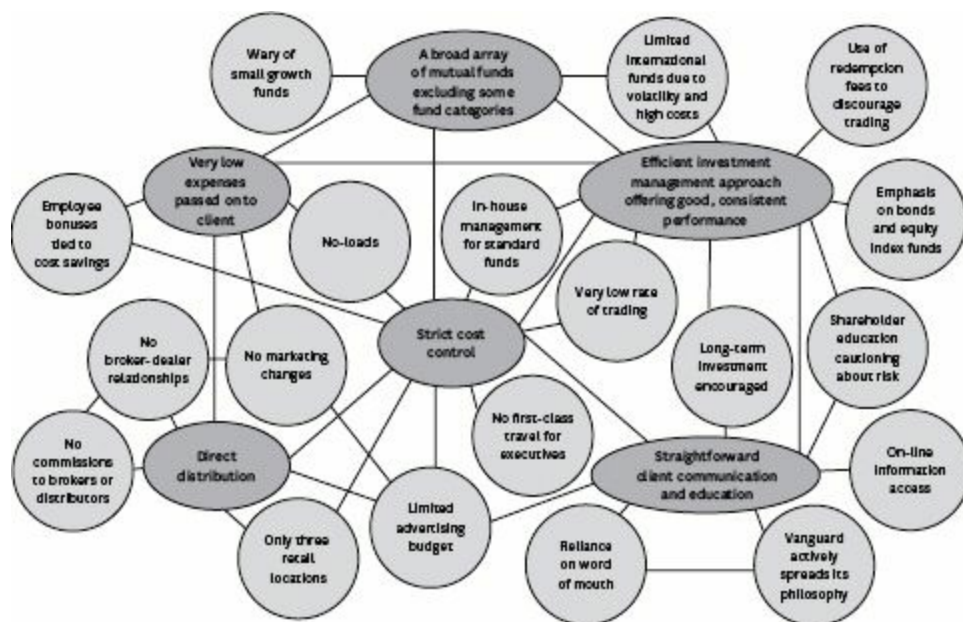
Activity-system maps, such as this one for Ikea, show how a company's strategic position is contained in a set of tailored activities designed to deliver it. In companies with a clear strategic position, a number of higher-order strategic themes (in dark grey) can be identified and implemented through clusters of tightly linked activities (in light grey).



Yet Bic goes beyond simple consistency because its activities are reinforcing. For example, the company uses point-of-sale displays and frequent packaging changes to stimulate impulse buying. To handle point-of-sale tasks, a company needs a large sales force. Bic's is the largest in its industry, and it handles point-of-sale activities better than its rivals do. Moreover, the combination of point-of-sale activity, heavy television advertising, and packaging changes yields far more impulse buying than any activity in isolation could.

Vanguard's activity system

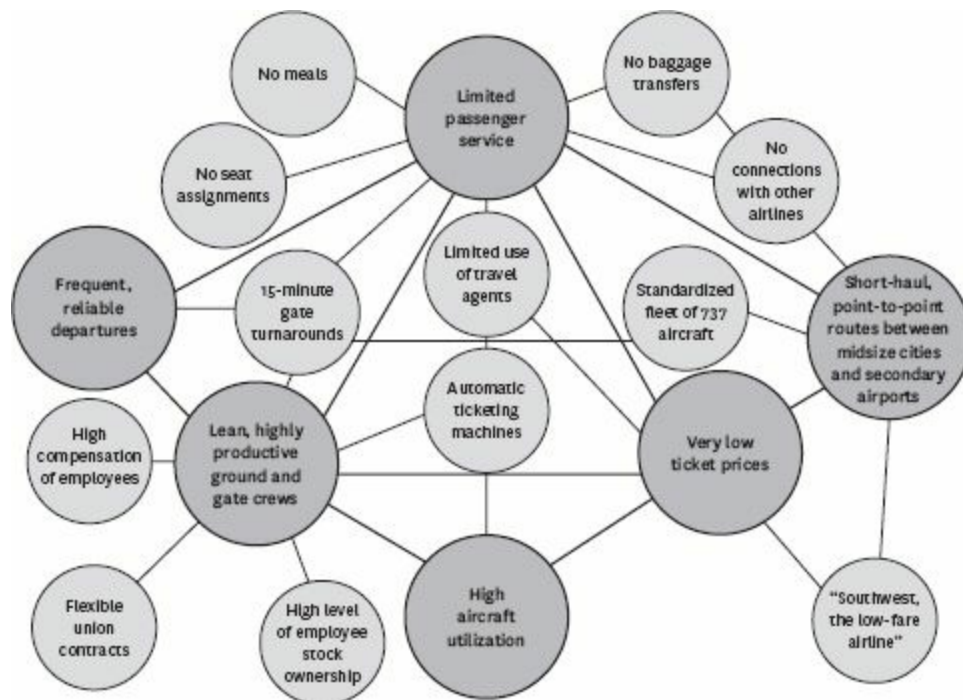
Activity-system maps can be useful for examining and strengthening strategic fit. A set of basic questions should guide the process. First, is each activity consistent with the overall positioning—the varieties produced, the needs served, and the type of customers accessed? Ask those responsible for each activity to identify how other activities within the company improve or detract from their performance. Second, are there ways to strengthen how activities and groups of activities reinforce one another? Finally, could changes in one activity eliminate the need to perform others?



Third-order fit goes beyond activity reinforcement to what I call *optimization of effort*. The Gap, a retailer of casual clothes, considers product availability in its stores a critical element of its strategy. The Gap could keep products either by holding store inventory or by restocking from warehouses. The Gap has optimized its effort across these activities by restocking its

selection of basic clothing almost daily out of three warehouses, thereby minimizing the need to carry large in-store inventories. The emphasis is on restocking because the Gap's merchandising strategy sticks to basic items in relatively few colors. While comparable retailers achieve turns of three to four times per year, the Gap turns its inventory seven and a half times per year. Rapid restocking, moreover, reduces the cost of implementing the Gap's short model cycle, which is six to eight weeks long.³

Southwest Airlines' activity system



Coordination and information exchange across activities to eliminate redundancy and minimize wasted effort are the most basic types of effort optimization. But there are higher levels as well. Product design choices, for example, can eliminate the need for after-sale service or make it possible for customers to perform service activities themselves. Similarly, coordination with suppliers or distribution channels can eliminate the need for some in-house activities, such as end-user training.

In all three types of fit, the whole matters more than any individual part. Competitive advantage grows out of the *entire system* of activities. The fit among activities substantially reduces cost or increases differentiation. Beyond that, the competitive value of individual activities—or the associated

skills, competencies, or resources—cannot be decoupled from the system or the strategy. Thus in competitive companies it can be misleading to explain success by specifying individual strengths, core competencies, or critical resources. The list of strengths cuts across many functions, and one strength blends into others. It is more useful to think in terms of themes that pervade many activities, such as low cost, a particular notion of customer service, or a particular conception of the value delivered. These themes are embodied in nests of tightly linked activities.

Fit and sustainability

Strategic fit among many activities is fundamental not only to competitive advantage but also to the sustainability of that advantage. It is harder for a rival to match an array of interlocked activities than it is merely to imitate a particular sales-force approach, match a process technology, or replicate a set of product features. Positions built on systems of activities are far more sustainable than those built on individual activities.

Consider this simple exercise. The probability that competitors can match any activity is often less than one. The probabilities then quickly compound to make matching the entire system highly unlikely ($.9 \times .9 = .81$; $.9 \times .9 \times .9 \times .9 = .66$, and so on). Existing companies that try to reposition or straddle will be forced to reconfigure many activities. And even new entrants, though they do not confront the trade-offs facing established rivals, still face formidable barriers to imitation.

The more a company's positioning rests on activity systems with second- and third-order fit, the more sustainable its advantage will be. Such systems, by their very nature, are usually difficult to untangle from outside the company and therefore hard to imitate. And even if rivals can identify the relevant interconnections, they will have difficulty replicating them. Achieving fit is difficult because it requires the integration of decisions and actions across many independent subunits.

A competitor seeking to match an activity system gains little by imitating only some activities and not matching the whole. Performance does not improve; it can decline. Recall Continental Lite's disastrous attempt to imitate Southwest.

Finally, fit among a company's activities creates pressures and incentives to improve operational effectiveness, which makes imitation even harder. Fit means that poor performance in one activity will degrade the performance in others, so that weaknesses are exposed and more prone to get attention. Conversely, improvements in one activity will pay dividends in others. Companies with strong fit among their activities are rarely inviting targets. Their superiority in strategy and in execution only compounds their advantages and raises the hurdle for imitators.

When activities complement one another, rivals will get little benefit from

imitation unless they successfully match the whole system. Such situations tend to promote winner-take-all competition. The company that builds the best activity system—Toys R Us, for instance—wins, while rivals with similar strategies—Child World and Lionel Leisure—fall behind. Thus finding a new strategic position is often preferable to being the second or third imitator of an occupied position.

The most viable positions are those whose activity systems are incompatible because of tradeoffs. Strategic positioning sets the trade-off rules that define how individual activities will be configured and integrated. Seeing strategy in terms of activity systems only makes it clearer why organizational structure, systems, and processes need to be strategy-specific. Tailoring organization to strategy, in turn, makes complementarities more achievable and contributes to sustainability.

One implication is that strategic positions should have a horizon of a decade or more, not of a single planning cycle. Continuity fosters improvements in individual activities and the fit across activities, allowing an organization to build unique capabilities and skills tailored to its strategy. Continuity also reinforces a company's identity.

Conversely, frequent shifts in positioning are costly. Not only must a company reconfigure individual activities, but it must also realign entire systems. Some activities may never catch up to the vacillating strategy. The inevitable result of frequent shifts in strategy, or of failure to choose a distinct position in the first place, is “me-too” or hedged activity configurations, inconsistencies across functions, and organizational dissonance.

What is strategy? We can now complete the answer to this question. Strategy is creating fit among a company's activities. The success of a strategy depends on doing many things well—not just a few—and integrating among them. If there is no fit among activities, there is no distinctive strategy and little sustainability. Management reverts to the simpler task of overseeing independent functions, and operational effectiveness determines an organization's relative performance.

V. Rediscovering Strategy

The failure to choose

Why do so many companies fail to have a strategy? Why do managers avoid making strategic choices? Or, having made them in the past, why do managers so often let strategies decay and blur?

Commonly, the threats to strategy are seen to emanate from outside a company because of changes in technology or the behavior of competitors. Although external changes can be the problem, the greater threat to strategy often comes from within. A sound strategy is undermined by a misguided view of competition, by organizational failures, and, especially, by the desire to grow.

Managers have become confused about the necessity of making choices. When many companies operate far from the productivity frontier, trade-offs appear unnecessary. It can seem that a well-run company should be able to beat its ineffective rivals on all dimensions simultaneously. Taught by popular management thinkers that they do not have to make trade-offs, managers have acquired a macho sense that to do so is a sign of weakness.

Unnerved by forecasts of hypercompetition, managers increase its likelihood by imitating everything about their competitors. Exhorted to think in terms of revolution, managers chase every new technology for its own sake.

The pursuit of operational effectiveness is seductive because it is concrete and actionable. Over the past decade, managers have been under increasing pressure to deliver tangible, measurable performance improvements. Programs in operational effectiveness produce reassuring progress, although superior profitability may remain elusive. Business publications and consultants flood the market with information about what other companies are doing, reinforcing the best-practice mentality. Caught up in the race for operational effectiveness, many managers simply do not understand the need to have a strategy.

Alternative Views of Strategy

The Implicit Strategy Model of the Past Decade

- One ideal competitive position in the industry
- Benchmarking of all activities and achieving best practice
- Aggressive outsourcing and partnering to gain efficiencies
- Advantages rest on a few key success factors, critical resources, core competencies
- Flexibility and rapid responses to all competitive and market changes

Sustainable Competitive Advantage

- Unique competitive position for the company
- Activities tailored to strategy
- Clear trade-offs and choices vis-à-vis competitors
- Competitive advantage arises from fit across activities
- Sustainability comes from the activity system, not the parts
- Operational effectiveness a given

Companies avoid or blur strategic choices for other reasons as well. Conventional wisdom within an industry is often strong, homogenizing competition. Some managers mistake “customer focus” to mean they must serve all customer needs or respond to every request from distribution channels. Others cite the desire to preserve flexibility.

Organizational realities also work against strategy. Trade-offs are frightening, and making no choice is sometimes preferred to risking blame for a bad choice. Companies imitate one another in a type of herd behavior, each assuming rivals know something they do not. Newly empowered employees, who are urged to seek every possible source of improvement, often lack a vision of the whole and the perspective to recognize trade-offs. The failure to choose sometimes comes down to the reluctance to disappoint valued managers or employees.

The growth trap

Among all other influences, the desire to grow has perhaps the most perverse effect on strategy. Trade-offs and limits appear to constrain growth. Serving one group of customers and excluding others, for instance, places a real or imagined limit on revenue growth. Broadly targeted strategies emphasizing low price result in lost sales with customers sensitive to features or service. Differentiators lose sales to price-sensitive customers.

Managers are constantly tempted to take incremental steps that surpass those limits but blur a company's strategic position. Eventually, pressures to grow or apparent saturation of the target market lead managers to broaden the position by extending product lines, adding new features, imitating competitors' popular services, matching processes, and even making acquisitions. For years, Maytag Corporation's success was based on its focus on reliable, durable washers and dryers, later extended to include dishwashers. However, conventional wisdom emerging within the industry supported the notion of selling a full line of products. Concerned with slow industry growth and competition from broad-line appliance makers, Maytag was pressured by dealers and encouraged by customers to extend its line. Maytag expanded into refrigerators and cooking products under the Maytag brand and acquired other brands—Jenn-Air, Hardwick Stove, Hoover, Admiral, and Magic Chef—with disparate positions. Maytag has grown substantially from \$684 million in 1985 to a peak of \$3.4 billion in 1994, but return on sales has declined from 8% to 12% in the 1970s and 1980s to an average of less than 1% between 1989 and 1995. Cost cutting will improve this performance, but laundry and dishwasher products still anchor Maytag's profitability.

Reconnecting with Strategy

Most companies owe their initial success to a unique strategic position involving clear trade-offs. Activities once were aligned with that position. The passage of time and the pressures of growth, however, led to compromises that were, at first, almost imperceptible. Through a succession of incremental changes that each seemed sensible at the time, many established companies have compromised their way to homogeneity with their rivals.

The issue here is not with the companies whose historical position is no longer viable; their challenge is to start over, just as a new entrant would. At issue is a far more common phenomenon: the established company achieving mediocre returns and lacking a clear strategy. Through incremental additions of product varieties, incremental efforts to serve new customer groups, and emulation of rivals' activities, the existing company loses its clear competitive position. Typically, the company has matched many of its competitors' offerings and practices and attempts to sell to most customer groups.

A number of approaches can help a company reconnect with strategy. The first is a careful look at what it already does. Within most well-established companies is a core of uniqueness. It is identified by answering questions such as the following:

- Which of our product or service varieties are the most distinctive?
- Which of our product or service varieties are the most profitable?
- Which of our customers are the most satisfied?
- Which customers, channels, or purchase occasions are the most profitable?
- Which of the activities in our value chain are the most different and effective?

Around this core of uniqueness are encrustations added incrementally over time. Like barnacles, they must be removed to reveal the underlying strategic positioning. A small percentage of varieties or customers may well account for most of a company's sales and especially its profits. The challenge, then, is to refocus on the unique core and realign the company's activities with it. Customers and product varieties at the periphery can be sold or allowed through inattention or price increases to fade away.

A company's history can also be instructive. What was the vision of the founder? What were the products and customers that made the company? Looking backward, one can reexamine the original strategy to see if it is still valid. Can the historical positioning be implemented in a modern way, one consistent with today's technologies and practices? This sort of thinking may lead to a commitment to renew the strategy and may challenge the organization to recover its distinctiveness. Such a challenge can be galvanizing and can instill the confidence to make the needed trade-offs.

Neutrogena may have fallen into the same trap. In the early 1990s, its U.S. distribution broadened to include mass merchandisers such as Wal-Mart Stores. Under the Neutrogena name, the company expanded into a wide variety of products—eye-makeup remover and shampoo, for example—in which it was not unique and which diluted its image, and it began turning to price promotions.

Compromises and inconsistencies in the pursuit of growth will erode the competitive advantage a company had with its original varieties or target

customers. Attempts to compete in several ways at once create confusion and undermine organizational motivation and focus. Profits fall, but more revenue is seen as the answer. Managers are unable to make choices, so the company embarks on a new round of broadening and compromises. Often, rivals continue to match each other until desperation breaks the cycle, resulting in a merger or downsizing to the original positioning.

Profitable growth

Many companies, after a decade of restructuring and cost-cutting, are turning their attention to growth. Too often, efforts to grow blur uniqueness, create compromises, reduce fit, and ultimately undermine competitive advantage. In fact, the growth imperative is hazardous to strategy.

What approaches to growth preserve and reinforce strategy? Broadly, the prescription is to concentrate on deepening a strategic position rather than broadening and compromising it. One approach is to look for extensions of the strategy that leverage the existing activity system by offering features or services that rivals would find impossible or costly to match on a stand-alone basis. In other words, managers can ask themselves which activities, features, or forms of competition are feasible or less costly to them because of complementary activities that their company performs.

Deepening a position involves making the company's activities more distinctive, strengthening fit, and communicating the strategy better to those customers who should value it. But many companies succumb to the temptation to chase "easy" growth by adding hot features, products, or services without screening them or adapting them to their strategy. Or they target new customers or markets in which the company has little special to offer. A company can often grow faster—and far more profitably—by better penetrating needs and varieties where it is distinctive than by slugging it out in potentially higher growth arenas in which the company lacks uniqueness. Carmike, now the largest theater chain in the United States, owes its rapid growth to its disciplined concentration on small markets. The company quickly sells any big-city theaters that come to it as part of an acquisition.

Emerging Industries and Technologies

Developing a strategy in a newly emerging industry or in a business undergoing revolutionary technological changes is a daunting proposition. In such cases, managers face a high level of uncertainty about the needs of customers, the products and services that will prove to be the most desired, and the best configuration of activities and technologies to deliver them. Because of all this uncertainty, imitation and hedging are rampant: unable to risk being wrong or left behind, companies match all features, offer all new services, and explore all technologies.

During such periods in an industry's development, its basic productivity frontier is being established or reestablished. Explosive growth can make such times profitable for many companies, but profits will be temporary because imitation and strategic convergence will ultimately destroy industry profitability. The companies that are enduringly successful will be those that begin as early as possible to define and embody in their activities a unique competitive position. A period of imitation may be inevitable in emerging industries, but that period reflects the level of uncertainty rather than a desired state of affairs.

In high-tech industries, this imitation phase often continues much longer than it should. Enraptured by technological change itself, companies pack more features—most of which are never used—into their products while slashing prices across the board. Rarely are trade-offs even considered. The drive for growth to satisfy market pressures leads companies into every product area. Although a few companies with fundamental advantages prosper, the majority are doomed to a rat race no one can win.

Ironically, the popular business press, focused on hot, emerging industries, is prone to presenting these special cases as proof that we have entered a new era of competition in which none of the old rules are valid. In fact, the opposite is true.

Globalization often allows growth that is consistent with strategy, opening up larger markets for a focused strategy. Unlike broadening domestically, expanding globally is likely to leverage and reinforce a company's unique position and identity.

Companies seeking growth through broadening within their industry can best contain the risks to strategy by creating stand-alone units, each with its own brand name and tailored activities. Maytag has clearly struggled with this issue. On the one hand, it has organized its premium and value brands into separate units with different strategic positions. On the other, it has created an umbrella appliance company for all its brands to gain critical mass. With shared design, manufacturing, distribution, and customer service, it will be hard to avoid homogenization. If a given business unit attempts to compete with different positions for different products or customers, avoiding compromise is nearly impossible.

The role of leadership

The challenge of developing or reestablishing a clear strategy is often primarily an organizational one and depends on leadership. With so many forces at work against making choices and tradeoffs in organizations, a clear intellectual framework to guide strategy is a necessary counterweight. Moreover, strong leaders willing to make choices are essential.

In many companies, leadership has degenerated into orchestrating operational improvements and making deals. But the leader's role is broader and far more important. General management is more than the stewardship of individual functions. Its core is strategy: defining and communicating the company's unique position, making trade-offs, and forging fit among activities. The leader must provide the discipline to decide which industry changes and customer needs the company will respond to, while avoiding organizational distractions and maintaining the company's distinctiveness. Managers at lower levels lack the perspective and the confidence to maintain a strategy. There will be constant pressures to compromise, relax trade-offs, and emulate rivals. One of the leader's jobs is to teach others in the organization about strategy—and to say no.

Strategy renders choices about what not to do as important as choices about what to do. Indeed, setting limits is another function of leadership. Deciding which target group of customers, varieties, and needs the company should serve is fundamental to developing a strategy. But so is deciding not to serve other customers or needs and not to offer certain features or services. Thus strategy requires constant discipline and clear communication. Indeed, one of the most important functions of an explicit, communicated strategy is to guide employees in making choices that arise because of trade-offs in their individual activities and in day-to-day decisions.

Improving operational effectiveness is a necessary part of management, but it is *not* strategy. In confusing the two, managers have unintentionally backed into a way of thinking about competition that is driving many industries toward competitive convergence, which is in no one's best interest and is not inevitable.

Managers must clearly distinguish operational effectiveness from strategy. Both are essential, but the two agendas are different.

The operational agenda involves continual improvement everywhere there are no trade-offs. Failure to do this creates vulnerability even for companies with a good strategy. The operational agenda is the proper place for constant change, flexibility, and relentless efforts to achieve best practice. In contrast, the strategic agenda is the right place for defining a unique position, making clear trade-offs, and tightening fit. It involves the continual search for ways to reinforce and extend the company's position. The strategic agenda demands discipline and continuity; its enemies are distraction and compromise.

Strategic continuity does not imply a static view of competition. A company must continually improve its operational effectiveness and actively try to shift the productivity frontier; at the same time, there needs to be ongoing effort to extend its uniqueness while strengthening the fit among its activities. Strategic continuity, in fact, should make an organization's continual improvement more effective.

A company may have to change its strategy if there are major structural changes in its industry. In fact, new strategic positions often arise because of industry changes, and new entrants unencumbered by history often can exploit them more easily. However, a company's choice of a new position must be driven by the ability to find new trade-offs and leverage a new system of complementary activities into a sustainable advantage.

Originally published in November 1996. Reprint 96608

Notes

[1.](#) I first described the concept of activities and its use in understanding competitive advantage in *Competitive Advantage* (New York: The Free Press, 1985). The ideas in this article build on and extend that thinking.

[2.](#) Paul Milgrom and John Roberts have begun to explore the economics of systems of complementary functions, activities, and functions. Their focus is on the emergence of “modern manufacturing” as a new set of complementary activities, on the tendency of companies to react to external changes with coherent bundles of internal responses, and on the need for central coordination—a strategy—to align functional managers. In the latter case, they model what has long been a bedrock principle of strategy. See Paul Milgrom and John Roberts, “The Economics of Modern Manufacturing: Technology, Strategy, and Organization,” *American Economic Review* 80 (1990): 511–528; Paul Milgrom, Yingyi Qian, and John Roberts, “Complementarities, Momentum, and Evolution of Modern Manufacturing,” *American Economic Review* 81 (1991) 84–88; and Paul Milgrom and John Roberts, “Complementarities and Fit: Strategy, Structure, and Organizational Changes in Manufacturing,” *Journal of Accounting and Economics*, vol. 19 (March–May 1995): 179–208.

[3.](#) Material on retail strategies is drawn in part from Jan Rivkin, “The Rise of Retail Category Killers,” unpublished working paper, January 1995. Nicolaj Siggelkow prepared the case study on the Gap.

The Core Competence of the Corporation

by C.K. Prahalad and Gary Hamel

THE MOST POWERFUL WAY to prevail in global competition is still invisible to many companies. During the 1980s, top executives were judged on their ability to restructure, declutter, and delay their corporations. In the 1990s, they'll be judged on their ability to identify, cultivate, and exploit the core competencies that make growth possible—indeed, they'll have to rethink the concept of the corporation itself.

Consider the last ten years of GTE and NEC. In the early 1980s, GTE was well positioned to become a major player in the evolving information technology industry. It was active in telecommunications. Its operations spanned a variety of businesses including telephones, switching and transmission systems, digital PABX, semiconductors, packet switching, satellites, defense systems, and lighting products. And GTE's Entertainment Products Group, which produced Sylvania color TVs, had a position in related display technologies. In 1980, GTE's sales were \$9.98 billion, and net cash flow was \$1.73 billion. NEC, in contrast, was much smaller, at \$3.8 billion in sales. It had a comparable technological base and computer businesses, but it had no experience as an operating telecommunications company.

Yet look at the positions of GTE and NEC in 1988. GTE's 1988 sales were \$16.46 billion, and NEC's sales were considerably higher at \$21.89 billion. GTE has, in effect, become a telephone operating company with a position in defense and lighting products. GTE's other businesses are small in global terms. GTE has divested Sylvania TV and Telenet, put switching, transmission, and digital PABX into joint ventures, and closed down semiconductors. As a result, the international position of GTE has eroded. Non-U.S. revenue as a percent of total revenue dropped from 20% to 15%

between 1980 and 1988.

NEC has emerged as the world leader in semiconductors and as a first-tier player in telecommunications products and computers. It has consolidated its position in mainframe computers. It has moved beyond public switching and transmission to include such lifestyle products as mobile telephones, facsimile machines, and laptop computers—bridging the gap between telecommunications and office automation. NEC is the only company in the world to be in the top five in revenue in telecommunications, semiconductors, and mainframes. Why did these two companies, starting with comparable business portfolios, perform so differently? Largely because NEC conceived of itself in terms of “core competencies,” and GTE did not.

Rethinking the Corporation

Once, the diversified corporation could simply point its business units at particular end product markets and admonish them to become world leaders. But with market boundaries changing ever more quickly, targets are elusive and capture is at best temporary. A few companies have proven themselves adept at inventing new markets, quickly entering emerging markets, and dramatically shifting patterns of customer choice in established markets. These are the ones to emulate. The critical task for management is to create an organization capable of infusing products with irresistible functionality or, better yet, creating products that customers need but have not yet even imagined.

This is a deceptively difficult task. Ultimately, it requires radical change in the management of major companies. It means, first of all, that top managements of Western companies must assume responsibility for competitive decline. Everyone knows about high interest rates, Japanese protectionism, outdated antitrust laws, obstreperous unions, and impatient investors. What is harder to see, or harder to acknowledge, is how little added momentum companies actually get from political or macroeconomic “relief.” Both the theory and practice of Western management have created a drag on our forward motion. It is the principles of management that are in need of reform.

Idea in Brief

Diversified giant NEC competed in seemingly disparate businesses—semiconductors, telecommunications, computing, and consumer electronics—and dominated them all.

How? It considered itself *not* a collection of strategic business units, but a portfolio of **core competencies**—the company’s collective knowledge about how to coordinate diverse production skills and technologies.

NEC used its core competencies to achieve what most companies only attempt: invent new markets, exploit emerging ones, delight customers with products they hadn’t even imagined—but definitely needed.

Think of a diversified company as a tree: the trunk and major limbs as core products, smaller branches as business units, leaves and fruit as end products. Nourishing and stabilizing everything is the root system: core competencies.

Focusing on core competencies creates unique, integrated systems that reinforce fit among your firm's diverse production and technology skills—a systemic advantage your competitors can't copy.

NEC versus GTE, again, is instructive and only one of many such comparative cases we analyzed to understand the changing basis for global leadership. Early in the 1970s, NEC articulated a strategic intent to exploit the convergence of computing and communications, what it called “C&C.”¹ Success, top management reckoned, would hinge on acquiring *competencies*, particularly in semiconductors. Management adopted an appropriate “strategic architecture,” summarized by C&C, and then communicated its intent to the whole organization and the outside world during the mid-1970s.

Idea in Practice

Clarify Core Competencies

When you clarify competencies, your entire organization knows how to support your competitive advantage—and readily allocates resources to build cross-unit technological and production links. Use these steps:

Articulate a strategic intent that defines your company and its markets (e.g., NEC's “exploit the convergence of computing and communications”).

Identify core competencies that support that intent. Ask:

- How long could we dominate our business if we didn't control this competency?
- What future opportunities would we lose without it?
- Does it provide access to multiple markets? (Casio's core competence with display systems let it succeed in calculators, laptop monitors, *and* car dashboards.)
- Do customer benefits revolve around it? (Honda's competence with high-revving, lightweight engines offers multiple consumer benefits.)

Build Core Competencies

Once you've identified core competencies, enhance them:

Invest in needed technologies. Citicorp trumped rivals by adopting an operating system that leveraged its competencies—and let it participate in world markets 24 hours a day.

Infuse resources throughout business units to outpace rivals in new business development. 3M and Honda won races for global brand dominance by creating wide varieties of products from their core competencies. Results? They built image, customer loyalty, and access to distribution channels for all their businesses.

Forge strategic alliances. NEC's collaboration with partners like Honeywell gave it access to the mainframe and semiconductor technologies it needed to build core competencies.

Cultivate a Core-Competency Mind-Set

Competency-savvy managers work well across organizational boundaries, willingly share resources, and think long term. To encourage this mind-set:

Stop thinking of business units as sacrosanct. That imprisons resources in units and motivates managers to hide talent as the company pursues hot opportunities.

Identify projects and people who embody the firm's core competencies. This sends a message: Core competencies are corporate—not unit—resources, and those who embody them can be reallocated. (When Canon spotted opportunities in digital laser printers, it let managers raid other units to assemble talent.)

Gather managers to identify next-generation competencies. Decide how much investment each needs, and how much capital and staff each division should contribute.

NEC constituted a “C&C Committee” of top managers to oversee the development of core products and core competencies. NEC put in place coordination groups and committees that cut across the interests of individual businesses. Consistent with its strategic architecture, NEC shifted enormous resources to strengthen its position in components and central processors. By using collaborative arrangements to multiply internal resources, NEC was able to accumulate a broad array of core competencies.

NEC carefully identified three interrelated streams of technological and market evolution. Top management determined that computing would evolve from large mainframes to distributed processing, components from simple ICs to VLSI, and communications from mechanical cross-bar exchange to complex digital systems we now call ISDN. As things evolved further, NEC reasoned, the computing, communications, and components businesses would so overlap that it would be very hard to distinguish among them, and that there would be enormous opportunities for any company that had built the competencies needed to serve all three markets.

NEC top management determined that semiconductors would be the company's most important "core product." It entered into myriad strategic alliances—over 100 as of 1987—aimed at building competencies rapidly and at low cost. In mainframe computers, its most noted relationship was with Honeywell and Bull. Almost all the collaborative arrangements in the semiconductor-component field were oriented toward technology access. As they entered collaborative arrangements, NEC's operating managers understood the rationale for these alliances and the goal of internalizing partner skills. NEC's director of research summed up its competence acquisition during the 1970s and 1980s this way: "From an investment standpoint, it was much quicker and cheaper to use foreign technology. There wasn't a need for us to develop new ideas."

No such clarity of strategic intent and strategic architecture appeared to exist at GTE. Although senior executives discussed the implications of the evolving information technology industry, no commonly accepted view of which competencies would be required to compete in that industry were communicated widely. While significant staff work was done to identify key technologies, senior line managers continued to act as if they were managing independent business units. Decentralization made it difficult to focus on core competencies. Instead, individual businesses became increasingly dependent on outsiders for critical skills, and collaboration became a route to staged exits. Today, with a new management team in place, GTE has repositioned itself to apply its competencies to emerging markets in telecommunications services.

The Roots of Competitive Advantage

The distinction we observed in the way NEC and GTE conceived of themselves—a portfolio of competencies versus a portfolio of businesses—was repeated across many industries. From 1980 to 1988, Canon grew by 264%, Honda by 200%. Compare that with Xerox and Chrysler. And if Western managers were once anxious about the low cost and high quality of Japanese imports, they are now overwhelmed by the pace at which Japanese rivals are inventing new markets, creating new products, and enhancing them. Canon has given us personal copiers; Honda has moved from motorcycles to four-wheel off-road buggies. Sony developed the 8mm camcorder, Yamaha, the digital piano. Komatsu developed an underwater remote-controlled bulldozer, while Casio's latest gambit is a small-screen color LCD television. Who would have anticipated the evolution of these vanguard markets?

In more established markets, the Japanese challenge has been just as disquieting. Japanese companies are generating a blizzard of features and functional enhancements that bring technological sophistication to everyday products. Japanese car producers have been pioneering four-wheel steering, four-valve-per-cylinder engines, in-car navigation systems, and sophisticated electronic engine-management systems. On the strength of its product features, Canon is now a player in facsimile transmission machines, desktop laser printers, even semi-conductor manufacturing equipment.

In the short run, a company's competitiveness derives from the price/performance attributes of current products. But the survivors of the first wave of global competition, Western and Japanese alike, are all converging on similar and formidable standards for product cost and quality—minimum hurdles for continued competition, but less and less important as sources of differential advantage. In the long run, competitiveness derives from an ability to build, at lower cost and more speedily than competitors, the core competencies that spawn unanticipated products. The real sources of advantage are to be found in management's ability to consolidate corporatewide technologies and production skills into competencies that empower individual businesses to adapt quickly to changing opportunities.

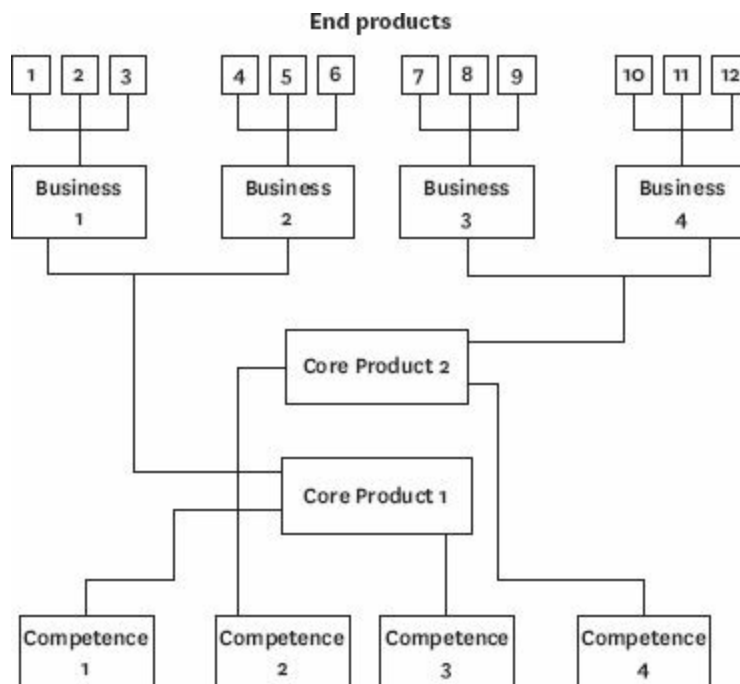
Senior executives who claim that they cannot build core competencies

either because they feel the autonomy of business units is sacrosanct or because their feet are held to the quarterly budget fire should think again. The problem in many Western companies is not that their senior executives are any less capable than those in Japan nor that Japanese companies possess greater technical capabilities. Instead, it is their adherence to a concept of the corporation that unnecessarily limits the ability of individual businesses to fully exploit the deep reservoir of technological capability that many American and European companies possess.

The diversified corporation is a large tree. The trunk and major limbs are core products, the smaller branches are business units; the leaves, flowers, and fruit are end products. The root system that provides nourishment, sustenance, and stability is the core competence. You can miss the strength of competitors by looking only at their end products, in the same way you miss the strength of a tree if you look only at its leaves. (See the chart “Competencies: The Roots of Competitiveness.”)

Competencies: the roots of competitiveness

The corporation, like a tree, grows from its roots. Core products are nourished by competencies and engender business units, whose fruit are end products.



Core competencies are the collective learning in the organization,

especially how to coordinate diverse production skills and integrate multiple streams of technologies. Consider Sony's capacity to miniaturize or Philips's optical-media expertise. The theoretical knowledge to put a radio on a chip does not in itself assure a company the skill to produce a miniature radio no bigger than a business card. To bring off this feat, Casio must harmonize know-how in miniaturization, microprocessor design, material science, and ultrathin precision casing—the same skills it applies in its miniature card calculators, pocket TVs, and digital watches.

If core competence is about harmonizing streams of technology, it is also about the organization of work and the delivery of value. Among Sony's competencies is miniaturization. To bring miniaturization to its products, Sony must ensure that technologists, engineers, and marketers have a shared understanding of customer needs and of technological possibilities. The force of core competence is felt as decisively in services as in manufacturing. Citicorp was ahead of others investing in an operating system that allowed it to participate in world markets 24 hours a day. Its competence in systems has provided the company the means to differentiate itself from many financial service institutions.

Core competence is communication, involvement, and a deep commitment to working across organizational boundaries. It involves many levels of people and all functions. World-class research in, for example, lasers or ceramics can take place in corporate laboratories without having an impact on any of the businesses of the company. The skills that together constitute core competence must coalesce around individuals whose efforts are not so narrowly focused that they cannot recognize the opportunities for blending their functional expertise with those of others in new and interesting ways.

Core competence does not diminish with use. Unlike physical assets, which do deteriorate over time, competencies are enhanced as they are applied and shared. But competencies still need to be nurtured and protected; knowledge fades if it is not used. Competencies are the glue that binds existing businesses. They are also the engine for new business development. Patterns of diversification and market entry may be guided by them, not just by the attractiveness of markets.

Consider 3M's competence with sticky tape. In dreaming up businesses as diverse as "Post-it" notes, magnetic tape, photographic film, pressure-sensitive tapes, and coated abrasives, the company has brought to bear widely

shared competencies in substrates, coatings, and adhesives and devised various ways to combine them. Indeed, 3M has invested consistently in them. What seems to be an extremely diversified portfolio of businesses belies a few shared core competencies.

In contrast, there are major companies that have had the potential to build core competencies but failed to do so because top management was unable to conceive of the company as anything other than a collection of discrete businesses. GE sold much of its consumer electronics business to Thomson of France, arguing that it was becoming increasingly difficult to maintain its competitiveness in this sector. That was undoubtedly so, but it is ironic that it sold several key businesses to competitors who were already competence leaders—Black & Decker in small electrical motors, and Thomson, which was eager to build its competence in microelectronics and had learned from the Japanese that a position in consumer electronics was vital to this challenge.

Management trapped in the strategic business unit (SBU) mind-set almost inevitably finds its individual businesses dependent on external sources for critical components, such as motors or compressors. But these are not just components. They are core products that contribute to the competitiveness of a wide range of end products. They are the physical embodiments of core competencies.

How Not to Think of Competence

Since companies are in a race to build the competencies that determine global leadership, successful companies have stopped imagining themselves as bundles of businesses making products. Canon, Honda, Casio, or NEC may seem to preside over portfolios of businesses unrelated in terms of customers, distribution channels, and merchandising strategy. Indeed, they have portfolios that may seem idiosyncratic at times: NEC is the only global company to be among leaders in computing, telecommunications, and semiconductors *and* to have a thriving consumer electronics business.

But looks are deceiving. In NEC, digital technology, especially VLSI and systems integration skills, is fundamental. In the core competencies underlying them, disparate businesses become coherent. It is Honda's core competence in engines and power trains that gives it a distinctive advantage in car, motorcycle, lawn mower, and generator businesses. Canon's core competencies in optics, imaging, and microprocessor controls have enabled it to enter, even dominate, markets as seemingly diverse as copiers, laser printers, cameras, and image scanners. Philips worked for more than 15 years to perfect its optical-media (laser disc) competence, as did JVC in building a leading position in video recording. Other examples of core competencies might include mechantronics (the ability to marry mechanical and electronic engineering), video displays, bioengineering, and microelectronics. In the early stages of its competence building, Philips could not have imagined all the products that would be spawned by its optical-media competence, nor could JVC have anticipated miniature camcorders when it first began exploring videotape technologies.

Unlike the battle for global brand dominance, which is visible in the world's broadcast and print media and is aimed at building global "share of mind," the battle to build world-class competencies is invisible to people who aren't deliberately looking for it. Top management often tracks the cost and quality of competitors' products, yet how many managers untangle the web of alliances their Japanese competitors have constructed to acquire competencies at low cost? In how many Western boardrooms is there an explicit, shared understanding of the competencies the company must build

for world leadership? Indeed, how many senior executives discuss the crucial distinction between competitive strategy at the level of a business and competitive strategy at the level of an entire company?

Let us be clear. Cultivating core competence does *not* mean outspending rivals on research and development. In 1983, when Canon surpassed Xerox in worldwide unit market share in the copier business, its R&D budget in reprographics was but a small fraction of Xerox's. Over the past 20 years, NEC has spent less on R&D as a percentage of sales than almost all of its American and European competitors.

Nor does core competence mean shared costs, as when two or more SBUs use a common facility—a plant, service facility, or sales force—or share a common component. The gains of sharing may be substantial, but the search for shared costs is typically a post hoc effort to rationalize production across existing businesses, not a premeditated effort to build the competencies out of which the businesses themselves grow.

Building core competencies is more ambitious and different than integrating vertically, moreover. Managers deciding whether to make or buy will start with end products and look upstream to the efficiencies of the supply chain and downstream toward distribution and customers. They do not take inventory of skills and look forward to applying them in nontraditional ways. (Of course, decisions about competencies *do* provide a logic for vertical integration. Canon is not particularly integrated in its copier business, except in those aspects of the vertical chain that support the competencies it regards as critical.)

Identifying Core Competencies—And Losing Them

At least three tests can be applied to identify core competencies in a company. First, a core competence provides potential access to a wide variety of markets. Competence in display systems, for example, enables a company to participate in such diverse businesses as calculators, miniature TV sets, monitors for laptop computers, and automotive dashboards—which is why Casio's entry into the handheld TV market was predictable. Second, a core competence should make a significant contribution to the perceived customer benefits of the end product. Clearly, Honda's engine expertise fills this bill.

Finally, a core competence should be difficult for competitors to imitate. And it *will* be difficult if it is a complex harmonization of individual technologies and production skills. A rival might acquire some of the technologies that comprise the core competence, but it will find it more difficult to duplicate the more or less comprehensive pattern of internal coordination and learning. JVC's decision in the early 1960s to pursue the development of a videotape competence passed the three tests outlined here. RCA's decision in the late 1970s to develop a stylus-based video turntable system did not.

Few companies are likely to build world leadership in more than five or six fundamental competencies. A company that compiles a list of 20 to 30 capabilities has probably not produced a list of core competencies. Still, it is probably a good discipline to generate a list of this sort and to see aggregate capabilities as building blocks. This tends to prompt the search for licensing deals and alliances through which the company may acquire, at low cost, missing pieces.

Most Western companies hardly think about competitiveness in these terms at all. It is time to take a tough-minded look at the risks they are running. Companies that judge competitiveness, their own and their competitors', primarily in terms of the price/performance of end products are courting the erosion of core competencies—or making too little effort to enhance them. The embedded skills that give rise to the next generation of competitive products cannot be “rented in” by outsourcing and OEM-supply relationships. In our view, too many companies have unwittingly surrendered

core competencies when they cut internal investment in what they mistakenly thought were just “cost centers” in favor of outside suppliers.

Consider Chrysler. Unlike Honda, it has tended to view engines and power trains as simply one more component. Chrysler is becoming increasingly dependent on Mitsubishi and Hyundai: between 1985 and 1987, the number of outsourced engines went from 252,000 to 382,000. It is difficult to imagine Honda yielding manufacturing responsibility, much less design, of so critical a part of a car’s function to an outside company—which is why Honda has made such an enormous commitment to Formula One auto racing. Honda has been able to pool its engine-related technologies; it has parlayed these into a corporatewide competency from which it develops world-beating products, despite R&D budgets smaller than those of GM and Toyota.

Of course, it is perfectly possible for a company to have a competitive product line-up but be a laggard in developing core competencies—at least for a while. If a company wanted to enter the copier business today, it would find a dozen Japanese companies more than willing to supply copiers on the basis of an OEM private label. But when fundamental technologies changed or if its supplier decided to enter the market directly and become a competitor, that company’s product line, along with all of its investments in marketing and distribution, could be vulnerable. Outsourcing can provide a shortcut to a more competitive product, but it typically contributes little to building the people-embodied skills that are needed to sustain product leadership.

Nor is it possible for a company to have an intelligent alliance or sourcing strategy if it has not made a choice about where it will build competence leadership. Clearly, Japanese companies have benefited from alliances. They’ve used them to learn from Western partners who were not fully committed to preserving core competencies of their own. As we’ve argued in these pages before, learning within an alliance takes a positive commitment of resources—the travel, a pool of dedicated people, test-bed facilities, time to internalize and test what has been learned.² A company may not make this effort if it doesn’t have clear goals for competence building.

Another way of losing is forgoing opportunities to establish competencies that are evolving in existing businesses. In the 1970s and 1980s, many American and European companies—like GE, Motorola, GTE, Thorn, and GEC—chose to exit the color television business, which they regarded as

mature. If by “mature” they meant that they had run out of new product ideas at precisely the moment global rivals had targeted the TV business for entry, then yes, the industry was mature. But it certainly wasn’t mature in the sense that all opportunities to enhance and apply video-based competencies had been exhausted.

In ridding themselves of their television businesses, these companies failed to distinguish between divesting the business and destroying their video media-based competencies. They not only got out of the TV business but they also closed the door on a whole stream of future opportunities reliant on video-based competencies. The television industry, considered by many U.S. companies in the 1970s to be unattractive, is today the focus of a fierce public policy debate about the inability of U.S. corporations to benefit from the \$20-billion-a-year opportunity that HDTV will represent in the mid- to late 1990s. Ironically, the U.S. government is being asked to fund a massive research project—in effect, to compensate U.S. companies for their failure to preserve critical core competencies when they had the chance.

In contrast, one can see a company like Sony reducing its emphasis on VCRs (where it has not been very successful and where Korean companies now threaten) without reducing its commitment to video-related competencies. Sony’s Betamax led to a debacle. But it emerged with its videotape recording competencies intact and is currently challenging Matsushita in the 8mm camcorder market.

There are two clear lessons here. First, the costs of losing a core competence can be only partly calculated in advance. The baby may be thrown out with the bathwater in divestment decisions. Second, since core competencies are built through a process of continuous improvement and enhancement that may span a decade or longer, a company that has failed to invest in core competence building will find it very difficult to enter an emerging market, unless, of course, it will be content simply to serve as a distribution channel.

American semiconductor companies like Motorola learned this painful lesson when they elected to forgo direct participation in the 256k generation of DRAM chips. Having skipped this round, Motorola, like most of its American competitors, needed a large infusion of technical help from Japanese partners to rejoin the battle in the 1-megabyte generation. When it comes to core competencies, it is difficult to get off the train, walk to the next station, and then reboard.

From Core Competencies to Core Products

The tangible link between identified core competencies and end products is what we call the core products—the physical embodiments of one or more core competencies. Honda's engines, for example, are core products, linchpins between design and development skills that ultimately lead to a proliferation of end products. Core products are the components or subassemblies that actually contribute to the value of the end products. Thinking in terms of core products forces a company to distinguish between the brand share it achieves in end product markets (for example, 40% of the U.S. refrigerator market) and the manufacturing share it achieves in any particular core product (for example, 5% of the world share of compressor output).

Canon is reputed to have an 84% world manufacturing share in desktop laser printer “engines,” even though its brand share in the laser printer business is minuscule. Similarly, Matsushita has a world manufacturing share of about 45% in key VCR components, far in excess of its brand share (Panasonic, JVC, and others) of 20%. And Matsushita has a commanding core product share in compressors worldwide, estimated at 40%, even though its brand share in both the air-conditioning and refrigerator businesses is quite small.

It is essential to make this distinction between core competencies, core products, and end products because global competition is played out by different rules and for different stakes at each level. To build or defend leadership over the long term, a corporation will probably be a winner at each level. At the level of core competence, the goal is to build world leadership in the design and development of a particular class of product functionality—be it compact data storage and retrieval, as with Philips's optical-media competence, or compactness and ease of use, as with Sony's micromotors and microprocessor controls.

To sustain leadership in their chosen core competence areas, these companies *seek to maximize their world manufacturing share in core products*. The manufacture of core products for a wide variety of external (and internal) customers yields the revenue and market feedback that, at least

partly, determines the pace at which core competencies can be enhanced and extended. This thinking was behind JVC's decision in the mid-1970s to establish VCR supply relationships with leading national consumer electronics companies in Europe and the United States. In supplying Thomson, Thorn, and Telefunken (all independent companies at that time) as well as U.S. partners, JVC was able to gain the cash and the diversity of market experience that ultimately enabled it to outpace Philips and Sony. (Philips developed videotape competencies in parallel with JVC, but it failed to build a worldwide network of OEM relationships that would have allowed it to accelerate the refinement of its videotape competence through the sale of core products.)

JVC's success has not been lost on Korean companies like Goldstar, Samsung, Kia, and Daewoo, who are building core product leadership in areas as diverse as displays, semiconductors, and automotive engines through their OEM-supply contracts with Western companies. Their avowed goal is to capture investment initiative away from potential competitors, often U.S. companies. In doing so, they accelerate their competence-building efforts while "hollowing out" their competitors. By focusing on competence and embedding it in core products, Asian competitors have built up advantages in component markets first and have then leveraged off their superior products to move downstream to build brand share. And they are not likely to remain the low-cost suppliers forever. As their reputation for brand leadership is consolidated, they may well gain price leadership. Honda has proven this with its Acura line, and other Japanese car makers are following suit.

Control over core products is critical for other reasons. A dominant position in core products allows a company to shape the evolution of applications and end markets. Such compact audio disc-related core products as data drives and lasers have enabled Sony and Philips to influence the evolution of the computer-peripheral business in optical-media storage. As a company multiplies the number of application arenas for its core products, it can consistently reduce the cost, time, and risk in new product development. In short, well-targeted core products can lead to economies of scale *and* scope.

The Tyranny of the SBU

The new terms of competitive engagement cannot be understood using analytical tools devised to manage the diversified corporation of 20 years ago, when competition was primarily domestic (GE versus Westinghouse, General Motors versus Ford) and all the key players were speaking the language of the same business schools and consultancies. Old prescriptions have potentially toxic side effects. The need for new principles is most obvious in companies organized exclusively according to the logic of SBUs. The implications of the two alternate concepts of the corporation are summarized in “Two Concepts of the Corporation: SBU or Core Competence.”

Two Concepts of the Corporation: SBU or Core Competence		
	SBU	Core Competence
Basis for competition	Competitiveness of today's products	Interfirm competition to build competencies
Corporate structure	Portfolio of businesses related in product-market terms	Portfolio of competencies, core products, and businesses
Status of the business unit	Autonomy is sacrosanct; the SBU “owns” all resources other than cash	SBU is a potential reservoir of core competencies
Resource allocation	Discrete businesses are the unit of analysis; capital is allocated business by business	Businesses and competencies are the unit of analysis: top management allocates capital and talent
Value added of top management	Optimizing corporate returns through capital allocation trade-offs among businesses	Enunciating strategic architecture and building competencies to secure the future

Obviously, diversified corporations have a portfolio of products and a portfolio of businesses. But we believe in a view of the company as a portfolio of competencies as well. U.S. companies do not lack the technical resources to build competencies, but their top management often lacks the vision to build them and the administrative means for assembling resources spread across multiple businesses. A shift in commitment will inevitably influence patterns of diversification, skill deployment, resource allocation priorities, and approaches to alliances and outsourcing.

We have described the three different planes on which battles for global leadership are waged: core competence, core products, and end products. A corporation has to know whether it is winning or losing on each plane. By sheer weight of investment, a company might be able to beat its rivals to blue-sky technologies yet still lose the race to build core competence leadership. If a company is winning the race to build core competencies (as opposed to building leadership in a few technologies), it will almost certainly outpace rivals in new business development. If a company is winning the race to capture world manufacturing share in core products, it will probably outpace rivals in improving product features and the price/performance ratio.

Determining whether one is winning or losing end-product battles is more difficult because measures of product market share do not necessarily reflect various companies' underlying competitiveness. Indeed, companies that attempt to build market share by relying on the competitiveness of others, rather than investing in core competencies and world core-product leadership, may be treading on quicksand. In the race for global brand dominance, companies like 3M, Black & Decker, Canon, Honda, NEC, and Citicorp have built global brand umbrellas by proliferating products out of their core competencies. This has allowed their individual businesses to build image, customer loyalty, and access to distribution channels.

When you think about this reconceptualization of the corporation, the primacy of the SBU—an organizational dogma for a generation—is now clearly an anachronism. Where the SBU is an article of faith, resistance to the seductions of decentralization can seem heretical. In many companies, the SBU prism means that only one plane of the global competitive battle, the battle to put competitive products on the shelf *today*, is visible to top management. What are the costs of this distortion?

Underinvestment in Developing Core Competencies and Core Products.

When the organization is conceived of as a multiplicity of SBUs, no single business may feel responsible for maintaining a viable position in core products nor be able to justify the investment required to build world leadership in some core competence. In the absence of a more comprehensive view imposed by corporate management, SBU managers will tend to underinvest. Recently, companies such as Kodak and Philips have recognized this as a potential problem and have begun searching for new organizational forms that will allow them to develop and manufacture core products for both internal and external customers.

SBU managers have traditionally conceived of competitors in the same way they've seen themselves. On the whole, they've failed to note the emphasis Asian competitors were placing on building leadership in core products or to understand the critical linkage between world manufacturing leadership and the ability to sustain development pace in core competence. They've failed to pursue OEM-supply opportunities or to look across their various product divisions in an attempt to identify opportunities for coordinated initiatives.

Imprisoned Resources. As an SBU evolves, it often develops unique competencies. Typically, the people who embody this competence are seen as the sole property of the business in which they grew up. The manager of another SBU who asks to borrow talented people is likely to get a cold rebuff. SBU managers are not only unwilling to lend their competence carriers but they may actually hide talent to prevent its redeployment in the pursuit of new opportunities. This may be compared to residents of an underdeveloped country hiding most of their cash under their mattresses. The benefits of competencies, like the benefits of the money supply, depend on the velocity of their circulation as well as on the size of the stock the company holds.

Western companies have traditionally had an advantage in the stock of skills they possess. But have they been able to reconfigure them quickly to respond to new opportunities? Canon, NEC, and Honda have had a lesser stock of the people and technologies that compose core competencies but could move them much quicker from one business unit to another. Corporate R&D spending at Canon is not fully indicative of the size of Canon's core competence stock and tells the casual observer nothing about the velocity with which Canon is able to move core competencies to exploit opportunities.

When competencies become imprisoned, the people who carry the competencies do not get assigned to the most exciting opportunities, and their skills begin to atrophy. Only by fully leveraging core competencies can small companies like Canon afford to compete with industry giants like Xerox. How strange that SBU managers, who are perfectly willing to compete for cash in the capital budgeting process, are unwilling to compete for people—the company's most precious asset. We find it ironic that top management devotes so much attention to the capital budgeting process yet typically has no comparable mechanism for allocating the human skills that embody core competencies. Top managers are seldom able to look four or five levels down into the organization, identify the people who embody critical competencies, and move them across organizational boundaries.

Bounded Innovation. If core competencies are not recognized, individual SBUs will pursue only those innovation opportunities that are close at hand—marginal product-line extensions or geographic expansions. Hybrid opportunities like fax machines, laptop computers, hand-held televisions, or portable music keyboards will emerge only when managers take off their SBU blinkers. Remember, Canon appeared to be in the camera business at the time it was preparing to become a world leader in copiers. Conceiving of the corporation in terms of core competencies widens the domain of innovation.

Developing Strategic Architecture

The fragmentation of core competencies becomes inevitable when a diversified company's information systems, patterns of communication, career paths, managerial rewards, and processes of strategy development do not transcend SBU lines. We believe that senior management should spend a significant amount of its time developing a corporatewide strategic architecture that establishes objectives for competence building. A strategic architecture is a road map of the future that identifies which core competencies to build and their constituent technologies.

By providing an impetus for learning from alliances and a focus for internal development efforts, a strategic architecture like NEC's C&C can dramatically reduce the investment needed to secure future market leadership. How can a company make partnerships intelligently without a clear understanding of the core competencies it is trying to build and those it is attempting to prevent from being unintentionally transferred?

Of course, all of this begs the question of what a strategic architecture should look like. The answer will be different for every company. But it is helpful to think again of that tree, of the corporation organized around core products and, ultimately, core competencies. To sink sufficiently strong roots, a company must answer some fundamental questions: How long could we preserve our competitiveness in this business if we did not control this particular core competence? How central is this core competence to perceived customer benefits? What future opportunities would be foreclosed if we were to lose this particular competence?

The architecture provides a logic for product and market diversification, moreover. An SBU manager would be asked: Does the new market opportunity add to the overall goal of becoming the best player in the world? Does it exploit or add to the core competence? At Vickers, for example, diversification options have been judged in the context of becoming the best power and motion control company in the world (see the sidebar "Vickers Learns the Value of Strategic Architecture").

Vickers Learns the Value of Strategic Architecture

The idea that top management should develop a corporate strategy for acquiring and deploying core competencies is relatively new in most U.S. companies. There are a few exceptions. An early convert was Trinova (previously Libbey Owens Ford), a Toledo-based corporation, which enjoys a worldwide position in power and motion controls and engineered plastics. One of its major divisions is Vickers, a premier supplier of hydraulics components like valves, pumps, actuators, and filtration devices to aerospace, marine, defense, automotive, earth-moving, and industrial markets.

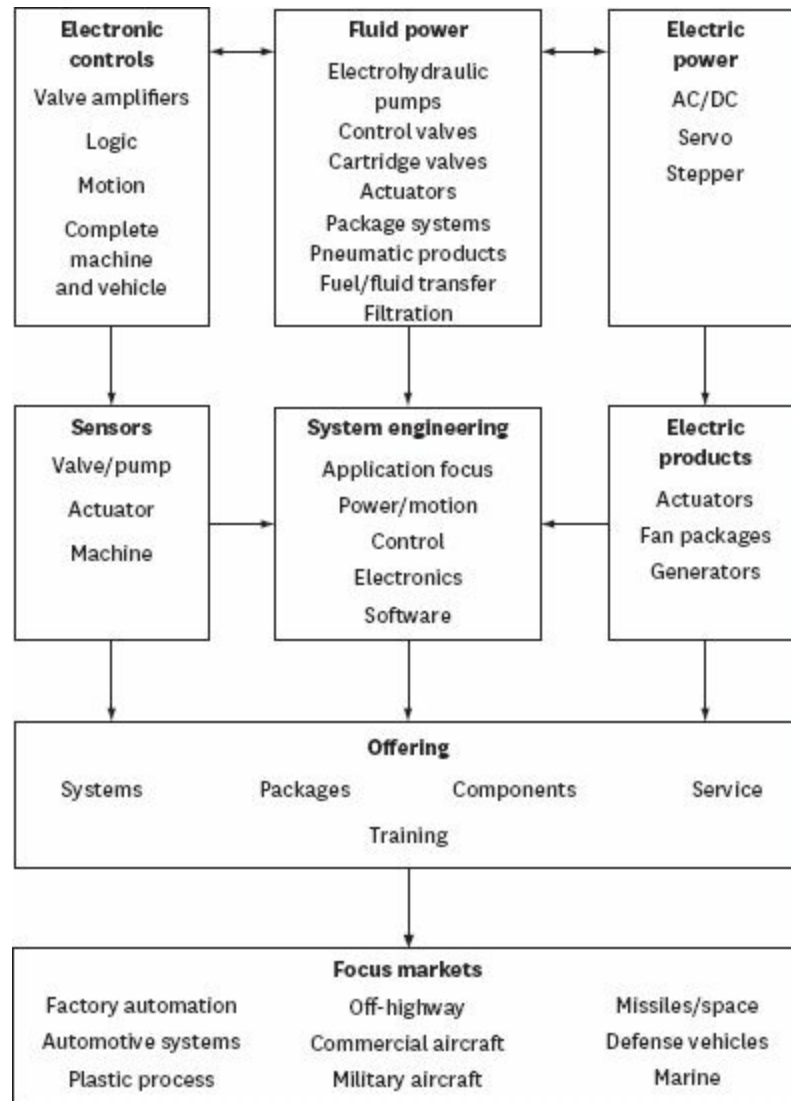
Vickers saw the potential for a transformation of its traditional business with the application of electronics disciplines in combination with its traditional technologies. The goal was “to ensure that change in technology does not displace Vickers from its customers.” This, to be sure, was initially a defensive move: Vickers recognized that unless it acquired new skills, it could not protect existing markets or capitalize on new growth opportunities. Managers at Vickers attempted to conceptualize the likely evolution of (a) technologies relevant to the power and motion control business, (b) functionalities that would satisfy emerging customer needs, and (c) new competencies needed to creatively manage the marriage of technology and customer needs.

Despite pressure for short-term earnings, top management looked to a 10- to 15-year time horizon in developing a map of emerging customer needs, changing technologies, and the core competencies that would be necessary to bridge the gap between the two. Its slogan was “Into the 21st Century.” (A simplified version of the overall architecture developed is shown here.) Vickers is currently in fluid-power components. The architecture identifies two additional competencies, electric-power components and electronic controls. A systems integration capability that would unite hardware, software, and service was also targeted for development.

The strategic architecture, as illustrated by the Vickers example, is not a forecast of specific products or specific technologies but a broad map of the evolving linkages between customer functionality requirements, potential technologies, and core competencies. It assumes that products and systems cannot be defined with certainty for the future but that preempting competitors in the development of new markets requires an early start to building core competencies. The strategic architecture developed by Vickers, while describing the future in competence terms, also provides the basis for making “here and now” decisions about product priorities, acquisitions, alliances, and recruitment.

Since 1986, Vickers has made more than ten clearly targeted acquisitions, each one focused on a specific component or technology gap identified in the overall architecture. The architecture is also the basis for internal development of new competencies. Vickers has undertaken, in parallel, a reorganization to enable the integration of electronics and electrical capabilities with mechanical-based competencies. We believe that it will take another two to three years before Vickers reaps the total benefits from developing the strategic architecture, communicating it widely to all its employees, customers, and investors, and building administrative systems consistent with the architecture.

Vickers map of competencies



The strategic architecture should make resource allocation priorities transparent to the entire organization. It provides a template for allocation decisions by top management. It helps lower-level managers understand the logic of allocation priorities and disciplines senior management to maintain consistency. In short, it yields a definition of the company and the markets it serves. 3M, Vickers, NEC, Canon, and Honda all qualify on this score. Honda *knew* it was exploiting what it had learned from motorcycles—how to

make high-revving, smooth-running, lightweight engines—when it entered the car business. The task of creating a strategic architecture forces the organization to identify and commit to the technical and production linkages across SBUs that will provide a distinct competitive advantage.

It is consistency of resource allocation and the development of an administrative infrastructure appropriate to it that breathes life into a strategic architecture and creates a managerial culture, teamwork, a capacity to change, and a willingness to share resources, to protect proprietary skills, and to think long term. That is also the reason the specific architecture cannot be copied easily or overnight by competitors. Strategic architecture is a tool for communicating with customers and other external constituents. It reveals the broad direction without giving away every step.

Redeploying to Exploit Competencies

If the company's core competencies are its critical resource and if top management must ensure that competence carriers are not held hostage by some particular business, then it follows that SBUs should bid for core competencies in the same way they bid for capital. We've made this point glancingly. It is important enough to consider more deeply.

Once top management (with the help of divisional and SBU managers) has identified overarching competencies, it must ask businesses to identify the projects and people closely connected with them. Corporate officers should direct an audit of the location, number, and quality of the people who embody competence.

This sends an important signal to middle managers: core competencies are *corporate* resources and may be reallocated by corporate management. An individual business doesn't own anybody. SBUs are entitled to the services of individual employees so long as SBU management can demonstrate that the opportunity it is pursuing yields the highest possible pay-off on the investment in their skills. This message is further underlined if each year in the strategic planning or budgeting process, unit managers must justify their hold on the people who carry the company's core competencies.

Elements of Canon's core competence in optics are spread across businesses as diverse as cameras, copiers, and semiconductor lithographic equipment and are shown in "Core Competencies at Canon." When Canon identified an opportunity in digital laser printers, it gave SBU managers the right to raid other SBUs to pull together the required pool of talent. When Canon's reprographics products division undertook to develop microprocessor-controlled copiers, it turned to the photo products group, which had developed the world's first microprocessor-controlled camera.

Core competencies at Canon

	Precision mechanics	Fine optics	Micro- electronics
Basic camera	■	□	
Compact fashion camera	■	□	
Electronic camera	■	□	
EOS autofocus camera	■	□	■
Video still camera	■	□	■
Laser beam printer	■	□	■
Color video printer	■		■
Bubble jet printer	■		■
Basic fax	■		■
Laser fax	■		■
Calculator			■
Plain paper copier	■	□	■
Battery PPC	■	□	■
Color copier	■	□	■
Laser copier	■	□	■
Color laser copier	■	□	■
NAVI	■	□	■
Still video system	■	□	■
Laser imager	■	□	■
Cell analyzer	■	□	■
Mask aligners	■		■
Stepper aligners	■		■
Excimer laser aligners	■	□	■

Every Canon product is the result of at least one core competency.

Also reward systems that focus only on product-line results and career paths that seldom cross SBU boundaries engender patterns of behavior among unit managers that are destructively competitive. At NEC, divisional managers come together to identify next-generation competencies. Together they decide how much investment needs to be made to build up each future competency and the contribution in capital and staff support that each division will need to make. There is also a sense of equitable exchange. One division may make a disproportionate contribution or may benefit less from the progress made, but such short-term inequalities will balance out over the long term.

Incidentally, the positive contribution of the SBU manager should be made visible across the company. An SBU manager is unlikely to surrender

key people if only the other business (or the general manager of that business who may be a competitor for promotion) is going to benefit from the redeployment. Cooperative SBU managers should be celebrated as team players. Where priorities are clear, transfers are less likely to be seen as idiosyncratic and politically motivated.

Transfers for the sake of building core competence must be recorded and appreciated in the corporate memory. It is reasonable to expect a business that has surrendered core skills on behalf of corporate opportunities in other areas to lose, for a time, some of its competitiveness. If these losses in performance bring immediate censure, SBUs will be unlikely to assent to skills transfers next time.

Finally, there are ways to wean key employees off the idea that they belong in perpetuity to any particular business. Early in their careers, people may be exposed to a variety of businesses through a carefully planned rotation program. At Canon, critical people move regularly between the camera business and the copier business and between the copier business and the professional optical-products business. In mid-career, periodic assignments to cross-divisional project teams may be necessary, both for diffusing core competencies and for loosening the bonds that might tie an individual to one business even when brighter opportunities beckon elsewhere. Those who embody critical core competencies should know that their careers are tracked and guided by corporate human resource professionals. In the early 1980s at Canon, all engineers under 30 were invited to apply for membership on a seven-person committee that was to spend two years plotting Canon's future direction, including its strategic architecture.

Competence carriers should be regularly brought together from across the corporation to trade notes and ideas. The goal is to build a strong feeling of community among these people. To a great extent, their loyalty should be to the integrity of the core competence area they represent and not just to particular businesses. In traveling regularly, talking frequently to customers, and meeting with peers, competence carriers may be encouraged to discover new market opportunities.

Core competencies are the wellspring of new business development. They should constitute the focus for strategy at the corporate level. Managers have to win manufacturing leadership in core products and capture global share through brand-building programs aimed at exploiting economies of scope.

Only if the company is conceived of as a hierarchy of core competencies, core products, and market-focused business units will it be fit to fight.

Nor can top management be just another layer of accounting consolidation, which it often is in a regime of radical decentralization. Top management must add value by enunciating the strategic architecture that guides the competence acquisition process. We believe an obsession with competence building will characterize the global winners of the 1990s. With the decade under way, the time for rethinking the concept of the corporation is already overdue.

Originally published in May 1990. Reprint 90311

Notes

[1.](#) For a fuller discussion, see our article, “Strategic Intent,” HBR, May–June 1989, p. 63.

[2.](#) “Collaborate with Your Competitors and Win,” HBR, January–February 1989, p. 133, with Yves L. Doz.

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First eBook Edition: January 2011

ISBN: 978-1-4221-5799-2

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How Will You Measure Your Life?

by Clayton M. Christensen

BEFORE I PUBLISHED *The Innovator's Dilemma*, I got a call from Andrew Grove, then the chairman of Intel. He had read one of my early papers about disruptive technology, and he asked if I could talk to his direct reports and explain my research and what it implied for Intel. Excited, I flew to Silicon Valley and showed up at the appointed time, only to have Grove say, "Look, stuff has happened. We have only 10 minutes for you. Tell us what your model of disruption means for Intel." I said that I couldn't—that I needed a full 30 minutes to explain the model, because only with it as context would any comments about Intel make sense. Ten minutes into my explanation, Grove interrupted: "Look, I've got your model. Just tell us what it means for Intel."

I insisted that I needed 10 more minutes to describe how the process of disruption had worked its way through a very different industry, steel, so that he and his team could understand how disruption worked. I told the story of how Nucor and other steel minimills had begun by attacking the lowest end of the market—steel reinforcing bars, or rebar—and later moved up toward the high end, undercutting the traditional steel mills.

When I finished the minimill story, Grove said, "OK, I get it. What it means for Intel is ...," and then went on to articulate what would become the company's strategy for going to the bottom of the market to launch the Celeron processor.

I've thought about that a million times since. If I had been suckered into telling Andy Grove what he should think about the microprocessor business,

I'd have been killed. But instead of telling him what to think, I taught him how to think—and then he reached what I felt was the correct decision on his own.

That experience had a profound influence on me. When people ask what I think they should do, I rarely answer their question directly. Instead, I run the question aloud through one of my models. I'll describe how the process in the model worked its way through an industry quite different from their own. And then, more often than not, they'll say, "OK, I get it." And they'll answer their own question more insightfully than I could have.

My class at HBS is structured to help my students understand what good management theory is and how it is built. To that backbone I attach different models or theories that help students think about the various dimensions of a general manager's job in stimulating innovation and growth. In each session we look at one company through the lenses of those theories—using them to explain how the company got into its situation and to examine what managerial actions will yield the needed results.

Idea in Brief

Harvard Business School's Christensen teaches aspiring MBAs how to apply management and innovation theories to build stronger companies. But he also believes that these models can help people lead better lives. In this article, he explains how, exploring questions everyone needs to ask. How can I be happy in my career? How can I be sure that my relationship with my family is an enduring source of happiness? And how can I live my life with integrity? The answer to the first question comes from Frederick Herzberg's assertion that the most powerful motivator isn't money; it's the opportunity to learn, grow in responsibilities, contribute, and be recognized. That's why management, if practiced well, can be the noblest of occupations; no others offer as many ways to help people find those opportunities. It isn't about buying, selling, and investing in companies, as many think. The principles of resource allocation can help people attain happiness at home. If not managed masterfully, what emerges from a firm's resource allocation process can be very different from the strategy management intended to follow. That's true in life too: If you're not guided by a clear sense of purpose, you're likely to fritter away your time and energy on obtaining the most tangible, short-term signs of achievement, not what's really important to you. And just as a focus on marginal costs can cause bad corporate decisions, it can lead people astray. The marginal cost of doing something wrong "just this once" always seems alluringly low. You don't see the end result to which that path leads. The key is to define what you stand for and draw the line in a safe place.

On the last day of class, I ask my students to turn those theoretical lenses on themselves, to find cogent answers to three questions: First, how can I be sure that I'll be happy in my career? Second, how can I be sure that my relationships with my spouse and my family become an enduring source of happiness? Third, how can I be sure I'll stay out of jail? Though the last question sounds lighthearted, it's not. Two of the 32 people in my Rhodes scholar class spent time in jail. Jeff Skilling of Enron fame was a classmate of mine at HBS. These were good guys—but something in their lives sent them

off in the wrong direction.

As the students discuss the answers to these questions, I open my own life to them as a case study of sorts, to illustrate how they can use the theories from our course to guide their life decisions.

One of the theories that gives great insight on the first question—how to be sure we find happiness in our careers—is from Frederick Herzberg, who asserts that the powerful motivator in our lives isn't money; it's the opportunity to learn, grow in responsibilities, contribute to others, and be recognized for achievements. I tell the students about a vision of sorts I had while I was running the company I founded before becoming an academic. In my mind's eye I saw one of my managers leave for work one morning with a relatively strong level of self-esteem. Then I pictured her driving home to her family 10 hours later, feeling unappreciated, frustrated, underutilized, and demeaned. I imagined how profoundly her lowered self-esteem affected the way she interacted with her children. The vision in my mind then fast-forwarded to another day, when she drove home with greater self-esteem—feeling that she had learned a lot, been recognized for achieving valuable things, and played a significant role in the success of some important initiatives. I then imagined how positively that affected her as a spouse and a parent. My conclusion: Management is the most noble of professions if it's practiced well. No other occupation offers as many ways to help others learn and grow, take responsibility and be recognized for achievement, and contribute to the success of a team. More and more MBA students come to school thinking that a career in business means buying, selling, and investing in companies. That's unfortunate. Doing deals doesn't yield the deep rewards that come from building up people.

I want students to leave my classroom knowing that.

Create a Strategy for Your Life

A theory that is helpful in answering the second question—How can I ensure that my relationship with my family proves to be an enduring source of happiness?—concerns how strategy is defined and implemented. Its primary insight is that a company's strategy is determined by the types of initiatives that management invests in. If a company's resource allocation process is not managed masterfully, what emerges from it can be very different from what management intended. Because companies' decision-making systems are designed to steer investments to initiatives that offer the most tangible and immediate returns, companies shortchange investments in initiatives that are crucial to their long-term strategies.

Over the years I've watched the fates of my HBS classmates from 1979 unfold; I've seen more and more of them come to reunions unhappy, divorced, and alienated from their children. I can guarantee you that not a single one of them graduated with the deliberate strategy of getting divorced and raising children who would become estranged from them. And yet a shocking number of them implemented that strategy. The reason? They didn't keep the purpose of their lives front and center as they decided how to spend their time, talents, and energy.

The Class of 2010

“I CAME TO BUSINESS SCHOOL knowing exactly what I wanted to do—and I’m leaving choosing the exact opposite. I’ve worked in the private sector all my life, because everyone always told me that’s where smart people are. But I’ve decided to try government and see if I can find more meaning there.

“I used to think that industry was very safe. The recession has shown us that nothing is safe.”

Ruhana Hafiz, Harvard Business School, Class of 2010

Her Plans: To join the FBI as a special adviser (a management track position)

“You could see a shift happening at HBS. Money used to be number one in the job search. When you make a ton of money, you want more of it. Ironical thing. You start to forget what the drivers of happiness are and what things are really important. A lot of people on campus see money differently now. They think, ‘What’s the minimum I need to have, and what else drives my life?’ instead of ‘What’s the place where I can get the maximum of both?’”

Patrick Chun, Harvard Business School, Class of 2010

His Plans: To join Bain Capital

“The financial crisis helped me realize that you have to do what you really love in life. My current vision of success is based on the impact I can have, the experiences I can gain, and the happiness I can find personally, much more so than the pursuit of money or prestige. My main motivations are (1) to be with my family and people I care about; (2) to do something fun, exciting, and impactful; and (3) to pursue a long-term career in entrepreneurship, where I can build companies that change the way the world works.”

Matt Salzberg, Harvard Business School, Class of 2010

His Plans: To work for Bessemer Venture Partners

“Because I’m returning to McKinsey, it probably seems like not all that much has changed for me. But while I was at HBS, I decided to do the dual degree at the Kennedy School. With the elections in 2008 and the economy looking shaky, it seemed more compelling for me to get a

better understanding of the public and nonprofit sectors. In a way, that drove my return to McKinsey, where I'll have the ability to explore private, public, and nonprofit sectors.

"The recession has made us step back and take stock of how lucky we are. The crisis to us is 'Are we going to have a job by April?' Crisis to a lot of people is 'Are we going to stay in our home?'"

John Coleman, Harvard Business School, Class of 2010

His Plans: To return to McKinsey & Company

It's quite startling that a significant fraction of the 900 students that HBS draws each year from the world's best have given little thought to the purpose of their lives. I tell the students that HBS might be one of their last chances to reflect deeply on that question. If they think that they'll have more time and energy to reflect later, they're nuts, because life only gets more demanding: You take on a mortgage; you're working 70 hours a week; you have a spouse and children.

For me, having a clear purpose in my life has been essential. But it was something I had to think long and hard about before I understood it. When I was a Rhodes scholar, I was in a very demanding academic program, trying to cram an extra year's worth of work into my time at Oxford. I decided to spend an hour every night reading, thinking, and praying about why God put me on this earth. That was a very challenging commitment to keep, because every hour I spent doing that, I wasn't studying applied econometrics. I was conflicted about whether I could really afford to take that time away from my studies, but I stuck with it—and ultimately figured out the purpose of my life.

Had I instead spent that hour each day learning the latest techniques for mastering the problems of autocorrelation in regression analysis, I would have badly misspent my life. I apply the tools of econometrics a few times a year, but I apply my knowledge of the purpose of my life every day. It's the single most useful thing I've ever learned. I promise my students that if they take the time to figure out their life purpose, they'll look back on it as the most important thing they discovered at HBS. If they don't figure it out, they will just sail off without a rudder and get buffeted in the very rough seas of life. Clarity about their purpose will trump knowledge of activity-based costing, balanced scorecards, core competence, disruptive innovation, the four Ps, and the five forces.

My purpose grew out of my religious faith, but faith isn't the only thing

that gives people direction. For example, one of my former students decided that his purpose was to bring honesty and economic prosperity to his country and to raise children who were as capably committed to this cause, and to each other, as he was. His purpose is focused on family and others—as mine is.

The choice and successful pursuit of a profession is but one tool for achieving your purpose. But without a purpose, life can become hollow.

Allocate Your Resources

Your decisions about allocating your personal time, energy, and talent ultimately shape your life's strategy.

I have a bunch of “businesses” that compete for these resources: I’m trying to have a rewarding relationship with my wife, raise great kids, contribute to my community, succeed in my career, contribute to my church, and so on. And I have exactly the same problem that a corporation does. I have a limited amount of time and energy and talent. How much do I devote to each of these pursuits?

Allocation choices can make your life turn out to be very different from what you intended. Sometimes that’s good: Opportunities that you never planned for emerge. But if you misinvest your resources, the outcome can be bad. As I think about my former classmates who inadvertently invested for lives of hollow unhappiness, I can’t help believing that their troubles relate right back to a short-term perspective.

When people who have a high need for achievement—and that includes all Harvard Business School graduates—have an extra half hour of time or an extra ounce of energy, they’ll unconsciously allocate it to activities that yield the most tangible accomplishments. And our careers provide the most concrete evidence that we’re moving forward. You ship a product, finish a design, complete a presentation, close a sale, teach a class, publish a paper, get paid, get promoted. In contrast, investing time and energy in your relationship with your spouse and children typically doesn’t offer that same immediate sense of achievement. Kids misbehave every day. It’s really not until 20 years down the road that you can put your hands on your hips and say, “I raised a good son or a good daughter.” You can neglect your relationship with your spouse, and on a day-to-day basis, it doesn’t seem as if things are deteriorating. People who are driven to excel have this unconscious propensity to underinvest in their families and overinvest in their careers—even though intimate and loving relationships with their families are the most powerful and enduring source of happiness.

If you study the root causes of business disasters, over and over you'll find this predisposition toward endeavors that offer immediate gratification. If you look at personal lives through that lens, you'll see the same stunning and sobering pattern: people allocating fewer and fewer resources to the things they would have once said mattered most.

Create a Culture

There's an important model in our class called the Tools of Cooperation, which basically says that being a visionary manager isn't all it's cracked up to be. It's one thing to see into the foggy future with acuity and chart the course corrections that the company must make. But it's quite another to persuade employees who might not see the changes ahead to line up and work cooperatively to take the company in that new direction. Knowing what tools to wield to elicit the needed cooperation is a critical managerial skill.

The theory arrays these tools along two dimensions—the extent to which members of the organization agree on what they want from their participation in the enterprise, and the extent to which they agree on what actions will produce the desired results. When there is little agreement on both axes, you have to use “power tools”—coercion, threats, punishment, and so on—to secure cooperation. Many companies start in this quadrant, which is why the founding executive team must play such an assertive role in defining what must be done and how. If employees' ways of working together to address those tasks succeed over and over, consensus begins to form. MIT's Edgar Schein has described this process as the mechanism by which a culture is built. Ultimately, people don't even think about whether their way of doing things yields success. They embrace priorities and follow procedures by instinct and assumption rather than by explicit decision—which means that they've created a culture. Culture, in compelling but unspoken ways, dictates the proven, acceptable methods by which members of the group address recurrent problems. And culture defines the priority given to different types of problems. It can be a powerful management tool.

In using this model to address the question, How can I be sure that my family becomes an enduring source of happiness?, my students quickly see that the simplest tools that parents can wield to elicit cooperation from children are power tools. But there comes a point during the teen years when power tools no longer work. At that point parents start wishing that they had begun working with their children at a very young age to build a culture at

home in which children instinctively behave respectfully toward one another, obey their parents, and choose the right thing to do. Families have cultures, just as companies do. Those cultures can be built consciously or evolve inadvertently.

If you want your kids to have strong self-esteem and confidence that they can solve hard problems, those qualities won't magically materialize in high school. You have to design them into your family's culture—and you have to think about this very early on. Like employees, children build self-esteem by doing things that are hard and learning what works.

Avoid the “Marginal Costs” Mistake

We’re taught in finance and economics that in evaluating alternative investments, we should ignore sunk and fixed costs, and instead base decisions on the marginal costs and marginal revenues that each alternative entails. We learn in our course that this doctrine biases companies to leverage what they have put in place to succeed in the past, instead of guiding them to create the capabilities they’ll need in the future. If we knew the future would be exactly the same as the past, that approach would be fine. But if the future’s different—and it almost always is—then it’s the wrong thing to do.

This theory addresses the third question I discuss with my students—how to live a life of integrity (stay out of jail). Unconsciously, we often employ the marginal cost doctrine in our personal lives when we choose between right and wrong. A voice in our head says, “Look, I know that as a general rule, most people shouldn’t do this. But in this particular extenuating circumstance, just this once, it’s OK.” The marginal cost of doing something wrong “just this once” always seems alluringly low. It suckers you in, and you don’t ever look at where that path ultimately is headed and at the full costs that the choice entails. Justification for infidelity and dishonesty in all their manifestations lies in the marginal cost economics of “just this once.”

I’d like to share a story about how I came to understand the potential damage of “just this once” in my own life. I played on the Oxford University varsity basketball team. We worked our tails off and finished the season undefeated. The guys on the team were the best friends I’ve ever had in my life. We got to the British equivalent of the NCAA tournament—and made it to the final four. It turned out the championship game was scheduled to be played on a Sunday. I had made a personal commitment to God at age 16 that I would never play ball on Sunday. So I went to the coach and explained my problem. He was incredulous. My teammates were, too, because I was the starting center. Every one of the guys on the team came to me and said, “You’ve got to play. Can’t you break the rule just this one time?”

I’m a deeply religious man, so I went away and prayed about what I

should do. I got a very clear feeling that I shouldn't break my commitment—so I didn't play in the championship game.

In many ways that was a small decision—involving one of several thousand Sundays in my life. In theory, surely I could have crossed over the line just that one time and then not done it again. But looking back on it, resisting the temptation whose logic was “In this extenuating circumstance, just this once, it's OK” has proven to be one of the most important decisions of my life. Why? My life has been one unending stream of extenuating circumstances. Had I crossed the line that one time, I would have done it over and over in the years that followed.

The lesson I learned from this is that it's easier to hold to your principles 100% of the time than it is to hold to them 98% of the time. If you give in to “just this once,” based on a marginal cost analysis, as some of my former classmates have done, you'll regret where you end up. You've got to define for yourself what you stand for and draw the line in a safe place.

Remember the Importance of Humility

I got this insight when I was asked to teach a class on humility at Harvard College. I asked all the students to describe the most humble person they knew. One characteristic of these humble people stood out: They had a high level of self-esteem. They knew who they were, and they felt good about who they were. We also decided that humility was defined not by self-deprecating behavior or attitudes but by the esteem with which you regard others. Good behavior flows naturally from that kind of humility. For example, you would never steal from someone, because you respect that person too much. You'd never lie to someone, either.

It's crucial to take a sense of humility into the world. By the time you make it to a top graduate school, almost all your learning has come from people who are smarter and more experienced than you: parents, teachers, bosses. But once you've finished at Harvard Business School or any other top academic institution, the vast majority of people you'll interact with on a day-to-day basis may not be smarter than you. And if your attitude is that only smarter people have something to teach you, your learning opportunities will be very limited. But if you have a humble eagerness to learn something from everybody, your learning opportunities will be unlimited. Generally, you can be humble only if you feel really good about yourself—and you want to help those around you feel really good about themselves, too. When we see people acting in an abusive, arrogant, or demeaning manner toward others, their behavior almost always is a symptom of their lack of self-esteem. They need to put someone else down to feel good about themselves.

Choose the Right Yardstick

This past year I was diagnosed with cancer and faced the possibility that my life would end sooner than I'd planned. Thankfully, it now looks as if I'll be spared. But the experience has given me important insight into my life.

I have a pretty clear idea of how my ideas have generated enormous revenue for companies that have used my research; I know I've had a substantial impact. But as I've confronted this disease, it's been interesting to see how unimportant that impact is to me now. I've concluded that the metric by which God will assess my life isn't dollars but the individual people whose lives I've touched.

I think that's the way it will work for us all. Don't worry about the level of individual prominence you have achieved; worry about the individuals you have helped become better people. This is my final recommendation: Think about the metric by which your life will be judged, and make a resolution to live every day so that in the end, your life will be judged a success.

Originally published in July 2010. Reprint **R1007B**

Managing Oneself

by Peter F. Drucker

HISTORY'S GREAT ACHIEVERS—a Napoléon, a da Vinci, a Mozart—have always managed themselves. That, in large measure, is what makes them great achievers. But they are rare exceptions, so unusual both in their talents and their accomplishments as to be considered outside the boundaries of ordinary human existence. Now, most of us, even those of us with modest endowments, will have to learn to manage ourselves. We will have to learn to develop ourselves. We will have to place ourselves where we can make the greatest contribution. And we will have to stay mentally alert and engaged during a 50-year working life, which means knowing how and when to change the work we do.

What Are My Strengths?

Most people think they know what they are good at. They are usually wrong. More often, people know what they are not good at—and even then more people are wrong than right. And yet, a person can perform only from strength. One cannot build performance on weaknesses, let alone on something one cannot do at all.

Throughout history, people had little need to know their strengths. A person was born into a position and a line of work: The peasant's son would also be a peasant; the artisan's daughter, an artisan's wife; and so on. But now people have choices. We need to know our strengths in order to know where we belong.

The only way to discover your strengths is through feedback analysis. Whenever you make a key decision or take a key action, write down what you expect will happen. Nine or 12 months later, compare the actual results with your expectations. I have been practicing this method for 15 to 20 years now, and every time I do it, I am surprised. The feedback analysis showed me, for instance—and to my great surprise—that I have an intuitive understanding of technical people, whether they are engineers or accountants or market researchers. It also showed me that I don't really resonate with generalists.

Feedback analysis is by no means new. It was invented sometime in the fourteenth century by an otherwise totally obscure German theologian and picked up quite independently, some 150 years later, by John Calvin and Ignatius of Loyola, each of whom incorporated it into the practice of his followers. In fact, the steadfast focus on performance and results that this habit produces explains why the institutions these two men founded, the Calvinist church and the Jesuit order, came to dominate Europe within 30 years.

Practiced consistently, this simple method will show you within a fairly short period of time, maybe two or three years, where your strengths lie—and this is the most important thing to know. The method will show you what you

are doing or failing to do that deprives you of the full benefits of your strengths. It will show you where you are not particularly competent. And finally, it will show you where you have no strengths and cannot perform.

Several implications for action follow from feedback analysis. First and foremost, concentrate on your strengths. Put yourself where your strengths can produce results.

Second, work on improving your strengths. Analysis will rapidly show where you need to improve skills or acquire new ones. It will also show the gaps in your knowledge—and those can usually be filled. Mathematicians are born, but everyone can learn trigonometry.

Third, discover where your intellectual arrogance is causing disabling ignorance and overcome it. Far too many people—especially people with great expertise in one area—are contemptuous of knowledge in other areas or believe that being bright is a substitute for knowledge. First-rate engineers, for instance, tend to take pride in not knowing anything about people. Human beings, they believe, are much too disorderly for the good engineering mind. Human resources professionals, by contrast, often pride themselves on their ignorance of elementary accounting or of quantitative methods altogether. But taking pride in such ignorance is self-defeating. Go to work on acquiring the skills and knowledge you need to fully realize your strengths.

Idea in Brief

We live in an age of unprecedented opportunity: If you've got ambition, drive, and smarts, you can rise to the top of your chosen profession—regardless of where you started out. But with opportunity comes responsibility. Companies today aren't managing their knowledge workers' careers. Rather, we must each be our own chief executive officer.

Simply put, it's up to you to carve out your place in the work world and know when to change course. And it's up to you to keep yourself engaged and productive during a work life that may span some 50 years.

To do all of these things well, you'll need to cultivate a deep understanding of yourself. What are your most valuable strengths and most dangerous weaknesses? Equally important, how do you learn and work with others? What are your most deeply held values? And in what type of work environment can you make the greatest contribution?

The implication is clear: Only when you operate from a combination of your strengths and self-knowledge can you achieve true—and lasting—excellence.

It is equally essential to remedy your bad habits—the things you do or fail to do that inhibit your effectiveness and performance. Such habits will quickly show up in the feedback. For example, a planner may find that his beautiful plans fail because he does not follow through on them. Like so many brilliant people, he believes that ideas move mountains. But bulldozers move mountains; ideas show where the bulldozers should go to work. This planner will have to learn that the work does not stop when the plan is completed. He must find people to carry out the plan and explain it to them. He must adapt and change it as he puts it into action. And finally, he must decide when to stop pushing the plan.

Idea in Practice

To build a life of excellence, begin by asking yourself these questions:

“What are my strengths?”

To accurately identify your strengths, use **feedback analysis**. Every time you make a key decision, write down the outcome you expect. Several months later, compare the actual results with your expected results. Look for patterns in what you’re seeing: What results are you skilled at generating? What abilities do you need to enhance in order to get the results you want? What unproductive habits are preventing you from creating the outcomes you desire? In identifying opportunities for improvement, don’t waste time cultivating skill areas where you have little competence. Instead, concentrate on—and build on—your strengths.

“How do I work?”

In what ways do you work best? Do you process information most effectively by reading it, or by hearing others discuss it? Do you accomplish the most by working with other people, or by working alone? Do you perform best while making decisions, or while advising others on key matters? Are you in top form when things get stressful, or do you function optimally in a highly predictable environment?

“What are my values?”

What are your ethics? What do you see as your most important responsibilities for living a worthy, ethical life? Do your organization’s ethics resonate with your own values? If not, your career will likely be marked by frustration and poor performance.

“Where do I belong?”

Consider your strengths, preferred work style, and values. Based on these qualities, in what kind of work environment would you fit in best? Find the perfect fit, and you'll transform yourself from a merely acceptable employee into a star performer.

“What can I contribute?”

In earlier eras, companies told businesspeople what their contribution should be. Today, you have choices. To decide how you can best enhance your organization's performance, first ask what the situation requires. Based on your strengths, work style, and values, how might you make the greatest contribution to your organization's efforts?

At the same time, feedback will also reveal when the problem is a lack of manners. Manners are the lubricating oil of an organization. It is a law of nature that two moving bodies in contact with each other create friction. This is as true for human beings as it is for inanimate objects. Manners—simple things like saying “please” and “thank you” and knowing a person's name or asking after her family—enable two people to work together whether they like each other or not. Bright people, especially bright young people, often do not understand this. If analysis shows that someone's brilliant work fails again and again as soon as cooperation from others is required, it probably indicates a lack of courtesy—that is, a lack of manners.

Comparing your expectations with your results also indicates what not to do. We all have a vast number of areas in which we have no talent or skill and little chance of becoming even mediocre. In those areas a person—and especially a knowledge worker—should not take on work, jobs, and assignments. One should waste as little effort as possible on improving areas of low competence. It takes far more energy and work to improve from incompetence to mediocrity than it takes to improve from first-rate performance to excellence. And yet most people—especially most teachers and most organizations—concentrate on making incompetent performers into mediocre ones. Energy, resources, and time should go instead to making a competent person into a star performer.

How Do I Perform?

Amazingly few people know how they get things done. Indeed, most of us do not even know that different people work and perform differently. Too many people work in ways that are not their ways, and that almost guarantees nonperformance. For knowledge workers, How do I perform? may be an even more important question than What are my strengths?

Like one's strengths, how one performs is unique. It is a matter of personality. Whether personality be a matter of nature or nurture, it surely is formed long before a person goes to work. And *how* a person performs is a given, just as *what* a person is good at or not good at is a given. A person's way of performing can be slightly modified, but it is unlikely to be completely changed—and certainly not easily. Just as people achieve results by doing what they are good at, they also achieve results by working in ways that they best perform. A few common personality traits usually determine how a person performs.

Am I a reader or a listener?

The first thing to know is whether you are a reader or a listener. Far too few people even know that there are readers and listeners and that people are rarely both. Even fewer know which of the two they themselves are. But some examples will show how damaging such ignorance can be.

When Dwight Eisenhower was Supreme Commander of the Allied forces in Europe, he was the darling of the press. His press conferences were famous for their style—General Eisenhower showed total command of whatever question he was asked, and he was able to describe a situation and explain a policy in two or three beautifully polished and elegant sentences. Ten years later, the same journalists who had been his admirers held President Eisenhower in open contempt. He never addressed the questions, they complained, but rambled on endlessly about something else. And they constantly ridiculed him for butchering the King's English in incoherent and ungrammatical answers.

Eisenhower apparently did not know that he was a reader, not a listener. When he was Supreme Commander in Europe, his aides made sure that every question from the press was presented in writing at least half an hour before a conference was to begin. And then Eisenhower was in total command. When he became president, he succeeded two listeners, Franklin D. Roosevelt and Harry Truman. Both men knew themselves to be listeners and both enjoyed free-for-all press conferences. Eisenhower may have felt that he had to do what his two predecessors had done. As a result, he never even heard the questions journalists asked. And Eisenhower is not even an extreme case of a nonlistener.

A few years later, Lyndon Johnson destroyed his presidency, in large measure, by not knowing that he was a listener. His predecessor, John Kennedy, was a reader who had assembled a brilliant group of writers as his assistants, making sure that they wrote to him before discussing their memos in person. Johnson kept these people on his staff—and they kept on writing. He never, apparently, understood one word of what they wrote. Yet as a senator, Johnson had been superb; for parliamentarians have to be, above all,

listeners.

Few listeners can be made, or can make themselves, into competent readers—and vice versa. The listener who tries to be a reader will, therefore, suffer the fate of Lyndon Johnson, whereas the reader who tries to be a listener will suffer the fate of Dwight Eisenhower. They will not perform or achieve.

How do I learn?

The second thing to know about how one performs is to know how one learns. Many first-class writers—Winston Churchill is but one example—do poorly in school. They tend to remember their schooling as pure torture. Yet few of their classmates remember it the same way. They may not have enjoyed the school very much, but the worst they suffered was boredom. The explanation is that writers do not, as a rule, learn by listening and reading. They learn by writing. Because schools do not allow them to learn this way, they get poor grades.

Schools everywhere are organized on the assumption that there is only one right way to learn and that it is the same way for everybody. But to be forced to learn the way a school teaches is sheer hell for students who learn differently. Indeed, there are probably half a dozen different ways to learn.

There are people, like Churchill, who learn by writing. Some people learn by taking copious notes. Beethoven, for example, left behind an enormous number of sketchbooks, yet he said he never actually looked at them when he composed. Asked why he kept them, he is reported to have replied, “If I don’t write it down immediately, I forget it right away. If I put it into a sketchbook, I never forget it and I never have to look it up again.” Some people learn by doing. Others learn by hearing themselves talk.

A chief executive I know who converted a small and mediocre family business into the leading company in its industry was one of those people who learn by talking. He was in the habit of calling his entire senior staff into his office once a week and then talking at them for two or three hours. He would raise policy issues and argue three different positions on each one. He rarely asked his associates for comments or questions; he simply needed an audience to hear himself talk. That’s how he learned. And although he is a fairly extreme case, learning through talking is by no means an unusual method. Successful trial lawyers learn the same way, as do many medical diagnosticians (and so do I).

Of all the important pieces of self-knowledge, understanding how you learn is the easiest to acquire. When I ask people, “How do you learn?” most

of them know the answer. But when I ask, “Do you act on this knowledge?” few answer yes. And yet, acting on this knowledge is the key to performance; or rather, *not* acting on this knowledge condemns one to nonperformance.

Am I a reader or a listener? and How do I learn? are the first questions to ask. But they are by no means the only ones. To manage yourself effectively, you also have to ask, Do I work well with people, or am I a loner? And if you do work well with people, you then must ask, In what relationship?

Some people work best as subordinates. General George Patton, the great American military hero of World War II, is a prime example. Patton was America’s top troop commander. Yet when he was proposed for an independent command, General George Marshall, the U.S. chief of staff—and probably the most successful picker of men in U.S. history—said, “Patton is the best subordinate the American army has ever produced, but he would be the worst commander.”

Some people work best as team members. Others work best alone. Some are exceptionally talented as coaches and mentors; others are simply incompetent as mentors.

Another crucial question is, Do I produce results as a decision maker or as an adviser? A great many people perform best as advisers but cannot take the burden and pressure of making the decision. A good many other people, by contrast, need an adviser to force themselves to think; then they can make decisions and act on them with speed, self-confidence, and courage.

This is a reason, by the way, that the number two person in an organization often fails when promoted to the number one position. The top spot requires a decision maker. Strong decision makers often put somebody they trust into the number two spot as their adviser—and in that position the person is outstanding. But in the number one spot, the same person fails. He or she knows what the decision should be but cannot accept the responsibility of actually making it.

Other important questions to ask include, Do I perform well under stress, or do I need a highly structured and predictable environment? Do I work best in a big organization or a small one? Few people work well in all kinds of environments. Again and again, I have seen people who were very successful in large organizations flounder miserably when they moved into smaller ones. And the reverse is equally true.

The conclusion bears repeating: Do not try to change yourself—you are unlikely to succeed. But work hard to improve the way you perform. And try

not to take on work you cannot perform or will only perform poorly.

What Are My Values?

To be able to manage yourself, you finally have to ask, What are my values? This is not a question of ethics. With respect to ethics, the rules are the same for everybody, and the test is a simple one. I call it the “mirror test.”

In the early years of this century, the most highly respected diplomat of all the great powers was the German ambassador in London. He was clearly destined for great things—to become his country’s foreign minister, at least, if not its federal chancellor. Yet in 1906 he abruptly resigned rather than preside over a dinner given by the diplomatic corps for Edward VII. The king was a notorious womanizer and made it clear what kind of dinner he wanted. The ambassador is reported to have said, “I refuse to see a pimp in the mirror in the morning when I shave.”

That is the mirror test. Ethics requires that you ask yourself, What kind of person do I want to see in the mirror in the morning? What is ethical behavior in one kind of organization or situation is ethical behavior in another. But ethics is only part of a value system—especially of an organization’s value system.

To work in an organization whose value system is unacceptable or incompatible with one’s own condemns a person both to frustration and to nonperformance.

Consider the experience of a highly successful human resources executive whose company was acquired by a bigger organization. After the acquisition, she was promoted to do the kind of work she did best, which included selecting people for important positions. The executive deeply believed that a company should hire people for such positions from the outside only after exhausting all the inside possibilities. But her new company believed in first looking outside “to bring in fresh blood.” There is something to be said for both approaches—in my experience, the proper one is to do some of both. They are, however, fundamentally incompatible—not as policies but as values. They bespeak different views of the relationship between organizations and people; different views of the responsibility of an

organization to its people and their development; and different views of a person's most important contribution to an enterprise. After several years of frustration, the executive quit—at considerable financial loss. Her values and the values of the organization simply were not compatible.

Similarly, whether a pharmaceutical company tries to obtain results by making constant, small improvements or by achieving occasional, highly expensive, and risky “breakthroughs” is not primarily an economic question. The results of either strategy may be pretty much the same. At bottom, there is a conflict between a value system that sees the company's contribution in terms of helping physicians do better what they already do and a value system that is oriented toward making scientific discoveries.

Whether a business should be run for short-term results or with a focus on the long term is likewise a question of values. Financial analysts believe that businesses can be run for both simultaneously. Successful businesspeople know better. To be sure, every company has to produce short-term results. But in any conflict between short-term results and long-term growth, each company will determine its own priority. This is not primarily a disagreement about economics. It is fundamentally a value conflict regarding the function of a business and the responsibility of management.

Value conflicts are not limited to business organizations. One of the fastest-growing pastoral churches in the United States measures success by the number of new parishioners. Its leadership believes that what matters is how many newcomers join the congregation. The Good Lord will then minister to their spiritual needs or at least to the needs of a sufficient percentage. Another pastoral, evangelical church believes that what matters is people's spiritual growth. The church eases out newcomers who join but do not enter into its spiritual life.

Again, this is not a matter of numbers. At first glance, it appears that the second church grows more slowly. But it retains a far larger proportion of newcomers than the first one does. Its growth, in other words, is more solid. This is also not a theological problem, or only secondarily so. It is a problem about values. In a public debate, one pastor argued, “Unless you first come to church, you will never find the gate to the Kingdom of Heaven.”

“No,” answered the other. “Until you first look for the gate to the Kingdom of Heaven, you don't belong in church.”

Organizations, like people, have values. To be effective in an organization, a person's values must be compatible with the organization's

values. They do not need to be the same, but they must be close enough to coexist. Otherwise, the person will not only be frustrated but also will not produce results.

A person's strengths and the way that person performs rarely conflict; the two are complementary. But there is sometimes a conflict between a person's values and his or her strengths. What one does well—even very well and successfully—may not fit with one's value system. In that case, the work may not appear to be worth devoting one's life to (or even a substantial portion thereof).

If I may, allow me to interject a personal note. Many years ago, I too had to decide between my values and what I was doing successfully. I was doing very well as a young investment banker in London in the mid-1930s, and the work clearly fit my strengths. Yet I did not see myself making a contribution as an asset manager. People, I realized, were what I valued, and I saw no point in being the richest man in the cemetery. I had no money and no other job prospects. Despite the continuing Depression, I quit—and it was the right thing to do. Values, in other words, are and should be the ultimate test.

Where Do I Belong?

A small number of people know very early where they belong. Mathematicians, musicians, and cooks, for instance, are usually mathematicians, musicians, and cooks by the time they are four or five years old. Physicians usually decide on their careers in their teens, if not earlier. But most people, especially highly gifted people, do not really know where they belong until they are well past their mid-twenties. By that time, however, they should know the answers to the three questions: What are my strengths? How do I perform? and, What are my values? And then they can and should decide where they belong.

Or rather, they should be able to decide where they do *not* belong. The person who has learned that he or she does not perform well in a big organization should have learned to say no to a position in one. The person who has learned that he or she is not a decision maker should have learned to say no to a decision-making assignment. A General Patton (who probably never learned this himself) should have learned to say no to an independent command.

Equally important, knowing the answer to these questions enables a person to say to an opportunity, an offer, or an assignment, “Yes, I will do that. But this is the way I should be doing it. This is the way it should be structured. This is the way the relationships should be. These are the kind of results you should expect from me, and in this time frame, because this is who I am.”

Successful careers are not planned. They develop when people are prepared for opportunities because they know their strengths, their method of work, and their values. Knowing where one belongs can transform an ordinary person—hardworking and competent but otherwise mediocre—into an outstanding performer.

What Should I Contribute?

Throughout history, the great majority of people never had to ask the question, What should I contribute? They were told what to contribute, and their tasks were dictated either by the work itself—as it was for the peasant or artisan—or by a master or a mistress—as it was for domestic servants. And until very recently, it was taken for granted that most people were subordinates who did as they were told. Even in the 1950s and 1960s, the new knowledge workers (the so-called organization men) looked to their company's personnel department to plan their careers.

Then in the late 1960s, no one wanted to be told what to do any longer. Young men and women began to ask, What do *I* want to do? And what they heard was that the way to contribute was to “do your own thing.” But this solution was as wrong as the organization men's had been. Very few of the people who believed that doing one's own thing would lead to contribution, self-fulfillment, and success achieved any of the three.

But still, there is no return to the old answer of doing what you are told or assigned to do. Knowledge workers in particular have to learn to ask a question that has not been asked before: What *should* my contribution be? To answer it, they must address three distinct elements: What does the situation require? Given my strengths, my way of performing, and my values, how can I make the greatest contribution to what needs to be done? And finally, What results have to be achieved to make a difference?

Consider the experience of a newly appointed hospital administrator. The hospital was big and prestigious, but it had been coasting on its reputation for 30 years. The new administrator decided that his contribution should be to establish a standard of excellence in one important area within two years. He chose to focus on the emergency room, which was big, visible, and sloppy. He decided that every patient who came into the ER had to be seen by a qualified nurse within 60 seconds. Within 12 months, the hospital's emergency room had become a model for all hospitals in the United States, and within another two years, the whole hospital had been transformed.

As this example suggests, it is rarely possible—or even particularly fruitful—to look too far ahead. A plan can usually cover no more than 18 months and still be reasonably clear and specific. So the question in most cases should be, Where and how can I achieve results that will make a difference within the next year and a half? The answer must balance several things. First, the results should be hard to achieve—they should require “stretching,” to use the current buzzword. But also, they should be within reach. To aim at results that cannot be achieved—or that can be only under the most unlikely circumstances—is not being ambitious; it is being foolish. Second, the results should be meaningful. They should make a difference. Finally, results should be visible and, if at all possible, measurable. From this will come a course of action: what to do, where and how to start, and what goals and deadlines to set.

Responsibility for Relationships

Very few people work by themselves and achieve results by themselves—a few great artists, a few great scientists, a few great athletes. Most people work with others and are effective with other people. That is true whether they are members of an organization or independently employed. Managing yourself requires taking responsibility for relationships. This has two parts.

The first is to accept the fact that other people are as much individuals as you yourself are. They perversely insist on behaving like human beings. This means that they too have their strengths; they too have their ways of getting things done; they too have their values. To be effective, therefore, you have to know the strengths, the performance modes, and the values of your coworkers.

That sounds obvious, but few people pay attention to it. Typical is the person who was trained to write reports in his or her first assignment because that boss was a reader. Even if the next boss is a listener, the person goes on writing reports that, invariably, produce no results. Invariably the boss will think the employee is stupid, incompetent, and lazy, and he or she will fail. But that could have been avoided if the employee had only looked at the new boss and analyzed how *this* boss performs.

Bosses are neither a title on the organization chart nor a “function.” They are individuals and are entitled to do their work in the way they do it best. It is incumbent on the people who work with them to observe them, to find out how they work, and to adapt themselves to what makes their bosses most effective. This, in fact, is the secret of “managing” the boss.

The same holds true for all your coworkers. Each works his or her way, not your way. And each is entitled to work in his or her way. What matters is whether they perform and what their values are. As for how they perform—each is likely to do it differently. The first secret of effectiveness is to understand the people you work with and depend on so that you can make use of their strengths, their ways of working, and their values. Working relationships are as much based on the people as they are on the work.

The second part of relationship responsibility is taking responsibility for communication. Whenever I, or any other consultant, start to work with an organization, the first thing I hear about are all the personality conflicts. Most of these arise from the fact that people do not know what other people are doing and how they do their work, or what contribution the other people are concentrating on and what results they expect. And the reason they do not know is that they have not asked and therefore have not been told.

This failure to ask reflects human stupidity less than it reflects human history. Until recently, it was unnecessary to tell any of these things to anybody. In the medieval city, everyone in a district plied the same trade. In the countryside, everyone in a valley planted the same crop as soon as the frost was out of the ground. Even those few people who did things that were not “common” worked alone, so they did not have to tell anyone what they were doing.

Today the great majority of people work with others who have different tasks and responsibilities. The marketing vice president may have come out of sales and know everything about sales, but she knows nothing about the things she has never done—pricing, advertising, packaging, and the like. So the people who do these things must make sure that the marketing vice president understands what they are trying to do, why they are trying to do it, how they are going to do it, and what results to expect.

If the marketing vice president does not understand what these high-grade knowledge specialists are doing, it is primarily their fault, not hers. They have not educated her. Conversely, it is the marketing vice president’s responsibility to make sure that all of her coworkers understand how she looks at marketing: what her goals are, how she works, and what she expects of herself and of each one of them.

Even people who understand the importance of taking responsibility for relationships often do not communicate sufficiently with their associates. They are afraid of being thought presumptuous or inquisitive or stupid. They are wrong. Whenever someone goes to his or her associates and says, “This is what I am good at. This is how I work. These are my values. This is the contribution I plan to concentrate on and the results I should be expected to deliver,” the response is always, “This is most helpful. But why didn’t you tell me earlier?”

And one gets the same reaction—without exception, in my experience—if one continues by asking, “And what do I need to know about your strengths,

how you perform, your values, and your proposed contribution?” In fact, knowledge workers should request this of everyone with whom they work, whether as subordinate, superior, colleague, or team member. And again, whenever this is done, the reaction is always, “Thanks for asking me. But why didn’t you ask me earlier?”

Organizations are no longer built on force but on trust. The existence of trust between people does not necessarily mean that they like one another. It means that they understand one another. Taking responsibility for relationships is therefore an absolute necessity. It is a duty. Whether one is a member of the organization, a consultant to it, a supplier, or a distributor, one owes that responsibility to all one’s coworkers: those whose work one depends on as well as those who depend on one’s own work.

The Second Half of Your Life

When work for most people meant manual labor, there was no need to worry about the second half of your life. You simply kept on doing what you had always done. And if you were lucky enough to survive 40 years of hard work in the mill or on the railroad, you were quite happy to spend the rest of your life doing nothing. Today, however, most work is knowledge work, and knowledge workers are not “finished” after 40 years on the job, they are merely bored.

We hear a great deal of talk about the midlife crisis of the executive. It is mostly boredom. At 45, most executives have reached the peak of their business careers, and they know it. After 20 years of doing very much the same kind of work, they are very good at their jobs. But they are not learning or contributing or deriving challenge and satisfaction from the job. And yet they are still likely to face another 20 if not 25 years of work. That is why managing oneself increasingly leads one to begin a second career.

There are three ways to develop a second career. The first is actually to start one. Often this takes nothing more than moving from one kind of organization to another: the divisional controller in a large corporation, for instance, becomes the controller of a medium-sized hospital. But there are also growing numbers of people who move into different lines of work altogether: the business executive or government official who enters the ministry at 45, for instance; or the midlevel manager who leaves corporate life after 20 years to attend law school and become a small-town attorney.

We will see many more second careers undertaken by people who have achieved modest success in their first jobs. Such people have substantial skills, and they know how to work. They need a community—the house is empty with the children gone—and they need income as well. But above all, they need challenge.

The second way to prepare for the second half of your life is to develop a parallel career. Many people who are very successful in their first careers stay in the work they have been doing, either on a full-time or part-time or

consulting basis. But in addition, they create a parallel job, usually in a nonprofit organization, that takes another ten hours of work a week. They might take over the administration of their church, for instance, or the presidency of the local Girl Scouts council. They might run the battered women's shelter, work as a children's librarian for the local public library, sit on the school board, and so on.

Finally, there are the social entrepreneurs. These are usually people who have been very successful in their first careers. They love their work, but it no longer challenges them. In many cases they keep on doing what they have been doing all along but spend less and less of their time on it. They also start another activity, usually a nonprofit. My friend Bob Buford, for example, built a very successful television company that he still runs. But he has also founded and built a successful nonprofit organization that works with Protestant churches, and he is building another to teach social entrepreneurs how to manage their own nonprofit ventures while still running their original businesses.

People who manage the second half of their lives may always be a minority. The majority may "retire on the job" and count the years until their actual retirement. But it is this minority, the men and women who see a long working-life expectancy as an opportunity both for themselves and for society, who will become leaders and models.

There is one prerequisite for managing the second half of your life: You must begin long before you enter it. When it first became clear 30 years ago that working-life expectancies were lengthening very fast, many observers (including myself) believed that retired people would increasingly become volunteers for nonprofit institutions. That has not happened. If one does not begin to volunteer before one is 40 or so, one will not volunteer once past 60.

Similarly, all the social entrepreneurs I know began to work in their chosen second enterprise long before they reached their peak in their original business. Consider the example of a successful lawyer, the legal counsel to a large corporation, who has started a venture to establish model schools in his state. He began to do volunteer legal work for the schools when he was around 35. He was elected to the school board at age 40. At age 50, when he had amassed a fortune, he started his own enterprise to build and to run model schools. He is, however, still working nearly full-time as the lead counsel in the company he helped found as a young lawyer.

There is another reason to develop a second major interest, and to develop

it early. No one can expect to live very long without experiencing a serious setback in his or her life or work. There is the competent engineer who is passed over for promotion at age 45. There is the competent college professor who realizes at age 42 that she will never get a professorship at a big university, even though she may be fully qualified for it. There are tragedies in one's family life: the breakup of one's marriage or the loss of a child. At such times, a second major interest—not just a hobby—may make all the difference. The engineer, for example, now knows that he has not been very successful in his job. But in his outside activity—as church treasurer, for example—he is a success. One's family may break up, but in that outside activity there is still a community.

In a society in which success has become so terribly important, having options will become increasingly vital. Historically, there was no such thing as “success.” The overwhelming majority of people did not expect anything but to stay in their “proper station,” as an old English prayer has it. The only mobility was downward mobility.

In a knowledge society, however, we expect everyone to be a success. This is clearly an impossibility. For a great many people, there is at best an absence of failure. Wherever there is success, there has to be failure. And then it is vitally important for the individual, and equally for the individual's family, to have an area in which he or she can contribute, make a difference, and be *somebody*. That means finding a second area—whether in a second career, a parallel career, or a social venture—that offers an opportunity for being a leader, for being respected, for being a success.

The challenges of managing oneself may seem obvious, if not elementary. And the answers may seem self-evident to the point of appearing naïve. But managing oneself requires new and unprecedented things from the individual, and especially from the knowledge worker. In effect, managing oneself demands that each knowledge worker think and behave like a chief executive officer. Further, the shift from manual workers who do as they are told to knowledge workers who have to manage themselves profoundly challenges social structure. Every existing society, even the most individualistic one, takes two things for granted, if only subconsciously: that organizations outlive workers, and that most people stay put.

But today the opposite is true. Knowledge workers outlive organizations, and they are mobile. The need to manage oneself is therefore creating a revolution in human affairs.

Originally published in January 1999. Reprint R0501K

Management Time: Who's Got the Monkey?

by William Oncken, Jr., and Donald L. Wass

WHY IS IT THAT MANAGERS are typically running out of time while their subordinates are typically running out of work? Here we shall explore the meaning of management time as it relates to the interaction between managers and their bosses, their peers, and their subordinates.

Specifically, we shall deal with three kinds of management time:

- *Boss-imposed time*—used to accomplish those activities that the boss requires and that the manager cannot disregard without direct and swift penalty.
- *System-imposed time*—used to accommodate requests from peers for active support. Neglecting these requests will also result in penalties, though not always as direct or swift.
- *Self-imposed time*—used to do those things that the manager originates or agrees to do. A certain portion of this kind of time, however, will be taken by subordinates and is called *subordinate-imposed time*. The remaining portion will be the manager's own and is called *discretionary time*. Self-imposed time is not subject to penalty since neither the boss nor the system can discipline the manager for not doing what they didn't know he had intended to do in the first place.

To accommodate those demands, managers need to control the timing and the content of what they do. Since what their bosses and the system impose on them are subject to penalty, managers cannot tamper with those requirements. Thus their self-imposed time becomes their major area of concern.

Managers should try to increase the discretionary component of their self-imposed time by minimizing or doing away with the subordinate component. They will then use the added increment to get better control over their boss-imposed and system-imposed activities. Most managers spend much more time dealing with subordinates' problems than they even faintly realize. Hence we shall use the monkey-on-the-back metaphor to examine how subordinate-imposed time comes into being and what the superior can do about it.

Where Is the Monkey?

Let us imagine that a manager is walking down the hall and that he notices one of his subordinates, Jones, coming his way. When the two meet, Jones greets the manager with, “Good morning. By the way, we’ve got a problem. You see....” As Jones continues, the manager recognizes in this problem the two characteristics common to all the problems his subordinates gratuitously bring to his attention. Namely, the manager knows (a) enough to get involved, but (b) not enough to make the on-the-spot decision expected of him. Eventually, the manager says, “So glad you brought this up. I’m in a rush right now. Meanwhile, let me think about it, and I’ll let you know.” Then he and Jones part company.

Let us analyze what just happened. Before the two of them met, on whose back was the “monkey”? The subordinate’s. After they parted, on whose back was it? The manager’s. Subordinate-imposed time begins the moment a monkey successfully leaps from the back of a subordinate to the back of his or her superior and does not end until the monkey is returned to its proper owner for care and feeding. In accepting the monkey, the manager has voluntarily assumed a position subordinate to his subordinate. That is, he has allowed Jones to make him her subordinate by doing two things a subordinate is generally expected to do for a boss—the manager has accepted a responsibility from his subordinate, and the manager has promised her a progress report.

Idea in Brief

You're racing down the hall. An employee stops you and says, "We've got a problem." You assume you should get involved but can't make an on-the-spot decision. You say, "Let me think about it."

You've just allowed a "monkey" to leap from your subordinate's back to yours. *You're* now working for your *subordinate*. Take on enough monkeys, and you won't have time to handle your *real* job: fulfilling your own boss's mandates and helping peers generate business results.

How to avoid accumulating monkeys? Develop your subordinates' initiative, say Oncken and Wass. For example, when an employee tries to hand you a problem, clarify whether he should: recommend and implement a solution, take action then brief you immediately, or act and report the outcome at a regular update.

When you encourage employees to handle their own monkeys, they acquire new skills—and you liberate time to do your own job.

The subordinate, to make sure the manager does not miss this point, will later stick her head in the manager's office and cheerily query, "How's it coming?" (This is called supervision.)

Or let us imagine in concluding a conference with Johnson, another subordinate, the manager's parting words are, "Fine. Send me a memo on that."

Let us analyze this one. The monkey is now on the subordinate's back because the next move is his, but it is poised for a leap. Watch that monkey. Johnson dutifully writes the requested memo and drops it in his out-basket. Shortly thereafter, the manager plucks it from his in-basket and reads it. Whose move is it now? The manager's. If he does not make that move soon, he will get a follow-up memo from the subordinate. (This is another form of supervision.) The longer the manager delays, the more frustrated the subordinate will become (he'll be spinning his wheels) and the more guilty the manager will feel (his backlog of subordinate-imposed time will be mounting).

Idea in Practice

How to return monkeys to their proper owners? Oncken, Wass, and Steven Covey (in an afterword to this classic article) offer these suggestions.

Make Appointments to Deal with Monkeys

Avoid discussing any monkey on an ad hoc basis—for example, when you pass a subordinate in the hallway. You won't convey the proper seriousness. Instead, schedule an appointment to discuss the issue.

Specify Level of Initiative

Your employees can exercise five levels of initiative in handling on-the-job problems. From lowest to highest, the levels are:

1. Wait until told what to do.
2. Ask what to do.
3. Recommend an action, then with your approval, implement it.
4. Take independent action but advise you at once.
5. Take independent action and update you through routine procedure.

When an employee brings a problem to you, outlaw use of level 1 or 2. Agree on and assign level 3, 4, or 5 to the monkey. Take no more than 15 minutes to discuss the problem.

Agree on a Status Update

After deciding how to proceed, agree on a time and place when the employee will give you a progress report.

Examine Your Own Motives

Some managers secretly worry that if they encourage subordinates to take more initiative, they'll appear less strong, more vulnerable, and less useful. Instead, cultivate an inward sense of security that frees you to relinquish direct control and support employees' growth.

Develop Employees' Skills

Employees try to hand off monkeys when they lack the desire or ability to handle them. Help employees develop needed problem-solving skills. It's initially more time consuming than tackling problems yourself—but it saves time in the long run.

Foster Trust

Developing employees' initiative requires a trusting relationship between you and your subordinates. If they're afraid of failing, they'll keep bringing their monkeys to you rather than working to solve their own problems. To promote trust, reassure them it's safe to make mistakes.

Or suppose once again that at a meeting with a third subordinate, Smith, the manager agrees to provide all the necessary backing for a public relations proposal he has just asked Smith to develop. The manager's parting words to her are, "Just let me know how I can help."

Now let us analyze this. Again the monkey is initially on the subordinate's back. But for how long? Smith realizes that she cannot let the manager "know" until her proposal has the manager's approval. And from experience, she also realizes that her proposal will likely be sitting in the manager's briefcase for weeks before he eventually gets to it. Who's really got the monkey? Who will be checking up on whom? Wheel spinning and bottlenecking are well on their way again.

A fourth subordinate, Reed, has just been transferred from another part of the company so that he can launch and eventually manage a newly created business venture. The manager has said they should get together soon to hammer out a set of objectives for the new job, adding, "I will draw up an

initial draft for discussion with you.”

Let us analyze this one, too. The subordinate has the new job (by formal assignment) and the full responsibility (by formal delegation), but the manager has the next move. Until he makes it, he will have the monkey, and the subordinate will be immobilized.

Why does all of this happen? Because in each instance the manager and the subordinate assume at the outset, wittingly or unwittingly, that the matter under consideration is a joint problem. The monkey in each case begins its career astride both their backs. All it has to do is move the wrong leg, and—presto!—the subordinate deftly disappears. The manager is thus left with another acquisition for his menagerie. Of course, monkeys can be trained not to move the wrong leg. But it is easier to prevent them from straddling backs in the first place.

Who Is Working for Whom?

Let us suppose that these same four subordinates are so thoughtful and considerate of their superior's time that they take pains to allow no more than three monkeys to leap from each of their backs to his in any one day. In a five-day week, the manager will have picked up 60 screaming monkeys—far too many to do anything about them individually. So he spends his subordinate-imposed time juggling his “priorities.”

Late Friday afternoon, the manager is in his office with the door closed for privacy so he can contemplate the situation, while his subordinates are waiting outside to get their last chance before the weekend to remind him that he will have to “fish or cut bait.” Imagine what they are saying to one another about the manager as they wait: “What a bottleneck. He just can't make up his mind. How anyone ever got that high up in our company without being able to make a decision we'll never know.”

Worst of all, the reason the manager cannot make any of these “next moves” is that his time is almost entirely eaten up by meeting his own boss-imposed and system-imposed requirements. To control those tasks, he needs discretionary time that is in turn denied him when he is preoccupied with all these monkeys. The manager is caught in a vicious circle. But time is a-wasting (an understatement). The manager calls his secretary on the intercom and instructs her to tell his subordinates that he won't be able to see them until Monday morning. At 7 PM, he drives home, intending with firm resolve to return to the office tomorrow to get caught up over the weekend. He returns bright and early the next day only to see, on the nearest green of the golf course across from his office window, a foursome. Guess who?

That does it. He now knows who is really working for whom. Moreover, he now sees that if he actually accomplishes during this weekend what he came to accomplish, his subordinates' morale will go up so sharply that they will each raise the limit on the number of monkeys they will let jump from their backs to his. In short, he now sees, with the clarity of a revelation on a mountaintop, that the more he gets caught up, the more he will fall behind.

He leaves the office with the speed of a person running away from a plague. His plan? To get caught up on something else he hasn't had time for in years: a weekend with his family. (This is one of the many varieties of discretionary time.)

Sunday night he enjoys ten hours of sweet, untroubled slumber, because he has clear-cut plans for Monday. He is going to get rid of his subordinate-imposed time. In exchange, he will get an equal amount of discretionary time, part of which he will spend with his subordinates to make sure that they learn the difficult but rewarding managerial art called "The Care and Feeding of Monkeys."

The manager will also have plenty of discretionary time left over for getting control of the timing and the content not only of his boss-imposed time but also of his system-imposed time. It may take months, but compared with the way things have been, the rewards will be enormous. His ultimate objective is to manage his time.

Getting Rid of the Monkeys

The manager returns to the office Monday morning just late enough so that his four subordinates have collected outside his office waiting to see him about their monkeys. He calls them in one by one. The purpose of each interview is to take a monkey, place it on the desk between them, and figure out together how the next move might conceivably be the subordinate's. For certain monkeys, that will take some doing. The subordinate's next move may be so elusive that the manager may decide—just for now—merely to let the monkey sleep on the subordinate's back overnight and have him or her return with it at an appointed time the next morning to continue the joint quest for a more substantive move by the subordinate. (Monkeys sleep just as soundly overnight on subordinates' backs as they do on superiors'.)

As each subordinate leaves the office, the manager is rewarded by the sight of a monkey leaving his office on the subordinate's back. For the next 24 hours, the subordinate will not be waiting for the manager; instead, the manager will be waiting for the subordinate.

Later, as if to remind himself that there is no law against his engaging in a constructive exercise in the interim, the manager strolls by the subordinate's office, sticks his head in the door, and cheerily asks, "How's it coming?" (The time consumed in doing this is discretionary for the manager and boss imposed for the subordinate.)

Making Time for Gorillas

by Stephen R. Covey

WHEN BILL ONCKEN WROTE this article in 1974, managers were in a terrible bind. They were desperate for a way to free up their time, but command and control was the status quo. Managers felt they weren't allowed to empower their subordinates to make decisions. Too dangerous. Too risky. That's why Oncken's message—give the monkey back to its rightful owner—involved a critically important paradigm shift. Many managers working today owe him a debt of gratitude.

It is something of an understatement, however, to observe that much has changed since Oncken's radical recommendation. Command and control as a management philosophy is all but dead, and "empowerment" is the word of the day in most organizations trying to thrive in global, intensely competitive markets. But command and control stubbornly remains a common practice. Management thinkers and executives have discovered in the last decade that bosses cannot just give a monkey back to their subordinates and then merrily get on with their own business. Empowering subordinates is hard and complicated work.

The reason: when you give problems back to subordinates to solve themselves, you have to be sure that they have both the desire and the ability to do so. As every executive knows, that isn't always the case. Enter a whole new set of problems. Empowerment often means you have to develop people, which is initially much more time consuming than solving the problem on your own.

Just as important, empowerment can only thrive when the whole organization buys into it—when formal systems and the informal culture support it. Managers need to be rewarded for delegating decisions and developing people. Otherwise, the degree of real empowerment in an organization will vary according to the beliefs and practices of individual managers.

But perhaps the most important lesson about empowerment is that effective delegation—the kind Oncken advocated—depends on a

trusting relationship between a manager and his subordinate. Oncken's message may have been ahead of his time, but what he suggested was still a fairly dictatorial solution. He basically told bosses, "Give the problem back!" Today, we know that this approach by itself is too authoritarian. To delegate effectively, executives need to establish a running dialogue with subordinates. They need to establish a partnership. After all, if subordinates are afraid of failing in front of their boss, they'll keep coming back for help rather than truly take initiative.

Oncken's article also doesn't address an aspect of delegation that has greatly interested me during the past two decades—that many managers are actually *eager* to take on their subordinates' monkeys. Nearly all the managers I talk with agree that their people are underutilized in their present jobs. But even some of the most successful, seemingly self-assured executives have talked about how hard it is to give up control to their subordinates.

I've come to attribute that eagerness for control to a common, deep-seated belief that rewards in life are scarce and fragile. Whether they learn it from their family, school, or athletics, many people establish an identity by comparing themselves with others. When they see others gain power, information, money, or recognition, for instance, they experience what the psychologist Abraham Maslow called "a feeling of deficiency"—a sense that something is being taken from them. That makes it hard for them to be genuinely happy about the success of others—even of their loved ones. Oncken implies that managers can easily give back or refuse monkeys, but many managers may subconsciously fear that a subordinate taking the initiative will make them appear a little less strong and a little more vulnerable.

How, then, do managers develop the inward security, the mentality of "abundance," that would enable them to relinquish control and seek the growth and development of those around them? The work I've done with numerous organizations suggests that managers who live with integrity according to a principle-based value system are most likely to sustain an empowering style of leadership.

Given the times in which he wrote, it was no wonder that Oncken's message resonated with managers. But it was reinforced by Oncken's wonderful gift for storytelling. I got to know Oncken on the speaker's circuit in the 1970s, and I was always impressed by how he dramatized

his ideas in colorful detail. Like the Dilbert comic strip, Oncken had a tongue-in-cheek style that got to the core of managers' frustrations and made them want to take back control of their time. And the monkey on your back wasn't just a metaphor for Oncken—it was his personal symbol. I saw him several times walking through airports with a stuffed monkey on his shoulder.

I'm not surprised that his article is one of the two best-selling HBR articles ever. Even with all we know about empowerment, its vivid message is even more important and relevant now than it was 25 years ago. Indeed, Oncken's insight is a basis for my own work on time management, in which I have people categorize their activities according to urgency and importance. I've heard from executives again and again that half or more of their time is spent on matters that are urgent but not important. They're trapped in an endless cycle of dealing with other people's monkeys, yet they're reluctant to help those people take their own initiative. As a result, they're often too busy to spend the time they need on the real gorillas in their organization. Oncken's article remains a powerful wake-up call for managers who need to delegate effectively.

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When the subordinate (with the monkey on his or her back) and the manager meet at the appointed hour the next day, the manager explains the ground rules in words to this effect:

“At no time while I am helping you with this or any other problem will your problem become my problem. The instant your problem becomes mine, you no longer have a problem. I cannot help a person who hasn't got a problem.

“When this meeting is over, the problem will leave this office exactly the way it came in—on your back. You may ask my help at any appointed time, and we will make a joint determination of what the next move will be and which of us will make it.

“In those rare instances where the next move turns out to be mine, you and I will determine it together. I will not make any move alone.”

The manager follows this same line of thought with each subordinate until

about 11 AM, when he realizes that he doesn't have to close his door. His monkeys are gone. They will return—but by appointment only. His calendar will assure this.

Transferring the Initiative

What we have been driving at in this monkey-on-the-back analogy is that managers can transfer initiative back to their subordinates and keep it there. We have tried to highlight a truism as obvious as it is subtle: namely, before developing initiative in subordinates, the manager must see to it that they *have* the initiative. Once the manager takes it back, he will no longer have it and he can kiss his discretionary time good-bye. It will all revert to subordinate-imposed time.

Nor can the manager and the subordinate effectively have the same initiative at the same time. The opener, “Boss, we’ve got a problem,” implies this duality and represents, as noted earlier, a monkey astride two backs, which is a very bad way to start a monkey on its career. Let us, therefore, take a few moments to examine what we call “The Anatomy of Managerial Initiative.”

There are five degrees of initiative that the manager can exercise in relation to the boss and to the system:

1. wait until told (lowest initiative);
2. ask what to do;
3. recommend, then take resulting action;
4. act, but advise at once;
5. and act on own, then routinely report (highest initiative).

Clearly, the manager should be professional enough not to indulge in initiatives 1 and 2 in relation either to the boss or to the system. A manager who uses initiative 1 has no control over either the timing or the content of boss-imposed or system-imposed time and thereby forfeits any right to complain about what he or she is told to do or when. The manager who uses initiative 2 has control over the timing but not over the content. Initiatives 3,

4, and 5 leave the manager in control of both, with the greatest amount of control being exercised at level 5.

In relation to subordinates, the manager's job is twofold. First, to outlaw the use of initiatives 1 and 2, thus giving subordinates no choice but to learn and master "Completed Staff Work." Second, to see that for each problem leaving his or her office there is an agreed-upon level of initiative assigned to it, in addition to an agreed-upon time and place for the next manager-subordinate conference. The latter should be duly noted on the manager's calendar.

The Care and Feeding of Monkeys

To further clarify our analogy between the monkey on the back and the processes of assigning and controlling, we shall refer briefly to the manager's appointment schedule, which calls for five hard-and-fast rules governing the "Care and Feeding of Monkeys." (Violation of these rules will cost discretionary time.)

Rule 1

Monkeys should be fed or shot. Otherwise, they will starve to death, and the manager will waste valuable time on postmortems or attempted resurrections.

Rule 2

The monkey population should be kept below the maximum number the manager has time to feed. Subordinates will find time to work as many monkeys as he or she finds time to feed, but no more. It shouldn't take more than five to 15 minutes to feed a properly maintained monkey.

Rule 3

Monkeys should be fed by appointment only. The manager should not have to hunt down starving monkeys and feed them on a catch-as-catch-can basis.

Rule 4

Monkeys should be fed face-to-face or by telephone, but never by mail. (Remember—with mail, the next move will be the manager's.) Documentation may add to the feeding process, but it cannot take the place of feeding.

Rule 5

Every monkey should have an assigned next feeding time and degree of initiative. These may be revised at any time by mutual consent but never allowed to become vague or indefinite. Otherwise, the monkey will either starve to death or wind up on the manager's back.

“Get control over the timing and content of what you do” is appropriate advice for managing time. The first order of business is for the manager to enlarge his or her discretionary time by eliminating subordinate-imposed time. The second is for the manager to use a portion of this newfound discretionary time to see to it that each subordinate actually has the initiative and applies it. The third is for the manager to use another portion of the increased discretionary time to get and keep control of the timing and content of both boss-imposed and system-imposed time. All these steps will increase the manager's leverage and enable the value of each hour spent in managing management time to multiply without theoretical limit.

Originally published in November 1999. Reprint 99609

How Resilience Works

by Diane L. Coutu

WHEN I BEGAN MY CAREER IN JOURNALISM—I was a reporter at a national magazine in those days—there was a man I'll call Claus Schmidt. He was in his mid-fifties, and to my impressionable eyes, he was the quintessential newsman: cynical at times, but unrelentingly curious and full of life, and often hilariously funny in a sandpaper-dry kind of way. He churned out hard-hitting cover stories and features with a speed and elegance I could only dream of. It always astounded me that he was never promoted to managing editor.

But people who knew Claus better than I did thought of him not just as a great newsman but as a quintessential survivor, someone who had endured in an environment often hostile to talent. He had lived through at least three major changes in the magazine's leadership, losing most of his best friends and colleagues on the way. At home, two of his children succumbed to incurable illnesses, and a third was killed in a traffic accident. Despite all this—or maybe because of it—he milled around the newsroom day after day, mentoring the cub reporters, talking about the novels he was writing—always looking forward to what the future held for him.

Why do some people suffer real hardships and not falter? Claus Schmidt could have reacted very differently. We've all seen that happen: One person cannot seem to get the confidence back after a layoff; another, persistently depressed, takes a few years off from life after her divorce. The question we would all like answered is, Why? What exactly is that quality of resilience that carries people through life?

It's a question that has fascinated me ever since I first learned of the Holocaust survivors in elementary school. In college, and later in my studies as an affiliate scholar at the Boston Psychoanalytic Society and Institute, I returned to the subject. For the past several months, however, I have looked on it with a new urgency, for it seems to me that the terrorism, war, and recession of recent months have made understanding resilience more important than ever. I have considered both the nature of individual resilience and what makes some organizations as a whole more resilient than others. Why do some people and some companies buckle under pressure? And what makes others bend and ultimately bounce back?

My exploration has taught me much about resilience, although it's a subject none of us will ever understand fully. Indeed, resilience is one of the great puzzles of human nature, like creativity or the religious instinct. But in sifting through psychological research and in reflecting on the many stories of resilience I've heard, I have seen a little more deeply into the hearts and minds of people like Claus Schmidt and, in doing so, looked more deeply into the human psyche as well.

The Buzz About Resilience

Resilience is a hot topic in business these days. Not long ago, I was talking to a senior partner at a respected consulting firm about how to land the very best MBAs—the name of the game in that particular industry. The partner, Daniel Savageau (not his real name), ticked off a long list of qualities his firm sought in its hires: intelligence, ambition, integrity, analytic ability, and so on. “What about resilience?” I asked. “Well, that’s very popular right now,” he said. “It’s the new buzzword. Candidates even tell us they’re resilient; they volunteer the information. But frankly, they’re just too young to know that about themselves. Resilience is something you realize you have *after* the fact.”

Idea in Brief

These are dark days: people are losing jobs, taking pay cuts, suffering foreclosure on their homes. Some of them are snapping—sinking into depression or suffering a permanent loss of confidence.

But others are snapping back; for example, taking advantage of a layoff to build a new career. What carries them through tough times? Resilience.

Resilient people possess three defining characteristics: They coolly accept the harsh realities facing them. They find meaning in terrible times. And they have an uncanny ability to improvise, making do with whatever's at hand.

In deep recessions, resilience becomes more important than ever. Fortunately, you can learn to be resilient.

“But if you could, would you test for it?” I asked. “Does it matter in business?”

Savageau paused. He's a man in his late forties and a success personally and professionally. Yet it hadn't been a smooth ride to the top. He'd started his life as a poor French Canadian in Woonsocket, Rhode Island, and had lost his father at six. He lucked into a football scholarship but was kicked out of Boston University twice for drinking. He turned his life around in his twenties, married, divorced, remarried, and raised five children. Along the way, he made and lost two fortunes before helping to found the consulting firm he now runs. “Yes, it does matter,” he said at last. “In fact, it probably matters more than any of the usual things we look for.” In the course of reporting this article, I heard the same assertion time and again. As Dean Becker, the president and CEO of Adaptiv Learning Systems, a four-year-old company in King of Prussia, Pennsylvania, that develops and delivers programs about resilience training, puts it: “More than education, more than experience, more than training, a person's level of resilience will determine who succeeds and who fails. That's true in the cancer ward, it's true in the Olympics, and it's true in the boardroom.”

Academic research into resilience started about 40 years ago with

pioneering studies by Norman Garmezy, now a professor emeritus at the University of Minnesota in Minneapolis. After studying why many children of schizophrenic parents did not suffer psychological illness as a result of growing up with them, he concluded that a certain quality of resilience played a greater role in mental health than anyone had previously suspected.

Today, theories abound about what makes resilience. Looking at Holocaust victims, Maurice Vanderpol, a former president of the Boston Psychoanalytic Society and Institute, found that many of the healthy survivors of concentration camps had what he calls a “plastic shield.” The shield was comprised of several factors, including a sense of humor. Often the humor was black, but nonetheless it provided a critical sense of perspective. Other core characteristics that helped included the ability to form attachments to others and the possession of an inner psychological space that protected the survivors from the intrusions of abusive others. Research about other groups uncovered different qualities associated with resilience. The Search Institute, a Minneapolis-based nonprofit organization that focuses on resilience and youth, found that the more resilient kids have an uncanny ability to get adults to help them out. Still other research showed that resilient inner-city youth often have talents such as athletic abilities that attract others to them.

Idea in Practice

Resilience can help you survive and recover from even the most brutal experiences. To cultivate resilience, apply these practices.

Face Down Reality

Instead of slipping into denial to cope with hardship, take a sober, down-to-earth view of the reality of your situation. You'll prepare yourself to act in ways that enable you to endure—training yourself to survive before the fact.

Example: Admiral Jim Stockdale survived being held prisoner and tortured by the Vietcong in part by accepting he could be held for a long time. (He was held for eight years.) Those who didn't make it out of the camps kept optimistically assuming they'd be released on shorter timetables—by Christmas, by Easter, by the Fourth of July. "I think they all died of broken hearts," Stockdale said.

Search for Meaning

When hard times strike, resist any impulse to view yourself as a victim and to cry, "Why me?" Rather, devise constructs about your suffering to create meaning for yourself and others. You'll build bridges from your present-day ordeal to a fuller, better future. Those bridges will make the present manageable, by removing the sense that the present is overwhelming.

Example: Austrian psychiatrist and Auschwitz survivor Victor Frankl realized that to survive the camp, he had to find some purpose. He did so by imagining himself giving a lecture after the war on the psychology of the concentration camp to help outsiders understand what he had been through. By creating concrete goals for himself, he rose above the sufferings of the moment.

Continually Improvise

When disaster hits, be inventive. Make the most of what you have, putting resources to unfamiliar uses and imagining possibilities others don't see.

Example: Mike founded a business with his friend Paul, selling educational materials to schools, businesses, and consulting firms. When a recession hit, they lost many core clients. Paul went through a bitter divorce, suffered a depression, and couldn't work. When Mike offered to buy him out, Paul slapped him with a lawsuit claiming Mike was trying to steal the business.

Mike kept the company going any way he could—going into joint ventures to sell English-language training materials to Russian and Chinese competitors, publishing newsletters for clients, and even writing video scripts for competitors. The lawsuit was eventually settled in his favor, and he had a new and much more solid business than the one he started out with.

Many of the early theories about resilience stressed the role of genetics. Some people are just born resilient, so the arguments went. There's some truth to that, of course, but an increasing body of empirical evidence shows that resilience—whether in children, survivors of concentration camps, or businesses back from the brink—can be learned. For example, George Vaillant, the director of the Study of Adult Development at Harvard Medical School in Boston, observes that within various groups studied during a 60-year period, some people became markedly more resilient over their lifetimes. Other psychologists claim that unresilient people more easily develop resiliency skills than those with head starts.

Most of the resilience theories I encountered in my research make good common sense. But I also observed that almost all the theories overlap in three ways. Resilient people, they posit, possess three characteristics: a staunch acceptance of reality; a deep belief, often buttressed by strongly held values, that life is meaningful; and an uncanny ability to improvise. You can bounce back from hardship with just one or two of these qualities, but you will only be truly resilient with all three. These three characteristics hold true for resilient organizations as well. Let's take a look at each of them in turn.

Facing Down Reality

A common belief about resilience is that it stems from an optimistic nature. That's true but only as long as such optimism doesn't distort your sense of reality. In extremely adverse situations, rose-colored thinking can actually spell disaster. This point was made poignantly to me by management researcher and writer Jim Collins, who happened upon this concept while researching *Good to Great*, his book on how companies transform themselves out of mediocrity. Collins had a hunch (an exactly wrong hunch) that resilient companies were filled with optimistic people. He tried out that idea on Admiral Jim Stockdale, who was held prisoner and tortured by the Vietcong for eight years.

Collins recalls: "I asked Stockdale: 'Who didn't make it out of the camps?' And he said, 'Oh, that's easy. It was the optimists. They were the ones who said we were going to be out by Christmas. And then they said we'd be out by Easter and then out by Fourth of July and out by Thanksgiving, and then it was Christmas again.' Then Stockdale turned to me and said, 'You know, I think they all died of broken hearts.'"

In the business world, Collins found the same unblinking attitude shared by executives at all the most successful companies he studied. Like Stockdale, resilient people have very sober and down-to-earth views of those parts of reality that matter for survival. That's not to say that optimism doesn't have its place: In turning around a demoralized sales force, for instance, conjuring a sense of possibility can be a very powerful tool. But for bigger challenges, a cool, almost pessimistic, sense of reality is far more important.

Perhaps you're asking yourself, "Do I truly understand—and accept—the reality of my situation? Does my organization?" Those are good questions, particularly because research suggests most people slip into denial as a coping mechanism. Facing reality, really facing it, is grueling work. Indeed, it can be unpleasant and often emotionally wrenching. Consider the following story of organizational resilience, and see what it means to confront reality.

Prior to September 11, 2001, Morgan Stanley, the famous investment bank, was the largest tenant in the World Trade Center. The company had some 2,700 employees working in the south tower on 22 floors between the 43rd and the 74th. On that horrible day, the first plane hit the north tower at 8:46 AM, and Morgan Stanley started evacuating just one minute later, at 8:47 AM. When the second plane crashed into the south tower 15 minutes after that, Morgan Stanley's offices were largely empty. All told, the company lost only seven employees despite receiving an almost direct hit.

Of course, the organization was just plain lucky to be in the second tower. Cantor Fitzgerald, whose offices were hit in the first attack, couldn't have done anything to save its employees. Still, it was Morgan Stanley's hard-nosed realism that enabled the company to benefit from its luck. Soon after the 1993 attack on the World Trade Center, senior management recognized that working in such a symbolic center of U.S. commercial power made the company vulnerable to attention from terrorists and possible attack.

With this grim realization, Morgan Stanley launched a program of preparedness at the micro level. Few companies take their fire drills seriously. Not so Morgan Stanley, whose VP of security for the Individual Investor Group, Rick Rescorla, brought a military discipline to the job. Rescorla, himself a highly resilient, decorated Vietnam vet, made sure that people were fully drilled about what to do in a catastrophe. When disaster struck on September 11, Rescorla was on a bullhorn telling Morgan Stanley employees to stay calm and follow their well-practiced drill, even though some building supervisors were telling occupants that all was well. Sadly, Rescorla himself, whose life story has been widely covered in recent months, was one of the seven who didn't make it out.

"When you're in financial services where so much depends on technology, contingency planning is a major part of your business," says President and COO Robert G. Scott. But Morgan Stanley was prepared for the very toughest reality. It had not just one, but three, recovery sites where employees could congregate and business could take place if work locales were ever disrupted. "Multiple backup sites seemed like an incredible extravagance on September 10," concedes Scott. "But on September 12, they seemed like genius."

Maybe it was genius; it was undoubtedly resilience at work. The fact is, when we truly stare down reality, we prepare ourselves to act in ways that allow us to endure and survive extraordinary hardship. We train ourselves

how to survive before the fact.

The Search for Meaning

The ability to see reality is closely linked to the second building block of resilience, the propensity to make meaning of terrible times. We all know people who, under duress, throw up their hands and cry, “How can this be happening to me?” Such people see themselves as victims, and living through hardship carries no lessons for them. But resilient people devise constructs about their suffering to create some sort of meaning for themselves and others.

I have a friend I’ll call Jackie Oiseaux who suffered repeated psychoses over a ten-year period due to an undiagnosed bipolar disorder. Today, she holds down a big job in one of the top publishing companies in the country, has a family, and is a prominent member of her church community. When people ask her how she bounced back from her crises, she runs her hands through her hair. “People sometimes say, ‘Why me?’ But I’ve always said, ‘Why *not* me?’ True, I lost many things during my illness,” she says, “but I found many more—incredible friends who saw me through the bleakest times and who will give meaning to my life forever.”

This dynamic of meaning making is, most researchers agree, the way resilient people build bridges from present-day hardships to a fuller, better constructed future. Those bridges make the present manageable, for lack of a better word, removing the sense that the present is overwhelming. This concept was beautifully articulated by Viktor E. Frankl, an Austrian psychiatrist and an Auschwitz survivor. In the midst of staggering suffering, Frankl invented “meaning therapy,” a humanistic therapy technique that helps individuals make the kinds of decisions that will create significance in their lives.

In his book *Man’s Search for Meaning*, Frankl described the pivotal moment in the camp when he developed meaning therapy. He was on his way to work one day, worrying whether he should trade his last cigarette for a bowl of soup. He wondered how he was going to work with a new foreman whom he knew to be particularly sadistic. Suddenly, he was disgusted by just

how trivial and meaningless his life had become. He realized that to survive, he had to find some purpose. Frankl did so by imagining himself giving a lecture after the war on the psychology of the concentration camp, to help outsiders understand what he had been through. Although he wasn't even sure he would survive, Frankl created some concrete goals for himself. In doing so, he succeeded in rising above the sufferings of the moment. As he put it in his book: "We must never forget that we may also find meaning in life even when confronted with a hopeless situation, when facing a fate that cannot be changed."

Frankl's theory underlies most resilience coaching in business. Indeed, I was struck by how often businesspeople referred to his work. "Resilience training—what we call hardiness—is a way for us to help people construct meaning in their everyday lives," explains Salvatore R. Maddi, a University of California, Irvine psychology professor and the director of the Hardiness Institute in Newport Beach, California. "When people realize the power of resilience training, they often say, 'Doc, is this what psychotherapy is?' But psychotherapy is for people whose lives have fallen apart badly and need repair. We see our work as showing people life skills and attitudes. Maybe those things should be taught at home, maybe they should be taught in schools, but they're not. So we end up doing it in business."

Yet the challenge confronting resilience trainers is often more difficult than we might imagine. Meaning can be elusive, and just because you found it once doesn't mean you'll keep it or find it again. Consider Aleksandr Solzhenitsyn, who survived the war against the Nazis, imprisonment in the gulag, and cancer. Yet when he moved to a farm in peaceful, safe Vermont, he could not cope with the "infantile West." He was unable to discern any real meaning in what he felt to be the destructive and irresponsible freedom of the West. Upset by his critics, he withdrew into his farmhouse, behind a locked fence, seldom to be seen in public. In 1994, a bitter man, Solzhenitsyn moved back to Russia.

Since finding meaning in one's environment is such an important aspect of resilience, it should come as no surprise that the most successful organizations and people possess strong value systems. Strong values infuse an environment with meaning because they offer ways to interpret and shape events. While it's popular these days to ridicule values, it's surely no coincidence that the most resilient organization in the world has been the Catholic Church, which has survived wars, corruption, and schism for more

than 2,000 years, thanks largely to its immutable set of values. Businesses that survive also have their creeds, which give them purposes beyond just making money. Strikingly, many companies describe their value systems in religious terms. Pharmaceutical giant Johnson & Johnson, for instance, calls its value system, set out in a document given to every new employee at orientation, the Credo. Parcel company UPS talks constantly about its Noble Purpose.

Value systems at resilient companies change very little over the years and are used as scaffolding in times of trouble. UPS Chairman and CEO Mike Eskew believes that the Noble Purpose helped the company to rally after the agonizing strike in 1997. Says Eskew: “It was a hugely difficult time, like a family feud. Everyone had close friends on both sides of the fence, and it was tough for us to pick sides. But what saved us was our Noble Purpose. Whatever side people were on, they all shared a common set of values. Those values are core to us and never change; they frame most of our important decisions. Our strategy and our mission may change, but our values never do.”

The religious connotations of words like “credo,” “values,” and “noble purpose,” however, should not be confused with the actual content of the values. Companies can hold ethically questionable values and still be very resilient. Consider Phillip Morris, which has demonstrated impressive resilience in the face of increasing unpopularity. As Jim Collins points out, Phillip Morris has very strong values, although we might not agree with them—for instance, the value of “adult choice.” But there’s no doubt that Phillip Morris executives believe strongly in its values, and the strength of their beliefs sets the company apart from most of the other tobacco companies. In this context, it is worth noting that resilience is neither ethically good nor bad. It is merely the skill and the capacity to be robust under conditions of enormous stress and change. As Viktor Frankl wrote: “On the average, only those prisoners could keep alive who, after years of trekking from camp to camp, had lost all scruples in their fight for existence; they were prepared to use every means, honest and otherwise, even brutal..., in order to save themselves. We who have come back... we know: The best of us did not return.”

Values, positive or negative, are actually more important for organizational resilience than having resilient people on the payroll. If resilient employees are all interpreting reality in different ways, their

decisions and actions may well conflict, calling into doubt the survival of their organization. And as the weakness of an organization becomes apparent, highly resilient individuals are more likely to jettison the organization than to imperil their own survival.

Ritualized Ingenuity

The third building block of resilience is the ability to make do with whatever is at hand. Psychologists follow the lead of French anthropologist Claude Levi-Strauss in calling this skill *bricolage*.¹ Intriguingly, the roots of that word are closely tied to the concept of resilience, which literally means “bouncing back.” Says Levi-Strauss: “In its old sense, the verb *bricoler*... was always used with reference to some extraneous movement: a ball rebounding, a dog straying, or a horse swerving from its direct course to avoid an obstacle.”

Bricolage in the modern sense can be defined as a kind of inventiveness, an ability to improvise a solution to a problem without proper or obvious tools or materials. *Bricoleurs* are always tinkering—building radios from household effects or fixing their own cars. They make the most of what they have, putting objects to unfamiliar uses. In the concentration camps, for example, resilient inmates knew to pocket pieces of string or wire whenever they found them. The string or wire might later become useful—to fix a pair of shoes, perhaps, which in freezing conditions might make the difference between life and death.

When situations unravel, bricoleurs muddle through, imagining possibilities where others are confounded. I have two friends, whom I’ll call Paul Shields and Mike Andrews, who were roommates throughout their college years. To no one’s surprise, when they graduated, they set up a business together, selling educational materials to schools, businesses, and consulting firms. At first, the company was a great success, making both founders paper millionaires. But the recession of the early 1990s hit the company hard, and many core clients fell away. At the same time, Paul experienced a bitter divorce and a depression that made it impossible for him to work. Mike offered to buy Paul out but was instead slapped with a lawsuit claiming that Mike was trying to steal the business. At this point, a less resilient person might have just walked away from the mess. Not Mike. As the case wound through the courts, he kept the company going any way he

could—constantly morphing the business until he found a model that worked: going into joint ventures to sell English-language training materials to Russian and Chinese companies. Later, he branched off into publishing newsletters for clients. At one point, he was even writing video scripts for his competitors. Thanks to all this bricolage, by the time the lawsuit was settled in his favor, Mike had an entirely different, and much more solid, business than the one he had started with.

Bricolage can be practiced on a higher level as well. Richard Feynman, winner of the 1965 Nobel Prize in physics, exemplified what I like to think of as intellectual bricolage. Out of pure curiosity, Feynman made himself an expert on cracking safes, not only looking at the mechanics of safecracking but also cobbling together psychological insights about people who used safes and set the locks. He cracked many of the safes at Los Alamos, for instance, because he guessed that theoretical physicists would not set the locks with random code numbers they might forget but would instead use a sequence with mathematical significance. It turned out that the three safes containing all the secrets to the atomic bomb were set to the same mathematical constant, e , whose first six digits are 2.71828.

Resilient organizations are stuffed with bricoleurs, though not all of them, of course, are Richard Feynmans. Indeed, companies that survive regard improvisation as a core skill. Consider UPS, which empowers its drivers to do whatever it takes to deliver packages on time. Says CEO Eskew: “We tell our employees to get the job done. If that means they need to improvise, they improvise. Otherwise we just couldn’t do what we do every day. Just think what can go wrong: a busted traffic light, a flat tire, a bridge washed out. If a snowstorm hits Louisville tonight, a group of people will sit together and discuss how to handle the problem. Nobody tells them to do that. They come together because it’s our tradition to do so.”

That tradition meant that the company was delivering parcels in southeast Florida just one day after Hurricane Andrew devastated the region in 1992, causing billions of dollars in damage. Many people were living in their cars because their homes had been destroyed, yet UPS drivers and managers sorted packages at a diversion site and made deliveries even to those who were stranded in their cars. It was largely UPS’s improvisational skills that enabled it to keep functioning after the catastrophic hit. And the fact that the company continued on gave others a sense of purpose or meaning amid the chaos.

Improvisation of the sort practiced by UPS, however, is a far cry from unbridled creativity. Indeed, much like the military, UPS lives on rules and regulations. As Eskew says: “Drivers always put their keys in the same place. They close the doors the same way. They wear their uniforms the same way. We are a company of precision.” He believes that although they may seem stifling, UPS’s rules were what allowed the company to bounce back immediately after Hurricane Andrew, for they enabled people to focus on the one or two fixes they needed to make in order to keep going.

Eskew’s opinion is echoed by Karl E. Weick, a professor of organizational behavior at the University of Michigan Business School in Ann Arbor and one of the most respected thinkers on organizational psychology. “There is good evidence that when people are put under pressure, they regress to their most habituated ways of responding,” Weick has written. “What we do not expect under life-threatening pressure is creativity.” In other words, the rules and regulations that make some companies appear less creative may actually make them more resilient in times of real turbulence.

Claus Schmidt, the newsman I mentioned earlier, died about five years ago, but I’m not sure I could have interviewed him about his own resilience even if he were alive. It would have felt strange, I think, to ask him, “Claus, did you really face down reality? Did you make meaning out of your hardships? Did you improvise your recovery after each professional and personal disaster?” He may not have been able to answer. In my experience, resilient people don’t often describe themselves that way. They shrug off their survival stories and very often assign them to luck.

Obviously, luck does have a lot to do with surviving. It was luck that Morgan Stanley was situated in the south tower and could put its preparedness training to work. But being lucky is not the same as being resilient. Resilience is a reflex, a way of facing and understanding the world, that is deeply etched into a person’s mind and soul. Resilient people and companies face reality with staunchness, make meaning of hardship instead of crying out in despair, and improvise solutions from thin air. Others do not. This is the nature of resilience, and we will never completely understand it.

Originally published in May 2002. Reprint R0205B

Note

[1.](#) See, e.g., Karl E. Weick, “The Collapse of Sense-making in Organizations: The Mann Gulch Disaster,” *Administrative Science Quarterly*, December 1993.

Manage Your Energy, Not Your Time

by Tony Schwartz and Catherine McCarthy

STEVE WANNER IS A HIGHLY respected 37-year-old partner at Ernst & Young, married with four young children. When we met him a year ago, he was working 12- to 14-hour days, felt perpetually exhausted, and found it difficult to fully engage with his family in the evenings, which left him feeling guilty and dissatisfied. He slept poorly, made no time to exercise, and seldom ate healthy meals, instead grabbing a bite to eat on the run or while working at his desk.

Wanner's experience is not uncommon. Most of us respond to rising demands in the workplace by putting in longer hours, which inevitably take a toll on us physically, mentally, and emotionally. That leads to declining levels of engagement, increasing levels of distraction, high turnover rates, and soaring medical costs among employees. We at the Energy Project have worked with thousands of leaders and managers in the course of doing consulting and coaching at large organizations during the past five years. With remarkable consistency, these executives tell us they're pushing themselves harder than ever to keep up and increasingly feel they are at a breaking point.

The core problem with working longer hours is that time is a finite resource. Energy is a different story. Defined in physics as the capacity to work, energy comes from four main wellsprings in human beings: the body, emotions, mind, and spirit. In each, energy can be systematically expanded and regularly renewed by establishing specific rituals—behaviors that are intentionally practiced and precisely scheduled, with the goal of making them

unconscious and automatic as quickly as possible.

To effectively reenergize their workforces, organizations need to shift their emphasis from getting more out of people to investing more in them, so they are motivated—and able—to bring more of themselves to work every day. To recharge themselves, individuals need to recognize the costs of energy-depleting behaviors and then take responsibility for changing them, regardless of the circumstances they're facing.

The rituals and behaviors Wanner established to better manage his energy transformed his life. He set an earlier bedtime and gave up drinking, which had disrupted his sleep. As a consequence, when he woke up he felt more rested and more motivated to exercise, which he now does almost every morning. In less than two months he lost 15 pounds. After working out he now sits down with his family for breakfast. Wanner still puts in long hours on the job, but he renews himself regularly along the way. He leaves his desk for lunch and usually takes a morning and an afternoon walk outside. When he arrives at home in the evening, he's more relaxed and better able to connect with his wife and children.

Establishing simple rituals like these can lead to striking results across organizations. At Wachovia Bank, we took a group of employees through a pilot energy management program and then measured their performance against that of a control group. The participants outperformed the controls on a series of financial metrics, such as the value of loans they generated. They also reported substantial improvements in their customer relationships, their engagement with work, and their personal satisfaction. In this article, we'll describe the Wachovia study in a little more detail. Then we'll explain what executives and managers can do to increase and regularly renew work capacity—the approach used by the Energy Project, which builds on, deepens, and extends several core concepts developed by Tony's former partner Jim Loehr in his seminal work with athletes.

Idea in Brief

Organizations are demanding ever-higher performance from their workforces. People are trying to comply, but the usual method—putting in longer hours—has backfired. They're getting exhausted, disengaged, and sick. And they're defecting to healthier job environments.

Longer days at the office don't work because time is a limited resource. But personal energy is renewable, say Schwartz and McCarthy. By fostering deceptively simple **rituals** that help employees regularly replenish their energy, organizations build workers' physical, emotional, and mental resilience. These rituals include taking brief breaks at specific intervals, expressing appreciation to others, reducing interruptions, and spending more time on activities people do best and enjoy most.

Help your employees systematically rejuvenate their personal energy, and the benefits go straight to your bottom line. Take Wachovia Bank: Participants in an energy renewal program produced 13 percentage points greater year-over-year in revenues from loans than a control group did. And they exceeded the control group's gains in revenues from deposits by 20 percentage points.

Linking Capacity and Performance at Wachovia

Most large organizations invest in developing employees' skills, knowledge, and competence. Very few help build and sustain their capacity—their energy—which is typically taken for granted. In fact, greater capacity makes it possible to get more done in less time at a higher level of engagement and with more sustainability. Our experience at Wachovia bore this out.

In early 2006 we took 106 employees at 12 regional banks in southern New Jersey through a curriculum of four modules, each of which focused on specific strategies for strengthening one of the four main dimensions of energy. We delivered it at one-month intervals to groups of approximately 20 to 25, ranging from senior leaders to lower-level managers. We also assigned each attendee a fellow employee as a source of support between sessions. Using Wachovia's own key performance metrics, we evaluated how the participant group performed compared with a group of employees at similar levels at a nearby set of Wachovia banks who did not go through the training. To create a credible basis for comparison, we looked at year-over-year percentage changes in performance across several metrics.

Idea in Practice

Schwartz and McCarthy recommend these practices for renewing four dimensions of personal energy.

Physical Energy

- Enhance your sleep by setting an earlier bedtime and reducing alcohol use.
- Reduce stress by engaging in cardiovascular activity at least three times a week and strength training at least once.
- Eat small meals and light snacks every three hours.
- Learn to notice signs of imminent energy flagging, including restlessness, yawning, hunger, and difficulty concentrating.
- Take brief but regular breaks, away from your desk, at 90- to 120-minute intervals throughout the day.

Emotional Energy

- Defuse negative emotions—irritability, impatience, anxiety, insecurity—through deep abdominal breathing.
- Fuel positive emotions in yourself and others by regularly expressing appreciation to others in detailed, specific terms through notes, e-mails, calls, or conversations.
- Look at upsetting situations through new lenses. Adopt a “reverse lens” to ask, “What would the other person in this conflict say, and how might he be right?” Use a “long lens” to ask, “How will I likely view this situation in six months?” Employ a “wide lens” to ask, “How can I grow and learn from this situation?”

Mental Energy

- Reduce interruptions by performing high-concentration tasks away from phones and e-mail.
- Respond to voice mails and e-mails at designated times during the day.
- Every night, identify the most important challenge for the next day. Then make it your first priority when you arrive at work in the morning.

Spiritual Energy

- Identify your “sweet spot” activities—those that give you feelings of effectiveness, effortless absorption, and fulfillment. Find ways to do more of these. One executive who hated doing sales reports delegated them to someone who loved that activity.
- Allocate time and energy to what you consider most important. For example, spend the last 20 minutes of your evening commute relaxing, so you can connect with your family once you’re home.
- Live your core values. For instance, if consideration is important to you but you’re perpetually late for meetings, practice intentionally showing up five minutes early for meetings.

How Companies Can Help

To support energy renewal rituals in your firm:

- Build “renewal rooms” where people can go to relax and refuel.
- Subsidize gym memberships.
- Encourage managers to gather employees for midday workouts.
- Suggest that people stop checking e-mails during meetings.

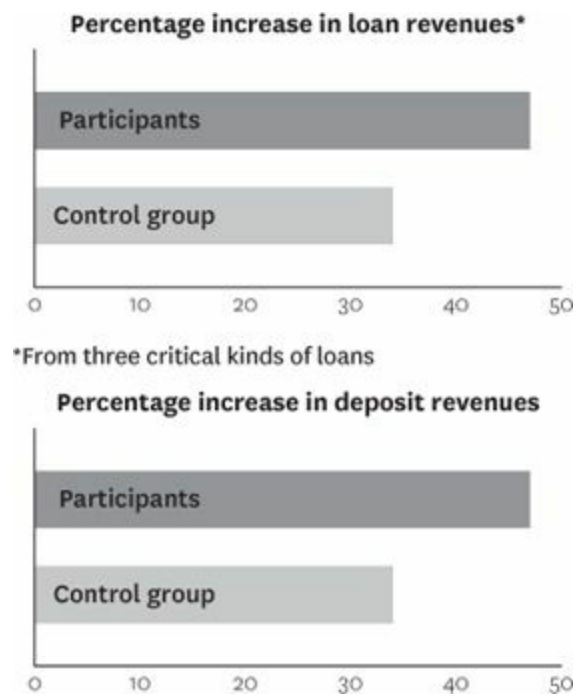
On a measure called the “Big 3”—revenues from three kinds of loans—the participants showed a year-over-year increase that was 13 percentage points greater than the control group’s in the first three months of our study. On revenues from deposits, the participants exceeded the control group’s year-over-year gain by 20 percentage points during that same period. The precise gains varied month by month, but with only a handful of exceptions, the participants continued to significantly outperform the control group for a full year after completing the program. Although other variables undoubtedly influenced these outcomes, the participants’ superior performance was notable in its consistency. (See the exhibit “How Energy Renewal Programs Boosted Productivity at Wachovia.”)

We also asked participants how the program influenced them personally. Sixty-eight percent reported that it had a positive impact on their relationships with clients and customers. Seventy-one percent said that it had a noticeable or substantial positive impact on their productivity and performance. These findings corroborated a raft of anecdotal evidence we’ve gathered about the effectiveness of this approach among leaders at other large companies such as Ernst & Young, Sony, Deutsche Bank, Nokia, ING Direct, Ford, and MasterCard.

How energy renewal programs boosted productivity at Wachovia

At Wachovia Bank, employees participating in an energy renewal program outperformed a control group of employees, demonstrating significantly

greater improvements in year-over-year performance during the first quarter of 2006.



The Body: Physical Energy

Our program begins by focusing on physical energy. It is scarcely news that inadequate nutrition, exercise, sleep, and rest diminish people's basic energy levels, as well as their ability to manage their emotions and focus their attention. Nonetheless, many executives don't find ways to practice consistently healthy behaviors, given all the other demands in their lives.

Before participants in our program begin to explore ways to increase their physical energy, they take an energy audit, which includes four questions in each energy dimension—body, emotions, mind, and spirit. (See the exhibit “Are You Headed for an Energy Crisis?”) On average, participants get eight to ten of those 16 questions “wrong,” meaning they're doing things such as skipping breakfast, failing to express appreciation to others, struggling to focus on one thing at a time, or spending too little time on activities that give them a sense of purpose. While most participants aren't surprised to learn these behaviors are counterproductive, having them all listed in one place is often uncomfortable, sobering, and galvanizing. The audit highlights employees' greatest energy deficits. Participants also fill out charts designed to raise their awareness about how their exercise, diet, and sleep practices influence their energy levels.

The next step is to identify rituals for building and renewing physical energy. When Gary Faro, a vice president at Wachovia, began the program, he was significantly overweight, ate poorly, lacked a regular exercise routine, worked long hours, and typically slept no more than five or six hours a night. That is not an unusual profile among the leaders and managers we see. Over the course of the program, Faro began regular cardiovascular and strength training. He started going to bed at a designated time and sleeping longer. He changed his eating habits from two big meals a day (“Where I usually gorged myself,” he says) to smaller meals and light snacks every three hours. The aim was to help him stabilize his glucose levels over the course of the day, avoiding peaks and valleys. He lost 50 pounds in the process, and his energy levels soared. “I used to schedule tough projects for the morning, when I

knew that I would be more focused,” Faro says. “I don’t have to do that anymore because I find that I’m just as focused now at 5 PM as I am at 8 AM.”

Another key ritual Faro adopted was to take brief but regular breaks at specific intervals throughout the workday—always leaving his desk. The value of such breaks is grounded in our physiology. “Ultradian rhythms” refer to 90- to 120-minute cycles during which our bodies slowly move from a high-energy state into a physiological trough. Toward the end of each cycle, the body begins to crave a period of recovery. The signals include physical restlessness, yawning, hunger, and difficulty concentrating, but many of us ignore them and keep working. The consequence is that our energy reservoir—our remaining capacity—burns down as the day wears on.

Are you headed for an energy crisis?

Please check the statements below that are true for you.

Body

- ☐ I don’t regularly get at least seven to eight hours of sleep, and I often wake up feeling tired.
- ☐ I frequently skip breakfast, or I settle for something that isn’t nutritious.
- ☐ I don’t work out enough (meaning cardiovascular training at least three times a week and strength training at least once a week).
- ☐ I don’t take regular breaks during the day to truly renew and recharge, or I often eat lunch at my desk, if I eat it at all.

Emotions

- ☐ I frequently find myself feeling irritable, impatient, or anxious at work, especially when work is demanding.
- ☐ I don’t have enough time with my family and loved ones, and when I’m with them, I’m not always really with them.
- ☐ I have too little time for the activities that I most deeply enjoy.
- ☐ I don’t stop frequently enough to express my appreciation to

others or to savor my accomplishments and blessings.

Mind

- ▣ I have difficulty focusing on one thing at a time, and I am easily distracted during the day, especially by e-mail.
- ▣ I spend much of my day reacting to immediate crises and demands rather than focusing on activities with longer-term value and high leverage.
- ▣ I don't take enough time for reflection, strategizing, and creative thinking.
- ▣ I work in the evenings or on weekends, and I almost never take an e-mail-free vacation.

Spirit

- ▣ I don't spend enough time at work doing what I do best and enjoy most.
 - ▣ There are significant gaps between what I say is most important to me in my life and how I actually allocate my time and energy.
 - ▣ My decisions at work are more often influenced by external demands than by a strong, clear sense of my own purpose.
 - ▣ I don't invest enough time and energy in making a positive difference to others or to the world.
-

How is your overall energy?

Total number of statements checked: —

Guide to scores

- 0–3: Excellent energy management skills
- 4–6: Reasonable energy management skills
- 7–10: Significant energy management deficits
- 11–16: A full-fledged energy management crisis

What do you need to work on?

Number of checks in each category:

Body ____

Mind ____

Emotions ____

Spirit ____

Guide to category scores

0: Excellent energy management skills

1: Strong energy management skills

2: Significant deficits

3: Poor energy management skills

4: A full-fledged energy crisis

Intermittent breaks for renewal, we have found, result in higher and more sustainable performance. The length of renewal is less important than the quality. It is possible to get a great deal of recovery in a short time—as little as several minutes—if it involves a ritual that allows you to disengage from work and truly change channels. That could range from getting up to talk to a colleague about something other than work, to listening to music on an iPod, to walking up and down stairs in an office building. While breaks are countercultural in most organizations and counterintuitive for many high achievers, their value is multifaceted.

Matthew Lang is a managing director for Sony in South Africa. He adopted some of the same rituals that Faro did, including a 20-minute walk in the afternoons. Lang's walk not only gives him a mental and emotional breather and some exercise but also has become the time when he gets his best creative ideas. That's because when he walks he is not actively thinking, which allows the dominant left hemisphere of his brain to give way to the right hemisphere with its greater capacity to see the big picture and make imaginative leaps.

The Emotions: Quality of Energy

When people are able to take more control of their emotions, they can improve the quality of their energy, regardless of the external pressures they're facing. To do this, they first must become more aware of how they feel at various points during the workday and of the impact these emotions have on their effectiveness. Most people realize that they tend to perform best when they're feeling positive energy. What they find surprising is that they're not able to perform well or to lead effectively when they're feeling any other way.

Unfortunately, without intermittent recovery, we're not physiologically capable of sustaining highly positive emotions for long periods. Confronted with relentless demands and unexpected challenges, people tend to slip into negative emotions—the fight-or-flight mode—often multiple times in a day. They become irritable and impatient, or anxious and insecure. Such states of mind drain people's energy and cause friction in their relationships. Fight-or-flight emotions also make it impossible to think clearly, logically, and reflectively. When executives learn to recognize what kinds of events trigger their negative emotions, they gain greater capacity to take control of their reactions.

One simple but powerful ritual for defusing negative emotions is what we call “buying time.” Deep abdominal breathing is one way to do that. Exhaling slowly for five or six seconds induces relaxation and recovery, and turns off the fight-or-flight response. When we began working with Fujio Nishida, president of Sony Europe, he had a habit of lighting up a cigarette each time something especially stressful occurred—at least two or three times a day. Otherwise, he didn't smoke. We taught him the breathing exercise as an alternative, and it worked immediately: Nishida found he no longer had the desire for a cigarette. It wasn't the smoking that had given him relief from the stress, we concluded, but the relaxation prompted by the deep inhalation and exhalation.

A powerful ritual that fuels positive emotions is expressing appreciation

to others, a practice that seems to be as beneficial to the giver as to the receiver. It can take the form of a handwritten note, an e-mail, a call, or a conversation—and the more detailed and specific, the higher the impact. As with all rituals, setting aside a particular time to do it vastly increases the chances of success. Ben Jenkins, vice chairman and president of the General Bank at Wachovia in Charlotte, North Carolina, built his appreciation ritual into time set aside for mentoring. He began scheduling lunches or dinners regularly with people who worked for him. Previously, the only sit-downs he'd had with his direct reports were to hear monthly reports on their numbers or to give them yearly performance reviews. Now, over meals, he makes it a priority to recognize their accomplishments and also to talk with them about their lives and their aspirations rather than their immediate work responsibilities.

Finally, people can cultivate positive emotions by learning to change the stories they tell themselves about the events in their lives. Often, people in conflict cast themselves in the role of victim, blaming others or external circumstances for their problems. Becoming aware of the difference between the facts in a given situation and the way we interpret those facts can be powerful in itself. It's been a revelation for many of the people we work with to discover they have a choice about how to view a given event and to recognize how powerfully the story they tell influences the emotions they feel. We teach them to tell the most hopeful and personally empowering story possible in any given situation, without denying or minimizing the facts.

The most effective way people can change a story is to view it through any of three new lenses, which are all alternatives to seeing the world from the victim perspective. With the *reverse lens*, for example, people ask themselves, "What would the other person in this conflict say and in what ways might that be true?" With the *long lens* they ask, "How will I most likely view this situation in six months?" With the *wide lens* they ask themselves, "Regardless of the outcome of this issue, how can I grow and learn from it?" Each of these lenses can help people intentionally cultivate more positive emotions.

Nicolas Babin, director of corporate communications for Sony Europe, was the point person for calls from reporters when Sony went through several recalls of its batteries in 2006. Over time he found his work increasingly exhausting and dispiriting. After practicing the lens exercises, he began finding ways to tell himself a more positive and empowering story about his

role. “I realized,” he explains, “that this was an opportunity for me to build stronger relationships with journalists by being accessible to them and to increase Sony’s credibility by being straightforward and honest.”

The Mind: Focus of Energy

Many executives view multitasking as a necessity in the face of all the demands they juggle, but it actually undermines productivity. Distractions are costly: A temporary shift in attention from one task to another—stopping to answer an e-mail or take a phone call, for instance—increases the amount of time necessary to finish the primary task by as much as 25%, a phenomenon known as “switching time.” It’s far more efficient to fully focus for 90 to 120 minutes, take a true break, and then fully focus on the next activity. We refer to these work periods as “ultradian sprints.”

Once people see how much they struggle to concentrate, they can create rituals to reduce the relentless interruptions that technology has introduced in their lives. We start out with an exercise that forces them to face the impact of daily distractions. They attempt to complete a complex task and are regularly interrupted—an experience that, people report, ends up feeling much like everyday life.

Dan Cluna, a vice president at Wachovia, designed two rituals to better focus his attention. The first one is to leave his desk and go into a conference room, away from phones and e-mail, whenever he has a task that requires concentration. He now finishes reports in a third of the time they used to require. Cluna built his second ritual around meetings at branches with the financial specialists who report to him. Previously, he would answer his phone whenever it rang during these meetings. As a consequence, the meetings he scheduled for an hour often stretched to two, and he rarely gave anyone his full attention. Now Cluna lets his phone go to voice mail, so that he can focus completely on the person in front of him. He now answers the accumulated voice-mail messages when he has downtime between meetings.

E&Y’s hard-charging Wanner used to answer e-mail constantly throughout the day—whenever he heard a “ping.” Then he created a ritual of checking his e-mail just twice a day—at 10:15 AM and 2:30 PM. Whereas previously he couldn’t keep up with all his messages, he discovered he could clear his in-box each time he opened it—the reward of fully focusing his

attention on e-mail for 45 minutes at a time. Wanner has also reset the expectations of all the people he regularly communicates with by e-mail. "I've told them if it's an emergency and they need an instant response, they can call me and I'll always pick up," he says. Nine months later he has yet to receive such a call.

Michael Henke, a senior manager at E&Y, sat his team down at the start of the busy season last winter and told them that at certain points during the day he was going to turn off his Sametime (an in-house instant-message system). The result, he said, was that he would be less available to them for questions. Like Wanner, he told his team to call him if any emergency arose, but they rarely did. He also encouraged the group to take regular breaks throughout the day and to eat more regularly. They finished the busy season under budget and more profitable than other teams that hadn't followed the energy renewal program. "We got the same amount of work done in less time," says Henke. "It made for a win-win."

Another way to mobilize mental energy is to focus systematically on activities that have the most long-term leverage. Unless people intentionally schedule time for more challenging work, they tend not to get to it at all or rush through it at the last minute. Perhaps the most effective focus ritual the executives we work with have adopted is to identify each night the most important challenge for the next day and make it their very first priority when they arrive in the morning. Jean Luc Duquesne, a vice president for Sony Europe in Paris, used to answer his e-mail as soon as he got to the office, just as many people do. He now tries to concentrate the first hour of every day on the most important topic. He finds that he often emerges at 10 AM feeling as if he's already had a productive day.

The Human Spirit: Energy of Meaning and Purpose

People tap into the energy of the human spirit when their everyday work and activities are consistent with what they value most and with what gives them a sense of meaning and purpose. If the work they're doing really matters to them, they typically feel more positive energy, focus better, and demonstrate greater perseverance. Regrettably, the high demands and fast pace of corporate life don't leave much time to pay attention to these issues, and many people don't even recognize meaning and purpose as potential sources of energy. Indeed, if we tried to begin our program by focusing on the human spirit, it would likely have minimal impact. Only when participants have experienced the value of the rituals they establish in the other dimensions do they start to see that being attentive to their own deeper needs dramatically influences their effectiveness and satisfaction at work.

For E&Y partner Jonathan Anspacher, simply having the opportunity to ask himself a series of questions about what really mattered to him was both illuminating and energizing. "I think it's important to be a little introspective and say, 'What do you want to be remembered for?'" he told us. "You don't want to be remembered as the crazy partner who worked these long hours and had his people be miserable. When my kids call me and ask, 'Can you come to my band concert?' I want to say, 'Yes, I'll be there and I'll be in the front row.' I don't want to be the father that comes in and sits in the back and is on his Blackberry and has to step out to take a phone call."

To access the energy of the human spirit, people need to clarify priorities and establish accompanying rituals in three categories: doing what they do best and enjoy most at work; consciously allocating time and energy to the areas of their lives—work, family, health, service to others—they deem most important; and living their core values in their daily behaviors.

When you're attempting to discover what you do best and what you enjoy most, it's important to realize that these two things aren't necessarily mutually inclusive. You may get lots of positive feedback about something you're very good at but not truly enjoy it. Conversely, you can love doing

something but have no gift for it, so that achieving success requires much more energy than it makes sense to invest.

To help program participants discover their areas of strength, we ask them to recall at least two work experiences in the past several months during which they found themselves in their “sweet spot”—feeling effective, effortlessly absorbed, inspired, and fulfilled. Then we have them deconstruct those experiences to understand precisely what energized them so positively and what specific talents they were drawing on. If leading strategy feels like a sweet spot, for example, is it being in charge that’s most invigorating or participating in a creative endeavor? Or is it using a skill that comes to you easily and so feels good to exercise? Finally, we have people establish a ritual that will encourage them to do more of exactly that kind of activity at work.

A senior leader we worked with realized that one of the activities he least liked was reading and summarizing detailed sales reports, whereas one of his favorites was brainstorming new strategies. The leader found a direct report who loved immersing himself in numbers and delegated the sales report task to him—happily settling for brief oral summaries from him each day. The leader also began scheduling a free-form 90-minute strategy session every other week with the most creative people in his group.

In the second category, devoting time and energy to what’s important to you, there is often a similar divide between what people say is important and what they actually do. Rituals can help close this gap. When Jean Luc Duquesne, the Sony Europe vice president, thought hard about his personal priorities, he realized that spending time with his family was what mattered most to him, but it often got squeezed out of his day. So he instituted a ritual in which he switches off for at least three hours every evening when he gets home, so he can focus on his family. “I’m still not an expert on PlayStation,” he told us, “but according to my youngest son, I’m learning and I’m a good student.” Steve Wanner, who used to talk on the cell phone all the way to his front door on his commute home, has chosen a specific spot 20 minutes from his house where he ends whatever call he’s on and puts away the phone. He spends the rest of his commute relaxing so that when he does arrive home, he’s less preoccupied with work and more available to his wife and children.

The third category, practicing your core values in your everyday behavior, is a challenge for many as well. Most people are living at such a furious pace that they rarely stop to ask themselves what they stand for and who they want to be. As a consequence, they let external demands dictate their actions.

We don't suggest that people explicitly define their values, because the results are usually too predictable. Instead, we seek to uncover them, in part by asking questions that are inadvertently revealing, such as, "What are the qualities that you find most off-putting when you see them in others?" By describing what they can't stand, people unintentionally divulge what they stand for. If you are very offended by stinginess, for example, generosity is probably one of your key values. If you are especially put off by rudeness in others, it's likely that consideration is a high value for you. As in the other categories, establishing rituals can help bridge the gap between the values you aspire to and how you currently behave. If you discover that consideration is a key value, but you are perpetually late for meetings, the ritual might be to end the meetings you run five minutes earlier than usual and intentionally show up five minutes early for the meeting that follows.

Addressing these three categories helps people go a long way toward achieving a greater sense of alignment, satisfaction, and well-being in their lives on and off the job. Those feelings are a source of positive energy in their own right and reinforce people's desire to persist at rituals in other energy dimensions as well.

This new way of working takes hold only to the degree that organizations support their people in adopting new behaviors. We have learned, sometimes painfully, that not all executives and companies are prepared to embrace the notion that personal renewal for employees will lead to better and more sustainable performance. To succeed, renewal efforts need solid support and commitment from senior management, beginning with the key decision maker.

At Wachovia, Susanne Svizeny, the president of the region in which we conducted our study, was the primary cheerleader for the program. She embraced the principles in her own life and made a series of personal changes, including a visible commitment to building more regular renewal rituals into her work life. Next, she took it upon herself to foster the excitement and commitment of her leadership team. Finally, she regularly reached out by e-mail to all participants in the project to encourage them in their rituals and seek their feedback. It was clear to everyone that she took the

work seriously. Her enthusiasm was infectious, and the results spoke for themselves.

At Sony Europe, several hundred leaders have embraced the principles of energy management. Over the next year, more than 2,000 of their direct reports will go through the energy renewal program. From Fujio Nishida on down, it has become increasingly culturally acceptable at Sony to take intermittent breaks, work out at midday, answer e-mail only at designated times, and even ask colleagues who seem irritable or impatient what stories they're telling themselves.

Organizational support also entails shifts in policies, practices, and cultural messages. A number of firms we worked with have built "renewal rooms" where people can regularly go to relax and refuel. Others offer subsidized gym memberships. In some cases, leaders themselves gather groups of employees for midday workouts. One company instituted a no-meeting zone between 8 and 9 AM to ensure that people had at least one hour absolutely free of meetings. At several companies, including Sony, senior leaders collectively agreed to stop checking e-mail during meetings as a way to make the meetings more focused and efficient.

One factor that can get in the way of success is a crisis mentality. The optimal candidates for energy renewal programs are organizations that are feeling enough pain to be eager for new solutions but not so much that they're completely overwhelmed. At one organization where we had the active support of the CEO, the company was under intense pressure to grow rapidly, and the senior team couldn't tear themselves away from their focus on immediate survival—even though taking time out for renewal might have allowed them to be more productive at a more sustainable level.

By contrast, the group at Ernst & Young successfully went through the process at the height of tax season. With the permission of their leaders, they practiced defusing negative emotions by breathing or telling themselves different stories, and alternated highly focused periods of work with renewal breaks. Most people in the group reported that this busy season was the least stressful they'd ever experienced.

The implicit contract between organizations and their employees today is that each will try to get as much from the other as they can, as quickly as possible, and then move on without looking back. We believe that is mutually self-defeating. Both individuals and the organizations they work for end up depleted rather than enriched. Employees feel increasingly beleaguered and

burned out. Organizations are forced to settle for employees who are less than fully engaged and to constantly hire and train new people to replace those who choose to leave. We envision a new and explicit contract that benefits all parties: Organizations invest in their people across all dimensions of their lives to help them build and sustain their value. Individuals respond by bringing all their multidimensional energy wholeheartedly to work every day. Both grow in value as a result.

Originally published in October 2007. Reprint R0710B

Overloaded Circuits

by Edward M. Hallowell

DAVID DRUMS HIS FINGERS on his desk as he scans the e-mail on his computer screen. At the same time, he's talking on the phone to an executive halfway around the world. His knee bounces up and down like a jackhammer. He intermittently bites his lip and reaches for his constant companion, the coffee cup. He's so deeply involved in multitasking that he has forgotten the appointment his Outlook calendar reminded him of 15 minutes ago.

Jane, a senior vice president, and Mike, her CEO, have adjoining offices so they can communicate quickly, yet communication never seems to happen. "Whenever I go into Mike's office, his phone lights up, my cell phone goes off, someone knocks on the door, he suddenly turns to his screen and writes an e-mail, or he tells me about a new issue he wants me to address," Jane complains. "We're working flat out just to stay afloat, and we're not getting anything important accomplished. It's driving me crazy."

David, Jane, and Mike aren't crazy, but they're certainly crazed. Their experience is becoming the norm for overworked managers who suffer—like many of your colleagues, and possibly like you—from a very real but unrecognized neurological phenomenon that I call attention deficit trait, or ADT. Caused by brain overload, ADT is now epidemic in organizations. The core symptoms are distractibility, inner frenzy, and impatience. People with ADT have difficulty staying organized, setting priorities, and managing time. These symptoms can undermine the work of an otherwise gifted executive. If David, Jane, Mike, and the millions like them understood themselves in neurological terms, they could actively manage their lives instead of reacting

to problems as they happen.

As a psychiatrist who has diagnosed and treated thousands of people over the past 25 years for a medical condition called attention deficit disorder, or ADD (now known clinically as attention-deficit/ hyperactivity disorder), I have observed firsthand how a rapidly growing segment of the adult population is developing this new, related condition. The number of people with ADT coming into my clinical practice has mushroomed by a factor of ten in the past decade. Unfortunately, most of the remedies for chronic overload proposed by time-management consultants and executive coaches do not address the underlying causes of ADT.

Unlike ADD, a neurological disorder that has a genetic component and can be aggravated by environmental and physical factors, ADT springs entirely from the environment. Like the traffic jam, ADT is an artifact of modern life. It is brought on by the demands on our time and attention that have exploded over the past two decades. As our minds fill with noise—feckless synaptic events signifying nothing—the brain gradually loses its capacity to attend fully and thoroughly to anything.

The symptoms of ADT come upon a person gradually. The sufferer doesn't experience a single crisis but rather a series of minor emergencies while he or she tries harder and harder to keep up. Shouldering a responsibility to “suck it up” and not complain as the workload increases, executives with ADT do whatever they can to handle a load they simply cannot manage as well as they'd like. The ADT sufferer therefore feels a constant low level of panic and guilt. Facing a tidal wave of tasks, the executive becomes increasingly hurried, curt, peremptory, and unfocused, while pretending that everything is fine.

To control ADT, we first have to recognize it. And control it we must, if we as individuals and organizational leaders are to be effective. In the following pages, I'll offer an analysis of the origins of ADT and provide some suggestions that may help you manage it.

Idea in Brief

Frenzied executives who fidget through meetings, miss appointments, and jab at the elevator's "door close" button aren't crazy—just crazed. They're suffering from a newly recognized neurological phenomenon called **attention deficit trait (ADT)**. Marked by distractibility, inner frenzy, and impatience, ADT prevents managers from clarifying priorities, making smart decisions, and managing their time. This insidious condition turns otherwise talented performers into harried underachievers. And it's reaching epidemic proportions.

ADT isn't an illness or character defect. It's our brains' natural response to exploding demands on our time and attention. As data increasingly floods our brains, we lose our ability to solve problems and handle the unknown. Creativity shrivels; mistakes multiply. Some sufferers eventually melt down.

How to control ADT's ravaging impact on performance? *Foster positive emotions* by connecting face-to-face with people you like throughout the day. *Take physical care of your brain* by getting enough sleep, eating healthfully, and exercising regularly. *Organize for ADT*, designating part of each day for thinking and planning, and setting up your office to foster mental functioning (for example, keeping part of your desk clear at all times).

These strategies may seem like no-brainers. But they'll help you vanquish the ADT demon before it can strike.

Attention Deficit Cousins

To understand the nature and treatment of ADT, it's useful to know something of its cousin, ADD.

Usually seen as a learning disability in children, ADD also afflicts about 5% of the adult population. Researchers using MRI scans have found that people with ADD suffer a slightly diminished volume in four specific brain regions that have various functions such as modulating emotion (especially anger and frustration) and assisting in learning. One of the regions, made up of the frontal and prefrontal lobes, generates thoughts, makes decisions, sets priorities, and organizes activities. While the medications used to treat ADD don't change the anatomy of the brain, they alter brain chemistry, which in turn improves function in each of the four regions and so dramatically bolsters the performance of ADD sufferers.

Idea in Practice

How You Can Combat ADT

Promote positive emotions. Negative emotions—especially fear—can hamper productive brain functioning. To promote positive feelings, especially during highly stressful times, interact directly with someone you like at least every four to six hours. In environments where people are in physical contact with people they trust, brain functioning hums. By connecting comfortably with colleagues, you'll help your brain's "executive" center (responsible for decision making, planning, and information prioritizing) perform at its best.

Take physical care of your brain. Ample sleep, a good diet, and exercise are critical for staving off ADT. You're getting enough sleep if you can awake without an alarm clock. You're eating well if you're avoiding sugar and white flour and consuming more fruits, whole grains, vegetables, and protein instead. You're exercising enough if you're taking a brisk walk or going up and down a flight of stairs a few times a day.

Organize for ADT. Instead of getting sucked into the vortices of e-mail or voice mail first thing in the morning, attend to a critical task. With paperwork, apply the OHIO ("Only handle it once") rule: Whenever you touch a document, act on it, file it, or throw it away. Do crucial work during times of the day when you perform at your best. Use whatever small strategies help you function well mentally—whether it's listening to music or walking around while working, or doodling during meetings. And before you leave for the day, list three to five priority items you'll need to address tomorrow.

What Your Company Can Do. In firms that ignore ADT symptoms, employees underachieve, create clutter, and cut corners. Careless mistakes, illness, and turnover increase, as people squander their brainpower. To counteract ADT and harness employees' brainpower, invest in amenities that foster a positive, productive atmosphere.

Example: Major software company SAS Institute creates a warm, connected, and relaxed work environment by offering employees perks such as a seven-hour workday that ends at 5:00; large on-site gym and day-care facility; and cafeteria that provides baby seats and high chairs so parents can eat lunch with their children. The payoff? Employees return the favors with high productivity. And SAS's turnover never exceeds 5%—saving the company millions on recruiting, training, and severance.

ADD confers both disadvantages and advantages. The negative characteristics include a tendency to procrastinate and miss deadlines. People with ADD struggle with disorganization and tardiness; they can be forgetful and drift away mentally in the middle of a conversation or while reading. Their performance can be inconsistent: brilliant one moment and unsatisfactory the next. ADD sufferers also tend to demonstrate impatience and lose focus unless, oddly enough, they are under stress or handling multiple inputs. (This is because stress leads to the production of adrenaline, which is chemically similar to the medications we use to treat ADD.) Finally, people with ADD sometimes also self-medicate with excessive alcohol or other substances.

On the positive side, those with ADD usually possess rare talents and gifts. Those gifts often go unnoticed or undeveloped, however, because of the problems caused by the condition's negative symptoms. ADD sufferers can be remarkably creative and original. They are unusually persistent under certain circumstances and often possess an entrepreneurial flair. They display ingenuity and encourage that trait in others. They tend to improvise well under pressure. Because they have the ability to field multiple inputs simultaneously, they can be strong leaders during times of change. They also tend to rebound quickly after setbacks and bring fresh energy to the company every day.

Executives with ADD typically achieve inconsistent results. Sometimes they fail miserably because they're disorganized and make mistakes. At other times, they perform brilliantly, offering original ideas and strategies that lead to performance at the highest level.

David Neeleman, the CEO of JetBlue Airways, has ADD. School was torture; unable to focus, he hated to study and procrastinated endlessly. "I felt like I should be out doing things, moving things along, but here I was, stuck studying statistics, which I knew had no application to my life," Neeleman told me. "I knew I had to have an education, but at the first opportunity to start a business, I just blew out of college." He climbed quickly in the corporate world, making use of his strengths—original thinking, high energy, an ability to draw out the best in people—and getting help with organization and time management.

Like most people with ADD, Neeleman could sometimes offend with his blunt words, but his ideas were good enough to change the airline industry. For example, he invented the electronic ticket. "When I proposed that idea, people laughed at me, saying no one would go to the airport without a paper ticket," he says. "Now everyone does, and it has saved the industry millions of dollars." It seems fitting that someone with ADD would invent a way around having to remember to bring a paper ticket. Neeleman believes ADD is one of the keys to his success. Far from regretting having it, he celebrates it. But he understands that he must manage his ADD carefully.

Attention deficit trait is characterized by ADD's negative symptoms. Rather than being rooted in genetics, however, ADT is purely a response to the hyperkinetic environment in which we live. Indeed, modern culture all but requires many of us to develop ADT. Never in history has the human brain been asked to track so many data points. Everywhere, people rely on their cell phones, e-mail, and digital assistants in the race to gather and transmit data, plans, and ideas faster and faster. One could argue that the chief value of the modern era is speed, which the novelist Milan Kundera described as "the form of ecstasy that technology has bestowed upon modern man." Addicted to speed, we demand it even when we can't possibly go faster. James Gleick wryly noted in *Faster: The Acceleration of Just About Everything* that the "close door" button in elevators is often the one with the paint worn off. As the human brain struggles to keep up, it falters and then falls into the world of ADT.

This Is Your Brain

While brain scans cannot display anatomical differences between people with “normal” brains and people suffering from ADT, studies have shown that as the human brain is asked to process dizzying amounts of data, its ability to solve problems flexibly and creatively declines and the number of mistakes increases. To find out why, let’s go on a brief neurological journey.

Blessed with the largest cortex in all of nature, owners of this trillion-celled organ today put singular pressure on the frontal and prefrontal lobes, which I’ll refer to in this article as simply the frontal lobes. This region governs what is called, aptly enough, executive functioning (EF). EF guides decision making and planning; the organization and prioritization of information and ideas; time management; and various other sophisticated, uniquely human, managerial tasks. As long as our frontal lobes remain in charge, everything is fine.

Beneath the frontal lobes lie the parts of the brain devoted to survival. These deep centers govern basic functions like sleep, hunger, sexual desire, breathing, and heart rate, as well as crudely positive and negative emotions. When you are doing well and operating at peak level, the deep centers send up messages of excitement, satisfaction, and joy. They pump up your motivation, help you maintain attention, and don’t interfere with working memory, the number of data points you can keep track of at once. But when you are confronted with the sixth decision after the fifth interruption in the midst of a search for the ninth missing piece of information on the day that the third deal has collapsed and the 12th impossible request has blipped unbidden across your computer screen, your brain begins to panic, reacting just as if that sixth decision were a bloodthirsty, man-eating tiger.

As a specialist in learning disabilities, I have found that the most dangerous disability is not any formally diagnosable condition like dyslexia or ADD. It is fear. Fear shifts us into survival mode and thus prevents fluid learning and nuanced understanding. Certainly, if a real tiger is about to attack you, survival is the mode you want to be in. But if you’re trying to deal

intelligently with a subtle task, survival mode is highly unpleasant and counterproductive.

When the frontal lobes approach capacity and we begin to fear that we can't keep up, the relationship between the higher and lower regions of the brain takes an ominous turn. Thousands of years of evolution have taught the higher brain not to ignore the lower brain's distress signals. In survival mode, the deep areas of the brain assume control and begin to direct the higher regions. As a result, the whole brain gets caught in a neurological catch-22. The deep regions interpret the messages of overload they receive from the frontal lobes in the same way they interpret everything: primitively. They furiously fire signals of fear, anxiety, impatience, irritability, anger, or panic. These alarm signals shanghai the attention of the frontal lobes, forcing them to forfeit much of their power. Because survival signals are irresistible, the frontal lobes get stuck sending messages back to the deep centers saying, "Message received. Trying to work on it but without success." These messages further perturb the deep centers, which send even more powerful messages of distress back up to the frontal lobes.

Meanwhile, in response to what's going on in the brain, the rest of the body—particularly the endocrine, respiratory, cardiovascular, musculoskeletal, and peripheral nervous systems—has shifted into crisis mode and changed its baseline physiology from peace and quiet to red alert. The brain and body are locked in a reverberating circuit while the frontal lobes lose their sophistication, as if vinegar were added to wine. In this state, EF reverts to simpleminded black-and-white thinking; perspective and shades of gray disappear. Intelligence dims. In a futile attempt to do more than is possible, the brain paradoxically reduces its ability to think clearly.

This neurological event occurs when a manager is desperately trying to deal with more input than he possibly can. In survival mode, the manager makes impulsive judgments, angrily rushing to bring closure to whatever matter is at hand. He feels compelled to get the problem under control immediately, to extinguish the perceived danger lest it destroy him. He is robbed of his flexibility, his sense of humor, his ability to deal with the unknown. He forgets the big picture and the goals and values he stands for. He loses his creativity and his ability to change plans. He desperately wants to kill the metaphorical tiger. At these moments he is prone to melting down, to throwing a tantrum, to blaming others, and to sabotaging himself. Or he may go in the opposite direction, falling into denial and total avoidance of the

problems attacking him, only to be devoured. This is ADT at its worst.

Though ADT does not always reach such extreme proportions, it does wreak havoc among harried workers. Because no two brains are alike, some people deal with the condition better than others. Regardless of how well executives appear to function, however, no one has total control over his or her executive functioning.

Managing ADT

Unfortunately, top management has so far viewed the symptoms of ADT through the distorting lens of morality or character. Employees who seem unable to keep up the pace are seen as deficient or weak. Consider the case of an executive who came to see me when he was completely overloaded. I suggested he talk the situation over with his superior and ask for help. When my client did so, he was told that if he couldn't handle the work, he ought to think about resigning. Even though his performance assessments were stellar and he'd earned praise for being one of the most creative people in the organization, he was allowed to leave. Because the firm sought to preserve the myth that no straw would ever break its people's backs, it could not tolerate the manager's stating that his back was breaking. After he went out on his own, he flourished.

How can we control the rampaging effects of ADT, both in ourselves and in our organizations? While ADD often requires medication, the treatment of ADT certainly does not. ADT can be controlled only by creatively engineering one's environment and one's emotional and physical health. I have found that the following preventive measures go a long way toward helping executives control their symptoms of ADT.

Promote positive emotions

The most important step in controlling ADT is not to buy a superturbocharged BlackBerry and fill it up with to-dos but rather to create an environment in which the brain can function at its best. This means building a positive, fear-free emotional atmosphere, because emotion is the on/off switch for executive functioning.

There are neurological reasons why ADT occurs less in environments where people are in physical contact and where they trust and respect one another. When you comfortably connect with a colleague, even if you are dealing with an overwhelming problem, the deep centers of the brain send messages through the pleasure center to the area that assigns resources to the frontal lobes. Even when you're under extreme stress, this sense of human connection causes executive functioning to hum.

By contrast, people who work in physical isolation are more likely to suffer from ADT, for the more isolated we are, the more stressed we become. I witnessed a dramatic example of the danger of a disconnected environment and the healing power of a connected one when I consulted for one of the world's foremost university chemistry departments. In the department's formerly hard-driven culture, ADT was rampant, exacerbated by an ethic that forbade anyone to ask for help or even state that anything was wrong. People did not trust one another; they worked on projects alone, which led to more mistrust. Most people were in emotional pain, but implicit in the department's culture was the notion that great pain led to great gain.

In the late 1990s, one of the department's most gifted graduate students killed himself. His suicide note explicitly blamed the university for pushing him past his limit. The department's culture was literally lethal.

Instead of trying to sweep the tragedy under the rug, the chair of the department and his successor acted boldly and creatively. They immediately changed the structure of the supervisory system so that each graduate student and postdoc was assigned three supervisors, rather than a single one with a death grip on the trainee's career. The department set up informal biweekly buffets that allowed people to connect. (Even the most reclusive chemist

came out of hiding for food, one of life's great connectors.) The department heads went as far as changing the architecture of the department's main building, taking down walls and adding common areas and an espresso bar complete with a grand piano. They provided lectures and written information to all students about the danger signs of mental wear and tear and offered confidential procedures for students who needed help. These steps, along with regular meetings that included senior faculty and university administrators, led to a more humane, productive culture in which the students and faculty felt fully engaged. The department's performance remained first-rate, and creative research blossomed.

The bottom line is this: Fostering connections and reducing fear promote brainpower. When you make time at least every four to six hours for a "human moment," a face-to-face exchange with a person you like, you are giving your brain what it needs.

Take physical care of your brain

Sleep, a good diet, and exercise are critical for staving off ADT. Though this sounds like a no-brainer, too many of us abuse our brains by neglecting obvious principles of care.

You may try to cope with ADT by sleeping less, in the vain hope that you can get more done. This is the opposite of what you need to do, for ADT sets in when you don't get enough sleep. There is ample documentation to suggest that sleep deprivation engenders a host of problems, from impaired decision making and reduced creativity to reckless behavior and paranoia. We vary in how much sleep we require; a good rule of thumb is that you're getting enough sleep if you can wake up without an alarm clock.

Diet also plays a crucial role in brain health. Many hardworking people habitually inhale carbohydrates, which cause blood glucose levels to yo-yo. This leads to a vicious cycle: Rapid fluctuations in insulin levels further increase the craving for carbohydrates. The brain, which relies on glucose for energy, is left either glutted or gasping, neither of which makes for optimal cognitive functioning.

The brain does much better if the blood glucose level can be held relatively stable. To do this, avoid simple carbohydrates containing sugar and white flour (pastries, white bread, and pasta, for example). Rely on the complex carbohydrates found in fruits, whole grains, and vegetables. Protein is important: Instead of starting your day with coffee and a Danish, try tea and an egg or a piece of smoked salmon on wheat toast. Take a multivitamin every day as well as supplementary omega-3 fatty acids, an excellent source of which is fish oil. The omega-3s and the E and B complex contained in multivitamins promote healthy brain function and may even stave off Alzheimer's disease and inflammatory ills (which can be the starting point for major killers like heart disease, stroke, diabetes, and cancer). Moderate your intake of alcohol, too, because too much kills brain cells and accelerates the development of memory loss and even dementia. As you change your diet to promote optimal brain function and good general health, your body will also shed excess pounds.

If you think you can't afford the time to exercise, think again. Sitting at a desk for hours on end decreases mental acuity, not only because of reduced blood flow to the brain but for other biochemical reasons as well. Physical exercise induces the body to produce an array of chemicals that the brain loves, including endorphins, serotonin, dopamine, epinephrine, and norepinephrine, as well as two recently discovered compounds, brain-derived neurotrophic factor (BDNF) and nerve growth factor (NGF). Both BDNF and NGF promote cell health and development in the brain, stave off the ravages of aging and stress, and keep the brain in tip-top condition. Nothing stimulates the production of BDNF and NGF as robustly as physical exercise, which explains why those who exercise regularly talk about the letdown and sluggishness they experience if they miss their exercise for a few days. You will more than compensate for the time you invest on the treadmill with improved productivity and efficiency. To fend off the symptoms of ADT while you're at work, get up from your desk and go up and down a flight of stairs a few times or walk briskly down a hallway. These quick, simple efforts will push your brain's reset button.

Organize for ADT

It's important to develop tactics for getting organized, but not in the sense of empty New Year's resolutions. Rather, your goal is to order your work in a way that suits you, so that disorganization does not keep you from reaching your goals.

First, devise strategies to help your frontal lobes stay in control. These might include breaking down large tasks into smaller ones and keeping a section of your work space or desk clear at all times. (You do not need to have a neat office, just a neat section of your office.) Similarly, you might try keeping a portion of your day free of appointments, e-mail, and other distractions so that you have time to think and plan. Because e-mail is a wonderful way to procrastinate and set yourself up for ADT at the same time, you might consider holding specific "e-mail hours," since it isn't necessary to reply to every e-mail right away.

When you start your day, don't allow yourself to get sucked into vortices of e-mail or voice mail or into attending to minor tasks that eat up your time but don't pack a punch. Attend to a critical task instead. Before you leave for the day, make a list of no more than five priority items that will require your attention tomorrow. Short lists force you to prioritize and complete your tasks. Additionally, keep torrents of documents at bay. One of my patients, an executive with ADD, uses the OHIO rule: Only handle it once. If he touches a document, he acts on it, files it, or throws it away. "I don't put it in a pile," he says. "Piles are like weeds. If you let them grow, they take over everything."

Pay attention to the times of day when you feel that you perform at your best; do your most important work then and save the rote work for other times. Set up your office in a way that helps mental functioning. If you focus better with music, have music (if need be, use earphones). If you think best on your feet, work standing up or walk around frequently. If doodling or drumming your fingers helps, figure out a way to do so without bothering anyone, or get a fidget toy to bring to meetings. These small strategies sound mundane, but they address the ADT devil that resides in distracting details.

Protect your frontal lobes

To stay out of survival mode and keep your lower brain from usurping control, slow down. Take the time you need to comprehend what is going on, to listen, to ask questions, and to digest what's been said so that you don't get confused and send your brain into panic. Empower an assistant to ride herd on you; insist that he or she tell you to stop e-mailing, get off the telephone, or leave the office.

If you do begin to feel overwhelmed, try the following mind-clearing tricks. Do an easy rote task, such as resetting the calendar on your watch or writing a memo on a neutral topic. If you feel anxious about beginning a project, pull out a sheet of paper or fire up your word processor and write a paragraph about something unrelated to the project (a description of your house, your car, your shoes—anything you know well). You can also tackle the easiest part of the task; for example, write just the title of a memo about it. Open a dictionary and read a few definitions, or spend five minutes doing a crossword puzzle. Each of these little tasks quiets your lower brain by tricking it into shutting off alarmist messages and puts your frontal lobes back in full control.

Finally, be ready for the next attack of ADT by posting the sidebar “Control Your ADT” near your desk where you can see it. Knowing that you are prepared diminishes the likelihood of an attack, because you're not susceptible to panic.

Control Your ADT

In General

- Get adequate sleep.
- Watch what you eat. Avoid simple, sugary carbohydrates, moderate your intake of alcohol, add protein, stick to complex carbohydrates (vegetables, whole grains, fruit).
- Exercise at least 30 minutes at least every other day.
- Take a daily multivitamin and an omega-3 fatty acid supplement.

At Work

- Do all you can to create a trusting, connected work environment.
- Have a friendly, face-to-face talk with a person you like every four to six hours.
- Break large tasks into smaller ones.
- Keep a section of your work space or desk clear at all times.
- Each day, reserve some “think time” that’s free from appointments, e-mail, and phone calls.
- Set aside e-mail until you’ve completed at least one or two more important tasks.
- Before you leave work each day, create a short list of three to five items you will attend to the next day.
- Try to act on, file, or toss every document you touch.
- Don’t let papers accumulate.
- Pay attention to the times of day when you feel that you are at your best; do your most important work then, and save the rote work for

other times.

- Do whatever you need to do to work in a more focused way: Add background music, walk around, and so on.
- Ask a colleague or an assistant to help you stop talking on the telephone, e-mailing, or working too late.

When You Feel Overwhelmed

- Slow down.
- Do an easy rote task: Reset your watch, write a note about a neutral topic (such as a description of your house), read a few dictionary definitions, do a short crossword puzzle.
- Move around: Go up and down a flight of stairs or walk briskly.
- Ask for help, delegate a task, or brainstorm with a colleague. In short, do not worry alone.

What Leaders Can Do

All too often, companies induce and exacerbate ADT in their employees by demanding fast thinking rather than deep thinking. Firms also ask employees to work on multiple overlapping projects and initiatives, resulting in second-rate thinking. Worse, companies that ask their employees to do too much at once tend to reward those who say yes to overload while punishing those who choose to focus and say no.

Moreover, organizations make the mistake of forcing their employees to do more and more with less and less by eliminating support staff. Such companies end up losing money in the long run, for the more time a manager has to spend being his own administrative assistant and the less he is able to

delegate, the less effective he will be in doing the important work of moving the organization forward. Additionally, firms that ignore the symptoms of ADT in their employees suffer its ill effects: Employees underachieve, create clutter, cut corners, make careless mistakes, and squander their brainpower. As demands continue to increase, a toxic, high-pressure environment leads to high rates of employee illness and turnover.

To counteract ADT and harness employee brainpower, firms should invest in amenities that contribute to a positive atmosphere. One company that has done an excellent job in this regard is SAS Institute, a major software company in North Carolina. The company famously offers its employees a long list of perks: a 36,000-square-foot, on-site gym; a seven-hour workday that ends at 5 PM; the largest on-site day care facility in North Carolina; a cafeteria that provides baby seats and high chairs so parents can eat lunch with their children; unlimited sick days; and much more. The atmosphere at SAS is warm, connected, and relaxed. The effect on the bottom line is profoundly positive; turnover is never higher than 5%. The company saves the millions other software companies spend on recruiting, training, and severance (estimated to be at least 1.5 times salary in the software industry). Employees return the favors with high productivity. The forces of ADT that shred other organizations never gain momentum at SAS.

Leaders can also help prevent ADT by matching employees' skills to tasks. When managers assign goals that stretch people too far or ask workers to focus on what they're not good at rather than what they do well, stress rises. By contrast, managers who understand the dangers of ADT can find ways of keeping themselves and their organizations on track. JetBlue's David Neeleman, for example, has shamelessly and publicly identified what he is not good at and found ways to deal with his shortcomings, either by delegating or by empowering his assistant to direct him. Neeleman also models this behavior for everyone else in the organization. His openness about the challenges of his ADD gives others permission to speak about their own attention deficit difficulties and to garner the support they need. He also encourages his managers to match people with tasks that fit their cognitive and emotional styles, knowing that no one style is best. Neeleman believes that helping people work to their strengths is not just a mark of sophisticated management; it's also an excellent way to boost worker productivity and morale.

ADT is a very real threat to all of us. If we do not manage it, it manages us. But an understanding of ADT and its ravages allows us to apply practical methods to improve our work and our lives. In the end, the most critical step an enlightened leader can take to address the problem of ADT is to name it. Bringing ADT out of the closet and describing its symptoms removes the stigma and eliminates the moral condemnation companies have for so long mistakenly leveled at overburdened employees. By giving people permission to ask for help and remaining vigilant for signs of stress, organizations will go a long way toward fostering more productive, well-balanced, and intelligent work environments.

Originally published in January 2005. Reprint R0501E

Be a Better Leader, Have a Richer Life

by Stewart D. Friedman

IN MY RESEARCH AND COACHING WORK over the past two decades, I have met many people who feel unfulfilled, overwhelmed, or stagnant because they are forsaking performance in one or more aspects of their lives. They aren't bringing their leadership abilities to bear in all of life's domains—work, home, community, and self (mind, body, and spirit). Of course, there will always be some tension among the different roles we play. But, contrary to the common wisdom, there's no reason to assume that it's a zero-sum game. It makes more sense to pursue excellent performance as a leader in all four domains—achieving what I call “four-way wins”—not trading off one for another but finding mutual value among them.

This is the main idea in a program called Total Leadership that I teach at the Wharton School and at companies and workshops around the world. “Total” because it's about the whole person and “Leadership” because it's about creating sustainable change to benefit not just you but the most important people around you.

Scoring four-way wins starts by taking a clear view of what you want from and can contribute to each domain of your life, now and in the future, with thoughtful consideration of the people who matter most to you and the expectations you have for one another. This is followed by systematically designing and implementing carefully crafted experiments—doing something new for a short period to see how it affects all four domains. If an experiment doesn't work out, you stop or adjust, and little is lost. If it does work out, it's a small win; over time these add up so that your overall efforts are focused

increasingly on what and who matter most. Either way, you learn more about how to lead in all parts of your life.

This process doesn't require inordinate risk. On the contrary, it works because it entails realistic expectations, short-term changes that are in your control, and the explicit support of those around you. Take, for instance, Kenneth Chen, a manager I met at a workshop in 2005. (All names in this article are pseudonyms.) His professional goal was to become CEO, but he had other goals as well, which on the face of it might have appeared conflicting. He had recently moved to Philadelphia and wanted to get more involved with his community. He also wished to strengthen bonds with his family. To further all of these goals, he decided to join a city-based community board, which would not only allow him to hone his leadership skills (in support of his professional goal) but also have benefits in the family domain. It would give him more in common with his sister, a teacher who gave back to the community every day, and he hoped his fiancée would participate as well, enabling them to do something together for the greater good. He would feel more spiritually alive and this, in turn, would increase his self-confidence at work.

Now, about three years later, he reports that he is not only on a community board with his fiancée but also on the formal succession track for CEO. He's a better leader in all aspects of his life because he is acting in ways that are more consistent with his values. He is creatively enhancing his performance in all domains of his life and leading others to improve their performance by encouraging them to better integrate the different parts of their lives, too.

Kenneth is not alone. Workshop participants assess themselves at the beginning and the end of the program, and they consistently report improvements in their effectiveness, as well as a greater sense of harmony among the once-competing domains of their lives. In a study over a four-month period of more than 300 business professionals (whose average age was about 35), their *satisfaction* increased by an average of 20% in their work lives, 28% in their home lives, and 31% in their community lives. Perhaps most significant, their satisfaction in the domain of the self—their physical and emotional health and their intellectual and spiritual growth—increased by 39%. But they also reported that their *performance* improved: at work (by 9%), at home (15%), in the community (12%), and personally (25%). Paradoxically, these gains were made even as participants spent less

time on work and more on other aspects of their lives. They're working smarter—and they're more focused, passionate, and committed to what they're doing.

Idea in Brief

Life's a zero-sum game, right? The more you strive to win in one dimension (e.g., your work), the more the other three dimensions (your self, your home, and your community) must lose. Not according to Friedman. You don't have to make trade-offs among life's domains. Nor should you: trading off can leave you feeling exhausted, unfulfilled, or isolated. And it hurts the people you care about most.

To excel in all dimensions of life, use Friedman's **Total Leadership** process. First, articulate who and what matters most in your life. Then experiment with small changes that enhance your satisfaction and performance in *all four domains*. For example, exercising three mornings a week gives you more energy for work and improves your self-esteem and health, which makes you a better parent and friend.

Friedman's research suggests that people who focus on the concept of Total Leadership have a 20%–39% increase in satisfaction in all life domains, and a 9% improvement in job performance—even while working shorter weeks.

While hundreds of leaders at all levels go through this program every year, you don't need a workshop to identify worthwhile experiments. The process is pretty straightforward, though not simple. In the sections that follow, I will give you an overview of the process and take you through the basics of designing and implementing experiments to produce four-way wins.

Idea in Practice

Total Leadership helps you mitigate a range of problems that stem from making trade-offs among the different dimensions of your life:

- Feeling **unfulfilled** because you're not doing what you love
- Feeling **inauthentic** because you're not acting according to your values
- Feeling **disconnected** from people who matter to you
- Feeling **exhausted** by trying to keep up with it all

To tackle such problems using Total Leadership, take these steps.

1. Reflect

For each of the four domains of your life—work, home, community, and self, reflect on how important each is to you, how much time and energy you devote to each, and how satisfied you are in each. Are there discrepancies between what is important to you and how you spend your time and energy? What is your overall life satisfaction?

2. Brainstorm Possibilities

Based on the insights you've achieved during your four-way reflection, brainstorm a long list of small experiments that may help you move closer to greater satisfaction in all four domains. These are new ways of doing things that would carry minimal risk and let you see results quickly. For example:

- Turning off cell phones during family dinners could help you sharpen your focus on the people who matter most to you.
- Exercising several times a week could give you more energy.

- Joining a club with coworkers could help you forge closer friendships with them.
- Preparing for the week ahead on Sunday evenings could help you sleep better and go into the new week refreshed.

3. Choose Experiments

Narrow the list of experiments you've brainstormed to the three most promising. They should:

- Improve your satisfaction and performance in all four dimensions of your life.
- Have effects viewed as positive by the people who matter to you in every dimension of your life.
- Be the most costly—in regret and missed opportunities—if you *don't* do them.
- Position you to practice skills you most want to develop and do more of what you *want* to be doing.

4. Measure Progress

Develop a scorecard for each experiment you've chosen. For example:

Exercise three mornings a week with spouse.

Life dimension	Experiment's goals	How I will measure success	Implementation steps
Work	Improved alertness and productivity	No caffeine to get through the day; more productive sales calls	• Get doctor's feedback on exercise plan. • Join gym. • Set alarm earlier on exercise days. • Tell coworkers, family, and friends about my plan, how I need their help, and how it will benefit them.
Home	Increased closeness with spouse	Fewer arguments with spouse	
Community	Greater strength to participate in athletic fundraising events with friends	Three 10K fundraising walks completed by end of year	
Self	Improved self-esteem	Greater confidence	

The Total Leadership Process

The Total Leadership concept rests on three principles:

- Be real: Act with authenticity by clarifying what's important.
- Be whole: Act with integrity by respecting the whole person.
- Be innovative: Act with creativity by experimenting with how things get done.

You begin the process by thinking, writing, and talking with peer coaches to identify your core values, your leadership vision, and the current alignment of your actions and values—clarifying what's important. Peer coaching is enormously valuable, at this stage and throughout, because an outside perspective provides a sounding board for your ideas, challenges you, gives you a fresh way to see the possibilities for innovation, and helps hold you accountable to your commitments.

You then identify the most important people—"key stakeholders"—in all domains and the performance expectations you have of one another. Then you talk with them: If you're like most participants, you'll be surprised to find that what, and how much, your key stakeholders actually need from you is different from, and less than, what you thought beforehand.

These insights create opportunities for you to focus your attention more intelligently, spurring innovative action. Now, with a firmer grounding in what's most important, and a more complete picture of your inner circle, you begin to see new ways of making life better, not just for you but for the people around you.

The next step is to design experiments and then try them out during a controlled period of time. The best experiments are changes that your stakeholders wish for as much as, if not more than, you do.

Designing Experiments

To pursue a four-way win means to produce a change intended to fulfill multiple goals that benefit each and every domain of your life. In the domain of work, typical goals for an experiment can be captured under these broad headings: taking advantage of new opportunities for increasing productivity, reducing hidden costs, and improving the work environment. Goals for home and community tend to revolve around improving relationships and contributing more to society. For the self, it's usually about improving health and finding greater meaning in life.

As you think through the goals for your experiment, keep in mind the interests and opinions of your key stakeholders and anyone else who might be affected by the changes you are envisioning. In exploring the idea of joining a community board, for instance, Kenneth Chen sought advice from his boss, who had served on many boards, and also from the company's charitable director and the vice president of talent. In this way, he got their support. His employers could see how his participation on a board would benefit the company by developing Kenneth's leadership skills and his social network.

Some experiments benefit only a single domain directly while having indirect benefits in the others. For example, setting aside three mornings a week to exercise improves your health directly but may indirectly give you more energy for your work and raise your self-esteem, which in turn might make you a better father and friend. Other activities—such as running a half-marathon with your kids to raise funds for a charity sponsored by your company—occur in, and directly benefit, all four domains simultaneously. Whether the benefits are direct or indirect, achieving a four-way win is the goal. That's what makes the changes sustainable: Everyone benefits. The expected gains need not accrue until sometime in the future, so keep in mind that some benefits may not be obvious—far-off career advancements, for instance, or a contact who might ultimately offer valuable connections.

Identify possibilities

Open your mind to what's possible and try to think of as many potential experiments as you can, describing in a sentence or two what you would do in each. This is a time to let your imagination run free. Don't worry about all the potential obstacles at this point.

At first blush, conceiving of experiments that produce benefits for all the different realms may seem a formidable task. After all, if it were easy, people wouldn't be feeling so much tension between work and the rest of their lives. But I've found that most people realize it's not that hard once they approach the challenge systematically. And, like a puzzle, it can be fun, especially if you keep in mind that experiments must fit your particular circumstances. Experiments can and do take myriad forms. But having sifted through hundreds of experiment designs, my research team and I have found that they tend to fall into nine general types. Use the nine categories described in the exhibit "How Can I Design an Experiment to Improve All Domains of My Life?" to organize your thinking.

How can I design an experiment to improve all domains of my life?

Our research has revealed that most successful experiments combine components of nine general categories. Thinking about possibilities in this way will make it easier for you to conceive of the small changes you can make that will mutually benefit your work, your home, your community, and yourself. Most experiments are a hybrid of some combination of these categories.

Tracking and Reflecting

Keeping a record of activities, thoughts, and feelings (and perhaps distributing it to friends, family, and coworkers) to assess progress on personal and professional goals, thereby increasing self-awareness and maintaining priorities.

Examples

- Record visits to the gym along with changes in energy levels
- Track the times of day when you feel most engaged or most lethargic

Planning and Organizing

Taking actions designed to better use time and prepare and plan for the future.

Examples

- Use a PDA for all activities, not just work
- Share your schedule with someone else
- Prepare for the week on Sunday evening

Rejuvenating and Restoring

Attending to body, mind, and spirit so that the tasks of daily living and working are undertaken with renewed power, focus, and commitment.

Examples

- Quit unhealthy physical habits (smoking, drinking)
- Make time for reading a novel
- Engage in activities that improve emotional and spiritual health (yoga, meditation, etc.)

Appreciating and Caring

Having fun with people (typically, by doing things with coworkers outside work), caring for others, and appreciating relationships as a way of bonding at a basic human level to respect the whole person, which increases trust.

Examples

- Join a book group or health club with coworkers
- Help your son complete his homework
- Devote one day a month to community service

Focusing and Concentrating

Being physically present, psychologically present, or both when needed to pay attention to stakeholders who matter most. Sometimes this means saying no to opportunities or obligations. Includes attempts to show more respect to important people encountered in different domains and the need to be accessible to them.

Examples

- Turn off digital communication devices at a set time

- Set aside a specific time to focus on one thing or person
- Review e-mail at preset times during the day

Revealing and Engaging

Sharing more of yourself with others—and listening—so they can better support your values and the steps you want to take toward your leadership vision. By enhancing communication about different aspects of life, you demonstrate respect for the whole person.

Examples

- Have weekly conversations about religion with spouse
- Describe your vision to others
- Mentor a new employee

Time Shifting and “Re-Placing”

Working remotely or during different hours to increase flexibility and thus better fit in community, family, and personal activities while increasing efficiency; questioning traditional assumptions and trying new ways to get things done.

Examples

- Work from home
- Take music lessons during your lunch hour
- Do work during your commute

Delegating and Developing

Reallocating tasks in ways that increase trust, free up time, and develop skills in yourself and others; working smarter by reducing or eliminating low-priority activities.

Examples

- Hire a personal assistant
- Have a subordinate take on some of your responsibilities

Exploring and Venturing

Taking steps toward a new job, career, or other activity that better aligns your work, home, community, and self with your core values and aspirations.

Examples

- Take on new roles at work, such as a cross-functional assignment
- Try a new coaching style
- Join the board of your child's day care center

One category of experiment involves changes in where and when work gets done. One workshop participant, a sales director for a global cement producer, tried working online from his local public library one day a week to free himself from his very long commute. This was a break from a company culture that didn't traditionally support employees working remotely, but the change benefited everyone. He had more time for outside interests, and he was more engaged and productive at work.

Another category has to do with regular self-reflection. As an example, you might keep a record of your activities, thoughts, and feelings over the course of a month to see how various actions influence your performance and quality of life. Still another category focuses on planning and organizing your time—such as trying out a new technology that coordinates commitments at work with those in the other domains.

Conversations about work and the rest of life tend to emphasize segmentation: How do I shut out the office when I am with my family? How can I eliminate distractions and concentrate purely on work? But, in some cases, it might be better to make boundaries between domains more

permeable, not thicker. The very technologies that make it hard for us to maintain healthy boundaries among domains also enable us to blend them in ways—unfathomable even a decade ago—that can render us more productive and more fulfilled. These tools give us choices. The challenge we all face is learning how to use them wisely, and smart experiments give you an opportunity to increase your skill in doing so. The main point is to identify possibilities that will work well in your unique situation.

All effective experiments require that you question traditional assumptions about how things get done, as the sales director did. It's easier to feel free to do this, and to take innovative action, when you know that your goal is to improve performance in all domains and that you'll be gathering data about the impact of your experiment to determine if indeed it is working—for your key stakeholders and for you.

Whatever type you choose, the most useful experiments feel like something of a stretch: not too easy, not too daunting. It might be something quite mundane for someone else, but that doesn't matter. What's critical is that *you* see it as a moderately difficult challenge.

Choose a few, get started, and adapt

Coming up with possibilities is an exercise in unbounded imagination. But when it comes time to take action, it's not practical to try out more than three experiments at once. Typically, two turn out to be relatively successful and one goes haywire, so you will earn some small wins, and learn something useful about leadership, without biting off more than you can chew. Now the priority is to narrow the list to the three most-promising candidates by reviewing which will:

- Give you the best overall return on your investment
- Be the most costly in regret and missed opportunities if you don't do it
- Allow you to practice the leadership skills you most want to develop
- Be the most fun by involving more of what you want to be doing
- Move you furthest toward your vision of how you want to lead your life

Once you choose and begin to move down the road with your experiment, however, be prepared to adapt to the unforeseen. Don't become too wedded to the details of any one experiment's plan, because you will at some point be surprised and need to adjust. An executive I'll call Lim, for example, chose as one experiment to run the Chicago Marathon. He had been feeling out of shape, which in turn diminished his energy and focus both at work and at home. His wife, Joanne, was pregnant with their first child and initially supported the plan because she believed that the focus required by the training and the physical outlet it provided would make Lim a better father. The family also had a strong tradition of athleticism, and Joanne herself was an accomplished athlete. Lim was training with his boss and other colleagues, and all agreed that it would be a healthy endeavor that would improve professional communication (as they thought there would be plenty of time to bond during training).

But as her delivery date approached, Joanne became apprehensive, which

she expressed to Lim as concern that he might get injured. Her real concern, though, was that he was spending so much time on an activity that might drain his energy at a point when the family needed him most. One adjustment that Lim made to reassure Joanne of his commitment to their family was to initiate another experiment in which he took the steps needed to allow him to work at home on Thursday afternoons. He had to set up some new technologies and agree to send a monthly memo to his boss summarizing what he was accomplishing on those afternoons. He also bought a baby sling, which would allow him to keep his new son with him while at home.

In the end, not only were Joanne and their baby on hand to cheer Lim on while he ran the marathon, but she ended up joining him for the second half of the race to give him a boost when she saw his energy flagging. His business unit's numbers improved during the period when he was training and working at home. So did the unit's morale—people began to see the company as more flexible, and they were encouraged to be more creative in how they got their own work done—and word got around. Executives throughout the firm began to come up with their own ideas for ways to pay more attention to other sides of their employees' lives and so build a stronger sense of community at work.

The investment in a well-designed experiment almost always pays off because you learn how to lead in new and creative ways in all parts of your life. And if your experiments turn out well—as they usually, but not always, do—it will benefit everyone: you, your business, your family, and your community.

Measuring Progress

The only way to fail with an experiment is to fail to learn from it, and this makes useful metrics essential. No doubt it's better to achieve the results you are after than to fall short, but hitting targets does not in itself advance you toward becoming the leader you want to be. Failed experiments give you, and those around you, information that helps create better ones in the future.

The exhibit “How Do I Know If My Experiment Is Working?” shows how Kenneth Chen measured his progress. He used this simple chart to spell out the intended benefits of his experiment in each of the four domains and how he would assess whether he had realized these benefits. To set up your own scorecard, use a separate sheet for each experiment; at the top of the page, write a brief description of it. Then record your goals for each domain in the first column. In the middle column, describe your results metrics: how you will measure whether the goals for each domain have been achieved. In the third column, describe your action metrics—the plan for the steps you will take to implement your experiment. As you begin to implement your plan, you may find that your initial indicators are too broad or too vague, so refine your scorecard as you go along to make it more useful for you. The main point is to have practical ways of measuring your outcomes and your progress toward them, and the approach you take only needs to work for you and your stakeholders.

How do I know if my experiment is working?

Using this tool, an executive I'll call Kenneth Chen systematically set out in detail his various goals, the metrics he would use to measure his progress, and the steps he would take in conducting an experiment that would further those goals—joining the board of a nonprofit organization. Kenneth's work sheet is merely an example: Every person's experiments, goals, and metrics are unique.

A Sample Scorecard

	EXPERIMENT'S GOALS	HOW I WILL MEASURE SUCCESS	IMPLEMENTATION STEPS
Work	▶ To fulfill the expectation that executives will give back to the local community ▶ To establish networks with other officers in my company and other professionals in the area ▶ To learn leadership skills from other board members and from the organization I join	▶ Collect business cards from everyone I meet on the board and during board meetings, and keep track of the number of professionals I meet ▶ After each meeting, regularly record the leadership skills of those I would like to emulate	☐ Meet with my manager, who has sat on many boards and can provide support and advice ☐ Meet with the director of my company's foundation to determine my real interests and to help assess what relationship our firm has with various community organizations ☐ Discuss my course of action with my fiancée and see whether joining a board interests her ☐ Sign up to attend the December 15 overview session of the Business on Board program ☐ Assess different opportunities within the community and then reach out to organizations I'm interested in ☐ Apply for membership to a community board
Home	▶ To join a board that can involve my fiancée, Celine ▶ To have something to discuss with my sister (a special-education instructor)	▶ See whether Celine gets involved in the board ▶ Record the number of conversations my sister and I have about community service for the next three months and see whether they have brought us closer	
Community	▶ To provide my leadership skills to a nonprofit organization ▶ To get more involved in giving back to the community	▶ Record what I learn about each nonprofit organization I research ▶ Record the number of times I attend board meetings	
Self	▶ To feel good about contributing to others' welfare ▶ To see others grow as a result of my efforts ▶ To become more compassionate	▶ Assess how I feel about myself in a daily journal ▶ Assess the effect I have on others in terms of potential number of people affected ▶ Ask for feedback from others about whether I've become more compassionate	

Workshop participants have used all kinds of metrics: cost savings from reduced travel, number of e-mail misunderstandings averted, degree of

satisfaction with family time, hours spent volunteering at a teen center, and so on. Metrics may be objective or subjective, qualitative or quantitative, reported by you or by others, and frequently or intermittently observed. When it comes to frequency, for instance, it helps to consider how long you'll be able to remember what you did. For example, if you were to go on a diet to get healthier, increase energy, and enhance key relationships, food intake would be an important metric. But would you be able to remember what you ate two days ago?

Small Wins for Big Change

Experiments shouldn't be massive, all-encompassing shifts in the way you live. Highly ambitious designs usually fail because they're too much to handle. The best experiments let you try something new while minimizing the inevitable risks associated with change. When the stakes are smaller, it's easier to overcome the fear of failure that inhibits innovation. You start to see results, and others take note, which both inspires you to go further and builds support from your key stakeholders.

Another benefit of the small-wins approach to experiments is that it opens doors that would otherwise be closed. You can say to people invested in the decision, "Let's just try this. If it doesn't work, we'll go back to the old way or try something different." By framing an experiment as a trial, you reduce resistance because people are more likely to try something new if they know it's not permanent and if they have control over deciding whether the experiment is working according to *their* performance expectations.

But "small" is a relative term—what might look like a small step for you could seem like a giant leap to me, and vice versa. So don't get hung up on the word. What's more, this isn't about the scope or importance of the changes you eventually make. Large-scale change is grounded in small steps toward a big idea. So while the steps in an experiment might be small, the goals are not. Ismail, a successful 50-year-old entrepreneur and CEO of an engineering services company, described the goal for his first experiment this way: "Restructure my company and my role in it." There's nothing small about that. He felt he was missing a sense of purpose.

Ismail designed practical steps that would allow him to move toward his large goal over time. His first experiments were small and achievable. He introduced a new method that both his colleagues and his wife could use to communicate with him. He began to hold sacrosanct time for his family and his church. As he looked for ways to free up more time, he initiated delegation experiments that had the effect of flattening his organization's structure. These small wins crossed over several domains, and eventually he

did indeed transform his company and his own role in it. When I spoke with him 18 months after he'd started, he acknowledged that he'd had a hard time coping with the loss of control over tactical business matters, but he described his experiments as "a testament to the idea of winning the small battles and letting the war be won as a result." He and his leadership team both felt more confident about the firm's new organizational structure.

People try the Total Leadership program for a variety of reasons. Some feel unfulfilled because they're not doing what they love. Some don't feel genuine because they're not acting according to their values. Others feel disconnected, isolated from people who matter to them. They crave stronger relationships, built on trust, and yearn for enriched social networks. Still others are just in a rut. They want to tap into their creative energy but don't know how (and sometimes lack the courage) to do so. They feel out of control and unable to fit in all that's important to them.

My hunch is that there are more four-way wins available to you than you'd think. They are there for the taking. You have to know how to look for them and then find the support and zeal to pursue them. By providing a blueprint for how you can be real, be whole, and be innovative as a leader in all parts of your life, this program helps you perform better according to the standards of the most important people in your life; feel better in all the domains of your life; and foster greater harmony among the domains by increasing the resources available to you to fit all the parts of your life together. No matter what your career stage or current position, you can be a better leader and have a richer life—if you are ready and willing to rise to the challenge.

Originally published in April 2008. Reprint R0804H

Reclaim Your Job

by Sumantra Ghoshal and Heike Bruch

ASK MOST MANAGERS WHAT GETS in the way of success at work, and you hear the familiar litany of complaints: Not enough time. Shrinking resources. Lack of opportunity. When you look more closely, you begin to see that these are, for the most part, excuses. What gets in the way of managers' success is something much more personal—a deep uncertainty about acting according to their own best judgment. Rather than doing what they really need to do to advance the company's fortunes—and their own careers—they spin their wheels doing what they presume everyone else wants them to do.

Over the past five years, we have studied hundreds of managers as they have gone about their daily work in a variety of settings, including a global airline and a large U.S. oil company. As we demonstrated in “Beware the Busy Manager” (HBR February 2002), fully 90% of the managers we observed wasted their time and frittered away their productivity, despite having well-defined projects, goals, and the knowledge necessary to get their jobs done. Such managers remain trapped in inefficiency because they simply assume that they do not have enough personal discretion or control. The ability to seize initiative is the most essential quality of any truly successful manager.

In most instances, the demands that managers accept as givens are actually discretionary in nature. We have repeatedly confronted in our research a curious but pervasive reality of corporate life: Most managers complain about having too little freedom in their jobs, while their bosses complain about managers' failure to grasp opportunities. The truly effective

managers we've observed are purposeful, trust in their own judgment, and adopt long-term, big-picture views to fulfill personal goals that tally with those of the organization as a whole. They break out of their perceived boxes, take control of their jobs, and become more productive by learning to do the following:

Manage demands

Most managers feel overwhelmed by demands. They assume that the business will come to a crashing halt without them and so allow real or imagined day-to-day work demands to subsume their own judgment. Effective managers proactively control their tasks and the expectations of their major stakeholders, which allows them to meet strategic goals rather than fight fires.

Generate resources

By following what they believe are strict orders from the top, many typical managers tend to concentrate on working within budget and resource constraints—thereby developing a boxed-in, “can’t do” mind-set. By contrast, effective managers develop inventive strategies for circumventing real or imagined limitations. They map out ways around constraints by developing and acting on long-term strategies, making trade-offs, and occasionally breaking rules to achieve their goals.

Recognize and exploit alternatives

Average managers don't have enough perspective on the company's overall business strategy to present an alternative view. Effective managers, by contrast, develop and use deep expertise about an individual area that dovetails with the company's strategy. This tactic allows them to come up with a variety of innovative approaches to a given situation.¹

In short, truly effective managers don't operate in the context of individual tasks or jobs but in the much broader context of their organizations and careers. That approach sounds simple enough, but it is sometimes hard to act on because some organizational cultures that tout "empowerment" actually discourage volition among their managers. Young, high-tech companies, for example, sometimes hold their managers hostage to frenzy, thus inhibiting the reflective and persistent pursuit of long-term goals. Other cultures—particularly those of old and established corporations with command-and-control hierarchies—can encourage people to go along with the status quo, regardless of the level of organizational dysfunction. In both kinds of environments, managers tend to fall into a reactive state of mind, assuming that any initiative they show will be either ignored or discouraged.

Idea in Brief

90% of managers waste time and fritter away their productivity by grappling with an endless list of demands from others. Why? We assume—wrongly—that those demands are *requirements*, and that we lack personal discretion or control over our jobs. The consequence? We remain trapped in inefficiency.

But we can escape this trap—if we learn how to grasp opportunities, trust our own judgment, and methodically fulfill personal goals that tally with our organizations' objectives. The keys? Set priorities—then stick to them, focusing on efforts that support those priorities. Overcome resource constraints by attacking goals strategically, demonstrating success at every step. And develop a range of alternatives to exploit when plan A fails.

We all want to make a difference in our organizations, as well as build satisfying careers. By understanding how we inhibit ourselves and taking purposeful, strategic action, we can seize control of our jobs—rather than letting our jobs control us. The payoff? Impressive results for our companies and rewarding work lives for us.

In most cases, however, it is not the environment that inhibits managers from taking purposeful action. Rather, it is managers themselves. We have found that managers can learn to act on their own potential and make a difference. Here's how.

Dealing with Demands

Almost everyone complains about not having enough time to deal with all the demands on them, but, in reality, a highly fragmented day is also a very lazy day. It can seem easier to fight fires than to set priorities and stick to them. The truth is that managers who carefully set boundaries and priorities achieve far more than busy ones do.

Idea in Practice

To reclaim your job and better support your company's priorities, apply three strategies.

Prioritize Demands

To achieve personal and organizational goals quickly, *slow down* and focus your time and attention.

Example: McKinsey associate principal Jessica Spungin took on too many projects that had little connection to her skills and interests. Result? Her project teams rated her second from the bottom among her peers.

Realizing her desire to be indispensable sprang from lack of confidence, Spungin took steps to manage demands. She clarified her goal: to become a partner. Then she set long-term priorities supporting that goal. She began managing her own development; for example, choosing assignments that most interested her. And she started orchestrating her time, meeting only with people who really needed her and working on long-term projects during months when she traveled less.

Her reward? She scored second from the top in her peer group—and was named a McKinsey partner.

Liberate Resources

To relax resource constraints and win the backing you want, attack your goals strategically. Be patient. The process can take years.

Example: As the new head of HR development at airline Lufthansa, Thomas Sattelberger dreamed of launching Germany's first corporate business school. Knowing he needed several years to establish his credibility, he first overhauled inefficient HR

processes. He then developed initiatives supporting the school, raising money for these projects by presenting compelling facts and arguments to his counterparts and CEO.

After four years of methodical work on Sattelberger's part, Lufthansa's CEO and board understood how his programs fit together. When he wrote a memo to directors requesting creation of the school before Daimler-Benz could beat Lufthansa to the punch, the board promptly approved the request.

Exploit Alternatives

Use your expertise to anticipate—and circumvent—possible obstacles to your goals. You'll expand the scope of opportunity for your company *and* yourself.

Example: Dan Andersson, a manager at oil refiner Conoco-Phillips, was part of a team exploring Conoco's entrance into the Finnish market. Conoco decided to store petrol in tanks in Finland that Shell had abandoned. But Andersson developed contingency plans. Plan B, for instance, involved building a new facility.

His efforts paid off. When research revealed the abandoned tanks were unsuitable for petrol storage, Andersson activated Plan B. Though the new-facility target site was contaminated, Andersson discovered that Shell was responsible for cleaning the site. Once cleanup ended, Conoco built the tanks.

Conoco became the most efficient operator of automated self-service filling stations in Finland. Andersson now heads Conoco's retail development in Europe.

To beat the busy habit, managers must overcome the psychological desire to be indispensable. Because their work is interactive and interdependent, most managers thrive on their sense of importance to others. When they are not worrying about meeting their superiors' (or their clients') expectations, they fret about their direct reports, often falling victim to the popular fallacy

that good bosses always make themselves available. At first, managers—particularly novices—seem to thrive on all this clamoring for their time; the busier they are, the more valuable they feel. Inevitably, however, things start to slip. Eventually, many managers simply burn out and fail, not only because they find little time to pursue their own agendas but also because, in trying to please everyone, they typically end up pleasing no one.

Jessica Spungin found herself caught in this trap when she was promoted to associate principal in McKinsey's London office. As an AP, a consultant is expected to take on more responsibilities of the partnership group, juggle multiple projects, serve as a team leader, and play an active role in office life. Spungin dove in to all these tasks headfirst. While she was handling two major client projects, she was asked to jointly lead recruitment for U.K. universities and business schools, participate in an internal research initiative, serve as a senior coach for six business analysts, run an office party for 750 people, get involved in internal training, and help out on a new project for a health care company.

In her first round of feedback from the three project teams she oversaw, she was rated second from the bottom among her peers. Spungin realized that her desire to be indispensable sprang from a lack of confidence. "I never said no to people in case they thought I couldn't cope. I never said no to a client who wanted me to be present at a meeting," she told us. "I did what I thought was expected—regardless of what I was good at, what was important, or what I could physically do."

The first step in Spungin's transformation from a busy to an effective manager was to develop a vision of what she really wanted to achieve at McKinsey: to be named a partner. In developing a clear mental picture of herself in that role, she traded in her habit of thinking in short time spans of three to six months to thinking in strategic time spans of one to five years.

This longer-term planning allowed Spungin to develop a set of long-term goals and priorities. Soon, she took control of her own development. For example, it became clear to Spungin that corporate banking—which her colleagues believed to be her area of expertise based on her past experience—did not hold any real interest for her, even though she had accepted one banking project after another. Instead, she decided to shift her focus to the organizational practice, something she really enjoyed. (McKinsey, like many companies, allows its consultants significant flexibility in terms of choosing assignments, but most managers do not avail themselves of this opportunity.)

By claiming a personal agenda and integrating short-, medium-, and long-term responsibilities into her broader master plan, Spungin felt much more motivated and excited about her work than she had when she was merely responding to everyday demands.

Finally, Spungin took charge of her time. She realized that trying to be accessible to everyone made her inaccessible to those who really needed her. She began prioritizing the time she spent with clients and team members. With her personal assistant's help, she streamlined her work. Previously, her assistant would schedule meetings in an ad hoc manner. Now, Spungin drove the calendar, so she could make the calls about which meetings she needed to attend. She began to recognize patterns of work intensity according to the time of year; for example, she travelled less in the fall, so Spungin set aside half a day each week to work on her long-term projects then. In the end, Spungin realized the irony of effective management: To quickly achieve the goals that mattered, she had to slow down and take control. To her surprise, the people who reported to her, as well as her supervisors and clients, responded well to her saying no.

Spungin was better able to respond to and shape the demands she chose to meet once she stopped trying to please everyone. She became more proactive—presenting her own goals and ideas to influence what others expected of her. By focusing on the most important demands, she exceeded expectations. One year after having been rated second from the bottom in her peer group, she scored second from the top. In June 2003, Spungin was named a McKinsey partner.

Developing Resources

In addition to lack of time, many managers complain about a shortage of people, money, and equipment, and a surplus of rules and regulations. They struggle with limited resources. While some feel frustrated and keep beating their heads against a wall to no avail, others just give up. Managers who develop a long-term strategy and attack their goals slowly, steadily, and strategically, on the other hand, can eventually win the backing they want.

Thomas Sattelberger faced all kinds of impossible constraints in 1994 when he left Daimler-Benz to join Lufthansa as the head of corporate management and human resources development. At the time, Lufthansa was in the middle of a strategic cost-savings program that required every unit to reduce its total expenditures by 4% each year for the next five years. Employees generally interpreted the cost-cutting directive to mean that investing in anything other than what was necessary to keep the lights on was verboten. Additionally, Lufthansa's HR processes were a mess; responses to routine requests often took months, and contracts frequently contained typographical errors. These kinds of operational problems had existed in the department for years.

For most managers in Sattelberger's position, the goals would have been simple: Get the HR department to a functional level without increasing costs, make sure it doesn't backslide, and collect a paycheck. But Sattelberger had much higher aspirations. He had come to Lufthansa with the dream of building Germany's most progressive corporate human resources organization, which would help transform the formerly state-operated company into a world-class airline. Specifically, he envisioned starting Germany's first corporate university, the Lufthansa School of Business, which would extend far beyond traditional approaches to training and development. The university would tighten the links between strategy and organizational and individual development. Its curricula, including master's and nondegree management programs, would be designed, run, and evaluated by academics and leaders from global companies, so Lufthansa's managers

would learn from the best.

In pursuing his dream, Sattelberger chose a methodical, clever, and patient mode of attack. First, he created an imaginary blueprint depicting his university as a kind of leadership development temple. The architectural conceit—the temple being built brick by brick and pillar by pillar—helped Sattelberger develop a long-term, strategic implementation plan. Cleaning up basic HR processes, he reasoned, was analogous to laying the foundation. With that accomplished, he would erect a series of development programs, each acting as a pillar that would hold up the “roof” of Lufthansa’s overall corporate strategy. Seeing his plan as a blueprint also helped Sattelberger separate the “must-haves” from the “nice-to-haves” and the “can-live-withouts,” which enabled him to focus on only the most vital and achievable elements.

Sattelberger understood that he had to be flexible and that building his temple would demand years of methodical work. He never spoke about his vision as a whole because its overall cost would have frightened most of the stakeholders. Instead, he secured their commitment for individual projects and programs and implemented the initiatives sequentially.

Step two was to lay the foundation that he had imagined. Over the course of two years, Sattelberger reorganized HR processes so that requests were met in a timely matter and operations made more efficient. Given the dismal state of Lufthansa’s HR systems, no one anticipated that Sattelberger could possibly meet, much less exceed, expectations. He showed them wrong.

Capitalizing on his new credibility, he next set to work on step three: building the individual pillars. One project, Explorer 21, was a comprehensive development initiative in which managers would learn from one another. A separate program, ProTeam, was designed for management trainees. And another large-scale program focused on emulating best practices from companies such as General Electric, Citibank, Deutsche Bank, Daimler-Benz, and SAS.

The spending cap was a significant hurdle. Sattelberger had persuaded top management to allow him to rent out some training rooms to other companies to raise money for these projects, but he needed more. He understood that there was a limit to how far and how fast he could push: If he pressed too hard, a backlash would ensue. So in petitioning for funds, Sattelberger made sure he was better prepared than his counterparts with arguments and facts. When the controller failed to give him the green light, he made his case

directly to Jürgen Weber, the CEO. Weber agreed in principle that the corporate university project was worthwhile, although the conversation was not an easy one. “For God’s sake, do it,” he ended up telling Sattelberger, “but do it right and stick to your budget.”

Weber and the board eventually began to see how Sattelberger’s development programs fit together. Then, in March 1998—when he learned that Daimler-Benz was about to beat Lufthansa to the punch with a corporate university of its own—Sattelberger made his final move. Determined not to let Daimler prevail, he wrote a memo requesting the creation of the Lufthansa School of Business to the board of directors. It approved the request without a moment’s hesitation or debate, and Lufthansa opened Europe’s first corporate university the following month.

The whole process took time, something purposeful managers, as we have shown previously, claim for themselves. Sattelberger coped with many setbacks and accepted significant delays and even cancellations of different aspects of his initiative. He delayed his plans for the corporate university for the first two years so he could focus solely on putting HR in order. Then, slowly and progressively, he worked to relax resource constraints. Although he started with much less than he expected, he never allowed his resolve to wither. Lufthansa has never measured the precise payback from its school of business, but the subjective judgment of top management is that the return has been much higher than the investment.

Exploiting Alternatives

When it comes to making decisions or pursuing initiatives, managers also fall victim to the trap of unexplored choices. Specifically, they either do not recognize that they have choices or do not take advantage of those they know they have. Because managers ignore their freedom to act, they surrender their options. Purposeful initiators, by contrast, hone their personal expertise, which confers confidence, a wide perspective of a particular arena, and greater credibility. These managers develop the ability to see, grasp, and fight for opportunities as they arise.

Dan Andersson was a midlevel manager who worked for the oil-refining company ConocoPhillips in Stockholm. As a native of Finland, he brought to Conoco a precious managerial commodity: deep knowledge of the Finnish market. This knowledge enabled him to convey information about specific regional conditions to senior managers, who did not speak the language or understand Finland's business issues. Because he had been mentored by the managing director of Conoco's Nordic operations, Andersson quickly grasped how the managerial invisibles—informal rules and norms, decision-making processes, interpersonal relationships, and social dynamics—influenced the reception of new ideas. He intuitively sensed the right way to present a proposal and the extent to which he could push at a particular point of time.

Andersson was assigned to a team charged with exploring Conoco's possible entrance into the Finnish market, which involved breaking a 50-year monopoly in the region. The first task was to set up storage facilities in Finland, an estimated \$1 million project that would allow Conoco to import its own petrol. After several months of intense searching, the team eventually found an existing tank terminal, located in the city of Turku, that Shell had abandoned decades previously. Built in the 1920s, the old tanks appeared to be clean and usable. The Conoco team thought the solution had been found. In the back of his mind, however, Andersson was already at work on contingency plans. Plan B was to build a new facility, plan C was to create a

joint venture with a competitor, and plan D was to find an investor for the tanks.

After months of negotiation, Turku's officials approved Conoco's lease of the old tanks. Then came the fateful phone call from Conoco's laboratory: There was too much carbon in the steel; the tanks were unsuitable for storing petrol. Without its own storage facility, Conoco could not enter the Finnish market. There was no other facility in the country that Conoco could buy. Abandoning the project seemed the only choice. Everyone on the team gave up except Andersson, who proposed putting plan B into action.

With the support of the local authorities, he persuaded the Conoco senior team to visit Finland for face-to-face discussions about the possibility of Conoco building its own tanks at the site. Once Andersson's boss saw the land and sensed the opportunity, he grew enthusiastic about a ground-up approach. As it happened, however, the land was contaminated; cleanup would have cost tens of millions of euros. Still, Andersson persisted. Working with city officials, he discovered the original contracts clearly showed that Shell was responsible for the cleanup of the land. Once the cleanup was complete, Conoco began work on the new tanks. When the first Conoco ship arrived at the harbor, three years after the project had begun, city representatives, hundreds of spectators, Finnish television crews, and Conoco's top management were present to celebrate. Today, Conoco is the most efficient operator of automated self-service filling stations in Finland.

As a manager, Andersson's allegiance was not merely to a job but to accomplishing, one way or another, the strategic goals of his company. By scanning the environment for possible obstacles and searching for ways around them, he was able to expand his company's, and his own, scope of opportunity. Today, he is responsible for ConocoPhillips' retail development in Europe.

A bias for action is not a special gift of a few. Most managers can develop this capacity. Spungin's story demonstrates how focusing on a clear, long-term goal widened her horizon. Sattelberger and Andersson countered limitations with plans of their own and showed their companies what was possible.

In our studies of managers, we have found that the difference between those who take the initiative and those who do not becomes particularly evident during phases of major change, when managerial work becomes relatively chaotic and unstructured. Managers who fret about conforming to the explicit or imagined expectations of others respond to lack of structure by becoming disoriented and paralyzed. Effective managers, by contrast, seize the opportunity to extend the scope of their jobs, expand their choices, and pursue ambitious goals.

Once managers command their agendas and sense their own freedom of choice, they come to relish their roles. They begin to search for situations that go beyond their scope and enjoy seizing opportunities as they arise. Above all, effective managers with a bias for action aren't managed by their jobs; rather, the reverse is true.

Originally published in March 2004. Reprint R0403B

Note

[1](#). The framework of demands, constraints, and choices as a way to think about managerial jobs was first suggested by Rosemary Stewart in her book *Managers and Their Jobs* (Macmillan, 1967). See also Rosemary Stewart, *Choices for the Manager* (Prentice Hall, 1982).

Moments of Greatness

Entering the Fundamental State of Leadership.

by Robert E. Quinn

AS LEADERS, SOMETIMES we're truly "on," and sometimes we're not. Why is that? What separates the episodes of excellence from those of mere competence? In striving to tip the balance toward excellence, we try to identify great leaders' qualities and behaviors so we can develop them ourselves. Nearly all corporate training programs and books on leadership are grounded in the assumption that we should study the behaviors of those who have been successful and teach people to emulate them.

But my colleagues and I have found that when leaders do their best work, they don't copy anyone. Instead, they draw on their own fundamental values and capabilities—operating in a frame of mind that is true to them yet, paradoxically, not their normal state of being. I call it the *fundamental state of leadership*. It's the way we lead when we encounter a crisis and finally choose to move forward. Think back to a time when you faced a significant life challenge: a promotion opportunity, the risk of professional failure, a serious illness, a divorce, the death of a loved one, or any other major jolt. Most likely, if you made decisions not to meet others' expectations but to suit what you instinctively understood to be right—in other words, if you were at your very best—you rose to the task because you were being tested.

Is it possible to enter the fundamental state of leadership without crisis? In my work coaching business executives, I've found that if we ask ourselves—and honestly answer—just four questions, we can make the shift at any time. It's a temporary state. Fatigue and external resistance pull us out of it. But each time we reach it, we return to our everyday selves a bit more capable, and we usually elevate the performance of the people around us as well. Over time, we all can become more effective leaders by deliberately choosing to enter the fundamental state of leadership rather than waiting for crisis to force

us there.

Defining the Fundamental State

Even those who are widely admired for their seemingly easy and natural leadership skills—presidents, prime ministers, CEOs—do not usually function in the fundamental state of leadership. Most of the time, they are in their normal state—a healthy and even necessary condition under many circumstances, but not one that’s conducive to coping with crisis. In the normal state, people tend to stay within their comfort zones and allow external forces to direct their behaviors and decisions. They lose moral influence and often rely on rational argument and the exercise of authority to bring about change. Others comply with what these leaders ask, out of fear, but the result is usually unimaginative and incremental—and largely reproduces what already exists.

To elevate the performance of others, we must elevate ourselves into the fundamental state of leadership. Getting there requires a shift along four dimensions. (See the exhibit “There’s Normal, and There’s Fundamental.”)

First, we move from being comfort centered to being results centered. The former feels safe but eventually leads to a sense of languishing and meaninglessness. In his book *The Path of Least Resistance*, Robert Fritz carefully explains how asking a single question can move us from the normal, reactive state to a much more generative condition. That question is this: What result do I want to create? Giving an honest answer pushes us off nature’s path of least resistance. It leads us from problem solving to purpose finding.

Idea in Brief

Like all leaders, sometimes you're "on," and sometimes you're not. How to tip the scale toward excellence and away from mere competence? Don't rely on imitating other leaders or poring over leadership manuals. Instead, enter the **fundamental state of leadership**: the way you lead when a crisis forces you to tap into your deepest values and instincts. In this state, you instinctively know what to do: You rise to the occasion and perform at your best.

Fortunately, you don't need a crisis to shift into the fundamental state of leadership. You can do so any time (before a crucial conversation, during a key meeting) by asking four questions:

- **"Am I results centered?"** Have you articulated the result you want to create?
- **"Am I internally directed?"** Are you willing to challenge others' expectations?
- **"Am I other focused?"** Have you put your organization's needs above your own?
- **"Am I externally open?"** Do you recognize signals suggesting the need for change?

No one can operate at the top of their game 24/7. But each time you enter the fundamental state of leadership, you make it easier to return to that state again. And you inspire others around you to higher levels of excellence.

Second, we move from being externally directed to being more internally directed. That means that we stop merely complying with others' expectations and conforming to the current culture. To become more internally directed is to clarify our core values and increase our integrity, confidence, and authenticity. As we become more confident and more

authentic, we behave differently. Others must make sense of our new behavior. Some will be attracted to it, and some will be offended by it. That's not prohibitive, though: When we are true to our values, we are willing to initiate such conflict.

Idea in Practice

To enter the fundamental state of leadership, apply these steps:

1. **Recognize you've already been there.** You've faced great challenges before and, in surmounting them, you entered the fundamental state. By recalling these moments' lessons, you release positive emotions and see new possibilities for your current situation.

2. **Analyze your current state.** Compare your normal performance with what you've done at your very best. You'll fuel a desire to elevate what you're doing now and instill confidence that you can reenter the fundamental state.

3. **Ask the four questions shown in the following chart.**

BY ASKING . . .	YOU SHIFT FROM . . .	TO . . .
Am I results centered?	Remaining in your comfort zone and solving familiar problems	Moving toward possibilities that don't yet exist
Am I internally directed?	Complying with others' expectations and conforming to existing conditions	Clarifying your core values, acting with authenticity and confidence, and willingly initiating productive conflict
Am I other focused?	Allowing pursuit of your own self-interest to shape your relationships	Committing to the collective good in your organization—even at personal cost
Am I externally open?	Controlling your environment, making incremental changes, and relying on established routines	Learning from your environment, acknowledging the need for major change, and departing from routines

Example: John Jones, a successful change leader, had turned around two struggling divisions in his corporation. Promised the presidency of the largest division when the incumbent retired, he was told meanwhile to bide his time overseeing a dying division's "funeral." He determined to turn the division around. After nine months, though, he'd seen little improvement. Employees weren't engaged.

To enter the fundamental state, John asked:

- **“Am I results oriented?”** He suddenly envisioned a new strategy for his struggling division, along with a plan (including staff reassignments) for implementing it. With a clear, compelling strategy in mind, his energy soared.
- **“Am I internally directed?”** He realized that his focus on the promised plum job had prevented him from doing the hard work needed to motivate his division’s people to give more.
- **“Am I other focused?”** He decided to turn down the presidency in favor of rescuing his failing division—a course truer to his leadership values. He thus traded personal security for a greater good.
- **“Am I externally open?”** He stopped deceiving himself into thinking he’d done all he could for his failing division and realized he had the capacity to improve things.

Third, we become less self-focused and more focused on others. We put the needs of the organization as a whole above our own. Few among us would admit that personal needs trump the collective good, but the impulse to control relationships in a way that feeds our own interests is natural and normal. That said, self-focus over time leads to feelings of isolation. When we put the collective good first, others reward us with their trust and respect. We form tighter, more sensitive bonds. Empathy increases, and cohesion follows. We create an enriched sense of community, and that helps us transcend the conflicts that are a necessary element in high-performing organizations.

Fourth, we become more open to outside signals or stimuli, including those that require us to do things we are not comfortable doing. In the normal state, we pay attention to signals that we know to be relevant. If they suggest incremental adjustments, we respond. If, however, they call for more dramatic changes, we may adopt a posture of defensiveness and denial; this mode of self-protection and self-deception separates us from the ever-changing external world. We live according to an outdated, less valid, image of what is real. But in the fundamental state of leadership, we are more aware of what is unfolding, and we generate new images all the time. We are

adaptive, credible, and unique. In this externally open state, no two people are alike.

There's normal, and there's fundamental

Under everyday circumstances, leaders can remain in their normal state of being and do what they need to do. But some challenges require a heightened perspective—what can be called the fundamental state of leadership. Here's how the two states differ.

In the normal state, I am . . .	In the fundamental state, I am . . .
COMFORT CENTERED I stick with what I know.	RESULTS CENTERED I venture beyond familiar territory to pursue ambitious new outcomes.
EXTERNALLY DIRECTED I comply with others' wishes in an effort to keep the peace.	INTERNALLY DIRECTED I behave according to my values.
SELF-FOCUSED I place my interests above those of the group.	OTHER FOCUSED I put the collective good first.
INTERNALLY CLOSED I block out external stimuli in order to stay on task and avoid risk.	EXTERNALLY OPEN I learn from my environment and recognize when there's a need for change.

These four qualities—being results centered, internally directed, other focused, and externally open—are at the heart of positive human influence, which is generative and attractive. A person without these four characteristics can also be highly influential, but his or her influence tends to be predicated on some form of control or force, which does not usually give rise to committed followers. By entering the fundamental state of leadership, we increase the likelihood of attracting others to an elevated level of community, a high-performance state that may continue even when we are not present.

Preparing for the Fundamental State

Because people usually do not leave their comfort zones unless forced, many find it helpful to follow a process when they choose to enter the fundamental state of leadership. I teach a technique to executives and use it in my own work. It simply involves asking four awareness-raising questions designed to help us transcend our natural denial mechanisms. When people become aware of their hypocrisies, they are more likely to change. Those who are new to the “fundamental state” concept, however, need to take two preliminary steps before they can understand and employ it.

Step 1: Recognize that you have previously entered the fundamental state of leadership

Every reader of this publication has reached, at one time or another, the fundamental state of leadership. We've all faced a great personal or professional challenge and spent time in the dark night of the soul. In successfully working through such episodes, we inevitably enter the fundamental state of leadership.

When I introduce people to this concept, I ask them to identify two demanding experiences from their past and ponder what happened in terms of intention, integrity, trust, and adaptability. At first, they resist the exercise because I am asking them to revisit times of great personal pain. But as they recount their experiences, they begin to see that they are also returning to moments of greatness. Our painful experiences often bring out our best selves. Recalling the lessons of such moments releases positive emotions and makes it easier to see what's possible in the present. In this exercise, I ask people to consider their behavior during these episodes in relation to the characteristics of the fundamental state of leadership. (See the exhibit "You've Already Been There" for analyses of two actual episodes.)

Sometimes I also ask workshop participants to share their stories with one another. Naturally, they are reluctant to talk about such dark moments. To help people open up, I share my own moments of great challenge, the ones I would normally keep to myself. By exhibiting vulnerability, I'm able to win the group's trust and embolden other people to exercise the same courage. I recently ran a workshop with a cynical group of executives. After I broke the testimonial ice, one of the participants told us of a time when he had accepted a new job that required him to relocate his family. Just before he was to start, his new boss called in a panic, asking him to cut his vacation short and begin work immediately. The entire New England engineering team had quit; clients in the region had no support whatsoever. The executive started his job early, and his family had to navigate the move without his help. He described the next few months as "the worst and best experience" of his life.

You've already been there

Two participants in a leadership workshop at the University of Michigan's Ross School of Business used this self-assessment tool to figure out how they've transcended their greatest life challenges by entering the fundamental state of leadership. You can use the same approach in analyzing how you've conquered your most significant challenges.

	PARTICIPANT A	PARTICIPANT B
The pivotal crisis:	I was thrust into a job that was crucial to the organization but greatly exceeded my capabilities. I had to get people to do things they did not want to do.	I was driving myself hard at work, and things kept getting worse at home. Finally my wife told me she wanted a divorce.
How did you become more results centered?	I kept trying to escape doing what was required, but I could not stand the guilt. I finally decided I had to change. I envisioned what success might look like, and I committed to making whatever changes were necessary.	I felt I'd lost everything: family, wealth, and stature. I withdrew from relationships. I started drinking heavily. I finally sought professional help for my sorrow and, with guidance, clarified my values and made choices about my future.
How did you become more internally directed?	I stopped worrying so much about how other people would evaluate and judge me. I was starting to operate from my own values. I felt more self-empowered than ever and realized how fear driven I had been.	I engaged in a lot of self-reflection and journal writing. It became clear that I was not defined by marriage, wealth, or stature. I was more than that. I began to focus on how I could make a difference for other people. I got more involved in my community.
How did you become more focused on others?	I realized how much I needed people, and I became more concerned about them. I was better able to hear what they were saying. I talked not just from my head but also from my heart. My colleagues responded. Today, I am still close to those people.	As I started to grow and feel more self-confident, I became better at relating. At work, I now ask more of people than I ever did before, but I also give them far more support. I care about them, and they can tell.
How did you become more externally open?	I experimented with new approaches. They often did not work, but they kept the brainstorming in motion. I paid attention to every kind of feedback. I was hungry to get it right. There was a lot of discovery. Each step forward was exhilarating.	I began to feel stronger. I was less intimidated when people gave me negative feedback. I think it was because I was less afraid of changing and growing.

Another executive shared that he'd found out he had cancer the same week he was promoted and relocated to Paris, not knowing how to speak French. His voice cracked as he recalled these stressful events. But then he told us about the good that came out of them—how he conquered both the disease and the job while also becoming a more authentic and influential leader.

Others came forward with their own stories, and I saw a great change in the group. The initial resistance and cynicism began to disappear, and participants started exploring the fundamental state of leadership in a serious way. They saw the power in the concept and recognized that hiding behind

their pride or reputation would only get in the way of future progress. In recounting their experiences, they came to realize that they had become more purposive, authentic, compassionate, and responsive.

Step 2: Analyze your current state

When we're in the fundamental state, we take on various positive characteristics, such as clarity of vision, self-empowerment, empathy, and creative thinking. (See the exhibit "Are You in the Fundamental State of Leadership?" for a checklist organized along the four dimensions.) Most of us would like to say we display these characteristics at all times, but we really do so only sporadically.

Are you in the fundamental state of leadership?

Think of a time when you reached the fundamental state of leadership—that is, when you were at your best as a leader—and use this checklist to identify the qualities you displayed. Then check off the items that describe your behavior today. Compare the past and present. If there's a significant difference, what changes do you need to make to get back to the fundamental state?

At my best I was ...	Today I am ...	
—	—	RESULTS CENTERED
—	—	Knowing what result I'd like to create
—	—	Holding high standards
—	—	Initiating actions
—	—	Challenging people
—	—	Disrupting the status quo
—	—	Capturing people's attention
—	—	Feeling a sense of shared purpose
—	—	Engaging in urgent conversations
—	—	INTERNALLY DIRECTED
—	—	Operating from my core values
—	—	Finding motivation from within
—	—	Feeling self-empowered
—	—	Leading courageously
—	—	Bringing hidden conflicts to the surface
—	—	Expressing what I really believe
—	—	Feeling a sense of shared reality
—	—	Engaging in authentic conversations
—	—	OTHER FOCUSED
—	—	Sacrificing personal interests for the common good
—	—	Seeing the potential in everyone
—	—	Trusting others and fostering interdependence
—	—	Empathizing with people's needs
—	—	Expressing concern
—	—	Supporting people
—	—	Feeling a sense of shared identity
—	—	Engaging in participative conversations
—	—	EXTERNALLY OPEN
—	—	Moving forward into uncertainty
—	—	Inviting feedback
—	—	Paying deep attention to what's unfolding
—	—	Learning exponentially
—	—	Watching for new opportunities
—	—	Growing continually
—	—	Feeling a sense of shared contribution
—	—	Engaging in creative conversations

Comparing our normal performance with what we have done at our very best often creates a desire to elevate what we are doing now. Knowing we've operated at a higher level in the past instills confidence that we can do so again; it quells our fear of stepping into unknown and risky territory.

Asking Four Transformative Questions

Of course, understanding the fundamental state of leadership and recognizing its power are not the same as being there. Entering that state is where the real work comes in. To get started, we can ask ourselves four questions that correspond with the four qualities of the fundamental state.

To show how each of these qualities affects our behavior while we're in the fundamental state of leadership, I'll draw on stories from two executives. One is a company president; we'll call him John Jones. The other, Robert Yamamoto, is the executive director of the Los Angeles Junior Chamber of Commerce. Both once struggled with major challenges that changed the way they thought about their jobs and their lives.

I met John in an executive course I was teaching. He was a successful change leader who had turned around two companies in his corporation. Yet he was frustrated. He had been promised he'd become president of the largest company in the corporation as soon as the current president retired, which would happen in the near future. In the meantime, he had been told to bide his time with a company that everyone considered dead. His assignment was simply to oversee the funeral, yet he took it as a personal challenge to turn the company around. After he had been there nine months, however, there was little improvement, and the people were still not very engaged.

As for Robert, he had been getting what he considered to be acceptable (if not exceptional) results in his company. So when the new board president asked him to prepare a letter of resignation, Robert was stunned. He underwent a period of anguished introspection, during which he began to distrust others and question his own management skills and leadership ability. Concerned for his family and his future, he started to seek another job and wrote the requested letter.

As you will see, however, even though things looked grim for both Robert and John, they were on the threshold of positive change.

Am I results centered?

Most of the time, we are comfort centered. We try to continue doing what we know how to do. We may think we are pursuing new outcomes, but if achieving them means leaving our comfort zones, we subtly—even unconsciously—find ways to avoid doing so. We typically advocate ambitious outcomes while designing our work for maximum administrative convenience, which allows us to avoid conflict but frequently ends up reproducing what already exists. Often, others collude with us to act out this deception. Being comfort centered is hypocritical, self-deceptive, and normal.

Clarifying the result we want to create requires us to reorganize our lives. Instead of moving away from a problem, we move toward a possibility that does not yet exist. We become more proactive, intentional, optimistic, invested, and persistent. We also tend to become more energized, and our impact on others becomes energizing.

Consider what happened with John. When I first spoke with him, he sketched out his strategy with little enthusiasm. Sensing that lack of passion, I asked him a question designed to test his commitment to the end he claimed he wanted to obtain:

What if you told your people the truth? Suppose you told them that nobody really expects you to succeed, that you were assigned to be a caretaker for 18 months, and that you have been promised a plum job once your assignment is through. And then you tell them that you have chosen instead to give up that plum job and bet your career on the people present. Then, from your newly acquired stance of optimism for the company's prospects, you issue some challenges beyond your employees' normal capacity.

To my surprise, John responded that he was beginning to think along similar lines. He grabbed a napkin and rapidly sketched out a new strategy along with a plan for carrying it out, including reassignments for his staff. It

was clear and compelling, and he was suddenly full of energy.

What happened here? John was the president of his company and therefore had authority. And he'd turned around two other companies—evidence that he had the knowledge and competencies of a change leader. Yet he was *failing* as a change leader. That's because he had slipped into his comfort zone. He was going through the motions, doing what had worked elsewhere. He was imitating a great leader—in this case, John himself. But imitation is not the way to enter the fundamental state of leadership. If I had accused John of not being committed to a real vision, he would have been incensed. He would have argued heatedly in denial of the truth. All I had to do, though, was nudge him in the right direction. As soon as he envisioned the result he wanted to create and committed himself to it, a new strategy emerged and he was reenergized.

Then there was Robert, who went to what he assumed would be his last board meeting and found that he had more support than he'd been led to believe. Shockingly, at the end of the meeting, he still had his job. Even so, this fortuitous turn brought on further soul-searching. Robert started to pay more attention to what he was doing; he began to see his tendency to be tactical and to gravitate toward routine tasks. He concluded that he was managing, not leading. He was playing a role and abdicating leadership to the board president—not because that person had the knowledge and vision to lead but because the position came with the statutory right to lead. “I suddenly decided to really lead my organization,” Robert said. “It was as if a new person emerged. The decision was not about me. I needed to do it for the good of the organization.”

In deciding to “really lead,” Robert started identifying the strategic outcomes he wanted to create. As he did this, he found himself leaving his zone of comfort—behaving in new ways and generating new outcomes.

Am I internally directed?

In the normal state, we comply with social pressures in order to avoid conflict and remain connected with our coworkers. However, we end up feeling *less* connected because conflict avoidance results in political compromise. We begin to lose our uniqueness and our sense of integrity. The agenda gradually shifts from creating an external result to preserving political peace. As this problem intensifies, we begin to lose hope and energy.

This loss was readily apparent in the case of John. He was his corporation's shining star. But since he was at least partially focused on the future reward—the plum job—he was not fully focused on doing the hard work he needed to do at the moment. So he didn't ask enough of the people he was leading. To get more from them, John needed to be more internally directed.

Am I other focused?

It's hard to admit, but most of us, most of the time, put our own needs above those of the whole. Indeed, it is healthy to do so; it's a survival mechanism. But when the pursuit of our own interests controls our relationships, we erode others' trust in us. Although people may comply with our wishes, they no longer derive energy from their relationships with us. Over time we drive away the very social support we seek.

To become more focused on others is to commit to the collective good in relationships, groups, or organizations, even if it means incurring personal costs. When John made the shift into the fundamental state of leadership, he committed to an uncertain future for himself. He had been promised a coveted job. All he had to do was wait a few months. Still, he was unhappy, so he chose to turn down the opportunity in favor of a course that was truer to his leadership values. When he shifted gears, he sacrificed his personal security in favor of a greater good.

Remember Robert's words: "The decision was not about me. I needed to do it for the good of the organization." After entering the fundamental state of leadership, he proposed a new strategic direction to the board's president and said that if the board didn't like it, he would walk away with no regrets. He knew that the strategy would benefit the organization, regardless of how it would affect him personally. Robert put the good of the organization first. When a leader does this, people notice, and the leader gains respect and trust. Group members, in turn, become more likely to put the collective good first. When they do, tasks that previously seemed impossible become doable.

Am I externally open?

Being closed to external stimuli has the benefit of keeping us on task, but it also allows us to ignore signals that suggest a need for change. Such signals would force us to cede control and face risk, so denying them is self-protective, but it is also self-deceptive. John convinced himself he'd done all he could for his failing company when, deep down, he knew that he had the capacity to improve things. Robert was self-deceptive, too, until crisis and renewed opportunity caused him to open up and explore the fact that he was playing a role accorded him but not using his knowledge and emotional capacity to transcend that role and truly lead his people.

Asking ourselves whether we're externally open shifts our focus from controlling our environment to learning from it and helps us recognize the need for change. Two things happen as a result. First, we are forced to improvise in response to previously unrecognized cues—that is, to depart from established routines. And second, because trial-and-error survival requires an accurate picture of the results we're creating, we actively and genuinely seek honest feedback. Since people trust us more when we're in this state, they tend to offer more accurate feedback, understanding that we are likely to learn from the message rather than kill the messenger. A cycle of learning and empowerment is created, allowing us to see things that people normally cannot see and to formulate transformational strategies.

Applying the Fundamental Principles

Just as I teach others about the fundamental state of leadership, I also try to apply the concept in my own life. I was a team leader on a project for the University of Michigan's Executive Education Center. Usually, the center runs weeklong courses that bring in 30 to 40 executives. It was proposed that we develop a new product, an integrated week of perspectives on leadership. C. K. Prahalad would begin with a strategic perspective, then Noel Tichy, Dave Ulrich, Karl Weick, and I would follow with our own presentations. The objective was to fill a 400-seat auditorium. Since each presenter had a reasonably large following in some domain of the executive world, we were confident we could fill the seats, so we scheduled the program for the month of July, when our facilities were typically underutilized.

In the early months of planning and organizing, everything went perfectly. A marketing consultant had said we could expect to secure half our enrollment three weeks prior to the event. When that time rolled around, slightly less than half of the target audience had signed up, so we thought all was well. But then a different consultant indicated that for our kind of event we would get few additional enrollments during the last three weeks. This stunning prediction meant that attendance would be half of what we expected and we would be lucky to break even.

As the team leader, I could envision the fallout. Our faculty members, accustomed to drawing a full house, would be offended by a half-empty room; the dean would want to know what went wrong; and the center's staff would probably point to the team leader as the problem. That night I spent several hours pacing the floor. I was filled with dread and shame. Finally I told myself that this kind of behavior was useless. I went to my desk and wrote down the four questions. As I considered them, I concluded that I was comfort centered, externally directed, self-focused, and internally closed.

So I asked myself, "What result do I want to create?" I wrote that I wanted the center to learn how to offer a new, world-class product that would be in demand over time. With that clarification came a freeing insight:

Because this was our first offering of the product, turning a large profit was not essential. That would be nice, of course, but we'd be happy to learn how to do such an event properly, break even, and lay the groundwork for making a profit in the future.

I then asked myself, "How can I become other focused?" At that moment, I was totally self-focused—I was worried about my reputation—and my first inclination was to be angry with the staff. But in shifting my focus to what they might be thinking that night, I realized they were most likely worried that I'd come to work in the morning ready to assign blame. Suddenly, I saw a need to both challenge and support them.

Finally, I thought about how I could become externally open. It would mean moving forward and learning something new, even if that made me uncomfortable. I needed to engage in an exploratory dialogue rather than preside as the expert in charge.

I immediately began making a list of marketing strategies, though I expected many of them would prove foolish since I knew nothing about marketing. The next day, I brought the staff together—and they, naturally, were guarded. I asked them what result we wanted to create. What happened next is a good example of how contagious the fundamental state of leadership can be.

We talked about strategies for increasing attendance, and after a while, I told the staff that I had some silly marketing ideas and was embarrassed to share them but was willing to do anything to help. They laughed at many of my naive thoughts about how to increase publicity and create pricing incentives. Yet my proposals also sparked serious discussion, and the group began to brainstorm its way into a collective strategy. Because I was externally open, there was space and time for everyone to lead. People came up with better ways of approaching media outlets and creating incentives. In that meeting, the group developed a shared sense of purpose, reality, identity, and contribution. They left feeling reasonable optimism and went forward as a committed team.

In the end, we did not get 400 participants, but we filled more than enough seats to have a successful event. We more than broke even, and we developed the skills we needed to run such an event better in the future. The program was a success because something transformational occurred among the staff. Yet the transformation did not originate in the meeting. It began the night before, when I asked myself the four questions and moved from the

normal, reactive state to the fundamental state of leadership. And my entry into the fundamental state encouraged the staff to enter as well.

While the fundamental state proves useful in times of crisis, it can also help us cope with more mundane challenges. If I am going to have an important conversation, attend a key meeting, participate in a significant event, or teach a class, part of my preparation is to try to reach the fundamental state of leadership. Whether I am working with an individual, a group, or an organization, I ask the same four questions. They often lead to high-performance outcomes, and the repetition of high-performance outcomes can eventually create a high-performance culture.

Inspiring Others to High Performance

When we enter the fundamental state of leadership, we immediately have new thoughts and engage in new behaviors. We can't remain in this state forever. It can last for hours, days, or sometimes months, but eventually we come back to our normal frame of mind. While the fundamental state is temporary, each time we are in it we learn more about people and our environment and increase the probability that we will be able to return to it. Moreover, we inspire those around us to higher levels of performance.

To this day, Robert marvels at the contrast between his organization's past and present. His transformation into a leader with positive energy and a willingness and ability to tackle challenges in new ways helped shape the L.A. Junior Chamber of Commerce into a high-functioning and creative enterprise. When I last spoke to Robert, here's what he had to say:

I have a critical mass of individuals on both the staff and the board who are willing to look at our challenges in a new way and work on solutions together. At our meetings, new energy is present. What previously seemed unimaginable now seems to happen with ease.

Any CEO would be delighted to be able to say these things. But the truth is, it's not a typical situation. When Robert shifted into the fundamental state of leadership, his group (which started off in a normal state) came to life, infused with his renewed energy and vision. Even after he'd left the fundamental state, the group sustained a higher level of performance. It continues to flourish, without significant staff changes or restructuring.

All this didn't happen because Robert read a book or an article about the best practices of some great leader. It did not happen because he was imitating someone else. It happened because he was jolted out of his comfort zone and was forced to enter the fundamental state of leadership. He was driven to clarify the result he wanted to create, to act courageously from his

core values, to surrender his self-interest to the collective good, and to open himself up to learning in real time. From Robert, and others like him, we can learn the value of challenging ourselves in this way—a painful process but one with great potential to make a positive impact on our own lives and on the people around us.

Originally published in July 2005. Reprint R0507F

What to Ask the Person in the Mirror

by Robert S. Kaplan

IF YOU'RE LIKE MOST successful leaders, you were, in the early stages of your career, given plenty of guidance and support. You were closely monitored, coached, and mentored. But as you moved up the ladder, the sources of honest and useful feedback became fewer, and after a certain point, you were pretty much on your own. Now, your boss—if you have one—is no longer giving much consideration to your day-to-day actions. By the time any mistakes come to light, it's probably too late to fix them—or your boss's perceptions of you. And by the time your management missteps negatively affect your business results, it's usually too late to make corrections that will get you back on course.

No matter how talented and successful you are, you will make mistakes. You will develop bad habits. The world will change subtly, without your even noticing, and behaviors that once worked will be rendered ineffective. Over a 22-year career at Goldman Sachs, I had the opportunity to run various businesses and to work with or coach numerous business leaders. I chaired the firm's senior leadership training efforts and cochaired its partnership committee, which focused on reviews, promotions, and development of managing directors. Through this experience and subsequent interviews with a large number of executives in a broad range of industries, I have observed that even outstanding leaders invariably struggle through stretches of their careers where they get off track for some period of time.

It's hard to see it when you're in the midst of it; changes in the environment, competitors, or even personal circumstances can quietly guide

you off your game. I have learned that a key characteristic of highly successful leaders is not that they figure out how to always stay on course, but that they develop techniques to help them recognize a deteriorating situation and get back on track as quickly as possible. In my experience, the best way to do that is to step back regularly, say, every three to six months (and certainly whenever things feel as though they aren't going well), and honestly ask yourself some questions about how you're doing and what you may need to do differently. As simple as this process sounds, people are often shocked by their own answers to basic management and leadership questions.

One manager in a large financial services company who had been passed over for promotion told me he was quite surprised by his year-end performance review, which highlighted several management issues that had not been previously brought to his attention. His boss read several comments from the review that faulted him for poor communication, failure to effectively articulate a strategy for the business, and a tendency to isolate himself from his team. He believed that the review was unfair. After 15 years at the company, he began to feel confused and misunderstood and wondered whether he still had a future there. He decided to seek feedback directly from five of his key contributors and longtime collaborators. In one-on-one meetings, he asked them for blunt feedback and advice. He was shocked to hear that they were highly critical of several of his recent actions, were confused about the direction he wanted to take the business, and felt he no longer valued their input. Their feedback helped him see that he had been so immersed in the day-to-day business that he had failed to step back and think about what he was doing. This was a serious wake-up call. He immediately took steps to change his behavior and address these issues. His review the following year was dramatically better, he was finally promoted, and his business's performance improved. The manager was lucky to have received this feedback in time to get his career back on track, although he regretted that he had waited for a negative review to ask basic questions about his leadership activities. He promised himself he would not make that mistake again.

Idea in Brief

If you're like most managers, the higher you go up the corporate ladder, the harder it is to get candid feedback on your performance. And without crucial input from bosses and colleagues, you can make mistakes that irreparably damage your organization—and your reputation.

How can you figure out how you're *really* doing and avoid business disasters? Kaplan recommends looking to *yourself* for answers. Regularly ask yourself questions like these: “Am I communicating a vision for my business to my employees?” “Am I spending my time in ways that enable me to achieve my priorities?” “Do I give people timely and direct feedback they can act on?” “How do I behave under pressure?”

It's far more important to ask the *right* questions than to have all the answers. By applying this process, you tackle the leadership challenges that inevitably arise during the course of your career—and craft new plans for staying on your game.

In this article, I outline seven types of questions that leaders should ask themselves on some periodic basis. I am not suggesting that there is a “right” answer to any of them or that they all will resonate with a given executive at any point in time. I am suggesting that successful executives can regularly improve their performance and preempt serious business problems by stepping back and taking the time to ask themselves certain key questions.

Vision and Priorities

It's surprising how often business leaders fail to ask themselves: *How frequently do I communicate a vision and priorities for my business? Would my employees, if asked, be able to articulate the vision and priorities?* Many leaders have, on paper, a wealth of leadership talents: interpersonal, strategic, and analytic skills; a knack for team building; and certainly the ability to develop a vision. Unfortunately, in the press of day-to-day activities, they often don't adequately communicate the vision to the organization, and in particular, they don't convey it in a way that helps their people understand what they are supposed to be doing to drive the business. It is very difficult to lead people if they don't have a firm grasp of where they're heading and what's expected of them.

Idea in Practice

Kaplan suggests periodically asking yourself questions related to seven leadership challenges.

To address this leadership challenge . . .	Ask ...	Because ...
Vision and priorities	How often do I communicate a vision and key priorities to achieve that vision?	Employees want to know where the business is going and what they need to focus on in order to help drive the business. As the world changes, they want to know how the vision and priorities might change.
Managing time	Does the way I spend my time match my key priorities?	Tracking your use of time can reveal startling—even horrifying—disconnects between your top priorities and your actions. Such disconnects send confusing messages to employees about your true priorities.
Feedback	Do I give people timely and direct feedback they can act on?	Employees want truthful, direct, and timely feedback. Retention and productivity improve when employees trust you to raise issues promptly and honestly.

Succession planning	Have I identified potential successors?	It's important to nurture future leaders who can grow the business. If you haven't identified possible successors, you're probably not delegating as much as you should, and you may even be a decision-making bottleneck.
Evaluation and alignment	Am I attuned to business changes that may require shifts in how we run the company?	All businesses encounter challenges posed by changes; for example, in customers' needs or the business's stage of maturity. To determine how best to evolve your business, regularly scan for changes, seek fresh perspectives from talented subordinates, and envision new organizational designs.
Leading under pressure	How do I behave under pressure?	During crises, employees watch you with a microscope—and mimic your behavior. By identifying your unproductive behaviors under pressure (such as blaming others or losing your temper), you can better manage those behaviors and avoid sending unintended messages to employees about how <i>they</i> should behave.
Staying true to yourself	Does my leadership style reflect who I truly am?	A business career is a marathon, not a sprint. If you've adopted a leadership style that doesn't suit your skills, values, and personality, you'll wear down.

This was the problem at a large *Fortune* 200 company that had decided to invest in its 1,000 top managers by having them attend an intensive, two-day management-training program, 100 at a time. Before each session, the participants went through a 360-degree nonevaluative review in which critical elements of their individual performance were ranked by ten of their subordinates. The company's senior management looked at the results, focusing on the top five and bottom five traits for each group. Despite this being an extremely well-managed firm, the ability to articulate a vision ranked in the bottom five for almost every group. Managers at that company did articulate a vision, but the feedback from their subordinates strongly indicated that they were not communicating it frequently or clearly enough to meet their people's tremendous hunger for guidance.

Employees want to know where the business is going and what they need to focus on. As the world changes, they want to know how the business vision and priorities might change along with it. While managers are taught to actively communicate, many either unintentionally undercommunicate or fail to articulate specific priorities that would give meaning to their vision. However often you think you discuss vision and strategy, you may not be

doing it frequently enough or in sufficient detail to suit the needs of your people. Look at the CEO of an emerging biotechnology company, who was quite frustrated with what he saw as a lack of alignment within his top management team. He strongly believed that the company needed to do a substantial equity financing within the next 18 months, but his senior managers wanted to wait a few years until two or three of the company's key drugs were further along in the FDA approval process. They preferred to tell their story to investors when the company was closer to generating revenue. When I asked him about the vision for the company, the CEO sheepishly realized that he had never actually written down a vision statement. He had a well-articulated tactical plan relating to each of the company's specific product efforts but no fully formed vision that would give further context to these efforts. He decided to organize an off-site meeting for his senior management team to discuss and specifically articulate a vision for the company.

After a vigorous debate, the group quickly agreed on a vision and strategic priorities. They realized that in order to achieve their shared goals, the business would in fact require substantial financing sooner rather than later—or they would need to scale back some of the initiatives that were central to their vision for the company. Once they fully appreciated this trade-off, they understood what the CEO was trying to accomplish and left the meeting united about their financing strategy. The CEO was quite surprised at how easy it had been to bring the members of his leadership team together. Because they agreed on where they were going as a company, specific issues were much easier to resolve.

A common pitfall in articulating a vision is a failure to boil it down to a manageable list of initiatives. Culling the list involves thinking through and then making difficult choices and trade-off decisions. These choices communicate volumes to your people about how they should be spending their time. I spoke with the manager of a national sales force who felt frustrated that his direct reports were not focusing on the tasks necessary to achieve their respective regional sales goals. As a result, sales were growing at a slower rate than budgeted at the beginning of the year. When I asked him to enumerate the three to five key priorities he expected his salespeople to focus on, he paused and then explained that there were 15 and it would be very difficult to narrow the list down to five.

Even as he spoke, a light went on in his head. He realized why there might

be a disconnect between him and his people: They didn't know precisely what he wanted because he had not told them in a prioritized, and therefore actionable, manner. He reflected on this issue for the next two weeks, thinking at length about his own experience as a regional manager and consulting with various colleagues. He then picked three priorities that he felt were crucial to achieving sales growth. The most important of these involved a major new-business targeting exercise followed by a substantial new-prospect calling effort. The regional managers immediately understood and began focusing on these initiatives. The fact is that having 15 priorities is the same as having none at all. Managers have a responsibility to translate their vision into a manageable number of priorities that their subordinates can understand and act on.

Failing to communicate your vision and priorities has direct costs to you in terms of time and business effectiveness. It's hard to delegate if your people don't have a good sense of the big picture; hence you end up doing more work yourself. This issue can cascade through the organization if your direct reports are, in turn, unable to communicate a vision and effectively leverage their own subordinates.

Managing Time

The second area to question is painfully simple and closely relates to the first: *How am I spending my time?* Once you know your priorities, you need to determine whether you're spending your time—your most precious asset—in a way that will allow you to achieve them. For example, if your two major priorities are senior talent development and global expansion but you're spending the majority of your time on domestic operational and administrative matters that could be delegated, then you need to recognize there is a disconnect and you'd better make some changes.

Testing Yourself

To assess your performance and stay on track, you should step back and ask yourself certain key questions.

Vision and Priorities

In the press of day-to-day activities, leaders often fail to adequately communicate their vision to the organization, and in particular, they don't communicate it in a way that helps their subordinates determine where to focus their own efforts.

- How often do I communicate a vision for my business?
- Have I identified and communicated three to five key priorities to achieve that vision?
- If asked, would my employees be able to articulate the vision and priorities?

Managing Time

Leaders need to know how they're spending their time. They also need to ensure that their time allocation (and that of their subordinates) matches their key priorities.

- How am I spending my time? Does it match my key priorities?
- How are my subordinates spending their time? Does that match the key priorities for the business?

Feedback

Leaders often fail to coach employees in a direct and timely fashion and, instead, wait until the year-end review. This approach may lead to unpleasant surprises and can undermine effective professional development. Just as important, leaders need to cultivate subordinates who can give them advice and feedback during the year.

- Do I give people timely and direct feedback that they can act on?
- Do I have five or six junior subordinates who will tell me things I may not want to hear but need to hear?

Succession Planning

When leaders fail to actively plan for succession, they do not delegate sufficiently and may become decision-making bottlenecks. Key employees may leave if they are not actively groomed and challenged.

- Have I, at least in my own mind, picked one or more potential successors?
- Am I coaching them and giving them challenging assignments?
- Am I delegating sufficiently? Have I become a decision-making bottleneck?

Evaluation and Alignment

The world is constantly changing, and leaders need to be able to adapt their businesses accordingly.

- Is the design of my company still aligned with the key success factors for the business?
- If I had to design my business with a clean sheet of paper, how would I design it? How would it differ from the current design?
- Should I create a task force of subordinates to answer these questions and make recommendations to me?

Leading Under Pressure

A leader's actions in times of stress are watched closely by subordinates and have a profound impact on the culture of the firm and employees' behavior. Successful leaders need to be aware of their own stress triggers and consciously modulate their behavior during these periods to make sure they are acting in ways that are consistent with their beliefs and core values.

- What types of events create pressure for me?
- How do I behave under pressure?
- What signals am I sending my subordinates? Are these signals helpful, or are they undermining the success of my business?

Staying True to Yourself

Successful executives develop leadership styles that fit the needs of their business but also fit their own beliefs and personality.

- Is my leadership style comfortable? Does it reflect who I truly am?
- Do I assert myself sufficiently, or have I become tentative?
- Am I too politically correct?

- Does worry about my next promotion or bonus cause me to pull punches or hesitate to express my views?

It's such a simple question, yet many leaders, myself included, just can't accurately answer at times. When leaders finally do track their time, they're often surprised by what they find. Most of us go through periods where unexpected events and day-to-day chaos cause us to be reactive rather than acting on a proscribed plan. Crises, surprises, personnel issues, and interruptions make the workweek seem like a blur. I have recommended to many leaders that they track how they spend each hour of each day for one week, then categorize the hours into types of activities: business development, people management, and strategic planning, for example. For most executives, the results of this exercise are startling—even horrifying—with obvious disconnects between what their top priorities are and how they are spending their time.

For example, the CEO of a midsize manufacturing company was frustrated because he was working 70 hours a week and never seemed to catch up. His family life suffered, and, at work, he was constantly unavailable for his people and major customers. I suggested he step back and review how he was managing his time hour-by-hour over the course of a week. We sat down to examine the results and noticed that he was spending a substantial amount of time approving company expenditures, some for as little as \$500—this in a business with \$500 million in sales. Sitting in my office, he struggled to explain why he had not delegated some portion of this responsibility; it turned out that the activity was a holdover from a time when the company was much smaller. By delegating authority to approve recurring operating expenses below \$25,000, he realized he could save as much as 15 hours per week. He was amazed that he had not recognized this issue and made this simple change much earlier.

How you spend your time is an important question not only for you but for your team. People tend to take their cues from the leader when it comes to time management—therefore, you want to make sure there's a match between your actions, your business priorities, and your team's activities. The CEO of a rapidly growing, 300-person professional services firm felt that, to

build the business, senior managers needed to develop stronger and more substantive relationships with clients. This meant that senior professionals would need to spend significantly more time out of their offices in meetings with clients. When asked how his own time was being spent, the CEO was unable to answer. After tracking it for a week, he was shocked to find that he was devoting a tremendous amount of his time to administrative activities related to managing the firm. He realized that the amount of attention he was paying to these matters did not reflect the business's priorities and was sending a confusing message to his people. He immediately began pushing himself to delegate a number of these administrative tasks and increase the amount of time he spent on the road with customers, setting a powerful example for his people. He directed each of his senior managers to do a similar time-allocation exercise to ensure they were dedicating sufficient time to clients.

Of course, the way a leader spends his or her time must be tailored to the needs of the business, which may vary depending on time of year, personnel changes, and external factors. The key here is, whatever you decide, time allocation needs to be a conscious decision that fits your vision and priorities for the business. Given the pressure of running a business, it is easy to lose focus, so it's important to ask yourself this question periodically. Just as you would step back and review a major investment decision, you need to dispassionately review the manner in which you invest your time.

Feedback

When you think about the ways you approach feedback, you should first ask: *Do I give people timely, direct, and constructive feedback?* And second: *Do I have five or six junior people who will tell me things I don't want to hear but need to hear?*

If they're like most ambitious employees, your subordinates want to be coached and developed in a truthful and direct manner. They want to get feedback while there's still an opportunity to act on it; if you've waited until the year-end review, it's often too late. In my experience, well-intentioned managers typically fail to give blunt, direct, and timely feedback to their subordinates.

One reason for this failure is that managers are often afraid that constructive feedback and criticism will demoralize their employees. In addition, critiquing a professional in a frank and timely manner may be perceived as overly confrontational. Lastly, many managers fear that this type of feedback will cause employees not to like them. Consequently, leaders often wait until year-end performance reviews. The year-end review is evaluative (that is, the verdict on the year) and therefore is not conducive to constructive coaching. The subordinate is typically on the defensive and not as open to criticism. This approach creates surprises, often unpleasant ones, which undermine trust and dramatically reduce the confidence of the subordinate in the manager.

The reality is that managers who don't give immediate and direct feedback often are "liked" until year-end—at which time they wind up being strongly disliked. If employees have fallen short of expectations, the failing is reflected in bonuses, raises, and promotions. The feeling of injustice can be enormous. What's worse is the knowledge that if an employee had received feedback earlier in the year, it is likely that he or she would have made meaningful efforts to improve and address the issues.

While people do like to hear positive feedback, ultimately, they desperately want to know the truth, and I have rarely seen someone quit over

hearing the truth or being challenged to do better—unless it’s too late. On the contrary, I would argue that people are more likely to stay if they understand what issues they need to address and they trust you to bring those issues to their attention in a straightforward and prompt fashion. They gain confidence that you will work with them to develop their skills and that they won’t be blindsided at the end of the year. Employees who don’t land a hoped-for promotion will be much more likely to forgive you if you’ve told them all along what they need to do better, even if they haven’t gotten there yet. They may well redouble their efforts to prove to you that they can overcome these issues.

During my career at Goldman Sachs, I consistently found that professional development was far more effective when coaching and direct feedback were given to employees throughout the year—well in advance of the annual performance review process. Internal surveys of managing directors showed that, in cases where feedback was confined to the year-end review, satisfaction with career development was dramatically lower than when it was offered throughout the year.

As hard as it is to give effective and timely feedback, many leaders find it much more challenging to get feedback from their employees. Once you reach a certain stage of your career, junior people are in a much better position than your boss to tell you how you’re doing. They see you in your day-to-day activities, and they experience your decisions directly. Your boss, at this stage, is much more removed and, as a result, typically needs to talk to your subordinates to assess your performance at the end of the year. In order to avoid your own year-end surprises, you need to develop a network of junior professionals who are willing to give you constructive feedback. The problem is that, while your direct reports know what you are doing wrong, most of them are not dying to tell you. With good reason—there’s very little upside and a tremendous amount of downside. The more senior and the more important you become, the less your subordinates will tell you the “awful truth”—things that are difficult to hear but that you need to know.

It takes a concerted effort to cultivate subordinates who will advise and coach you. It also takes patience and some relentlessness. When I ask subordinates for constructive feedback, they will typically and predictably tell me that I’m doing “very well.” When I follow up and ask “What should I do differently?” they respond, “Nothing that I can think of.” If I challenge them by saying, “There must be something!” still they say, “Nothing comes to

mind.” I then ask them to sit back and think—we have plenty of time. By this time, beads of sweat begin to become visible on their foreheads. After an awkward silence, they will eventually come up with something—and it’s often devastating to hear. It’s devastating because it’s a damning criticism and because you know it’s true.

What you do with this feedback is critical. If you act on it, you will improve your performance. Equally important, you will take a big step in building trust and laying the groundwork for a channel of honest feedback. When subordinates see that you respond positively to suggestions, they will often feel more ownership in the business and in your success. They’ll learn to give you criticisms on their own initiative because they know you will actually appreciate it and do something with it. Developing a network of “coaching” subordinates will help you take action to identify your own leadership issues and meaningfully improve your performance.

Succession Planning

Another question that managers know is important yet struggle to answer affirmatively is: *Have I, at least in my own mind, picked one or more potential successors?* This issue is critical because if you aren't identifying potential successors, you are probably not delegating as extensively as you should and you may well be a decision-making bottleneck. Being a bottleneck invariably means that you are not spending enough time on vital leadership priorities and are failing to develop your key subordinates. Ironically, when leaders believe they are so talented that they can perform tasks far better than any of their subordinates and therefore insist on doing the tasks themselves, they will typically cause their businesses to underperform, and, ultimately, their careers will suffer as well.

The succession question also has significant implications that cascade through an organization: If leaders do not develop successors, then the organization may lack a sufficient number of leaders to successfully grow the business. Worse, if junior employees are not developed, they may leave the firm for better opportunities elsewhere. For these reasons, many well-managed companies will hesitate to promote executives who have failed to develop successors.

It is sufficient to identify possible successors without actually telling them you've done so—as long as this identification causes you to manage them differently. In particular, you will want to delegate more of your major responsibilities to these professionals. This will speed their maturation and prepare them to step up to the next level. By giving demanding assignments to these subordinates, you strongly signal an interest in their development and career progression—which will encourage them to turn down offers from competitors. Leaders who do this are much better able to keep their teams together and avoid losing up-and-coming stars to competitors.

A loss of talent is highly damaging to a company. It is particularly painful if you could have retained key employees by simply challenging them more intensively. I spoke with a division head of a large company who was

concerned about what he perceived to be a talent deficit in his organization. He felt that he could not use his time to the fullest because he viewed his direct reports as incapable of assuming some of his major responsibilities. He believed this talent deficit was keeping him from launching several new product and market initiatives. In the midst of all this, he lost two essential subordinates over six months—each had left to take on increased responsibilities at major competitors. He had tried to persuade them to stay, emphasizing that he was actively considering them for significant new leadership assignments. Because they had not seen evidence of this previously, they were skeptical and left anyway. I asked him whether, prior to the defections, he had identified them (or anyone else) as potential successors, put increased responsibilities in their hands, or actively ratcheted up his coaching of these professionals. He answered that, in the chaos of daily events and in the effort to keep up with the business, he had not done so. He also admitted that he had underestimated the potential of these two employees and realized he was probably underestimating the abilities of several others in the company. He immediately sat down and made a list of potential stars and next to each name wrote out a career and responsibility game plan. He immediately got to work on this formative succession plan, although he suspected that he had probably waited too long already.

When you're challenging and testing people, you delegate to them more often, which frees you to focus on the most critical strategic matters facing the business. This will make you more successful and a more attractive candidate for your own future promotion.

Evaluation and Alignment

The world is constantly changing. Your customers' needs change; your business evolves (going, for instance, from high growth to mature); new products and distribution methods emerge as threats. When these changes happen, if you don't change along with them, you can get seriously out of alignment. The types of people you hire, the way you organize them, the economic incentives you offer them, and even the nature of the tasks you delegate no longer create the culture and outcomes that are critical to the success of your business. It's your job to make sure that the design of your organization is aligned with the key success factors for the business. Ask yourself: *Am I attuned to changes in the business environment that would require a change in the way we organize and run our business?*

Such clear-sightedness is, of course, hard to achieve. As a leader, you may be too close to the business to see subtle changes that are continually occurring. Because you probably played a central role in building and designing the business, it may be emotionally very difficult to make meaningful changes. You may have to fire certain employees—people you recruited and hired. You may also have to acknowledge that you made some mistakes and be open to changing your own operating style in a way that is uncomfortable for some period of time.

Because of the difficulty in facing these issues, it's sometimes wise to call on high-potential subordinates to take a fresh look at the business. This approach can be quite effective because junior employees are often not as emotionally invested as you are and can see more objectively what needs to be done. This approach is also a good way to challenge your future leaders and give them a valuable development experience. You'll give them a chance to exercise their strategic skills; you'll get a glimpse of their potential (which relates to the earlier discussion of succession planning), and you might just get some terrific new ideas for how to run the business.

This approach worked for the CEO of a high technology business in northern California, whose company had been one of the early innovators in

its product space but, in recent years, had begun to falter and lose market share. In its early days, the company's primary success factors had been product innovation and satisfying customer needs. It had aggressively hired innovative engineers and marketing personnel. As new competitors emerged, customers began to focus more on cost and service (in the form of more sophisticated applications development). Stepping back, the CEO sensed that he needed to redesign the company with a different mix of people, a new organization, and a revised incentive structure. Rather than try to come up with a new model himself, he asked a more junior group of executives to formulate a new company design as if they had a "clean sheet of paper." Their study took a number of weeks, but upon completion, it led to several recommendations that the CEO immediately began to implement. For example, they suggested colocating the engineering and sales departments and creating integrated account coverage teams. They also recommended that the company push more of its engineers to interact with customers and focus on this skill in recruiting. The CEO regretted that he had not asked the question—and conducted this assignment—12 months earlier.

Even the most successful business is susceptible to new challenges posed by a changing world. Effective executives regularly look at their businesses with a clean sheet of paper—seeking advice and other perspectives from people who are less emotionally invested in the business—in order to determine whether key aspects of the way they run their organizations are still appropriate.

Leading Under Pressure

Pressure is a part of business. Changes in business conditions create urgent problems. New entrants in the market demand a competitive response. Valued employees quit, often at the most inopportune times. Leaders and their teams, no matter how smart they are, make mistakes.

The interesting thing about stressful events is that they affect each person differently—what causes you anxiety may not bother someone else, and vice versa. For some, extreme anxiety may be triggered by the prospect of a promotion; for others, by making a serious mistake; still others, by losing a piece of business to a competitor. Regardless of the source of stress, every leader experiences it, so a good question to ask yourself is: *How do I behave under pressure, and what signals am I sending my employees?*

As a leader, you're watched closely. During a crisis, your people watch you with a microscope, noting every move you make. In such times, your subordinates learn a great deal about you and what you really believe, as opposed to what you say. Do you accept responsibility for mistakes, or do you look for someone to blame? Do you support your employees, or do you turn on them? Are you cool and calm, or do you lose your temper? Do you stand up for what you believe, or do you take the expedient route and advocate what you think your seniors want to hear? You need to be self-aware enough to recognize the situations that create severe anxiety for you and manage your behavior to avoid sending unproductive messages to your people.

I've met a number of leaders who behave in a very composed and thoughtful manner the great majority of the time. Unfortunately, when they're under severe stress, they react in ways that set a very negative tone. They inadvertently train their employees to mimic that behavior and behave in a similar fashion. If your instinct is to shield yourself from blame, to take credit rather than sharing it with your subordinates, or to avoid admitting when you have made a mistake, you will give your employees license to do the same.

The CEO of a large asset-management firm was frustrated that he was

unable to build a culture of accountability and teamwork in his growing business. At his request, I spoke to a number of his team members. I asked in particular about the actions of the CEO when investments they recommended declined in value. They recounted his frequent temper tantrums and accusatory diatribes, which led to an overwhelming atmosphere of blame and finger-pointing. The investment decisions had, in fact, been made jointly through a carefully constructed process involving portfolio managers, industry analysts, and the CEO. As a result of these episodes, employees learned that when investments went wrong it would be good to try to find someone else to blame. Hearing these stories, the CEO realized his actions under pressure were far more persuasive to employees than his speeches about teamwork and culture. He understood that he would have to learn to moderate his behavior under stress and, subsequently, took steps to avoid reacting so angrily to negative investment results. He also became more aware that subordinates typically felt quite regretful and demoralized when their investments declined and were more likely to need a pat on the back and coaching than a kick in the pants.

It's extremely difficult to expect employees to alert you to looming problems when they fear your reaction—and even more so when they think it's better to distance themselves from potential problems. This can create an atmosphere where surprises are, in fact, more likely as the company's natural early-warning system has been inadvertently disarmed. If you have created this kind of culture, it is quite unlikely that you will learn about problems from subordinates spontaneously—unless they want to commit career suicide.

Part of the process of maturing as a leader is learning to step back and think about what creates pressure for you, being self-aware in these situations, and disciplining your behavior to ensure that you act in a manner consistent with your core values.

Staying True to Yourself

Most business leaders ask themselves whether their leadership style fits the needs of their business. Fewer managers ask whether their style also fits their own beliefs and personality. The question here is: *Does my leadership style reflect who I truly am?*

A business career is a marathon, not a sprint, and if you aren't true to yourself, eventually you're going to wear down. As you are developing in your career, it is advisable to observe various leadership styles, and pick and choose elements that feel comfortable to you. Bear in mind, though, that observing and adopting aspects of other styles does not mean you should try to be someone else. During my career, I was fortunate to have had several superb bosses and colleagues with distinctive and unique leadership skills. While I tried to adopt some of their techniques, I also learned that I needed to develop an overall style that fit my unique skills and personality. Your style needs to fit you; even an unorthodox style can be enormously effective if it reflects your skills, values, and personality.

As you become more senior, you'll need to ask yourself an additional set of questions relating to style: *Do I assert myself sufficiently, or have I become tentative? Am I too politically correct? Does worry about my next promotion or my year-end bonus cause me to pull punches or hesitate to clearly express my views?* In many companies, ambitious executives may try to avoid confronting sensitive issues or making waves. Worse than that, they may spend an inordinate amount of energy trying to ascertain what their boss thinks and then act like they think the same thing. If they're very skilled at this, they may even get a chance to make their comments before the boss has a chance to express his opinion—and feel the warm glow of approval from the boss.

The problem is that confrontation and disagreement are crucial to effective decision making. Some of the worst decisions I've been involved in were made after a group of intelligent people had unanimously agreed to the course of action—though, later, several participants admitted that they had

misgivings but were hesitant to diverge from the apparent group consensus. Conversely, it's hard for me to recall a poor decision I was involved in that was made after a thorough debate in which opposing views were vigorously expressed (even if I disagreed with the ultimate decision). Companies need their leaders to express strongly held views rather than mimic what they believe to be the party line. As a leader, therefore, you must ask yourself whether you are expressing your views or holding back and being too politic. At the same time, leaders must encourage their own subordinates to express their unvarnished opinions, make waves as appropriate, and stop tiptoeing around significant issues.

Successful leaders periodically struggle during stretches of their careers. To get back on track, they must devise techniques for stepping back, getting perspective, and developing a new game plan. In this process, having the answers is often far less important than taking time to ask yourself the right questions and gain key insights. The questions posed in this article are intended to spark your thinking. Only a subset of these may resonate with you, and you may find it more useful to come up with your own list. In either event, a self-questioning process conducted on a periodic basis will help you work through leadership challenges and issues that you invariably must tackle over the course of your career.

Originally published in January 2007. Reprint R0701H

Primal Leadership

The Hidden Driver of Great Performance.

by Daniel Goleman, Richard Boyatzis, and Annie McKee

WHEN THE THEORY OF EMOTIONAL intelligence at work began to receive widespread attention, we frequently heard executives say—in the same breath, mind you—“That’s incredible,” and, “Well, I’ve known that all along.” They were responding to our research that showed an incontrovertible link between an executive’s emotional maturity, exemplified by such capabilities as self-awareness and empathy, and his or her financial performance. Simply put, the research showed that “good guys”—that is, emotionally intelligent men and women—finish first.

We’ve recently compiled two years of new research that, we suspect, will elicit the same kind of reaction. People will first exclaim, “No way,” then quickly add, “But of course.” We found that of all the elements affecting bottom-line performance, the importance of the leader’s mood and its attendant behaviors are most surprising. That powerful pair set off a chain reaction: The leader’s mood and behaviors drive the moods and behaviors of everyone else. A cranky and ruthless boss creates a toxic organization filled with negative underachievers who ignore opportunities; an inspirational, inclusive leader spawns acolytes for whom any challenge is surmountable. The final link in the chain is performance: profit or loss.

Our observation about the overwhelming impact of the leader’s “emotional style,” as we call it, is not a wholesale departure from our research into emotional intelligence. It does, however, represent a deeper analysis of our earlier assertion that a leader’s emotional intelligence creates a certain culture or work environment. High levels of emotional intelligence, our research showed, create climates in which information sharing, trust, healthy risk-taking, and learning flourish. Low levels of emotional intelligence create climates rife with fear and anxiety. Because tense or

terrified employees can be very productive in the short term, their organizations may post good results, but they never last.

Our investigation was designed in part to look at how emotional intelligence drives performance—in particular, at how it travels from the leader through the organization to bottom-line results. “What mechanism,” we asked, “binds the chain together?” To answer that question, we turned to the latest neurological and psychological research. We also drew on our work with business leaders, observations by our colleagues of hundreds of leaders, and Hay Group data on the leadership styles of thousands of executives. From this body of research, we discovered that emotional intelligence is carried through an organization like electricity through wires. To be more specific, the leader’s mood is quite literally contagious, spreading quickly and inexorably throughout the business.

We’ll discuss the science of mood contagion in more depth later, but first let’s turn to the key implications of our finding. If a leader’s mood and accompanying behaviors are indeed such potent drivers of business success, then a leader’s premier task—we would even say his primal task—is emotional leadership. A leader needs to make sure that not only is he regularly in an optimistic, authentic, high-energy mood, but also that, through his chosen actions, his followers feel and act that way, too. Managing for financial results, then, begins with the leader managing his inner life so that the right emotional and behavioral chain reaction occurs.

Managing one’s inner life is not easy, of course. For many of us, it’s our most difficult challenge. And accurately gauging how one’s emotions affect others can be just as difficult. We know of one CEO, for example, who was certain that everyone saw him as upbeat and reliable; his direct reports told us they found his cheerfulness strained, even fake, and his decisions erratic. (We call this common disconnect “CEO disease.”) The implication is that primal leadership demands more than putting on a game face every day. It requires an executive to determine, through reflective analysis, how his emotional leadership drives the moods and actions of the organization, and then, with equal discipline, to adjust his behavior accordingly.

Idea in Brief

What *most* influences your company's bottom-line performance? The answer will surprise you—and make perfect sense: It's a leader's own mood.

Executives' emotional intelligence—their self-awareness, empathy, rapport with others—has clear links to their own performance. But new research shows that a leader's emotional style also drives everyone *else's* moods and behaviors—through a neurological process called **mood contagion**. It's akin to “Smile and the whole world smiles with you.”

Emotional intelligence travels through an organization like electricity over telephone wires. Depressed, ruthless bosses create toxic organizations filled with negative underachievers. But if you're an upbeat, inspirational leader, you cultivate positive employees who embrace and surmount even the toughest challenges.

Emotional leadership isn't just putting on a game face every day. It means understanding your impact on others—then adjusting your style accordingly. A difficult process of self-discovery—but essential *before* you can tackle your leadership responsibilities.

That's not to say that leaders can't have a bad day or week: Life happens. And our research doesn't suggest that good moods have to be high-pitched or nonstop—optimistic, sincere, and realistic will do. But there is no escaping the conclusion that a leader must first attend to the impact of his mood and behaviors before moving on to his wide panoply of other critical responsibilities. In this article, we introduce a process that executives can follow to assess how others experience their leadership, and we discuss ways to calibrate that impact. But first, we'll look at why moods aren't often discussed in the workplace, how the brain works to make moods contagious, and what you need to know about CEO disease.

Idea in Practice

Strengthening Your Emotional Leadership

Since few people have the guts to tell you the truth about your emotional impact, you must discover it on your own. The following process can help. It's based on brain science, as well as years of field research with executives. Use these steps to rewire your brain for greater emotional intelligence.

1. Who do you want to be? Imagine yourself as a highly effective leader. What do you see?

Example: Sofia, a senior manager, often micromanaged others to ensure work was done “right.” So she *imagined* herself in the future as an effective leader of her own company, enjoying trusting relationships with coworkers. She saw herself as relaxed, happy, and empowering. The exercise revealed gaps in her current emotional style.

2. Who are you now? To see your leadership style as others do, gather 360-degree feedback, especially from peers and subordinates. Identify your weaknesses *and* strengths.

3. How do you get from here to there? Devise a plan for closing the gap between who you are and who you want to be.

Example: Juan, a marketing executive, was intimidating, impossible to please—a grouch. Charged with growing his company, he *needed* to be encouraging, optimistic—a coach with a vision. Setting out to understand others, he coached soccer, volunteered at a crisis center, and got to know subordinates by meeting outside of work. These new situations stimulated him to break old habits and try new responses.

4. How do you make change stick? Repeatedly rehearse new behaviors—physically *and* mentally—until they're automatic.

Example: Tom, an executive, wanted to learn how to coach rather than castigate struggling employees. Using his commuting time to visualize a difficult meeting with one employee, he envisioned asking questions and listening, and mentally rehearsed how he'd handle feeling impatient. This exercise prepared him to adopt new behaviors at the

actual meeting.

5. Who can help you? Don't try to build your emotional skills alone—identify others who can help you navigate this difficult process. Managers at Unilever formed learning groups that helped them strengthen their leadership abilities by exchanging frank feedback and developing strong mutual trust.

No Way! Yes Way

When we said earlier that people will likely respond to our new finding by saying “No way,” we weren’t joking. The fact is, the emotional impact of a leader is almost never discussed in the workplace, let alone in the literature on leadership and performance. For most people, “mood” feels too personal. Even though Americans can be shockingly candid about personal matters—witness the *Jerry Springer Show* and its ilk—we are also the most legally bound. We can’t even ask the age of a job applicant. Thus, a conversation about an executive’s mood or the moods he creates in his employees might be construed as an invasion of privacy.

We also might avoid talking about a leader’s emotional style and its impact because, frankly, the topic feels soft. When was the last time you evaluated a subordinate’s mood as part of her performance appraisal? You may have alluded to it—“Your work is hindered by an often negative perspective,” or “Your enthusiasm is terrific”—but it is unlikely you mentioned mood outright, let alone discussed its impact on the organization’s results.

And yet our research undoubtedly will elicit a “But of course” reaction, too. Everyone knows how much a leader’s emotional state drives performance because everyone has had, at one time or another, the inspirational experience of working for an upbeat manager or the crushing experience of toiling for a sour-spirited boss. The former made everything feel possible, and as a result, stretch goals were achieved, competitors beaten, and new customers won. The latter made work grueling. In the shadow of the boss’s dark mood, other parts of the organization became “the enemy,” colleagues became suspicious of one another, and customers slipped away.

Our research, and research by other social scientists, confirms the verity of these experiences. (There are, of course, rare cases when a brutal boss produces terrific results. We explore that dynamic in the sidebar “Those Wicked Bosses Who Win.”) The studies are too numerous to mention here but, in aggregate, they show that when the leader is in a happy mood, the

people around him view everything in a more positive light. That, in turn, makes them optimistic about achieving their goals, enhances their creativity and the efficiency of their decision making, and predisposes them to be helpful. Research conducted by Alice Isen at Cornell in 1999, for example, found that an upbeat environment fosters mental efficiency, making people better at taking in and understanding information, at using decision rules in complex judgments, and at being flexible in their thinking. Other research directly links mood and financial performance. In 1986, for instance, Martin Seligman and Peter Schulman of the University of Pennsylvania demonstrated that insurance agents who had a “glass half-full” outlook were far more able than their more pessimistic peers to persist despite rejections, and thus, they closed more sales. (For more information on these studies and a list of our research base, visit www.eiconsortium.org.)

Many leaders whose emotional styles create a dysfunctional environment are eventually fired. (Of course, that’s rarely the stated reason; poor results are.) But it doesn’t have to end that way. Just as a bad mood can be turned around, so can the spread of toxic feelings from an emotionally inept leader. A look inside the brain explains both why and how.

The Science of Moods

A growing body of research on the human brain proves that, for better or worse, leaders' moods affect the emotions of the people around them. The reason for that lies in what scientists call the open-loop nature of the brain's limbic system, our emotional center. A closed-loop system is self-regulating, whereas an open-loop system depends on external sources to manage itself. In other words, we rely on connections with other people to determine our moods. The open-loop limbic system was a winning design in evolution because it let people come to one another's emotional rescue—enabling a mother, for example, to soothe her crying infant.

Those Wicked Bosses Who Win

Everyone knows of a rude and coercive CEO who, by all appearances, epitomizes the antithesis of emotional intelligence yet seems to reap great business results. If a leader's mood matters so much, how can we explain those mean-spirited, successful SOB's?

First, let's take a closer look at them. Just because a particular executive is the most visible, he may not actually lead the company. A CEO who heads a conglomerate may have no followers to speak of; it's his division heads who actively lead people and affect profitability.

Second, sometimes an SOB leader has strengths that counterbalance his caustic behavior, but they don't attract as much attention in the business press. In his early days at GE, Jack Welch exhibited a strong hand at the helm as he undertook a radical company turnaround. At that time and in that situation, Welch's firm, top-down style was appropriate. What got less press was how Welch subsequently settled into a more emotionally intelligent leadership style, especially when he articulated a new vision for the company and mobilized people to follow it.

Those caveats aside, let's get back to those infamous corporate leaders who seem to have achieved sterling business results despite their brutish approaches to leadership. Skeptics cite Bill Gates, for example, as a leader who gets away with a harsh style that should theoretically damage his company.

But our leadership model, which shows the effectiveness of specific leadership styles in specific situations, puts Gates's supposedly negative behaviors in a different light. (Our model is explained in detail in the HBR article "Leadership That Gets Results," which appeared in the March–April 2000 issue.) Gates is the achievement-driven leader par excellence, in an organization that has cherry-picked highly talented and motivated people. His apparently harsh leadership style—baldly challenging employees to surpass their past performance—can be quite effective when employees are competent, motivated, and need little direction—all characteristics of Microsoft's engineers.

In short, it's all too easy for a skeptic to argue against the importance of leaders who manage their moods by citing a "rough and tough" leader

who achieved good business results despite his bad behavior. We contend that there are, of course, exceptions to the rule, and that in some specific business cases, an SOB boss resonates just fine. But in general, leaders who are jerks must reform or else their moods and actions will eventually catch up with them.

The open-loop design serves the same purpose today as it did thousands of years ago. Research in intensive care units has shown, for example, that the comforting presence of another person not only lowers the patient's blood pressure but also slows the secretion of fatty acids that block arteries. Another study found that three or more incidents of intense stress within a year (for example, serious financial trouble, being fired, or a divorce) triples the death rate in socially isolated middle-aged men, but it has no impact on the death rate of men with many close relationships.

Scientists describe the open loop as “interpersonal limbic regulation”; one person transmits signals that can alter hormone levels, cardiovascular functions, sleep rhythms, even immune functions, inside the body of another. That's how couples are able to trigger surges of oxytocin in each other's brains, creating a pleasant, affectionate feeling. But in all aspects of social life, our physiologies intermingle. Our limbic system's open-loop design lets other people change our very physiology and hence, our emotions.

Even though the open loop is so much a part of our lives, we usually don't notice the process. Scientists have captured the attunement of emotions in the laboratory by measuring the physiology— such as heart rate—of two people sharing a good conversation. As the interaction begins, their bodies operate at different rhythms. But after 15 minutes, the physiological profiles of their bodies look remarkably similar.

Researchers have seen again and again how emotions spread irresistibly in this way whenever people are near one another. As far back as 1981, psychologists Howard Friedman and Ronald Riggio found that even completely nonverbal expressiveness can affect other people. For example, when three strangers sit facing one another in silence for a minute or two, the most emotionally expressive of the three transmits his or her mood to the other two—without a single word being spoken.

Smile and the World Smiles with You

Remember that old cliché? It's not too far from the truth. As we've shown, mood contagion is a real neurological phenomenon, but not all emotions spread with the same ease. A 1999 study conducted by Sigal Barsade at the Yale School of Management showed that, among working groups, cheerfulness and warmth spread easily, while irritability caught on less so, and depression least of all.

It should come as no surprise that laughter is the most contagious of all emotions. Hearing laughter, we find it almost impossible not to laugh or smile, too. That's because some of our brain's open-loop circuits are designed to detect smiles and laughter, making us respond in kind. Scientists theorize that this dynamic was hardwired into our brains ages ago because smiles and laughter had a way of cementing alliances, thus helping the species survive.

The main implication here for leaders undertaking the primal task of managing their moods and the moods of others is this: Humor hastens the spread of an upbeat climate. But like the leader's mood in general, humor must resonate with the organization's culture and its reality. Smiles and laughter, we would posit, are only contagious when they're genuine.

The same holds true in the office, boardroom, or shop floor; group members inevitably “catch” feelings from one another. In 2000, Caroline Bartel at New York University and Richard Saavedra at the University of Michigan found that in 70 work teams across diverse industries, people in meetings together ended up sharing moods—both good and bad—within two hours. One study asked teams of nurses and accountants to monitor their moods over weeks; researchers discovered that their emotions tracked together, and they were largely independent of each team's shared hassles. Groups, therefore, like individuals, ride emotional roller coasters, sharing everything from jealousy to angst to euphoria. (A good mood, incidentally, spreads most swiftly by the judicious use of humor. For more on this, see the sidebar “Smile and the World Smiles with You.”)

Moods that start at the top tend to move the fastest because everyone watches the boss. They take their emotional cues from him. Even when the boss isn't highly visible—for example, the CEO who works behind closed doors on an upper floor—his attitude affects the moods of his direct reports, and a domino effect ripples throughout the company.

Get Happy, Carefully

Good moods galvanize good performance, but it doesn't make sense for a leader to be as chipper as a blue jay at dawn if sales are tanking or the business is going under. The most effective executives display moods and behaviors that match the situation at hand, with a healthy dose of optimism mixed in. They respect how other people are feeling—even if it is glum or defeated—but they also model what it looks like to move forward with hope and humor.

This kind of performance, which we call resonance, is for all intents and purposes the four components of emotional intelligence in action.

Self-awareness, perhaps the most essential of the emotional intelligence competencies, is the ability to read your own emotions. It allows people to know their strengths and limitations and feel confident about their self-worth. Resonant leaders use self-awareness to gauge their own moods accurately, and they intuitively know how they are affecting others.

Self-management is the ability to control your emotions and act with honesty and integrity in reliable and adaptable ways. Resonant leaders don't let their occasional bad moods seize the day; they use self-management to leave it outside the office or to explain its source to people in a reasonable manner, so they know where it's coming from and how long it might last.

Social awareness includes the key capabilities of empathy and organizational intuition. Socially aware executives do more than sense other people's emotions, they show that they care. Further, they are experts at reading the currents of office politics. Thus, resonant leaders often keenly understand how their words and actions make others feel, and they are sensitive enough to change them when that impact is negative.

Relationship management, the last of the emotional intelligence competencies, includes the abilities to communicate clearly and convincingly, disarm conflicts, and build strong personal bonds. Resonant leaders use these skills to spread their enthusiasm and solve disagreements, often with humor and kindness.

As effective as resonant leadership is, it is just as rare. Most people suffer through dissonant leaders whose toxic moods and upsetting behaviors wreak havoc before a hopeful and realistic leader repairs the situation.

Consider what happened recently at an experimental division of the BBC, the British media giant. Even though the group's 200 or so journalists and editors had given their best effort, management decided to close the division.

The shutdown itself was bad enough, but the brusque, contentious mood and manner of the executive sent to deliver the news to the assembled staff incited something beyond the expected frustration. People became enraged—at both the decision and the bearer of the news. The executive's cranky mood and delivery created an atmosphere so threatening that he had to call security to be ushered from the room.

The next day, another executive visited the same staff. His mood was somber and respectful, as was his behavior. He spoke about the importance of journalism to the vibrancy of a society and of the calling that had drawn them all to the field in the first place. He reminded them that no one goes into journalism to get rich—as a profession its finances have always been marginal, job security ebbing and flowing with the larger economic tides. He recalled a time in his own career when he had been let go and how he had struggled to find a new position—but how he had stayed dedicated to the profession. Finally, he wished them well in getting on with their careers.

The reaction from what had been an angry mob the day before? When this resonant leader finished speaking, the staff cheered.

Call That CEO a Doctor

If the leader's mood is so important, then he or she had better get into a good one, right? Yes, but the full answer is more complicated than that. A leader's mood has the greatest impact on performance when it is upbeat. But it must also be in tune with those around him. We call this dynamic *resonance*. (For more on this, see the sidebar "Get Happy, Carefully.")

We found that an alarming number of leaders do not really know if they have resonance with their organizations. Rather, they suffer from CEO disease; its one unpleasant symptom is the sufferer's near-total ignorance about how his mood and actions appear to the organization. It's not that leaders don't care how they are perceived; most do. But they incorrectly assume that they can decipher this information themselves. Worse, they think that if they are having a negative effect, someone will tell them. They're wrong.

As one CEO in our research explains, "I so often feel I'm not getting the truth. I can never put my finger on it, because no one is actually lying to me. But I can sense that people are hiding information or camouflaging key facts. They aren't lying, but neither are they telling me everything I need to know. I'm always second-guessing."

People don't tell leaders the whole truth about their emotional impact for many reasons. Sometimes they are scared of being the bearer of bad news—and getting shot. Others feel it isn't their place to comment on such a personal topic. Still others don't realize that what they really want to talk about is the effects of the leader's emotional style—that feels too vague. Whatever the reason, the CEO can't rely on his followers to spontaneously give him the full picture.

Taking Stock

The process we recommend for self-discovery and personal reinvention is neither newfangled nor born of pop psychology, like so many self-help programs offered to executives today. Rather, it is based on three streams of research into how executives can improve the emotional intelligence capabilities most closely linked to effective leadership. (Information on these research streams can also be found at www.eiconsortium.org.) In 1989, one of us (Richard Boyatzis) began drawing on this body of research to design the five-step process itself, and since then, thousands of executives have used it successfully.

Unlike more traditional forms of coaching, our process is based on brain science. A person's emotional skills—the attitude and abilities with which someone approaches life and work—are not genetically hardwired, like eye color and skin tone. But in some ways they might as well be, because they are so deeply embedded in our neurology.

A person's emotional skills do, in fact, have a genetic component. Scientists have discovered, for instance, the gene for shyness—which is not a mood, per se, but it can certainly drive a person toward a persistently quiet demeanor, which may be read as a “down” mood. Other people are preternaturally jolly—that is, their relentless cheerfulness seems preternatural until you meet their peppy parents. As one executive explains, “All I know is that ever since I was a baby, I have always been happy. It drives some people crazy, but I couldn't get blue if I tried. And my brother is the exact same way; he saw the bright side of life, even during his divorce.”

Even though emotional skills are partly inborn, experience plays a major role in how the genes are expressed. A happy baby whose parents die or who endures physical abuse may grow into a melancholy adult. A cranky toddler may turn into a cheerful adult after discovering a fulfilling avocation. Still, research suggests that our range of emotional skills is relatively set by our mid-20s and that our accompanying behaviors are, by that time, deep-seated habits. And therein lies the rub: The more we act a certain way—be it happy,

depressed, or cranky—the more the behavior becomes ingrained in our brain circuitry, and the more we will continue to feel and act that way.

That's why emotional intelligence matters so much for a leader. An emotionally intelligent leader can monitor his or her moods through self-awareness, change them for the better through self-management, understand their impact through empathy, and act in ways that boost others' moods through relationship management.

The following five-part process is designed to rewire the brain toward more emotionally intelligent behaviors. The process begins with imagining your ideal self and then coming to terms with your real self, as others experience you. The next step is creating a tactical plan to bridge the gap between ideal and real, and after that, to practice those activities. It concludes with creating a community of colleagues and family—call them change enforcers—to keep the process alive. Let's look at the steps in more detail.

“Who do I want to be?”

Sofia, a senior manager at a northern European telecommunications company, knew she needed to understand how her emotional leadership affected others. Whenever she felt stressed, she tended to communicate poorly and take over subordinates' work so that the job would be done “right.” Attending leadership seminars hadn't changed her habits, and neither had reading management books or working with mentors.

When Sofia came to us, we asked her to imagine herself eight years from now as an effective leader and to write a description of a typical day. “What would she be doing?” we asked. “Where would she live? Who would be there? How would it feel?” We urged her to consider her deepest values and loftiest dreams and to explain how those ideals had become a part of her everyday life.

Sofia pictured herself leading her own tight-knit company staffed by ten colleagues. She was enjoying an open relationship with her daughter and had trusting relationships with her friends and coworkers. She saw herself as a relaxed and happy leader and parent, and as loving and empowering to all those around her.

In general, Sofia had a low level of self-awareness: She was rarely able to pinpoint why she was struggling at work and at home. All she could say was, “Nothing is working right.” This exercise, which prompted her to picture what life would look like if everything were going right, opened her eyes to the missing elements in her emotional style. She was able to see the impact she had on people in her life.

“Who am I now?”

In the next step of the discovery process, you come to see your leadership style as others do. This is both difficult and dangerous. Difficult, because few people have the guts to tell the boss or a colleague what he’s really like. And dangerous, because such information can sting or even paralyze. A small bit of ignorance about yourself isn’t always a bad thing: Ego-defense mechanisms have their advantages. Research by Martin Seligman shows that high-functioning people generally feel more optimistic about their prospects and possibilities than average performers. Their rose-colored lenses, in fact, fuel the enthusiasm and energy that make the unexpected and the extraordinary achievable. Playwright Henrik Ibsen called such self-delusions “vital lies,” soothing mistruths we let ourselves believe in order to face a daunting world.

But self-delusion should come in very small doses. Executives should relentlessly seek the truth about themselves, especially since it is sure to be somewhat diluted when they hear it anyway. One way to get the truth is to keep an extremely open attitude toward critiques. Another is to seek out negative feedback, even cultivating a colleague or two to play devil’s advocate.

We also highly recommend gathering feedback from as many people as possible—including bosses, peers, and subordinates. Feedback from subordinates and peers is especially helpful because it most accurately predicts a leader’s effectiveness, two, four, and even seven years out, according to research by Glenn McEvoy at Utah State and Richard Beatty at Rutgers University.

Of course, 360-degree feedback doesn’t specifically ask people to evaluate your moods, actions, and their impact. But it does reveal how people experience you. For instance, when people rate how well you listen, they are really reporting how well they think you hear them. Similarly, when 360-degree feedback elicits ratings about coaching effectiveness, the answers show whether or not people feel you understand and care about them. When the feedback uncovers low scores on, say, openness to new ideas, it means

that people experience you as inaccessible or unapproachable or both. In sum, all you need to know about your emotional impact is in 360-degree feedback, if you look for it.

One last note on this second step. It is, of course, crucial to identify your areas of weakness. But focusing only on your weaknesses can be dispiriting. That's why it is just as important, maybe even more so, to understand your strengths. Knowing where your real self overlaps with your ideal self will give you the positive energy you need to move forward to the next step in the process—bridging the gaps.

“How do I get from here to there?”

Once you know who you want to be and have compared it with how people see you, you need to devise an action plan. For Sofia, this meant planning for a real improvement in her level of self-awareness. So she asked each member of her team at work to give her feedback—weekly, anonymously, and in written form—about her mood and performance and their affect on people. She also committed herself to three tough but achievable tasks: spending an hour each day reflecting on her behavior in a journal, taking a class on group dynamics at a local college, and enlisting the help of a trusted colleague as an informal coach.

Consider, too, how Juan, a marketing executive for the Latin American division of a major integrated energy company, completed this step. Juan was charged with growing the company in his home country of Venezuela as well as in the entire region—a job that would require him to be a coach and a visionary and to have an encouraging, optimistic outlook. Yet 360-degree feedback revealed that Juan was seen as intimidating and internally focused. Many of his direct reports saw him as a grouch—impossible to please at his worst, and emotionally draining at his best.

Identifying this gap allowed Juan to craft a plan with manageable steps toward improvement. He knew he needed to hone his powers of empathy if he wanted to develop a coaching style, so he committed to various activities that would let him practice that skill. For instance, Juan decided to get to know each of his subordinates better; if he understood more about who they were, he thought, he'd be more able to help them reach their goals. He made plans with each employee to meet outside of work, where they might be more comfortable revealing their feelings.

Juan also looked for areas outside of his job to forge his missing links—for example, coaching his daughter's soccer team and volunteering at a local crisis center. Both activities helped him to experiment with how well he understood others and to try out new behaviors.

Again, let's look at the brain science at work. Juan was trying to overcome ingrained behaviors—his approach to work had taken hold over

time, without his realizing it. Bringing them into awareness was a crucial step toward changing them. As he paid more attention, the situations that arose—while listening to a colleague, coaching soccer, or talking on the phone to someone who was distraught—all became cues that stimulated him to break old habits and try new responses.

Resonance in Times of Crisis

When talking about leaders' moods, the importance of resonance cannot be overstated. While our research suggests that leaders should generally be upbeat, their behavior must be rooted in realism, especially when faced with a crisis.

Consider the response of Bob Mulholland, senior VP and head of the client relations group at Merrill Lynch, to the terrorist attacks in New York. On September 11, 2001, Mulholland and his staff in Two World Financial Center felt the building rock, then watched as smoke poured out of a gaping hole in the building directly across from theirs. People started panicking: Some ran frantically from window to window. Others were paralyzed with fear. Those with relatives working in the World Trade Center were terrified for their safety. Mulholland knew he had to act: "When there's a crisis, you've got to show people the way, step by step, and make sure you're taking care of their concerns."

He started by getting people the information they needed to "unfreeze." He found out, for instance, which floors employees' relatives worked on and assured them that they'd have enough time to escape. Then he calmed the panic-stricken, one at a time. "We're getting out of here now," he said quietly, "and you're coming with me. Not the elevator, take the stairs." He remained calm and decisive, yet he didn't minimize people's emotional responses. Thanks to him, everyone escaped before the towers collapsed.

Mulholland's leadership didn't end there. Recognizing that this event would touch each client personally, he and his team devised a way for financial consultants to connect with their clients on an emotional level. They called every client to ask, "How are you? Are your loved ones okay? How are you feeling?" As Mulholland explains, "There was no way to pick up and do business as usual. The first order of 'business' was letting our clients know we really do care."

Bob Mulholland courageously performed one of the most crucial emotional tasks of leadership: He helped himself and his people find meaning in the face of chaos and madness. To do so, he first attuned to and expressed the shared emotional reality. That's why the direction he

eventually articulated resonated at the gut level. His words and his actions reflected what people were feeling in their hearts.

This cueing for habit change is neural as well as perceptual. Researchers at the University of Pittsburgh and Carnegie Mellon University have shown that as we mentally prepare for a task, we activate the prefrontal cortex—the part of the brain that moves us into action. The greater the prior activation, the better we do at the task.

Such mental preparation becomes particularly important when we're trying to replace an old habit with a better one. As neuroscientist Cameron Carter at the University of Pittsburgh found, the prefrontal cortex becomes particularly active when a person prepares to overcome a habitual response. The aroused prefrontal cortex marks the brain's focus on what's about to happen. Without that arousal, a person will reenact tried-and-true but undesirable routines: The executive who just doesn't listen will once again cut off his subordinate, a ruthless leader will launch into yet another critical attack, and so on. That's why a learning agenda is so important. Without one, we literally do not have the brainpower to change.

“How do I make change stick?”

In short, making change last requires practice. The reason, again, lies in the brain. It takes doing and redoing, over and over, to break old neural habits. A leader must rehearse a new behavior until it becomes automatic—that is, until he’s mastered it at the level of implicit learning. Only then will the new wiring replace the old.

While it is best to practice new behaviors, as Juan did, sometimes just envisioning them will do. Take the case of Tom, an executive who wanted to close the gap between his real self (perceived by colleagues and subordinates to be cold and hard driving) and his ideal self (a visionary and a coach).

Tom’s learning plan involved finding opportunities to step back and coach his employees rather than jumping down their throats when he sensed they were wrong. Tom also began to spend idle moments during his commute thinking through how to handle encounters he would have that day. One morning, while en route to a breakfast meeting with an employee who seemed to be bungling a project, Tom ran through a positive scenario in his mind. He asked questions and listened to be sure he fully understood the situation before trying to solve the problem. He anticipated feeling impatient, and he rehearsed how he would handle these feelings.

Studies on the brain affirm the benefits of Tom’s visualization technique: Imagining something in vivid detail can fire the same brain cells actually involved in doing that activity. The new brain circuitry appears to go through its paces, strengthening connections, even when we merely repeat the sequence in our minds. So to alleviate the fears associated with trying out riskier ways of leading, we should first visualize some likely scenarios. Doing so will make us feel less awkward when we actually put the new skills into practice.

Experimenting with new behaviors and seizing opportunities inside and outside of work to practice them—as well as using such methods as mental rehearsal—eventually triggers in our brains the neural connections necessary for genuine change to occur. Even so, lasting change doesn’t happen through experimentation and brain-power alone. We need, as the song goes, a little

help from our friends.

“Who can help me?”

The fifth step in the self-discovery and reinvention process is creating a community of supporters. Take, for example, managers at Unilever who formed learning groups as part of their executive development process. At first, they gathered to discuss their careers and how to provide leadership. But because they were also charged with discussing their dreams and their learning goals, they soon realized that they were discussing both their work and their personal lives. They developed a strong mutual trust and began relying on one another for frank feedback as they worked on strengthening their leadership abilities. When this happens, the business benefits through stronger performance. Many professionals today have created similar groups, and for good reason. People we trust let us try out unfamiliar parts of our leadership repertoire without risk.

We cannot improve our emotional intelligence or change our leadership style without help from others. We not only practice with other people but also rely on them to create a safe environment in which to experiment. We need to get feedback about how our actions affect others and to assess our progress on our learning agenda.

In fact, perhaps paradoxically, in the self-directed learning process we draw on others every step of the way—from articulating and refining our ideal self and comparing it with the reality to the final assessment that affirms our progress. Our relationships offer us the very context in which we understand our progress and comprehend the usefulness of what we’re learning.

Mood over Matter

When we say that managing your mood and the moods of your followers is the task of primal leadership, we certainly don't mean to suggest that mood is all that matters. As we've noted, your actions are critical, and mood and actions together must resonate with the organization and with reality. Similarly, we acknowledge all the other challenges leaders must conquer—from strategy to hiring to new product development. It's all in a long day's work.

But taken as a whole, the message sent by neurological, psychological, and organizational research is startling in its clarity. Emotional leadership is the spark that ignites a company's performance, creating a bonfire of success or a landscape of ashes. Moods matter that much.

Originally published in December 2001. Reprint R0111C

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First eBook Edition: February 2011

ISBN: 978-1-4221-5801-2

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Leadership That Gets Results

by Daniel Goleman

ASK ANY GROUP OF businesspeople the question “What do effective leaders do?” and you’ll hear a sweep of answers. Leaders set strategy; they motivate; they create a mission; they build a culture. Then ask “What *should* leaders do?” If the group is seasoned, you’ll likely hear one response: the leader’s singular job is to get results.

But how? The mystery of what leaders can and ought to do in order to spark the best performance from their people is age-old. In recent years, that mystery has spawned an entire cottage industry: literally thousands of “leadership experts” have made careers of testing and coaching executives, all in pursuit of creating businesspeople who can turn bold objectives—be they strategic, financial, organizational, or all three—into reality.

Still, effective leadership eludes many people and organizations. One reason is that until recently, virtually no quantitative research has demonstrated which precise leadership behaviors yield positive results. Leadership experts proffer advice based on inference, experience, and instinct. Sometimes that advice is which precise leadership behaviors yield positive results. Leadership experts proffer advice based on inference, experience, and instinct. Sometimes that advice is right on target; sometimes it’s not.

But new research by the consulting firm Hay/McBer, which draws on a random sample of 3,871 executives selected from a database of more than 20,000 executives worldwide, takes much of the mystery out of effective leadership. The research found six distinct leadership styles, each springing from different components of emotional intelligence. The styles, taken individually, appear to have a direct and unique impact on the working atmosphere of a company, division, or team, and in turn, on its financial performance. And perhaps most important, the research indicates that leaders with the best results do not rely on only one leadership style; they use most of them in a given week—seamlessly and in different measure—depending on the business situation. Imagine the styles, then, as the array of clubs in a golf pro’s bag. Over the course of a game, the pro picks and chooses clubs based on the demands of the shot. Sometimes he has to ponder his selection, but usually it is automatic. The pro senses the challenge ahead, swiftly pulls out

the right tool, and elegantly puts it to work. That's how high-impact leaders operate, too.

What are the six styles of leadership? None will shock workplace veterans. Indeed, each style, by name and brief description alone, will likely resonate with anyone who leads, is led, or as is the case with most of us, does both. *Coercive leaders* demand immediate compliance. *Authoritative leaders* mobilize people toward a vision. *Affiliative leaders* create emotional bonds and harmony. *Democratic leaders* build consensus through participation. *Pacesetting leaders* expect excellence and self-direction. And *coaching leaders* develop people for the future.

Close your eyes and you can surely imagine a colleague who uses any one of these styles. You most likely use at least one yourself. What is new in this research, then, is its implications for action. First, it offers a fine-grained understanding of how different leadership styles affect performance and results. Second, it offers clear guidance on when a manager should switch between them. It also strongly suggests that switching flexibly is well advised. New, too, is the research's finding that each leadership style springs from different components of emotional intelligence.

Idea in Brief

Many managers mistakenly assume that leadership style is a function of personality rather than strategic choice. Instead of choosing the one style that suits their temperament, they should ask which style best addresses the demands of a particular situation.

Research has shown that the most successful leaders have strengths in the following emotional intelligence competencies: **self-awareness, self-regulation, motivation, empathy, and social skill**. There are six basic styles of leadership; each makes use of the key components of emotional intelligence in different combinations. The best leaders don't know just one style of leadership—they're skilled at several, and have the flexibility to switch between styles as the circumstances dictate.

Measuring Leadership's Impact

It has been more than a decade since research first linked aspects of emotional intelligence to business results. The late David McClelland, a noted Harvard University psychologist, found that leaders with strengths in a critical mass of six or more emotional intelligence competencies were far more effective than peers who lacked such strengths. For instance, when he analyzed the performance of division heads at a global food and beverage company, he found that among leaders with this critical mass of competence, 87% placed in the top third for annual salary bonuses based on their business performance. More telling, their divisions on average outperformed yearly revenue targets by 15% to 20%. Those executives who lacked emotional intelligence were rarely rated as outstanding in their annual performance reviews, and their divisions underperformed by an average of almost 20%.

Our research set out to gain a more molecular view of the links among leadership and emotional intelligence, and climate and performance. A team of McClelland's colleagues headed by Mary Fontaine and Ruth Jacobs from Hay/McBer studied data about or observed thousands of executives, noting specific behaviors and their impact on climate.¹ How did each individual motivate direct reports? Manage change initiatives? Handle crises? It was in a later phase of the research that we identified which emotional intelligence capabilities drive the six leadership styles. How does he rate in terms of self-control and social skill? Does a leader show high or low levels of empathy?

Idea in Practice

Managers often fail to appreciate how profoundly the organizational climate can influence financial results. It can account for nearly a third of financial performance. Organizational climate, in turn, is influenced by leadership style—by the way that managers motivate direct reports, gather and use information, make decisions, manage change initiatives, and handle crises. There are six basic leadership styles. Each derives from different emotional intelligence competencies, works best in particular situations, and affects the organizational climate in different ways.

1. **The coercive style.** This “Do what I say” approach can be very effective in a turnaround situation, a natural disaster, or when working with problem employees. But in most situations, coercive leadership inhibits the organization’s flexibility and dampens employees’ motivation.
2. **The authoritative style.** An authoritative leader takes a “Come with me” approach: she states the overall goal but gives people the freedom to choose their own means of achieving it. This style works especially well when a business is adrift. It is less effective when the leader is working with a team of experts who are more experienced than he is.
3. **The affiliative style.** The hallmark of the affiliative leader is a “People come first” attitude. This style is particularly useful for building team harmony or increasing morale. But its exclusive focus on praise can allow poor performance to go uncorrected. Also, affiliative leaders rarely offer advice, which often leaves employees in a quandary.
4. **The democratic style.** This style’s impact on organizational climate is not as high as you might imagine. By giving workers a voice in decisions, democratic leaders build organizational flexibility and responsibility and help generate fresh ideas. But sometimes the price is

endless meetings and confused employees who feel leaderless.

5. **The pacesetter style.** A leader who sets high performance standards and exemplifies them himself has a very positive impact on employees who are self-motivated and highly competent. But other employees tend to feel overwhelmed by such a leader's demands for excellence—and to resent his tendency to take over a situation.
6. **The coaching style.** This style focuses more on personal development than on immediate work-related tasks. It works well when employees are already aware of their weaknesses and want to improve, but not when they are resistant to changing their ways.

The more styles a leader has mastered, the better. In particular, being able to switch among the authoritative, affiliative, democratic, and coaching styles as conditions dictate creates the best organizational climate and optimizes business performance.

The team tested each executive's immediate sphere of influence for its climate. "Climate" is not an amorphous term. First defined by psychologists George Litwin and Richard Stringer and later refined by McClelland and his colleagues, it refers to six key factors that influence an organization's working environment: its *flexibility*—that is, how free employees feel to innovate unencumbered by red tape; their sense of *responsibility* to the organization; the level of *standards* that people set; the sense of accuracy about performance feedback and aptness of *rewards*; the *clarity* people have about mission and values; and finally, the level of *commitment* to a common purpose.

We found that all six leadership styles have a measurable effect on each aspect of climate. (For details, see "Getting Molecular: The Impact of Leadership Styles on Drivers of Climate.") Further, when we looked at the impact of climate on financial results—such as return on sales, revenue growth, efficiency, and profitability—we found a direct correlation between the two. Leaders who used styles that positively affected the climate had decidedly better financial results than those who did not. That is not to say

that organizational climate is the only driver of performance. Economic conditions and competitive dynamics matter enormously. But our analysis strongly suggests that climate accounts for nearly a third of results. And that's simply too much of an impact to ignore.

The Styles in Detail

Executives use six leadership styles, but only four of the six consistently have a positive effect on climate and results. Let's look then at each style of leadership in detail. (For a summary of the material that follows, see the chart "The Six Leadership Styles at a Glance.")

The coercive style

The computer company was in crisis mode—its sales and profits were falling, its stock was losing value precipitously, and its shareholders were in an uproar. The board brought in a new CEO with a reputation as a turnaround artist. He set to work chopping jobs, selling off divisions, and making the tough decisions that should have been executed years before. The company was saved, at least in the short-term.

From the start, though, the CEO created a reign of terror, bullying and demeaning his executives, roaring his displeasure at the slightest misstep. The company's top echelons were decimated not just by his erratic firings but also by defections. The CEO's direct reports, frightened by his tendency to blame the bearer of bad news, stopped bringing him any news at all. Morale was at an all-time low—a fact reflected in another downturn in the business after the short-term recovery. The CEO was eventually fired by the board of directors.

It's easy to understand why of all the leadership styles, the coercive one is the least effective in most situations. Consider what the style does to an organization's climate. Flexibility is the hardest hit. The leader's extreme top-down decision making kills new ideas on the vine. People feel so disrespected that they think, "I won't even bring my ideas up—they'll only be shot down." Likewise, people's sense of responsibility evaporates: unable to act on their own initiative, they lose their sense of ownership and feel little accountability for their performance. Some become so resentful they adopt the attitude, "I'm not going to help this bastard."

Coercive leadership also has a damaging effect on the rewards system. Most high-performing workers are motivated by more than money—they seek the satisfaction of work well done. The coercive style erodes such pride. And finally, the style undermines one of the leader's prime tools—motivating people by showing them how their job fits into a grand, shared mission. Such a loss, measured in terms of diminished clarity and commitment, leaves people alienated from their own jobs, wondering, "How does any of this matter?"

Given the impact of the coercive style, you might assume it should never be applied. Our research, however, uncovered a few occasions when it worked masterfully. Take the case of a division president who was brought in to change the direction of a food company that was losing money. His first act was to have the executive conference room demolished. To him, the room—with its long marble table that looked like “the deck of the Starship Enterprise”—symbolized the tradition-bound formality that was paralyzing the company. The destruction of the room, and the subsequent move to a smaller, more informal setting, sent a message no one could miss, and the division’s culture changed quickly in its wake.

That said, the coercive style should be used only with extreme caution and in the few situations when it is absolutely imperative, such as during a turnaround or when a hostile takeover is looming. In those cases, the coercive style can break failed business habits and shock people into new ways of working. It is always appropriate during a genuine emergency, like in the aftermath of an earthquake or a fire. And it can work with problem employees with whom all else has failed. But if a leader relies solely on this style or continues to use it once the emergency passes, the long-term impact of his insensitivity to the morale and feelings of those he leads will be ruinous.

The authoritative style

Tom was the vice president of marketing at a floundering national restaurant chain that specialized in pizza. Needless to say, the company's poor performance troubled the senior managers, but they were at a loss for what to do. Every Monday, they met to review recent sales, struggling to come up with fixes. To Tom, the approach didn't make sense. "We were always trying to figure out why our sales were down last week. We had the whole company looking backward instead of figuring out what we had to do tomorrow."

Emotional Intelligence: A Primer

Emotional intelligence—the ability to manage ourselves and our relationships effectively—consists of four fundamental capabilities: self-awareness, self-management, social awareness, and social skill. Each capability, in turn, is composed of specific sets of competencies. Below is a list of the capabilities and their corresponding traits.

Self-Awareness

- *Emotional self-awareness*: the ability to read and understand your emotions as well as recognize their impact on work performance, relationships, and the like.
- *Accurate self-assessment*: a realistic evaluation of your strengths and limitations.
- *Self-confidence*: a strong and positive sense of self-worth.

Self-Management

- *Self-control*: the ability to keep disruptive emotions and impulses under control.
- *Trustworthiness*: a consistent display of honesty and integrity.
- *Conscientiousness*: the ability to manage yourself and your responsibilities.
- *Adaptability*: skill at adjusting to changing situations and overcoming

obstacles.

- *Achievement orientation*: the drive to meet an internal standard of excellence.
- *Initiative*: a readiness to seize opportunities.

Social Awareness

- *Empathy*: skill at sensing other people's emotions, understanding their perspective, and taking an active interest in their concerns.
- *Organizational awareness*: the ability to read the currents of organizational life, build decision networks, and navigate politics.
- *Service orientation*: the ability to recognize and meet customers' needs.

Social Skill

- *Visionary leadership*: the ability to take charge and inspire with a compelling vision.
- *Influence*: the ability to wield a range of persuasive tactics.
- *Developing others*: the propensity to bolster the abilities of others through feedback and guidance.
- *Communication*: skill at listening and at sending clear, convincing, and well-tuned messages.
- *Change catalyst*: proficiency in initiating new ideas and leading people in a new direction.

- *Conflict management*: the ability to de-escalate disagreements and orchestrate resolutions.
- *Building bonds*: proficiency at cultivating and maintaining a web of relationships.
- *Teamwork and collaboration*: competence at promoting cooperation and building teams.

Tom saw an opportunity to change people's way of thinking at an off-site strategy meeting. There, the conversation began with stale truisms: the company had to drive up shareholder wealth and increase return on assets. Tom believed those concepts didn't have the power to inspire a restaurant manager to be innovative or to do better than a good-enough job.

So Tom made a bold move. In the middle of a meeting, he made an impassioned plea for his colleagues to think from the customer's perspective. Customers want convenience, he said. The company was not in the restaurant business, it was in the business of distributing high-quality, convenient-to-get pizza. That notion—and nothing else—should drive everything the company did.

Getting Molecular: The Impact of Leadership Styles on Drivers of Climate

Our research investigated how each leadership style affected the six drivers of climate, or working atmosphere. The figures below show the correlation between each leadership style and each aspect of climate. So, for instance, if we look at the climate driver of flexibility, we see that the coercive style has a $-.28$ correlation while the democratic style has a $.28$ correlation, equally strong in the opposite direction. Focusing on the authoritative leadership style, we find that it has a $.54$ correlation with rewards—strongly positive—and a $.21$ correlation with responsibility—positive, but not as strong. In other

words, the style's correlation with rewards was more than twice that with responsibility.

According to the data, the authoritative leadership style has the most positive effect on climate, but three others—affiliative, democratic, and coaching—follow close behind. That said, the research indicates that no style should be relied on exclusively, and all have at least short-term uses.

	Coercive	Authoritative	Affiliative	Democratic	Pacesetting	Coaching
Flexibility	−.28	.32	.27	.28	−.07	.17
Responsibility	−.37	.21	.16	.23	.04	.08
Standards	.02	.38	.31	.22	−.27	.39
Rewards	−.18	.54	.48	.42	−.29	.43
Clarity	−.11	.44	.37	.35	−.28	.38
Commitment	−.13	.35	.34	.26	−.20	.27
Overall Impact on climate	−.26	.54	.46	.43	−.25	.42

With his vibrant enthusiasm and clear vision—the hallmarks of the authoritative style—Tom filled a leadership vacuum at the company. Indeed, his concept became the core of the new mission statement. But this conceptual breakthrough was just the beginning. Tom made sure that the mission statement was built into the company's strategic planning process as the designated driver of growth. And he ensured that the vision was articulated so that local restaurant managers understood they were the key to the company's success and were free to find new ways to distribute pizza.

Changes came quickly. Within weeks, many local managers started guaranteeing fast, new delivery times. Even better, they started to act like entrepreneurs, finding ingenious locations to open new branches: kiosks on busy street corners and in bus and train stations, even from carts in airports and hotel lobbies.

Tom's success was no fluke. Our research indicates that of the six

leadership styles, the authoritative one is most effective, driving up every aspect of climate. Take clarity. The authoritative leader is a visionary; he motivates people by making clear to them how their work fits into a larger vision for the organization. People who work for such leaders understand that what they do matters and why. Authoritative leadership also maximizes commitment to the organization's goals and strategy. By framing the individual tasks within a grand vision, the authoritative leader defines standards that revolve around that vision. When he gives performance feedback—whether positive or negative—the singular criterion is whether or not that performance furthers the vision. The standards for success are clear to all, as are the rewards. Finally, consider the style's impact on flexibility. An authoritative leader states the end but generally gives people plenty of leeway to devise their own means. Authoritative leaders give people the freedom to innovate, experiment, and take calculated risks.

Because of its positive impact, the authoritative style works well in almost any business situation. But it is particularly effective when a business is adrift. An authoritative leader charts a new course and sells his people on a fresh long-term vision.

The authoritative style, powerful though it may be, will not work in every situation. The approach fails, for instance, when a leader is working with a team of experts or peers who are more experienced than he is; they may see the leader as pompous or out-of-touch. Another limitation: if a manager trying to be authoritative becomes overbearing, he can undermine the egalitarian spirit of an effective team. Yet even with such caveats, leaders would be wise to grab for the authoritative “club” more often than not. It may not guarantee a hole in one, but it certainly helps with the long drive.

The affiliative style

If the coercive leader demands, “Do what I say,” and the authoritative urges, “Come with me,” the affiliative leader says, “People come first.” This leadership style revolves around people—its proponents value individuals and their emotions more than tasks and goals. The affiliative leader strives to keep employees happy and to create harmony among them. He manages by building strong emotional bonds and then reaping the benefits of such an approach, namely fierce loyalty. The style also has a markedly positive effect on communication. People who like one another a lot talk a lot. They share ideas; they share inspiration. And the style drives up flexibility; friends trust one another, allowing habitual innovation and risk taking. Flexibility also rises because the affiliative leader, like a parent who adjusts household rules for a maturing adolescent, doesn’t impose unnecessary strictures on how employees get their work done. They give people the freedom to do their job in the way they think is most effective.

As for a sense of recognition and reward for work well done, the affiliative leader offers ample positive feedback. Such feedback has special potency in the workplace because it is all too rare: outside of an annual review, most people usually get no feedback on their day-to-day efforts—or only negative feedback. That makes the affiliative leader’s positive words all the more motivating. Finally, affiliative leaders are masters at building a sense of belonging. They are, for instance, likely to take their direct reports out for a meal or a drink, one-on-one, to see how they’re doing. They will bring in a cake to celebrate a group accomplishment. They are natural relationship builders.

Joe Torre, the heart and soul of the New York Yankees, is a classic affiliative leader. During the 1999 World Series, Torre tended ably to the psyches of his players as they endured the emotional pressure cooker of a pennant race. All season long, he made a special point to praise Scott Brosius, whose father had died during the season, for staying committed even as he mourned. At the celebration party after the team’s final game, Torre specifically sought out right fielder Paul O’Neill. Although he had received

the news of his father's death that morning, O'Neill chose to play in the decisive game—and he burst into tears the moment it ended. Torre made a point of acknowledging O'Neill's personal struggle, calling him a “warrior.” Torre also used the spotlight of the victory celebration to praise two players whose return the following year was threatened by contract disputes. In doing so, he sent a clear message to the team and to the club's owner that he valued the players immensely—too much to lose them.

Along with ministering to the emotions of his people, an affiliative leader may also tend to his own emotions openly. The year Torre's brother was near death awaiting a heart transplant, he shared his worries with his players. He also spoke candidly with the team about his treatment for prostate cancer.

The affiliative style's generally positive impact makes it a good all-weather approach, but leaders should employ it particularly when trying to build team harmony, increase morale, improve communication, or repair broken trust. For instance, one executive in our study was hired to replace a ruthless team leader. The former leader had taken credit for his employees' work and had attempted to pit them against one another. His efforts ultimately failed, but the team he left behind was suspicious and weary. The new executive managed to mend the situation by unstintingly showing emotional honesty and rebuilding ties. Several months in, her leadership had created a renewed sense of commitment and energy.

Despite its benefits, the affiliative style should not be used alone. Its exclusive focus on praise can allow poor performance to go uncorrected; employees may perceive that mediocrity is tolerated. And because affiliative leaders rarely offer constructive advice on how to improve, employees must figure out how to do so on their own. When people need clear directives to navigate through complex challenges, the affiliative style leaves them rudderless. Indeed, if overly relied on, this style can actually steer a group to failure. Perhaps that is why many affiliative leaders, including Torre, use this style in close conjunction with the authoritative style. Authoritative leaders state a vision, set standards, and let people know how their work is furthering the group's goals. Alternate that with the caring, nurturing approach of the affiliative leader, and you have a potent combination.

The Six Leadership Styles at a Glance

Our research found that leaders use six styles, each springing from different components of emotional intelligence. Here is a summary of the styles, their origin, when they work best, and their impact on an organization's climate and thus its performance.

	Coercive	Authoritative
The leader's modus operandi	Demands immediate compliance	Mobilizes people toward a vision
The style in a phrase	"Do what I tell you."	"Come with me."
Underlying emotional intelligence competencies	Drive to achieve, initiative, self-control	Self-confidence, empathy, change catalyst
When the style works best	In a crisis, to kick start a turnaround, or with problem employees	When changes require a new vision, or when a clear direction is needed
Overall impact on climate	Negative	Most strongly positive

The democratic style

Sister Mary ran a Catholic school system in a large metropolitan area. One of the schools—the only private school in an impoverished neighborhood—had been losing money for years, and the archdiocese could no longer afford to keep it open. When Sister Mary eventually got the order to shut it down, she didn't just lock the doors. She called a meeting of all the teachers and staff at the school and explained to them the details of the financial crisis—the first time anyone working at the school had been included in the business side of the institution. She asked for their ideas on ways to keep the school open and on how to handle the closing, should it come to that. Sister Mary spent much of her time at the meeting just listening.

She did the same at later meetings for school parents and for the community and during a successive series of meetings for the school's teachers and staff. After two months of meetings, the consensus was clear: the school would have to close. A plan was made to transfer students to other schools in the Catholic system.

Affiliative	Democratic	Pacesetting	Coaching
Creates harmony and builds emotional bonds	Forges consensus through participation	Sets high standards for performance	Develops people for the future
"People come first."	"What do you think?"	"Do as I do, now."	"Try this."
Empathy, building relationships, communication	Collaboration, team leadership, communication	Conscientiousness, drive to achieve, initiative	Developing others, empathy, self-awareness
To heal rifts in a team or to motivate people during stressful circumstances	To build buy-in or consensus, or to get input from valuable employees	To get quick results from a highly motivated and competent team	To help an employee improve performance or develop long-term strengths
Positive	Positive	Negative	Positive

The final outcome was no different than if Sister Mary had gone ahead and closed the school the day she was told to. But by allowing the school's constituents to reach that decision collectively, Sister Mary received none of the backlash that would have accompanied such a move. People mourned the loss of the school, but they understood its inevitability. Virtually no one objected.

Compare that with the experiences of a priest in our research who headed another Catholic school. He, too, was told to shut it down. And he did—by fiat. The result was disastrous: parents filed lawsuits, teachers and parents picketed, and local newspapers ran editorials attacking his decision. It took a year to resolve the disputes before he could finally go ahead and close the school.

Sister Mary exemplifies the democratic style in action—and its benefits. By spending time getting people's ideas and buy-in, a leader builds trust, respect, and commitment. By letting workers themselves have a say in decisions that affect their goals and how they do their work, the democratic leader drives up flexibility and responsibility. And by listening to employees' concerns, the democratic leader learns what to do to keep morale high. Finally, because they have a say in setting their goals and the standards for evaluating success, people operating in a democratic system tend to be very realistic about what can and cannot be accomplished.

However, the democratic style has its drawbacks, which is why its impact on climate is not as high as some of the other styles. One of its more exasperating consequences can be endless meetings where ideas are mulled over, consensus remains elusive, and the only visible result is scheduling more meetings. Some democratic leaders use the style to put off making crucial decisions, hoping that enough thrashing things out will eventually yield a blinding insight. In reality, their people end up feeling confused and leaderless. Such an approach can even escalate conflicts.

When does the style work best? This approach is ideal when a leader is himself uncertain about the best direction to take and needs ideas and guidance from able employees. And even if a leader has a strong vision, the democratic style works well to generate fresh ideas for executing that vision.

The democratic style, of course, makes much less sense when employees are not competent or informed enough to offer sound advice. And it almost goes without saying that building consensus is wrongheaded in times of

crisis. Take the case of a CEO whose computer company was severely threatened by changes in the market. He always sought consensus about what to do. As competitors stole customers and customers' needs changed, he kept appointing committees to consider the situation. When the market made a sudden shift because of a new technology, the CEO froze in his tracks. The board replaced him before he could appoint yet another task force to consider the situation. The new CEO, while occasionally democratic and affiliative, relied heavily on the authoritative style, especially in his first months.

The pacesetting style

Like the coercive style, the pacesetting style has its place in the leader's repertory, but it should be used sparingly. That's not what we expected to find. After all, the hallmarks of the pacesetting style sound admirable. The leader sets extremely high performance standards and exemplifies them himself. He is obsessive about doing things better and faster, and he asks the same of everyone around him. He quickly pinpoints poor performers and demands more from them. If they don't rise to the occasion, he replaces them with people who can. You would think such an approach would improve results, but it doesn't.

In fact, the pacesetting style destroys climate. Many employees feel overwhelmed by the pacesetter's demands for excellence, and their morale drops. Guidelines for working may be clear in the leader's head, but she does not state them clearly; she expects people to know what to do and even thinks, "If I have to tell you, you're the wrong person for the job." Work becomes not a matter of doing one's best along a clear course so much as second-guessing what the leader wants. At the same time, people often feel that the pacesetter doesn't trust them to work in their own way or to take initiative. Flexibility and responsibility evaporate; work becomes so task focused and routinized it's boring.

As for rewards, the pacesetter either gives no feedback on how people are doing or jumps in to take over when he thinks they're lagging. And if the leader should leave, people feel directionless—they're so used to "the expert" setting the rules. Finally, commitment dwindles under the regime of a pacesetting leader because people have no sense of how their personal efforts fit into the big picture.

For an example of the pacesetting style, take the case of Sam, a biochemist in R&D at a large pharmaceutical company. Sam's superb technical expertise made him an early star: he was the one everyone turned to when they needed help. Soon he was promoted to head of a team developing a new product. The other scientists on the team were as competent and self-motivated as Sam; his *métier* as team leader became offering himself as a

model of how to do first-class scientific work under tremendous deadline pressure, pitching in when needed. His team completed its task in record time.

But then came a new assignment: Sam was put in charge of R&D for his entire division. As his tasks expanded and he had to articulate a vision, coordinate projects, delegate responsibility, and help develop others, Sam began to slip. Not trusting that his subordinates were as capable as he was, he became a micromanager, obsessed with details and taking over for others when their performance slackened. Instead of trusting them to improve with guidance and development, Sam found himself working nights and weekends after stepping in to take over for the head of a floundering research team. Finally, his own boss suggested, to his relief, that he return to his old job as head of a product development team.

Although Sam faltered, the pacesetting style isn't always a disaster. The approach works well when all employees are self-motivated, highly competent, and need little direction or coordination—for example, it can work for leaders of highly skilled and self-motivated professionals, like R&D groups or legal teams. And, given a talented team to lead, pacesetting does exactly that: gets work done on time or even ahead of schedule. Yet like any leadership style, pacesetting should never be used by itself.

The coaching style

A product unit at a global computer company had seen sales plummet from twice as much as its competitors to only half as much. So Lawrence, the president of the manufacturing division, decided to close the unit and reassign its people and products. Upon hearing the news, James, the head of the doomed unit, decided to go over his boss's head and plead his case to the CEO.

What did Lawrence do? Instead of blowing up at James, he sat down with his rebellious direct report and talked over not just the decision to close the division but also James's future. He explained to James how moving to another division would help him develop new skills. It would make him a better leader and teach him more about the company's business.

Lawrence acted more like a counselor than a traditional boss. He listened to James's concerns and hopes, and he shared his own. He said he believed James had grown stale in his current job; it was, after all, the only place he'd worked in the company. He predicted that James would blossom in a new role.

The conversation then took a practical turn. James had not yet had his meeting with the CEO—the one he had impetuously demanded when he heard of his division's closing. Knowing this—and also knowing that the CEO unwaveringly supported the closing—Lawrence took the time to coach James on how to present his case in that meeting. “You don't get an audience with the CEO very often,” he noted, “let's make sure you impress him with your thoughtfulness.” He advised James not to plead his personal case but to focus on the business unit: “If he thinks you're in there for your own glory, he'll throw you out faster than you walked through the door.” And he urged him to put his ideas in writing; the CEO always appreciated that.

Lawrence's reason for coaching instead of scolding? “James is a good guy, very talented and promising,” the executive explained to us, “and I don't want this to derail his career. I want him to stay with the company, I want him to work out, I want him to learn, I want him to benefit and grow. Just because he screwed up doesn't mean he's terrible.”

Lawrence's actions illustrate the coaching style par excellence. Coaching leaders help employees identify their unique strengths and weaknesses and tie them to their personal and career aspirations. They encourage employees to establish long-term development goals and help them conceptualize a plan for attaining them. They make agreements with their employees about their role and responsibilities in enacting development plans, and they give plentiful instruction and feedback. Coaching leaders excel at delegating; they give employees challenging assignments, even if that means the tasks won't be accomplished quickly. In other words, these leaders are willing to put up with short-term failure if it furthers long-term learning.

Of the six styles, our research found that the coaching style is used least often. Many leaders told us they don't have the time in this high-pressure economy for the slow and tedious work of teaching people and helping them grow. But after a first session, it takes little or no extra time. Leaders who ignore this style are passing up a powerful tool: its impact on climate and performance are markedly positive.

Admittedly, there is a paradox in coaching's positive effect on business performance because coaching focuses primarily on personal development, not on immediate work-related tasks. Even so, coaching improves results. The reason: it requires constant dialogue, and that dialogue has a way of pushing up every driver of climate. Take flexibility. When an employee knows his boss watches him and cares about what he does, he feels free to experiment. After all, he's sure to get quick and constructive feedback. Similarly, the ongoing dialogue of coaching guarantees that people know what is expected of them and how their work fits into a larger vision or strategy. That affects responsibility and clarity. As for commitment, coaching helps there, too, because the style's implicit message is, "I believe in you, I'm investing in you, and I expect your best efforts." Employees very often rise to that challenge with their heart, mind, and soul.

The coaching style works well in many business situations, but it is perhaps most effective when people on the receiving end are "up for it." For instance, the coaching style works particularly well when employees are already aware of their weaknesses and would like to improve their performance. Similarly, the style works well when employees realize how cultivating new abilities can help them advance. In short, it works best with employees who want to be coached.

By contrast, the coaching style makes little sense when employees, for

whatever reason, are resistant to learning or changing their ways. And it flops if the leader lacks the expertise to help the employee along. The fact is, many managers are unfamiliar with or simply inept at coaching, particularly when it comes to giving ongoing performance feedback that motivates rather than creates fear or apathy. Some companies have realized the positive impact of the style and are trying to make it a core competence. At some companies, a significant portion of annual bonuses are tied to an executive's development of his or her direct reports. But many organizations have yet to take full advantage of this leadership style. Although the coaching style may not scream "bottom-line results," it delivers them.

Leaders Need Many Styles

Many studies, including this one, have shown that the more styles a leader exhibits, the better. Leaders who have mastered four or more—especially the authoritative, democratic, affiliative, and coaching styles—have the very best climate and business performance. And the most effective leaders switch flexibly among the leadership styles as needed. Although that may sound daunting, we witnessed it more often than you might guess, at both large corporations and tiny start-ups, by seasoned veterans who could explain exactly how and why they lead and by entrepreneurs who claim to lead by gut alone.

Such leaders don't mechanically match their style to fit a checklist of situations—they are far more fluid. They are exquisitely sensitive to the impact they are having on others and seamlessly adjust their style to get the best results. These are leaders, for example, who can read in the first minutes of conversation that a talented but underperforming employee has been demoralized by an unsympathetic, do-it-the-way-I-tell-you manager and needs to be inspired through a reminder of why her work matters. Or that leader might choose to reenergize the employee by asking her about her dreams and aspirations and finding ways to make her job more challenging. Or that initial conversation might signal that the employee needs an ultimatum: improve or leave.

For an example of fluid leadership in action, consider Joan, the general manager of a major division at a global food and beverage company. Joan was appointed to her job while the division was in a deep crisis. It had not made its profit targets for six years; in the most recent year, it had missed by \$50 million. Morale among the top management team was miserable; mistrust and resentments were rampant. Joan's directive from above was clear: turn the division around.

Joan did so with a nimbleness in switching among leadership styles that is rare. From the start, she realized she had a short window to demonstrate effective leadership and to establish rapport and trust. She also knew that she

urgently needed to be informed about what was not working, so her first task was to listen to key people.

Her first week on the job she had lunch and dinner meetings with each member of the management team. Joan sought to get each person's understanding of the current situation. But her focus was not so much on learning how each person diagnosed the problem as on getting to know each manager as a person. Here Joan employed the affiliative style: she explored their lives, dreams, and aspirations.

She also stepped into the coaching role, looking for ways she could help the team members achieve what they wanted in their careers. For instance, one manager who had been getting feedback that he was a poor team player confided his worries to her. He thought he was a good team member, but he was plagued by persistent complaints. Recognizing that he was a talented executive and a valuable asset to the company, Joan made an agreement with him to point out (in private) when his actions undermined his goal of being seen as a team player.

She followed the one-on-one conversations with a three-day off-site meeting. Her goal here was team building, so that everyone would own whatever solution for the business problems emerged. Her initial stance at the off-site meeting was that of a democratic leader. She encouraged everyone to express freely their frustrations and complaints.

The next day, Joan had the group focus on solutions: each person made three specific proposals about what needed to be done. As Joan clustered the suggestions, a natural consensus emerged about priorities for the business, such as cutting costs. As the group came up with specific action plans, Joan got the commitment and buy-in she sought.

With that vision in place, Joan shifted into the authoritative style, assigning accountability for each follow-up step to specific executives and holding them responsible for their accomplishment. For example, the division had been dropping prices on products without increasing its volume. One obvious solution was to raise prices, but the previous VP of sales had dithered and had let the problem fester. The new VP of sales now had responsibility to adjust the price points to fix the problem.

Over the following months, Joan's main stance was authoritative. She continually articulated the group's new vision in a way that reminded each member of how his or her role was crucial to achieving these goals. And, especially during the first few weeks of the plan's implementation, Joan felt

that the urgency of the business crisis justified an occasional shift into the coercive style should someone fail to meet his or her responsibility. As she put it, “I had to be brutal about this follow-up and make sure this stuff happened. It was going to take discipline and focus.”

The results? Every aspect of climate improved. People were innovating. They were talking about the division’s vision and crowing about their commitment to new, clear goals. The ultimate proof of Joan’s fluid leadership style is written in black ink: after only seven months, her division exceeded its yearly profit target by \$5 million.

Expanding Your Repertory

Few leaders, of course, have all six styles in their repertory, and even fewer know when and how to use them. In fact, as we have brought the findings of our research into many organizations, the most common responses have been, “But I have only two of those!” and, “I can’t use all those styles. It wouldn’t be natural.”

Such feelings are understandable, and in some cases, the antidote is relatively simple. The leader can build a team with members who employ styles she lacks. Take the case of a VP for manufacturing. She successfully ran a global factory system largely by using the affiliative style. She was on the road constantly, meeting with plant managers, attending to their pressing concerns, and letting them know how much she cared about them personally. She left the division’s strategy—extreme efficiency—to a trusted lieutenant with a keen understanding of technology, and she delegated its performance standards to a colleague who was adept at the authoritative approach. She also had a pacesetter on her team who always visited the plants with her.

An alternative approach, and one I would recommend more, is for leaders to expand their own style repertoires. To do so, leaders must first understand which emotional intelligence competencies underlie the leadership styles they are lacking. They can then work assiduously to increase their quotient of them.

Growing Your Emotional Intelligence

Unlike IQ, which is largely genetic—it changes little from childhood—the skills of emotional intelligence can be learned at any age. It's not easy, however. Growing your emotional intelligence takes practice and commitment. But the payoffs are well worth the investment.

Consider the case of a marketing director for a division of a global food company. Jack, as I'll call him, was a classic pacesetter: high-energy, always striving to find better ways to get things done, and too eager to step in and take over when, say, someone seemed about to miss a deadline. Worse, Jack was prone to pounce on anyone who didn't seem to meet his standards, flying off the handle if a person merely deviated from completing a job in the order Jack thought best.

Jack's leadership style had a predictably disastrous impact on climate and business results. After two years of stagnant performance, Jack's boss suggested he seek out a coach. Jack wasn't pleased but, realizing his own job was on the line, he complied.

The coach, an expert in teaching people how to increase their emotional intelligence, began with a 360-degree evaluation of Jack. A diagnosis from multiple viewpoints is essential in improving emotional intelligence because those who need the most help usually have blind spots. In fact, our research found that top-performing leaders overestimate their strengths on, at most, one emotional intelligence ability, whereas poor performers overrate themselves on four or more. Jack was not that far off, but he did rate himself more glowingly than his direct reports, who gave him especially low grades on emotional self-control and empathy.

Initially, Jack had some trouble accepting the feedback data. But when his coach showed him how those weaknesses were tied to his inability to display leadership styles dependent on those competencies—especially the authoritative, affiliative, and coaching styles—Jack realized he had to

improve if he wanted to advance in the company. Making such a connection is essential. The reason: improving emotional intelligence isn't done in a weekend or during a seminar—it takes diligent practice on the job, over several months. If people do not see the value of the change, they will not make that effort.

Once Jack zeroed in on areas for improvement and committed himself to making the effort, he and his coach worked up a plan to turn his day-to-day job into a learning laboratory. For instance, Jack discovered he was empathetic when things were calm, but in a crisis, he tuned out others. This tendency hampered his ability to listen to what people were telling him in the very moments he most needed to do so. Jack's plan required him to focus on his behavior during tough situations. As soon as he felt himself tensing up, his job was to immediately step back, let the other person speak, and then ask clarifying questions. The point was to not act judgmental or hostile under pressure.

The change didn't come easily, but with practice Jack learned to defuse his flare-ups by entering into a dialogue instead of launching a harangue. Although he didn't always agree with them, at least he gave people a chance to make their case. At the same time, Jack also practiced giving his direct reports more positive feedback and reminding them of how their work contributed to the group's mission. And he restrained himself from micromanaging them.

Jack met with his coach every week or two to review his progress and get advice on specific problems. For instance, occasionally Jack would find himself falling back on his old pacesetting tactics—cutting people off, jumping in to take over, and blowing up in a rage. Almost immediately, he would regret it. So he and his coach dissected those relapses to figure out what triggered the old ways and what to do the next time a similar moment arose. Such “relapse prevention” measures inoculate people against future lapses or just giving up. Over a six-month period, Jack made real improvement. His own records showed he had reduced the number of flare-ups from one or more a day at the beginning to just one or two a month. The climate had improved sharply, and the division's numbers were starting to creep upward.

Why does improving an emotional intelligence competence take months rather than days? Because the emotional centers of the brain, not just the neocortex, are involved. The neocortex, the thinking brain that learns technical skills and purely cognitive abilities, gains knowledge very quickly, but the emotional brain does not. To master a new behavior, the emotional centers need repetition and practice. Improving your emotional intelligence, then, is akin to changing your habits. Brain circuits that carry leadership habits have to unlearn the old ones and replace them with the new. The more often a behavioral sequence is repeated, the stronger the underlying brain circuits become. At some point, the new neural pathways become the brain's default option. When that happened, Jack was able to go through the paces of leadership effortlessly, using styles that worked for him—and the whole company.

For instance, an affiliative leader has strengths in three emotional intelligence competencies: in empathy, in building relationships, and in communication. Empathy—sensing how people are feeling in the moment—allows the affiliative leader to respond to employees in a way that is highly congruent with that person's emotions, thus building rapport. The affiliative leader also displays a natural ease in forming new relationships, getting to know someone as a person, and cultivating a bond. Finally, the outstanding affiliative leader has mastered the art of interpersonal communication, particularly in saying just the right thing or making the apt symbolic gesture at just the right moment.

So if you are primarily a pacesetter leader who wants to be able to use the affiliative style more often, you would need to improve your level of empathy and, perhaps, your skills at building relationships or communicating effectively. As another example, an authoritative leader who wants to add the democratic style to his repertory might need to work on the capabilities of collaboration and communication. Such advice about adding capabilities may seem simplistic—"Go change yourself"—but enhancing emotional intelligence is entirely possible with practice. (For more on how to improve emotional intelligence, see the sidebar "Growing Your Emotional Intelligence.")

More Science, Less Art

Like parenthood, leadership will never be an exact science. But neither should it be a complete mystery to those who practice it. In recent years, research has helped parents understand the genetic, psychological, and behavioral components that affect their “job performance.” With our new research, leaders, too, can get a clearer picture of what it takes to lead effectively. And perhaps as important, they can see how they can make that happen.

The business environment is continually changing, and a leader must respond in kind. Hour to hour, day to day, week to week, executives must play their leadership styles like a pro—using the right one at just the right time and in the right measure. The payoff is in the results.

Originally published in March 2000. Reprint R00204.

Notes

- [1.](#) Daniel Goleman consults with Hay/McBer on leadership development.

One More Time

How Do You Motivate Employees?

by Frederick Herzberg

HOW MANY ARTICLES, BOOKS, speeches, and workshops have pleaded plaintively, “How do I get an employee to do what I want?”

The psychology of motivation is tremendously complex, and what has been unraveled with any degree of assurance is small indeed. But the dismal ratio of knowledge to speculation has not dampened the enthusiasm for new forms of snake oil that are constantly coming on the market, many of them with academic testimonials. Doubtless this article will have no depressing impact on the market for snake oil, but since the ideas expressed in it have been tested in many corporations and other organizations, it will help—I hope—to redress the imbalance in the aforementioned ratio.

“Motivating” with KITA

In lectures to industry on the problem, I have found that the audiences are usually anxious for quick and practical answers, so I will begin with a straightforward, practical formula for moving people.

What is the simplest, surest, and most direct way of getting someone to do something? Ask? But if the person responds that he or she does not want to do it, then that calls for psychological consultation to determine the reason for such obstinacy. Tell the person? The response shows that he or she does not understand you, and now an expert in communication methods has to be brought in to show you how to get through. Give the person a monetary incentive? I do not need to remind the reader of the complexity and difficulty involved in setting up and administering an incentive system. Show the person? This means a costly training program. We need a simple way.

Every audience contains the “direct action” manager who shouts, “Kick the person!” And this type of manager is right. The surest and least circumlocuted way of getting someone to do something is to administer a kick in the pants—to give what might be called the KITA.

There are various forms of KITA, and here are some of them:

Negative physical KITA

This is a literal application of the term and was frequently used in the past. It has, however, three major drawbacks: 1) It is inelegant; 2) it contradicts the precious image of benevolence that most organizations cherish; and 3) since it is a physical attack, it directly stimulates the autonomic nervous system, and this often results in negative feedback—the employee may just kick you in return. These factors give rise to certain taboos against negative physical KITA.

In uncovering infinite sources of psychological vulnerabilities and the appropriate methods to play tunes on them, psychologists have come to the rescue of those who are no longer permitted to use negative physical KITA. “He took my rug away”; “I wonder what she meant by that”; “The boss is always going around me”—these symptomatic expressions of ego sores that have been rubbed raw are the result of application of:

Negative psychological KITA

This has several advantages over negative physical KITA. First, the cruelty is not visible; the bleeding is internal and comes much later. Second, since it affects the higher cortical centers of the brain with its inhibitory powers, it reduces the possibility of physical backlash. Third, since the number of psychological pains that a person can feel is almost infinite, the direction and site possibilities of the KITA are increased many times. Fourth, the person administering the kick can manage to be above it all and let the system accomplish the dirty work. Fifth, those who practice it receive some ego satisfaction (one-upmanship), whereas they would find drawing blood abhorrent. Finally, if the employee does complain, he or she can always be accused of being paranoid; there is no tangible evidence of an actual attack.

Idea in Brief

Imagine your workforce so motivated that employees relish *more* hours of work, not fewer, initiate increased responsibility themselves, and boast about their challenging work, not their paychecks or bonuses.

An impossible dream? Not if you understand the counterintuitive force behind motivation—and the ineffectiveness of most performance incentives. Despite media attention to the contrary, motivation does *not* come from perks, plush offices, or even promotions or pay. These **extrinsic incentives** may stimulate people to put their noses to the grindstone—but they'll likely perform only as long as it takes to get that next raise or promotion.

The truth? You and your organization have only limited power to motivate employees. Yes, unfair salaries may damage morale. But when you *do* offer fat paychecks and other extrinsic incentives, people *won't* necessarily work harder or smarter.

Why? Most of us are motivated by **intrinsic rewards**: interesting, challenging work, and the opportunity to achieve and grow into greater responsibility.

Of course, you have to provide some extrinsic incentives. After all, few of us can afford to work for *no* salary. But the *real* key to motivating your employees is enabling them to activate their own *internal* generators. Otherwise, you'll be stuck trying to recharge their batteries yourself—again and again.

Now, what does negative KITA accomplish? If I kick you in the rear (physically or psychologically), who is motivated? *I* am motivated; *you* move! Negative KITA does not lead to motivation, but to movement. So:

Idea in Practice

How do you help employees charge themselves up? **Enrich their jobs** by applying these principles:

- Increase individuals' accountability for their work by removing some controls.
- Give people responsibility for a *complete* process or unit of work.
- Make information available directly to employees rather than sending it through their managers first.
- Enable people to take on new, more difficult tasks they haven't handled before.
- Assign individuals specialized tasks that allow them to become experts.

The payoff? Employees gain an enhanced sense of responsibility and achievement, along with new opportunities to learn and grow—continually.

Example: A large firm began enriching stockholder correspondents' jobs by appointing subject-matter experts within each unit—then encouraging other unit members to consult with them before seeking supervisory help. It also held correspondents personally responsible for their communications' quality and quantity. Supervisors who had proofread and signed *all* letters now checked only 10% of them. And rather than harping on production quotas, supervisors no longer discussed daily quantities.

These deceptively modest changes paid big dividends: Within six months, the correspondents' motivation soared—as measured by their answers to

questions such as “How many opportunities do you feel you have in your job for making worthwhile contributions?” Equally valuable, their performance noticeably improved, as measured by their communications’ quality and accuracy, and their speed of response to stockholders.

Job enrichment isn’t easy. Managers may initially fear that they’ll no longer be needed once their direct reports take on more responsibility. Employees will likely require time to master new tasks and challenges.

But managers will eventually rediscover their real functions, for example, *developing* staff rather than simply checking their work. And employees’ enthusiasm and commitment will ultimately rise—along with your company’s overall performance.

Positive KITA

Let us consider motivation. If I say to you, “Do this for me or the company, and in return I will give you a reward, an incentive, more status, a promotion, all the quid pro quos that exist in the industrial organization,” am I motivating you? The overwhelming opinion I receive from management people is, “Yes, this is motivation.”

I have a year-old schnauzer. When it was a small puppy and I wanted it to move, I kicked it in the rear and it moved. Now that I have finished its obedience training, I hold up a dog biscuit when I want the schnauzer to move. In this instance, who is motivated—I or the dog? The dog wants the biscuit, but it is I who want it to move. Again, I am the one who is motivated, and the dog is the one who moves. In this instance all I did was apply KITA frontally; I exerted a pull instead of a push. When industry wishes to use such positive KITAs, it has available an incredible number and variety of dog biscuits (jelly beans for humans) to wave in front of employees to get them to jump.

Myths About Motivation

Why is KITA not motivation? If I kick my dog (from the front or the back), he will move. And when I want him to move again, what must I do? I must kick him again. Similarly, I can charge a person's battery, and then recharge it, and recharge it again. But it is only when one has a generator of one's own that we can talk about motivation. One then needs no outside stimulation. One *wants* to do it.

With this in mind, we can review some positive KITA personnel practices that were developed as attempts to instill "motivation":

1. Reducing time spent at work

This represents a marvelous way of motivating people to work—getting them off the job! We have reduced (formally and informally) the time spent on the job over the last 50 or 60 years until we are finally on the way to the "6-day weekend." An interesting variant of this approach is the development of off-hour recreation programs. The philosophy here seems to be that those who play together, work together. The fact is that motivated people seek more hours of work, not fewer.

2. Spiraling wages

Have these motivated people? Yes, to seek the next wage increase. Some medievalists still can be heard to say that a good depression will get employees moving. They feel that if rising wages don't or won't do the job, reducing them will.

3. Fringe benefits

Industry has outdone the most welfare-minded of welfare states in dispensing cradle-to-the-grave succor. One company I know of had an informal "fringe benefit of the month club" going for a while. The cost of fringe benefits in this country has reached approximately 25% of the wage dollar, and we still cry for motivation.

People spend less time working for more money and more security than

ever before, and the trend cannot be reversed. These benefits are no longer rewards; they are rights. A 6-day week is inhuman, a 10-hour day is exploitation, extended medical coverage is a basic decency, and stock options are the salvation of American initiative. Unless the ante is continuously raised, the psychological reaction of employees is that the company is turning back the clock.

When industry began to realize that both the economic nerve and the lazy nerve of their employees had insatiable appetites, it started to listen to the behavioral scientists who, more out of a humanist tradition than from scientific study, criticized management for not knowing how to deal with people. The next KITA easily followed.

4. Human relations training

More than 30 years of teaching and, in many instances, of practicing psychological approaches to handling people have resulted in costly human relations programs and, in the end, the same question: How do you motivate workers? Here, too, escalations have taken place. Thirty years ago it was necessary to request, "Please don't spit on the floor." Today the same admonition requires three "pleases" before the employee feels that a superior has demonstrated the psychologically proper attitude.

The failure of human relations training to produce motivation led to the conclusion that supervisors or managers themselves were not psychologically true to themselves in their practice of interpersonal decency. So an advanced form of human relations KITA, sensitivity training, was unfolded.

5. Sensitivity training

Do you really, really understand yourself? Do you really, really, really trust other people? Do you really, really, really, really cooperate? The failure of sensitivity training is now being explained, by those who have become opportunistic exploiters of the technique, as a failure to really (five times) conduct proper sensitivity training courses.

With the realization that there are only temporary gains from comfort and economic and interpersonal KITA, personnel managers concluded that the fault lay not in what they were doing, but in the employee's failure to appreciate what they were doing. This opened up the field of communications, a new area of "scientifically" sanctioned KITA.

6. Communications

The professor of communications was invited to join the faculty of management training programs and help in making employees understand what management was doing for them. House organs, briefing sessions, supervisory instruction on the importance of communication, and all sorts of propaganda have proliferated until today there is even an International Council of Industrial Editors. But no motivation resulted, and the obvious thought occurred that perhaps management was not hearing what the employees were saying. That led to the next KITA.

7. Two-way communication

Management ordered morale surveys, suggestion plans, and group participation programs. Then both management and employees were communicating and listening to each other more than ever, but without much improvement in motivation.

The behavioral scientists began to take another look at their conceptions and their data, and they took human relations one step further. A glimmer of truth was beginning to show through in the writings of the so-called higher-order-need psychologists. People, so they said, want to actualize themselves. Unfortunately, the “actualizing” psychologists got mixed up with the human relations psychologists, and a new KITA emerged.

8. Job participation

Though it may not have been the theoretical intention, job participation often became a “give them the big picture” approach. For example, if a man is tightening 10,000 nuts a day on an assembly line with a torque wrench, tell him he is building a Chevrolet. Another approach had the goal of giving employees a “feeling” that they are determining, in some measure, what they do on the job. The goal was to provide a *sense* of achievement rather than a substantive achievement in the task. Real achievement, of course, requires a task that makes it possible.

But still there was no motivation. This led to the inevitable conclusion that the employees must be sick, and therefore to the next KITA.

9. Employee counseling

The initial use of this form of KITA in a systematic fashion can be credited to the Hawthorne experiment of the Western Electric Company during the early

1930s. At that time, it was found that the employees harbored irrational feelings that were interfering with the rational operation of the factory. Counseling in this instance was a means of letting the employees unburden themselves by talking to someone about their problems. Although the counseling techniques were primitive, the program was large indeed.

The counseling approach suffered as a result of experiences during World War II, when the programs themselves were found to be interfering with the operation of the organizations; the counselors had forgotten their role of benevolent listeners and were attempting to do something about the problems that they heard about. Psychological counseling, however, has managed to survive the negative impact of World War II experiences and today is beginning to flourish with renewed sophistication. But, alas, many of these programs, like all the others, do not seem to have lessened the pressure of demands to find out how to motivate workers.

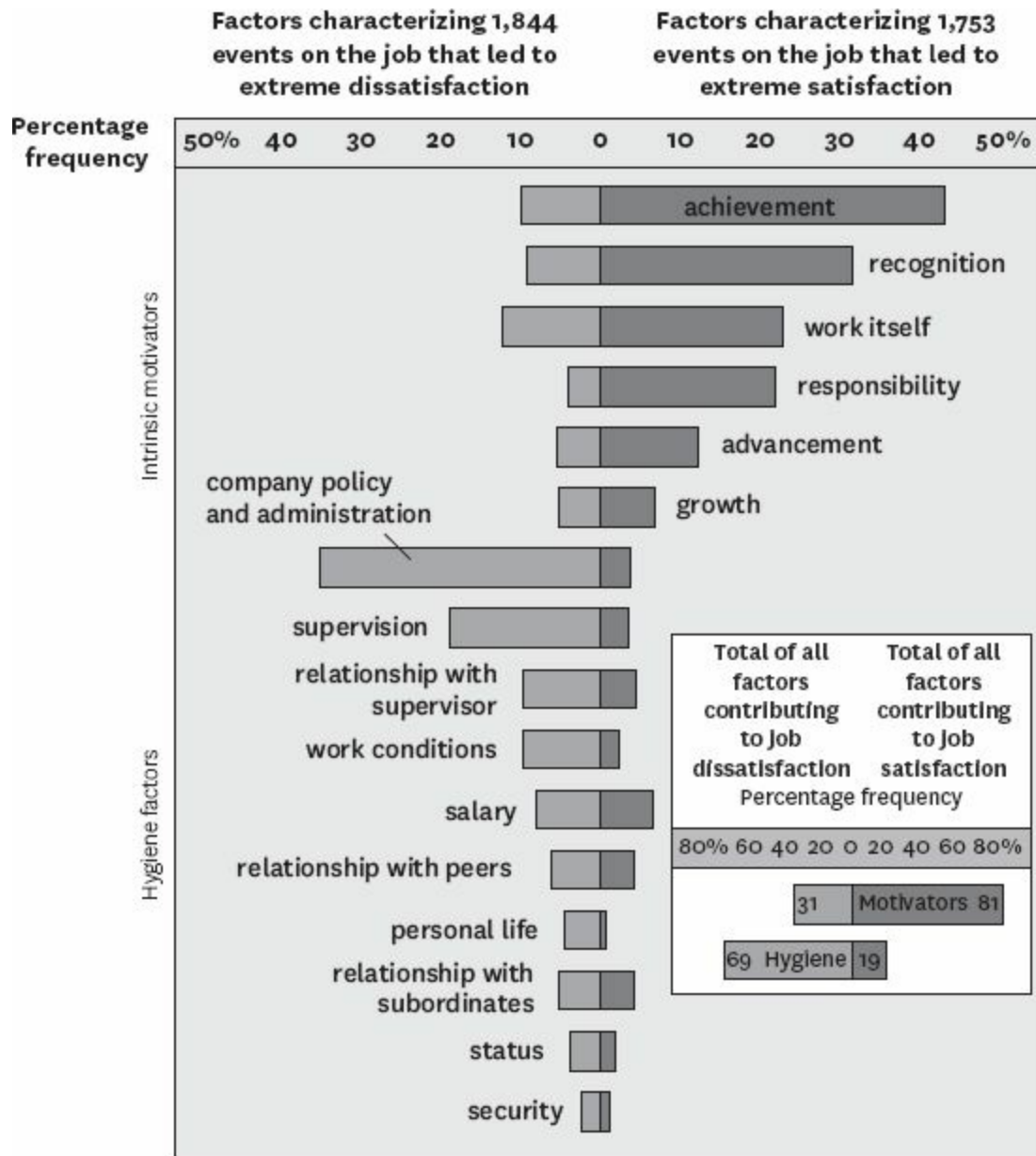
Since KITA results only in short-term movement, it is safe to predict that the cost of these programs will increase steadily and new varieties will be developed as old positive KITAs reach their satiation points.

Hygiene vs. Motivators

Let me rephrase the perennial question this way: How do you install a generator in an employee? A brief review of my motivation-hygiene theory of job attitudes is required before theoretical and practical suggestions can be offered. The theory was first drawn from an examination of events in the lives of engineers and accountants. At least 16 other investigations, using a wide variety of populations (including some in the Communist countries), have since been completed, making the original research one of the most replicated studies in the field of job attitudes.

The findings of these studies, along with corroboration from many other investigations using different procedures, suggest that the factors involved in producing job satisfaction (and motivation) are separate and distinct from the factors that lead to job dissatisfaction. (See “Factors affecting job attitudes as reported in 12 investigations,” which is further explained below.) Since separate factors need to be considered, depending on whether job satisfaction or job dissatisfaction is being examined, it follows that these two feelings are not opposites of each other. The opposite of job satisfaction is not job dissatisfaction but, rather, *no* job satisfaction; and similarly, the opposite of job dissatisfaction is not job satisfaction, but *no* job dissatisfaction.

Factors affecting job attitudes as reported in 12 investigations



Stating the concept presents a problem in semantics, for we normally think of satisfaction and dissatisfaction as opposites; i.e., what is not satisfying must be dissatisfying, and vice versa. But when it comes to understanding the behavior of people in their jobs, more than a play on words is involved.

Two different needs of human beings are involved here. One set of needs can be thought of as stemming from humankind's animal nature—the built-in drive to avoid pain from the environment, plus all the learned drives that

become conditioned to the basic biological needs. For example, hunger, a basic biological drive, makes it necessary to earn money, and then money becomes a specific drive. The other set of needs relates to that unique human characteristic, the ability to achieve and, through achievement, to experience psychological growth. The stimuli for the growth needs are tasks that induce growth; in the industrial setting, they are the job content. Contrariwise, the stimuli inducing pain-avoidance behavior are found in the job environment.

The growth or *motivator* factors that are intrinsic to the job are: achievement, recognition for achievement, the work itself, responsibility, and growth or advancement. The dissatisfaction-avoidance or hygiene (KITA) factors that are extrinsic to the job include: company policy and administration, supervision, interpersonal relationships, working conditions, salary, status, and security.

A composite of the factors that are involved in causing job satisfaction and job dissatisfaction, drawn from samples of 1,685 employees, is shown in “Factors affecting job attitudes as reported in 12 investigations.” The results indicate that motivators were the primary cause of satisfaction, and hygiene factors the primary cause of unhappiness on the job. The employees, studied in 12 different investigations, included lower level supervisors, professional women, agricultural administrators, men about to retire from management positions, hospital maintenance personnel, manufacturing supervisors, nurses, food handlers, military officers, engineers, scientists, housekeepers, teachers, technicians, female assemblers, accountants, Finnish foremen, and Hungarian engineers.

They were asked what job events had occurred in their work that had led to extreme satisfaction or extreme dissatisfaction on their part. Their responses are broken down in the figure into percentages of total “positive” job events and of total “negative” job events. (The figures total more than 100% on both the “hygiene” and “motivators” sides because often at least two factors can be attributed to a single event; advancement, for instance, often accompanies assumption of responsibility.)

To illustrate, a typical response involving achievement that had a negative effect for the employee was, “I was unhappy because I didn’t do the job successfully.” A typical response in the small number of positive job events in the company policy and administration grouping was, “I was happy because the company reorganized the section so that I didn’t report any longer to the guy I didn’t get along with.”

As the lower right-hand part of the figure shows, of all the factors contributing to job satisfaction, 81% were motivators. And of all the factors contributing to the employees' dissatisfaction over their work, 69% involved hygiene elements.

Eternal triangle

There are three general philosophies of personnel management. The first is based on organizational theory, the second on industrial engineering, and the third on behavioral science.

Organizational theorists believe that human needs are either so irrational or so varied and adjustable to specific situations that the major function of personnel management is to be as pragmatic as the occasion demands. If jobs are organized in a proper manner, they reason, the result will be the most efficient job structure, and the most favorable job attitudes will follow as a matter of course.

Industrial engineers hold that humankind is mechanistically oriented and economically motivated and that human needs are best met by attuning the individual to the most efficient work process. The goal of personnel management therefore should be to concoct the most appropriate incentive system and to design the specific working conditions in a way that facilitates the most efficient use of the human machine. By structuring jobs in a manner that leads to the most efficient operation, engineers believe that they can obtain the optimal organization of work and the proper work attitudes.

Behavioral scientists focus on group sentiments, attitudes of individual employees, and the organization's social and psychological climate. This persuasion emphasizes one or more of the various hygiene and motivator needs. Its approach to personnel management is generally to emphasize some form of human relations education, in the hope of instilling healthy employee attitudes and an organizational climate that is considered to be felicitous to human values. The belief is that proper attitudes will lead to efficient job and organizational structure.

There is always a lively debate concerning the overall effectiveness of the approaches of organizational theorists and industrial engineers. Manifestly, both have achieved much. But the nagging question for behavioral scientists has been: What is the cost in human problems that eventually cause more expense to the organization—for instance, turnover, absenteeism, errors, violation of safety rules, strikes, restriction of output, higher wages, and

greater fringe benefits? On the other hand, behavioral scientists are hard put to document much manifest improvement in personnel management, using their approach.

The motivation-hygiene theory suggests that work be *enriched* to bring about effective utilization of personnel. Such a systematic attempt to motivate employees by manipulating the motivator factors is just beginning. The term *job enrichment* describes this embryonic movement. An older term, job enlargement, should be avoided because it is associated with past failures stemming from a misunderstanding of the problem. Job enrichment provides the opportunity for the employee's psychological growth, while job enlargement merely makes a job structurally bigger. Since scientific job enrichment is very new, this article only suggests the principles and practical steps that have recently emerged from several successful experiments in industry.

Job loading

In attempting to enrich certain jobs, management often reduces the personal contribution of employees rather than giving them opportunities for growth in their accustomed jobs. Such endeavors, which I shall call horizontal job loading (as opposed to vertical loading, or providing motivator factors), have been the problem of earlier job enlargement programs. Job loading merely enlarges the meaninglessness of the job. Some examples of this approach, and their effect, are:

- Challenging the employee by increasing the amount of production expected. If each tightens 10,000 bolts a day, see if each can tighten 20,000 bolts a day. The arithmetic involved shows that multiplying zero by zero still equals zero.
- Adding another meaningless task to the existing one, usually some routine clerical activity. The arithmetic here is adding zero to zero.
- Rotating the assignments of a number of jobs that need to be enriched. This means washing dishes for a while, then washing silverware. The arithmetic is substituting one zero for another zero.
- Removing the most difficult parts of the assignment in order to free the worker to accomplish more of the less challenging assignments. This traditional industrial engineering approach amounts to subtraction in the hope of accomplishing addition.

These are common forms of horizontal loading that frequently come up in preliminary brainstorming sessions of job enrichment. The principles of

vertical loading have not all been worked out as yet, and they remain rather general, but I have furnished seven useful starting points for consideration in “Principles of vertical job loading.”

A successful application

An example from a highly successful job enrichment experiment can illustrate the distinction between horizontal and vertical loading of a job. The subjects of this study were the stockholder correspondents employed by a very large corporation. Seemingly, the task required of these carefully selected and highly trained correspondents was quite complex and challenging. But almost all indexes of performance and job attitudes were low, and exit interviewing confirmed that the challenge of the job existed merely as words.

Principles of vertical job loading

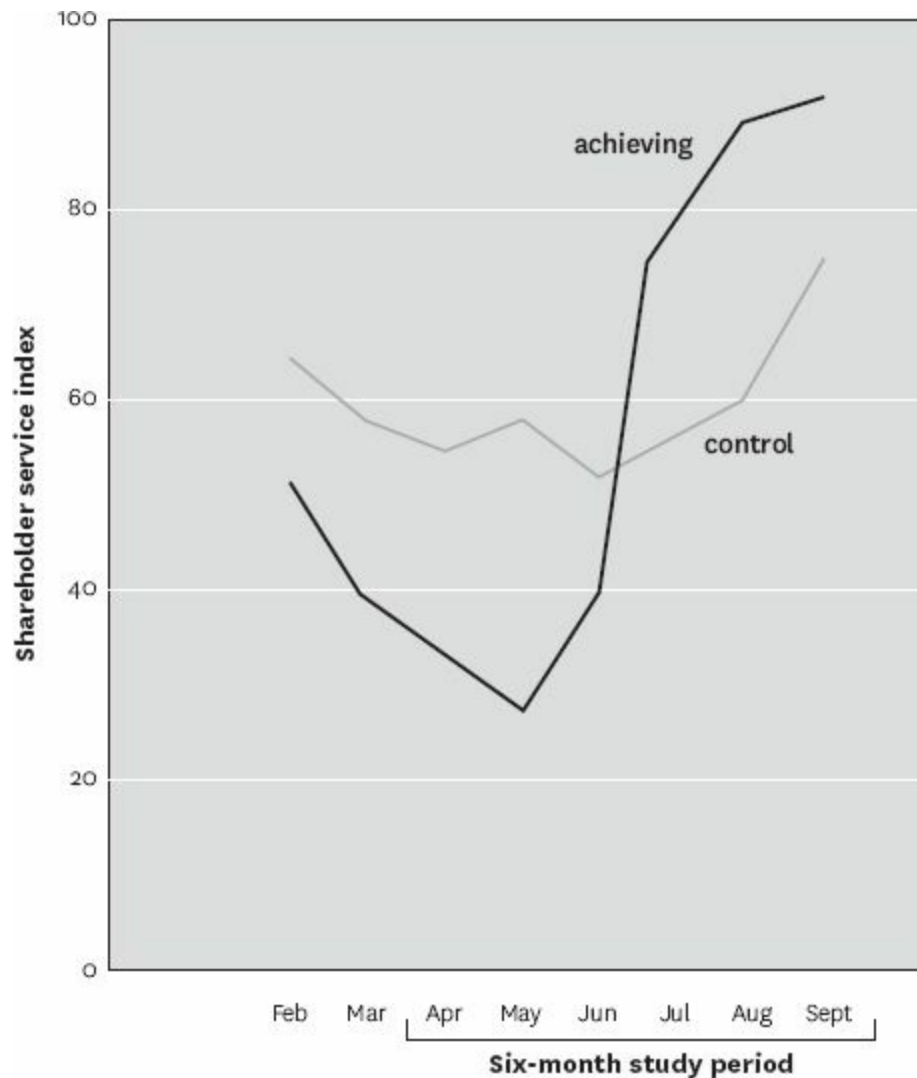
Principle	Motivators Involved
A. Removing some controls while retaining accountability	Responsibility and personal achievement
B. Increasing the accountability of individuals for own work	Responsibility and recognition
C. Giving a person a complete natural unit of work (module, division, area, and so on)	Responsibility, achievement, and recognition
D. Granting additional authority to employees in their activity; job freedom	Responsibility, achievement, and recognition
E. Making periodic reports directly available to the workers themselves rather than to supervisors	Internal recognition
F. Introducing new and more difficult tasks not previously handled	Growth and learning
G. Assigning individuals specific or specialized tasks, enabling them to become experts	Responsibility, growth, and advancement

A job enrichment project was initiated in the form of an experiment with one group, designated as an achieving unit, having its job enriched by the

principles described in “Principles of vertical job loading.” A control group continued to do its job in the traditional way. (There were also two “uncommitted” groups of correspondents formed to measure the so-called Hawthorne effect—that is, to gauge whether productivity and attitudes toward the job changed artificially merely because employees sensed that the company was paying more attention to them in doing something different or novel. The results for these groups were substantially the same as for the control group, and for the sake of simplicity I do not deal with them in this summary.) No changes in hygiene were introduced for either group other than those that would have been made anyway, such as normal pay increases.

Employee performance in company experiment

Three-month cumulative average



The changes for the achieving unit were introduced in the first two months, averaging one per week of the seven motivators listed in “Principles of vertical job loading.” At the end of six months the members of the achieving unit were found to be outperforming their counterparts in the control group and, in addition, indicated a marked increase in their liking for their jobs. Other results showed that the achieving group had lower absenteeism and, subsequently, a much higher rate of promotion.

“Employee performance in company experiment” illustrates the changes in performance, measured in February and March, before the study period began, and at the end of each month of the study period. The shareholder service index represents quality of letters, including accuracy of information,

and speed of response to stockholders' letters of inquiry. The index of a current month was averaged into the average of the two prior months, which means that improvement was harder to obtain if the indexes of the previous months were low. The "achievers" were performing less well before the six-month period started, and their performance service index continued to decline after the introduction of the motivators, evidently because of uncertainty after their newly granted responsibilities. In the third month, however, performance improved, and soon the members of this group had reached a high level of accomplishment.

"Change in attitudes toward tasks in company experiment" shows the two groups' attitudes toward their job, measured at the end of March, just before the first motivator was introduced, and again at the end of September. The correspondents were asked 16 questions, all involving motivation. A typical one was, "As you see it, how many opportunities do you feel that you have in your job for making worthwhile contributions?" The answers were scaled from 1 to 5, with 80 as the maximum possible score. The achievers became much more positive about their job, while the attitude of the control unit remained about the same (the drop is not statistically significant).

How was the job of these correspondents restructured? "Enlargement versus enrichment of correspondents' tasks in company experiment" lists the suggestions made that were deemed to be horizontal loading, and the actual vertical loading changes that were incorporated in the job of the achieving unit. The capital letters under "Principle" after "Vertical Loading" refer to the corresponding letters in "Principles of vertical job loading." The reader will note that the rejected forms of horizontal loading correspond closely to the list of common manifestations I mentioned earlier.

Steps for Job Enrichment

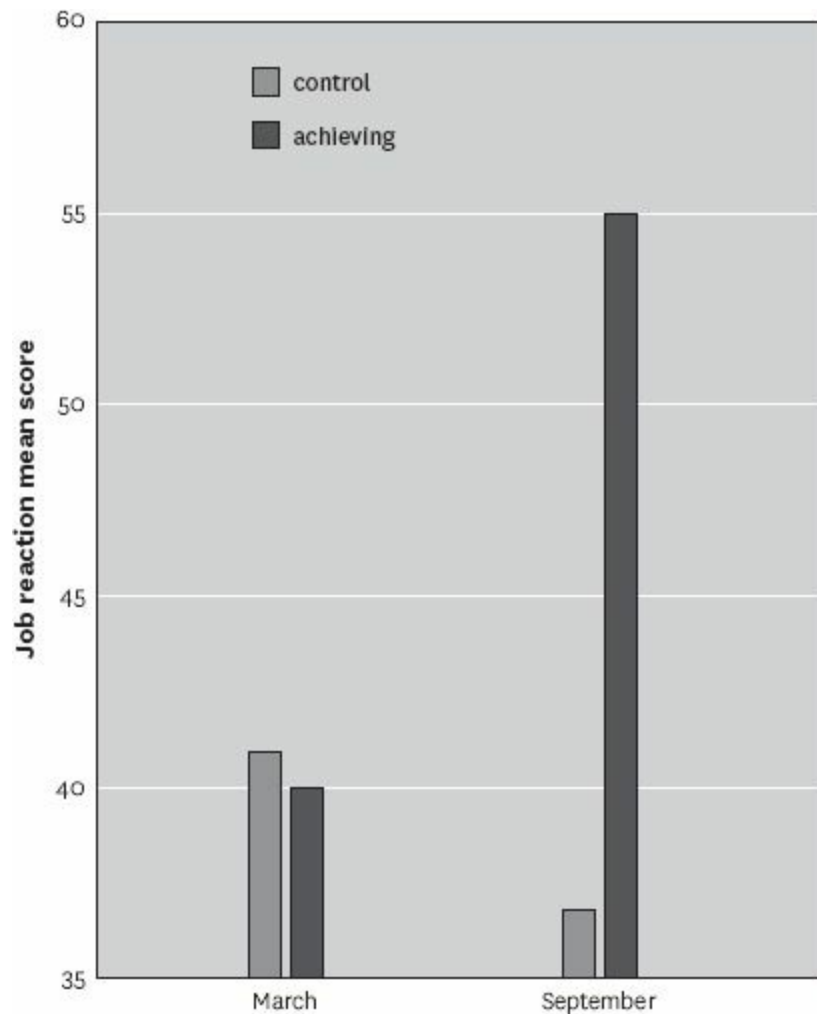
Now that the motivator idea has been described in practice, here are the steps that managers should take in instituting the principle with their employees:

1. Select those jobs in which a) the investment in industrial engineering does not make changes too costly, b) attitudes are poor, c) hygiene is becoming very costly, and d) motivation will make a difference in performance.
2. Approach these jobs with the conviction that they can be changed. Years of tradition have led managers to believe that job content is sacrosanct and the only scope of action that they have is in ways of stimulating people.
3. Brainstorm a list of changes that may enrich the jobs, without concern for their practicality.
4. Screen the list to eliminate suggestions that involve hygiene, rather than actual motivation.
5. Screen the list for generalities, such as “give them more responsibility,” that are rarely followed in practice. This might seem obvious, but the motivator words have never left industry; the substance has just been rationalized and organized out. Words like “responsibility,” “growth,” “achievement,” and “challenge,” for example, have been elevated to the lyrics of the patriotic anthem for all organizations. It is the old problem typified by the pledge of allegiance to the flag being more important than contributions to the country—of following the form, rather than the substance.

6. Screen the list to eliminate any *horizontal* loading suggestions.
7. Avoid direct participation by the employees whose jobs are to be enriched. Ideas they have expressed previously certainly constitute a valuable source for recommended changes, but their direct involvement contaminates the process with human relations *hygiene* and, more specifically, gives them only a *sense* of making a contribution. The job is to be changed, and it is the content that will produce the motivation, not attitudes about being involved or the challenge inherent in setting up a job. That process will be over shortly, and it is what the employees will be doing from then on that will determine their motivation. A sense of participation will result only in short-term movement.

Change in attitudes toward tasks in company experiment

Mean scores at beginning and end of six-month period



8. In the initial attempts at job enrichment, set up a controlled experiment. At least two equivalent groups should be chosen, one an experimental unit in which the motivators are systematically introduced over a period of time, and the other one a control group in which no changes are made. For both groups, hygiene should be allowed to follow its natural course for the duration of the experiment. Pre- and post-installation tests of performance and job attitudes are necessary to evaluate the effectiveness of the job enrichment program. The attitude test must be limited to motivator items in order to divorce employees' views of the jobs they are given from all the surrounding hygiene feelings that they might have.

9. Be prepared for a drop in performance in the experimental group the first few weeks. The changeover to a new job may lead to a temporary reduction in efficiency.
10. Expect your first-line supervisors to experience some anxiety and hostility over the changes you are making. The anxiety comes from their fear that the changes will result in poorer performance for their unit. Hostility will arise when the employees start assuming what the supervisors regard as their own responsibility for performance. The supervisor without checking duties to perform may then be left with little to do.

After successful experiment, however, the supervisors usually discover the supervisory and managerial functions they have neglected, or which were never theirs because all their time was given over to checking the work of their subordinates. For example, in the R&D division of one large chemical company I know of, the supervisors of the laboratory assistants were theoretically responsible for their training and evaluation. These functions, however, had come to be performed in a routine, unsubstantial fashion. After the job enrichment program, during which the supervisors were not merely passive observers of the assistants' performance, the supervisors actually were devoting their time to reviewing performance and administering thorough training.

Enlargement versus enrichment of correspondents' tasks in company experiment

Horizontal loading suggestions rejected

Firm quotas could be set for letters to be answered each day, using a rate that would be hard to reach.

The secretaries could type the letters themselves, as well as compose them, or take on any other clerical functions.

All difficult or complex inquiries could be channeled to a few secretaries so that the remainder could achieve high rates of output. These jobs could be exchanged from time to time.

The secretaries could be rotated through units handling different customers and then sent back to their own units.

Vertical loading suggestions adopted

Principle

Subject matter experts were appointed within each unit for other members of the unit to consult before seeking supervisory help. (The supervisor had been answering all specialized and difficult questions.)

G

Correspondents signed their own names on letters. (The supervisor had been signing all letters.)

B

The work of the more experienced correspondents was proofread less frequently by supervisors and was done at the correspondents' desks, dropping verification from 100% to 10%. (Previously, all correspondents' letters had been checked by the supervisor.)

A

Production was discussed, but only in terms such as "a full day's work is expected." As time went on, this was no longer mentioned. (Before, the group had been constantly reminded of the number of letters that needed to be answered.)

D

Outgoing mail went directly to the mailroom without going over supervisor's desks. (The letters had always been routed through the supervisors.)

A

Correspondents were encouraged to answer letters in a more personalized way. (Reliance on the form-letter approach had been standard practice.)

C

Each correspondent was held personally responsible for the quality and accuracy of letters. (This responsibility had been the province of the supervisor and the verifier.)

B, E

What has been called an employee-centered style of supervision will come about not through education of supervisors, but by changing the jobs that they do.

Job enrichment will not be a one-time proposition, but a continuous

management function. The initial changes should last for a very long period of time. There are a number of reasons for this:

- The changes should bring the job up to the level of challenge commensurate with the skill that was hired.
- Those who have still more ability eventually will be able to demonstrate it better and win promotion to higher level jobs.
- The very nature of motivators, as opposed to hygiene factors, is that they have a much longer-term effect on employees' attitudes. It is possible that the job will have to be enriched again, but this will not occur as frequently as the need for hygiene.

Not all jobs can be enriched, nor do all jobs need to be enriched. If only a small percentage of the time and money that is now devoted to hygiene, however, were given to job enrichment efforts, the return in human satisfaction and economic gain would be one of the largest dividends that industry and society have ever reaped through their efforts at better personnel management.

The argument for job enrichment can be summed up quite simply: If you have employees on a job, use them. If you can't use them on the job, get rid of them, either via automation or by selecting someone with lesser ability. If you can't use them and you can't get rid of them, you will have a motivation problem.

Originally published in September 1987. Reprint R0301F.

The Set-Up-to-Fail Syndrome

by Jean-François Manzoni and Jean-Louis Barsoux

WHEN AN EMPLOYEE FAILS—or even just performs poorly—managers typically do not blame themselves. The employee doesn't understand the work, a manager might contend. Or the employee isn't driven to succeed, can't set priorities, or won't take direction. Whatever the reason, the problem is assumed to be the employee's fault—and the employee's responsibility.

But is it? Sometimes, of course, the answer is yes. Some employees are not up to their assigned tasks and never will be, for lack of knowledge, skill, or simple desire. But sometimes—and we would venture to say often—an employee's poor performance can be blamed largely on his boss.

Perhaps "blamed" is too strong a word, but it is directionally correct. In fact, our research strongly suggests that bosses—albeit accidentally and usually with the best intentions—are often complicit in an employee's lack of success. (See the sidebar "About the Research.") How? By creating and reinforcing a dynamic that essentially sets up perceived underperformers to fail. If the Pygmalion effect describes the dynamic in which an individual lives up to great expectations, the set-up-to-fail syndrome explains the opposite. It describes a dynamic in which employees perceived to be mediocre or weak performers live down to the low expectations their managers have for them. The result is that they often end up leaving the organization—either of their own volition or not.

The syndrome usually begins surreptitiously. The initial impetus can be performance related, such as when an employee loses a client, undershoots a target, or misses a deadline. Often, however, the trigger is less specific. An

employee is transferred into a division with a lukewarm recommendation from a previous boss. Or perhaps the boss and the employee don't really get along on a personal basis—several studies have indeed shown that compatibility between boss and subordinate, based on similarity of attitudes, values, or social characteristics, can have a significant impact on a boss's impressions. In any case, the syndrome is set in motion when the boss begins to worry that the employee's performance is not up to par.

The boss then takes what seems like the obvious action in light of the subordinate's perceived shortcomings: he increases the time and attention he focuses on the employee. He requires the employee to get approval before making decisions, asks to see more paperwork documenting those decisions, or watches the employee at meetings more closely and critiques his comments more intensely.

These actions are intended to boost performance and prevent the subordinate from making errors. Unfortunately, however, subordinates often interpret the heightened supervision as a lack of trust and confidence. In time, because of low expectations, they come to doubt their own thinking and ability, and they lose the motivation to make autonomous decisions or to take any action at all. The boss, they figure, will just question everything they do—or do it himself anyway.

Ironically, the boss sees the subordinate's withdrawal as proof that the subordinate is indeed a poor performer. The subordinate, after all, isn't contributing his ideas or energy to the organization. So what does the boss do? He increases his pressure and supervision again—watching, questioning, and double-checking everything the subordinate does. Eventually, the subordinate gives up on his dreams of making a meaningful contribution. Boss and subordinate typically settle into a routine that is not really satisfactory but, aside from periodic clashes, is otherwise bearable for them. In the worst-case scenario, the boss's intense intervention and scrutiny end up paralyzing the employee into inaction and consume so much of the boss's time that the employee quits or is fired. (See “The set-up-to-fail syndrome: No harm intended: A relationship spirals from bad to worse.”)

Idea in Brief

That darned employee! His performance keeps deteriorating—*despite* your close monitoring. What's going on?

Brace yourself: *You* may be at fault, by unknowingly triggering the **set-up-to-fail syndrome**. Employees whom you (perhaps falsely) view as weak performers live *down* to your expectations. Here's how:

1. You start with a positive relationship.
2. Something—a missed deadline, a lost client—makes you question the employee's performance. You begin micromanaging him.
3. Suspecting your reduced confidence, the employee starts doubting *himself*. He stops giving his best, responds mechanically to your controls, and avoids decisions.
4. You view his new behavior as additional proof of mediocrity—and tighten the screws further.

Why not just fire him? Because you're likely to repeat the pattern with others. Better to *reverse* the dynamic instead. Unwinding the set-up-to-fail spiral actually pays big dividends: Your company gets the best from your employees—and from you.

Perhaps the most daunting aspect of the set-up-to-fail syndrome is that it is self-fulfilling and self-reinforcing—it is the quintessential vicious circle. The process is self-fulfilling because the boss's actions contribute to the very behavior that is expected from weak performers. It is self-reinforcing because

the boss's low expectations, in being fulfilled by his subordinates, trigger more of the same behavior on his part, which in turn triggers more of the same behavior on the part of subordinates. And on and on, unintentionally, the relationship spirals downward.

A case in point is the story of Steve, a manufacturing supervisor for a *Fortune* 100 company. When we first met Steve, he came across as highly motivated, energetic, and enterprising. He was on top of his operation, monitoring problems and addressing them quickly. His boss expressed great confidence in him and gave him an excellent performance rating. Because of his high performance, Steve was chosen to lead a new production line considered essential to the plant's future.

Idea in Practice

How Set-Up-to-Fail Starts

A manager categorizes employees as “in” or “out,” based on:

- early *perceptions* of employees’ motivation, initiative, creativity, strategic perspectives;
- previous bosses’ impressions;
- an early mishap; and
- boss-subordinate incompatibility.

The manager then notices *only* evidence supporting his categorization, while dismissing contradictory evidence. The boss also treats the groups differently:

- “In” groups get autonomy, feedback, and expressions of confidence.
- “Out” groups get controlling, formal management emphasizing rules.

The Costs of Set-Up-to-Fail

This syndrome hurts everyone:

- *Employees* stop volunteering ideas and information and asking for help, avoid contact with bosses, or grow defensive.
- The *organization* fails to get the most from employees.
- The *boss* loses energy to attend to other activities. His reputation suffers as other employees deem him unfair.
- *Team spirit* wilts as targeted performers are alienated and strong performers are overburdened.

How to Reverse Set-Up-to-Fail

If the syndrome hasn't started, prevent it:

- Establish expectations with new employees early. Loosen the reins as they master their jobs.
- Regularly challenge your own assumptions. Ask: "What are the *facts* regarding this employee's performance?" "Is he really that bad?"
- Convey openness, letting employees challenge your opinions. They'll feel comfortable discussing their performance and relationship with you.

If the syndrome has already erupted, discuss the dynamic with the employee:

1. Choose a neutral, nonthreatening location; use affirming language (“Let’s discuss our relationship and roles”); and acknowledge your part in the tension.
2. Agree on the employee’s weaknesses and strengths. Support assessments with facts, not feelings.
3. Unearth causes of the weaknesses. Do you disagree on priorities? Does your employee lack specific knowledge or skills? Ask: “How is my behavior making things worse for you?”
4. Identify ways to boost performance. Training? New experiences? Decide the quantity and type of supervision you’ll provide. Affirm your desire to improve matters.
5. Agree to communicate more openly: “Next time I do something that communicates low expectations, can you let me know immediately?”

In his new job, Steve reported to Jeff, who had just been promoted to a senior management position at the plant. In the first few weeks of the relationship, Jeff periodically asked Steve to write up short analyses of significant quality-control rejections. Although Jeff didn’t really explain this to Steve at the time, his request had two major objectives: to generate information that would help both of them learn the new production process, and to help Steve develop the habit of systematically performing root cause analysis of quality-related problems. Also, being new on the job himself, Jeff wanted to show his own boss that he was on top of the operation.

Unaware of Jeff’s motives, Steve balked. Why, he wondered, should he submit reports on information he understood and monitored himself? Partly due to lack of time, partly in response to what he considered interference from his boss, Steve invested little energy in the reports. Their tardiness and below-average quality annoyed Jeff, who began to suspect that Steve was not a particularly proactive manager. When he asked for the reports again, he was

more forceful. For Steve, this merely confirmed that Jeff did not trust him. He withdrew more and more from interaction with him, meeting his demands with increased passive resistance. Before long, Jeff became convinced that Steve was not effective enough and couldn't handle his job without help. He started to supervise Steve's every move—to Steve's predictable dismay. One year after excitedly taking on the new production line, Steve was so dispirited he was thinking of quitting.

How can managers break the set-up-to-fail syndrome? Before answering that question, let's take a closer look at the dynamics that set the syndrome in motion and keep it going.

Deconstructing the Syndrome

We said earlier that the set-up-to-fail syndrome usually starts surreptitiously—that is, it is a dynamic that usually creeps up on the boss and the subordinate until suddenly both of them realize that the relationship has gone sour. But underlying the syndrome are several assumptions about weaker performers that bosses appear to accept uniformly. Our research shows, in fact, that executives typically compare weaker performers with stronger performers using the following descriptors:

- less motivated, less energetic, and less likely to go beyond the call of duty;
- more passive when it comes to taking charge of problems or projects;
- less aggressive about anticipating problems;
- less innovative and less likely to suggest ideas;
- more parochial in their vision and strategic perspective;
- more prone to hoard information and assert their authority, making them poor bosses to their own subordinates.

It is not surprising that on the basis of these assumptions, bosses tend to treat weaker and stronger performers very differently. Indeed, numerous studies have shown that up to 90% of all managers treat some subordinates as though they were members of an in-group, while they consign others to membership in an out-group. Members of the in-group are considered the

trusted collaborators and therefore receive more autonomy, feedback, and expressions of confidence from their bosses. The boss-subordinate relationship for this group is one of mutual trust and reciprocal influence. Members of the out-group, on the other hand, are regarded more as hired hands and are managed in a more formal, less personal way, with more emphasis on rules, policies, and authority. (For more on how bosses treat weaker and stronger performers differently, see the chart “In with the In Crowd, Out with the Out.”)

Why do managers categorize subordinates into either in-groups or out-groups? For the same reason that we tend to typecast our family, friends, and acquaintances: it makes life easier. Labeling is something we all do, because it allows us to function more efficiently. It saves time by providing rough-and-ready guides for interpreting events and interacting with others. Managers, for instance, use categorical thinking to figure out quickly who should get what tasks. That’s the good news.

The downside of categorical thinking is that in organizations it leads to premature closure. Having made up his mind about a subordinate’s limited ability and poor motivation, a manager is likely to notice supporting evidence while selectively dismissing contrary evidence. (For example, a manager might interpret a terrific new product idea from an out-group subordinate as a lucky onetime event.) Unfortunately for some subordinates, several studies show that bosses tend to make decisions about in-groups and out-groups even as early as five days into their relationships with employees.

Are bosses aware of this sorting process and of their different approaches to “in” and “out” employees? Definitely. In fact, the bosses we have studied, regardless of nationality, company, or personal background, were usually quite conscious of behaving in a more controlling way with perceived weaker performers. Some of them preferred to label this approach as “supportive and helpful.” Many of them also acknowledged that—although they tried not to—they tended to become impatient with weaker performers more easily than with stronger performers. By and large, however, managers are aware of the controlling nature of their behavior toward perceived weaker performers. For them, this behavior is not an error in implementation; it is intentional.

About the Research

This article is based on two studies designed to understand better the causal relationship between leadership style and subordinate performance—in other words, to explore how bosses and subordinates mutually influence each other's behavior. The first study, which comprised surveys, interviews, and observations, involved 50 boss-subordinate pairs in four manufacturing operations in *Fortune* 100 companies. The second study, involving an informal survey of about 850 senior managers attending INSEAD executive-development programs over the last three years, was done to test and refine the findings generated by the first study. The executives in the second study represented a wide diversity of nationalities, industries, and personal backgrounds.

What bosses typically do *not* realize is that their tight controls end up hurting subordinates' performance by undermining their motivation in two ways: first, by depriving subordinates of autonomy on the job and, second, by making them feel undervalued. Tight controls are an indication that the boss assumes the subordinate can't perform well without strict guidelines. When the subordinate senses these low expectations, it can undermine his self-confidence. This is particularly problematic because numerous studies confirm that people perform up or down to the levels their bosses expect from them or, indeed, to the levels they expect from themselves.¹

Of course, executives often tell us, "Oh, but I'm very careful about this issue of expectations. I exert more control over my underperformers, but I make sure that it does not come across as a lack of trust or confidence in their ability." We believe what these executives tell us. That is, we believe that they do try hard to disguise their intentions. When we talk to their subordinates, however, we find that these efforts are for the most part futile. In fact, our research shows that most employees can—and do—"read their boss's mind." In particular, they know full well whether they fit into their boss's in-group or out-group. All they have to do is compare how they are treated with how their more highly regarded colleagues are treated.

The Set-Up-to-Fail Syndrome

No harm intended: A relationship spirals from bad to worse

1. Before the set-up-to-fail syndrome begins, the boss and the subordinate are typically engaged in a positive, or at least neutral, relationship.
2. The triggering event in the set-up-to-fail syndrome is often minor or surreptitious. The subordinate may miss a deadline, lose a client, or submit a subpar report. In other cases, the syndrome's genesis is the boss, who distances himself from the subordinate for personal or social reasons unrelated to performance.
3. Reacting to the triggering event, the boss increases his supervision of the subordinate, gives more specific instructions, and wrangles longer over courses of action.
4. The subordinate responds by beginning to suspect a lack of confidence and senses he's not part of the boss's in-group anymore.
He starts to withdraw emotionally from the boss and from work. He may also fight to change the boss's image of him, reaching too high or running too fast to be effective.
5. The boss interprets this problem-hoarding, overreaching, or tentativeness as signs that the subordinate has poor judgment and weak capabilities. If the subordinate does perform well, the boss does not acknowledge it or considers it a lucky "one off."
He limits the subordinate's discretion, withholds social contact, and shows, with increasing openness, his lack of confidence in and

frustration with the subordinate.

6. The subordinate feels boxed in and underappreciated. He increasingly withdraws from his boss and from work. He may even resort to ignoring instructions, openly disputing the boss, and occasionally lashing out because of feelings of rejection.

In general, he performs his job mechanically and devotes more energy to self-protection. Moreover, he refers all nonroutine decisions to the boss or avoids contact with him.

7. The boss feels increasingly frustrated and is now convinced that the subordinate cannot perform without intense oversight. He makes this known by his words and deeds, further undermining the subordinate's confidence and prompting inaction.

8. When the set-up-to-fail syndrome is in full swing, the boss pressures and controls the subordinate during interactions. Otherwise, he avoids contact and gives the subordinate routine assignments only.

For his part, the subordinate shuts down or leaves, either in dismay, frustration, or anger.

Just as the boss's assumptions about weaker performers and the right way to manage them explains his complicity in the set-up-to-fail syndrome, the subordinate's assumptions about what the boss is thinking explain his own complicity. The reason? When people perceive disapproval, criticism, or simply a lack of confidence and appreciation, they tend to shut down—a behavioral phenomenon that manifests itself in several ways.

Primarily, shutting down means disconnecting intellectually and emotionally. Subordinates simply stop giving their best. They grow tired of being overruled, and they lose the will to fight for their ideas. As one subordinate put it, "My boss tells me how to execute every detail. Rather than arguing with him, I've ended up wanting to say, 'Come on, just tell me what you want me to do, and I'll go do it.' You become a robot." Another perceived weak performer explained, "When my boss tells me to do

something, I just do it mechanically.”

In with the In Crowd, Out with the Out

Boss's behavior toward perceived stronger performers

Discusses project objectives, with a limited focus on project implementation. Gives subordinate the freedom to choose his own approach to solving problems or reaching goals.

Treats unfavorable variances, mistakes, or incorrect judgments as learning opportunities.

Makes himself available, as in “let me know if I can help.” Initiates casual and personal conversations.

Is open to subordinate's suggestions and discusses them with interest.

Gives subordinate interesting and challenging stretch assignments. Often allows subordinate to choose his own assignments.

Solicits opinions from subordinate on organizational strategy, execution, policy, and procedures.

Often defers to subordinate's opinion in disagreements.

Praises subordinate for work well done.

Boss's behavior toward perceived weaker performers

Is directive when discussing tasks and goals. Focuses on what needs get done as well as how it should get done.

Pays close attention to unfavorable variances, mistakes, or incorrect judgments.

Makes himself available to subordinate on a need-to-see basis. Bases conversations primarily on work-related topics.

Pays little interest to subordinate's comments or suggestions about how and why work is done.

Reluctantly gives subordinate anything but routine assignments. When handing out assignments, gives subordinate little choice. Monitors subordinate heavily.

Rarely asks subordinate for input about organizational or work-related matters.

Usually imposes own views in disagreements.

Emphasizes what the subordinate is doing poorly.

Shutting down also involves disengaging personally—essentially reducing contact with the boss. Partly, this disengagement is motivated by the nature of previous exchanges that have tended to be negative in tone. As one subordinate admitted, “I used to initiate much more contact with my boss until the only thing I received was negative feedback; then I started shying away.”

Besides the risk of a negative reaction, perceived weaker performers are concerned with not tainting their images further. Following the often-heard aphorism “Better to keep quiet and look like a fool than to open your mouth

and prove it,” they avoid asking for help for fear of further exposing their limitations. They also tend to volunteer less information—a simple “heads up” from a perceived under-performer can cause the boss to overreact and jump into action when none is required. As one perceived weak performer recalled, “I just wanted to let my boss know about a small matter, only slightly out of the routine, but as soon as I mentioned it, he was all over my case. I should have kept my mouth closed. I do now.”

Finally, shutting down can mean becoming defensive. Many perceived underperformers start devoting more energy to self-justification. Anticipating that they will be personally blamed for failures, they seek to find excuses early. They end up spending a lot of time looking in the rearview mirror and less time looking at the road ahead. In some cases—as in the case of Steve, the manufacturing supervisor described earlier—this defensiveness can lead to noncompliance or even systematic opposition to the boss’s views. While this idea of a weak subordinate going head to head with his boss may seem irrational, it may reflect what Albert Camus once observed: “When deprived of choice, the only freedom left is the freedom to say no.”

The Syndrome Is Costly

There are two obvious costs of the set-up-to-fail syndrome: the emotional cost paid by the subordinate and the organizational cost associated with the company's failure to get the best out of an employee. Yet there are other costs to consider, some of them indirect and long term.

The boss pays for the syndrome in several ways. First, uneasy relationships with perceived low performers often sap the boss's emotional and physical energy. It can be quite a strain to keep up a facade of courtesy and pretend everything is fine when both parties know it is not. In addition, the energy devoted to trying to fix these relationships or improve the subordinate's performance through increased supervision prevents the boss from attending to other activities—which often frustrates or even angers the boss.

Furthermore, the syndrome can take its toll on the boss's reputation, as other employees in the organization observe his behavior toward weaker performers. If the boss's treatment of a subordinate is deemed unfair or unsupportive, observers will be quick to draw their lessons. One outstanding performer commented on his boss's controlling and hypercritical behavior toward another subordinate: "It made us all feel like we're expendable." As organizations increasingly espouse the virtues of learning and empowerment, managers must cultivate their reputations as coaches, as well as get results.

The set-up-to-fail syndrome also has serious consequences for any team. A lack of faith in perceived weaker performers can tempt bosses to overload those whom they consider superior performers; bosses want to entrust critical assignments to those who can be counted on to deliver reliably and quickly and to those who will go beyond the call of duty because of their strong sense of shared fate. As one boss half-jokingly said, "Rule number one: if you want something done, give it to someone who's busy—there's a reason why that person is busy."

An increased workload may help perceived superior performers learn to manage their time better, especially as they start to delegate to their own

subordinates more effectively. In many cases, however, these performers simply absorb the greater load and higher stress which, over time, takes a personal toll and decreases the attention they can devote to other dimensions of their jobs, particularly those yielding longer-term benefits. In the worst-case scenario, overburdening strong performers can lead to burnout.

Team spirit can also suffer from the progressive alienation of one or more perceived low performers. Great teams share a sense of enthusiasm and commitment to a common mission. Even when members of the boss's out-group try to keep their pain to themselves, other team members feel the strain. One manager recalled the discomfort experienced by the whole team as they watched their boss grill one of their peers every week. As he explained, "A team is like a functioning organism. If one member is suffering, the whole team feels that pain."

In addition, alienated subordinates often do not keep their suffering to themselves. In the corridors or over lunch, they seek out sympathetic ears to vent their recriminations and complaints, not only wasting their own time but also pulling their colleagues away from productive work. Instead of focusing on the team's mission, valuable time and energy is diverted to the discussion of internal politics and dynamics.

Finally, the set-up-to-fail syndrome has consequences for the subordinates of the perceived weak performers. Consider the weakest kid in the school yard who gets pummeled by a bully. The abused child often goes home and pummels his smaller, weaker siblings. So it is with the people who are in the boss's out-group. When they have to manage their own employees, they frequently replicate the behavior that their bosses show to them. They fail to recognize good results or, more often, supervise their employees excessively.

Breaking Out Is Hard to Do

The set-up-to-fail syndrome is not irreversible. Subordinates can break out of it, but we have found that to be rare. The subordinate must consistently deliver such superior results that the boss is forced to change the employee from out-group to in-group status—a phenomenon made difficult by the context in which these subordinates operate. It is hard for subordinates to impress their bosses when they must work on unchallenging tasks, with no autonomy and limited resources; it is also hard for them to persist and maintain high standards when they receive little encouragement from their bosses.

Furthermore, even if the subordinate achieves better results, it may take some time for them to register with the boss because of his selective observation and recall. Indeed, research shows that bosses tend to attribute the good things that happen to weaker performers to external factors rather than to their efforts and ability (while the opposite is true for perceived high performers: successes tend to be seen as theirs, and failures tend to be attributed to external uncontrollable factors). The subordinate will therefore need to achieve a string of successes in order to have the boss even contemplate revising the initial categorization. Clearly, it takes a special kind of courage, self-confidence, competence, and persistence on the part of the subordinate to break out of the syndrome.

Instead, what often happens is that members of the out-group set excessively ambitious goals for themselves to impress the boss quickly and powerfully—promising to hit a deadline three weeks early, for instance, or attacking six projects at the same time, or simply attempting to handle a large problem without help. Sadly, such superhuman efforts are usually just that. And in setting goals so high that they are bound to fail, the subordinates also come across as having had very poor judgment in the first place.

The set-up-to-fail syndrome is not restricted to incompetent bosses. We have seen it happen to people perceived within their organizations to be excellent bosses. Their mismanagement of some subordinates need not

prevent them from achieving success, particularly when they and the perceived superior performers achieve high levels of individual performance. However, those bosses could be even more successful to the team, the organization, and themselves if they could break the syndrome.

Getting It Right

As a general rule, the first step in solving a problem is recognizing that one exists. This observation is especially relevant to the set-up-to-fail syndrome because of its self-fulfilling and self-reinforcing nature. Interrupting the syndrome requires that a manager understand the dynamic and, particularly, that he accept the possibility that his own behavior may be contributing to a subordinate's underperformance. The next step toward cracking the syndrome, however, is more difficult: it requires a carefully planned and structured intervention that takes the form of one (or several) candid conversations meant to bring to the surface and untangle the unhealthy dynamics that define the boss and the subordinate's relationship. The goal of such an intervention is to bring about a sustainable increase in the subordinate's performance while progressively reducing the boss's involvement.

It would be difficult—and indeed, detrimental—to provide a detailed script of what this kind of conversation should sound like. A boss who rigidly plans for this conversation with a subordinate will not be able to engage in real dialogue with him, because real dialogue requires flexibility. As a guiding framework, however, we offer five components that characterize effective interventions. Although they are not strictly sequential steps, all five components should be part of these interventions.

First, the boss must create the right context for the discussion

He must, for instance, select a time and place to conduct the meeting so that it presents as little threat as possible to the subordinate. A neutral location may be more conducive to open dialogue than an office where previous and perhaps unpleasant conversations have taken place. The boss must also use affirming language when asking the subordinate to meet with him. The session should not be billed as “feedback,” because such terms may suggest baggage from the past. “Feedback” could also be taken to mean that the conversation will be one-directional, a monologue delivered by the boss to the subordinate. Instead, the intervention should be described as a meeting to discuss the performance of the subordinate, the role of the boss, and the relationship between the subordinate and the boss. The boss might even acknowledge that he feels tension in the relationship and wants to use the conversation as a way to decrease it.

Finally, in setting the context, the boss should tell the perceived weaker performer that he would genuinely like the interaction to be an open dialogue. In particular, he should acknowledge that he may be partially responsible for the situation and that his own behavior toward the subordinate is fair game for discussion.

Second, the boss and the subordinate must use the intervention process to come to an agreement on the symptoms of the problem

Few employees are ineffective in all aspects of their performance. And few—if any—employees desire to do poorly on the job. Therefore, it is critical that the intervention result in a mutual understanding of the specific job responsibilities in which the subordinate is weak. In the case of Steve and Jeff, for instance, an exhaustive sorting of the evidence might have led to an agreement that Steve's underperformance was not universal but instead largely confined to the quality of the reports he submitted (or failed to submit). In another situation, it might be agreed that a purchasing manager was weak when it came to finding off-shore suppliers and to voicing his ideas in meetings. Or a new investment professional and his boss might come to agree that his performance was subpar when it came to timing the sales and purchase of stocks, but they might also agree that his financial analysis of stocks was quite strong. The idea here is that before working to improve performance or reduce tension in a relationship, an agreement must be reached about what areas of performance contribute to the contentiousness.

We used the word “evidence” above in discussing the case of Steve and Jeff. That is because a boss needs to back up his performance assessments with facts and data—that is, if the intervention is to be useful. They cannot be based on feelings—as in Jeff telling Steve, “I just have the feeling you're not putting enough energy into the reports.” Instead, Jeff needs to describe what a good report should look like and the ways in which Steve's reports fall short. Likewise, the subordinate must be allowed—indeed, encouraged—to defend his performance, compare it with colleagues' work, and point out areas in which he is strong. After all, just because it is the boss's opinion does not make it a fact.

Third, the boss and the subordinate should arrive at a common understanding of what might be causing the weak performance in certain areas

Once the areas of weak performance have been identified, it is time to unearth the reasons for those weaknesses. Does the subordinate have limited skills in organizing work, managing his time, or working with others? Is he lacking knowledge or capabilities? Do the boss and the subordinate agree on their priorities? Maybe the subordinate has been paying less attention to a particular dimension of his work because he does not realize its importance to the boss. Does the subordinate become less effective under pressure? Does he have lower standards for performance than the boss does?

It is also critical in the intervention that the boss bring up the subject of his own behavior toward the subordinate and how this affects the subordinate's performance. The boss might even try to describe the dynamics of the set-up-to-fail syndrome. "Does my behavior toward you make things worse for you?" he might ask, or, "What am I doing that is leading you to feel that I am putting too much pressure on you?"

This component of the discussion also needs to make explicit the assumptions that the boss and the subordinate have thus far been making about each other's intentions. Many misunderstandings start with untested assumptions. For example, Jeff might have said, "When you did not supply me with the reports I asked for, I came to the conclusion that you were not very proactive." That would have allowed Steve to bring his buried assumptions into the open. "No," he might have answered, "I just reacted negatively because you asked for the reports in writing, which I took as a sign of excessive control."

Fourth, the boss and the subordinate should arrive at an agreement about their performance objectives and on their desire to have the relationship move forward

In medicine, a course of treatment follows the diagnosis of an illness. Things are a bit more complex when repairing organizational dysfunction, since modifying behavior and developing complex skills can be more difficult than taking a few pills. Still, the principle that applies to medicine also applies to business: boss and subordinate must use the intervention to plot a course of treatment regarding the root problems they have jointly identified.

The contract between boss and subordinate should identify the ways they can improve on their skills, knowledge, experience, or personal relationship. It should also include an explicit discussion of how much and what type of future supervision the boss will have. No boss, of course, should suddenly abdicate his involvement; it is legitimate for bosses to monitor subordinates' work, particularly when a subordinate has shown limited abilities in one or more facets of his job. From the subordinate's point of view, however, such involvement by the boss is more likely to be accepted, and possibly even welcomed, if the goal is to help the subordinate develop and improve over time. Most subordinates can accept temporary involvement that is meant to decrease as their performance improves. The problem is intense monitoring that never seems to go away.

Fifth, the boss and the subordinate should agree to communicate more openly in the future

The boss could say, “Next time I do something that communicates low expectations, can you let me know immediately?” And the subordinate might say, or be encouraged to say, “Next time I do something that aggravates you or that you do not understand, can you also let me know right away?” Those simple requests can open the door to a more honest relationship almost instantly.

No Easy Answer

Our research suggests that interventions of this type do not take place very often. Face-to-face discussions about a subordinate's performance tend to come high on the list of workplace situations people would rather avoid, because such conversations have the potential to make both parties feel threatened or embarrassed. Subordinates are reluctant to trigger the discussion because they are worried about coming across as thin-skinned or whiny. Bosses tend to avoid initiating these talks because they are concerned about the way the subordinate might react; the discussion could force the boss to make explicit his lack of confidence in the subordinate, in turn putting the subordinate on the defensive and making the situation worse.²

As a result, bosses who observe the dynamics of the set-up-to-fail syndrome being played out may be tempted to avoid an explicit discussion. Instead, they will proceed tacitly by trying to encourage their perceived weak performers. That approach has the short-term benefit of bypassing the discomfort of an open discussion, but it has three major disadvantages.

First, a one-sided approach on the part of the boss is less likely to lead to lasting improvement because it focuses on only one symptom of the problem—the boss's behavior. It does not address the subordinate's role in the underperformance.

Second, even if the boss's encouragement were successful in improving the employee's performance, a unilateral approach would limit what both he and the subordinate could otherwise learn from a more up-front handling of the problem. The subordinate, in particular, would not have the benefit of observing and learning from how his boss handled the difficulties in their relationship—problems the subordinate may come across someday with the people he manages.

Finally, bosses trying to modify their behavior in a unilateral way often end up going overboard; they suddenly give the subordinate more autonomy and responsibility than he can handle productively. Predictably, the subordinate fails to deliver to the boss's satisfaction, which leaves the boss

even more frustrated and convinced that the subordinate cannot function without intense supervision.

We are not saying that intervention is always the best course of action. Sometimes, intervention is not possible or desirable. There may be, for instance, overwhelming evidence that the subordinate is not capable of doing his job. He was a hiring or promotion mistake, which is best handled by removing him from the position. In other cases, the relationship between the boss and the subordinate is too far gone—too much damage has occurred to repair it. And finally, sometimes bosses are too busy and under too much pressure to invest the kind of resources that intervention involves.

Yet often the biggest obstacle to effective intervention is the boss's mindset. When a boss believes that a subordinate is a weak performer and, on top of everything else, that person also aggravates him, he is not going to be able to cover up his feelings with words; his underlying convictions will come out in the meeting. That is why preparation for the intervention is crucial. Before even deciding to have a meeting, the boss must separate emotion from reality. Was the situation always as bad as it is now? Is the subordinate really as bad as I think he is? What is the hard evidence I have for that belief? Could there be other factors, aside from performance, that have led me to label this subordinate a weak performer? Aren't there a few things that he does well? He must have displayed above-average qualifications when we decided to hire him. Did these qualifications evaporate all of a sudden?

The boss might even want to mentally play out part of the conversation beforehand. If I say this to the subordinate, what might he answer? Yes, sure, he would say that it was not his fault and that the customer was unreasonable. Those excuses—are they really without merit? Could he have a point? Could it be that, under other circumstances, I might have looked more favorably upon them? And if I still believe I'm right, how can I help the subordinate see things more clearly?

The boss must also mentally prepare himself to be open to the subordinate's views, even if the subordinate challenges him about any evidence regarding his poor performance. It will be easier for the boss to be open if, when preparing for the meeting, he has already challenged his own preconceptions.

Even when well prepared, bosses typically experience some degree of discomfort during intervention meetings. That is not all bad. The subordinate will probably be somewhat uncomfortable as well, and it is reassuring for

him to see that his boss is a human being, too.

Calculating Costs and Benefits

As we've said, an intervention is not always advisable. But when it is, it results in a range of outcomes that are uniformly better than the alternative—that is, continued underperformance and tension. After all, bosses who systematically choose either to ignore their subordinates' underperformance or to opt for the more expedient solution of simply removing perceived weak performers are condemned to keep repeating the same mistakes. Finding and training replacements for perceived weak performers is a costly and recurrent expense. So is monitoring and controlling the deteriorating performance of a disenchanted subordinate. Getting results *in spite of* one's staff is not a sustainable solution. In other words, it makes sense to think of the intervention as an investment, not an expense—with the payback likely to be high.

How high that payback will be and what form it will take obviously depend on the outcome of the intervention, which will itself depend not only on the quality of the intervention but also on several key contextual factors: How long has that relationship been spiraling downward? Does the subordinate have the intellectual and emotional resources to make the effort that will be required? Does the boss have enough time and energy to do his part?

We have observed outcomes that can be clustered into three categories. In the best-case scenario, the intervention leads to a mixture of coaching, training, job redesign, and a clearing of the air; as a result, the relationship and the subordinate's performance improve, and the costs associated with the syndrome go away or, at least, decrease measurably.

In the second-best scenario, the subordinate's performance improves only marginally, but because the subordinate received an honest and open hearing from the boss, the relationship between the two becomes more productive. Boss and subordinate develop a better understanding of those job dimensions the subordinate can do well and those he struggles with. This improved understanding leads the boss and the subordinate to explore *together* how

they can develop a better fit between the job and the subordinate's strengths and weaknesses. That improved fit can be achieved by significantly modifying the subordinate's existing job or by transferring the subordinate to another job within the company. It may even result in the subordinate's choosing to leave the company.

While that outcome is not as successful as the first one, it is still productive; a more honest relationship eases the strain on both the boss and the subordinate, and in turn on the subordinate's subordinates. If the subordinate moves to a new job within the organization that better suits him, he will likely become a stronger performer. His relocation may also open up a spot in his old job for a better performer. The key point is that, having been treated fairly, the subordinate is much more likely to accept the outcome of the process. Indeed, recent studies show that the perceived fairness of a process has a major impact on employees' reactions to its outcomes. (See "Fair Process: Managing in the Knowledge Economy," by W. Chan Kim and Renée Mauborgne, HBR July–August 1997.)

Such fairness is a benefit even in the cases where, despite the boss's best efforts, neither the subordinate's performance nor his relationship with his boss improves significantly. Sometimes this happens: the subordinate truly lacks the ability to meet the job requirements, he has no interest in making the effort to improve, and the boss and the subordinate have both professional and personal differences that are irreconcilable. In those cases, however, the intervention still yields indirect benefits because, even if termination follows, other employees within the company are less likely to feel expendable or betrayed when they see that the subordinate received fair treatment.

Prevention Is the Best Medicine

The set-up-to-fail syndrome is not an organizational fait accompli. It can be unwound. The first step is for the boss to become aware of its existence and acknowledge the possibility that he might be part of the problem. The second step requires that the boss initiate a clear, focused intervention. Such an intervention demands an open exchange between the boss and the subordinate based on the evidence of poor performance, its underlying causes, and their joint responsibilities—culminating in a joint decision on how to work toward eliminating the syndrome itself.

Reversing the syndrome requires managers to challenge their own assumptions. It also demands that they have the courage to look within themselves for causes and solutions before placing the burden of responsibility where it does not fully belong. Prevention of the syndrome, however, is clearly the best option.

In our current research, we examine prevention directly. Our results are still preliminary, but it appears that bosses who manage to consistently avoid the set-up-to-fail syndrome have several traits in common. They do not, interestingly, behave the same way with all subordinates. They are more involved with some subordinates than others—they even monitor some subordinates more than others. However, they do so without disempowering and discouraging subordinates.

How? One answer is that those managers begin by being actively involved with all their employees, gradually reducing their involvement based on improved performance. Early guidance is not threatening to subordinates, because it is not triggered by performance shortcomings; it is systematic and meant to help set the conditions for future success. Frequent contact in the beginning of the relationship gives the boss ample opportunity to communicate with subordinates about priorities, performance measures, time allocation, and even expectations of the type and frequency of communication. That kind of clarity goes a long way toward preventing the dynamic of the set-up-to-fail syndrome, which is so often fueled by unstated

expectations and a lack of clarity about priorities.

For example, in the case of Steve and Jeff, Jeff could have made explicit very early on that he wanted Steve to set up a system that would analyze the root causes of quality control rejections systematically. He could have explained the benefits of establishing such a system during the initial stages of setting up the new production line, and he might have expressed his intention to be actively involved in the system's design and early operation. His future involvement might then have decreased in such a way that could have been jointly agreed on at that stage.

Another way managers appear to avoid the set-up-to-fail syndrome is by challenging their own assumptions and attitudes about employees on an ongoing basis. They work hard at resisting the temptation to categorize employees in simplistic ways. They also monitor their own reasoning. For example, when feeling frustrated about a subordinate's performance, they ask themselves, "What are the facts?" They examine whether they are expecting things from the employee that have not been articulated, and they try to be objective about how often and to what extent the employee has really failed. In other words, these bosses delve into their own assumptions and behavior before they initiate a full-blown intervention.

Finally, managers avoid the set-up-to-fail syndrome by creating an environment in which employees feel comfortable discussing their performance and their relationships with the boss. Such an environment is a function of several factors: the boss's openness, his comfort level with having his own opinions challenged, even his sense of humor. The net result is that the boss and the subordinate feel free to communicate frequently and to ask one another questions about their respective behaviors before problems mushroom or ossify.

The methods used to head off the set-up-to-fail syndrome do, admittedly, involve a great deal of emotional investment from bosses—just as interventions do. We believe, however, that this higher emotional involvement is the key to getting subordinates to work to their full potential. As with most things in life, you can only expect to get a lot back if you put a lot in. As a senior executive once said to us, "The respect you give is the respect you get." We concur. If you want—indeed, need—the people in your organization to devote their whole hearts and minds to their work, then you must, too.

Originally published in March 1998. Reprint 98209.

Notes

[1.](#) *The influence of expectations on performance has been observed in numerous experiments by Dov Eden and his colleagues. See Dov Eden, “Leadership and Expectations: Pygmalion Effects and Other Self-fulfilling Prophecies in Organizations,” Leadership Quarterly, Winter 1992, vol. 3, no. 4, pp. 271–305.*

[2.](#) *Chris Argyris has written extensively on how and why people tend to behave unproductively in situations they see as threatening or embarrassing. See, for example, Knowledge for Action: A Guide to Overcoming Barriers to Organizational Change (San Francisco: Jossey-Bass, 1993).*

Saving Your Rookie Managers from Themselves

by Carol A. Walker

TOM EDELMAN, LIKE A million freshly minted managers before him, had done a marvelous job as an individual contributor. He was smart, confident, forward thinking, and resourceful. His clients liked him, as did his boss and coworkers. Consequently, no one in the department was surprised when his boss offered him a managerial position. Tom accepted with some ambivalence—he loved working directly with clients and was loath to give that up—but on balance, he was thrilled.

Six months later, when I was called into coach Tom (I've disguised his name), I had trouble even picturing the confident insider he once had been. He looked like a deer caught in the headlights. Tom seemed overwhelmed and indeed even used that word several times to describe how he felt. He had started to doubt his abilities. His direct reports, once close colleagues, no longer seemed to respect or even like him. What's more, his department had been beset by a series of small crises, and Tom spent most of his time putting out these fires. He knew this wasn't the most effective use of his time, but he didn't know how to stop. These problems hadn't yet translated into poor business results, but he was in trouble nonetheless.

His boss realized that he was in danger of failing and brought me in to assist. With support and coaching, Tom got the help he needed and eventually became an effective manager. Indeed, he has been promoted twice since I worked with him, and he now runs a small division within the same company. But his near failure—and the path that brought him to that point—is surprisingly typical. Most organizations promote employees into

managerial positions based on their technical competence. Very often, however, those people fail to grasp how their roles have changed—that their jobs are no longer about personal achievement but instead about enabling others to achieve, that sometimes driving the bus means taking a backseat, and that building a team is often more important than cutting a deal. Even the best employees can have trouble adjusting to these new realities. That trouble may be exacerbated by normal insecurities that make rookie managers hesitant to ask for help, even when they find themselves in thoroughly unfamiliar territory. As these new managers internalize their stress, their focus becomes internal as well. They become insecure and self-focused and cannot properly support their teams. Inevitably, trust breaks down, staff members are alienated, and productivity suffers.

Many companies unwittingly support this downward spiral by assuming that their rookie managers will somehow learn critical management skills by osmosis. Some rookies do, to be sure, but in my experience they're the exceptions. Most need more help. In the absence of comprehensive training and intensive coaching—which most companies don't offer—the rookie manager's boss plays a key role. Of course, it's not possible for most senior managers to spend hours and hours every week overseeing a new manager's work, but if you know what typical challenges a rookie manager faces, you'll be able to anticipate some problems before they arise and nip others in the bud.

Delegating

Effective delegation may be one of the most difficult tasks for rookie managers. Senior managers bestow on them big responsibilities and tight deadlines, and they put a lot of pressure on them to produce results. The natural response of rookies when faced with such challenges is to “just do it,” thinking that’s what got them promoted in the first place. But their reluctance to delegate assignments also has its roots in some very real fears. First is the fear of losing stature: If I assign high-profile projects to my staff members, they’ll get the credit. What kind of visibility will I be left with? Will it be clear to my boss and my staff what value I’m adding? Second is the fear of abdicating control: If I allow Frank to do this, how can I be sure that he will do it correctly? In the face of this fear, the rookie manager may delegate tasks but supervise Frank so closely that he will never feel accountable. Finally, the rookie may be hesitant to delegate work because he’s afraid of overburdening his staff. He may be uncomfortable assigning work to former peers for fear that they’ll resent him. But the real resentment usually comes when staff members feel that lack of opportunity is blocking their advancement.

Idea in Brief

You've wisely promoted a top performer into management. Six months later, this rising star has fallen hard: He's overwhelmed, fearful, not respected by his staff. Why?

You probably promoted him based on his technical competence—then expected him to learn management skills by osmosis.

But he didn't grasp the real challenges of management—for example, empowering others versus striving for personal achievement. Insecure about asking for help, he turned inward. His team's morale plummeted; productivity faltered.

How to save your erstwhile star? Help him master delegating, thinking strategically, and communicating—basic skills that trip up *most* new managers.

Signs that these fears may be playing out include new managers who work excessively long hours, are hesitant to take on new responsibilities, have staff members who seem unengaged, or have a tendency to answer on behalf of employees instead of encouraging them to communicate with you directly.

The first step toward helping young managers delegate effectively is to get them to understand their new role. Acknowledge that their job fundamentally differs from an individual contributor's. Clarify what you and the organization value in leaders. Developing talented, promotable staff is critical in any company. Let new managers know that they will be rewarded for these less tangible efforts in addition to hitting numerical goals. Understanding this new role is half the battle for rookie managers, and one that many companies mistakenly assume is evident from the start.

Idea in Practice

Essential management skills for rookie managers:

Delegating. Under pressure to produce, rookies often “just do it” themselves because they fear losing control or overburdening others. But failure to delegate blocks their staffs’ advancement, making them resentful, and then disengaged.

How to help:

- Explain that developing staff is *as* essential as financial achievements.
- Lead by example. Trust and empower your rookie; he’ll engage his *own* team.
- Encourage him to take small risks in playing to his staff’s strengths. Early successes will build his confidence.
- Help him break complex projects into manageable chunks with clear milestones.

Getting support from above. Many rookie managers believe they’re in servitude to bosses, not in partnership. To avoid seeming vulnerable, they don’t ask for help. But if they don’t see you as a critical support source, they won’t see *themselves* as one for their team.

How to help:

- Emphasize that open communication is essential to your rookie's success. Discourage covering up problems.
- Introduce him to other managers as resources.
- Have *him* prepare agendas for your regular meetings. The process will help him organize his thoughts.

Projecting confidence. Rookies who don't project confidence won't energize their teams. Frantic, arrogant, or insecure demeanors may repel others in the company.

How to help:

- Encourage “conscious comportment”: constant awareness of the image your rookie is projecting.
- Let him express his feelings—but in your office, behind closed doors.
- Keep him from undermining his own authority; e.g., by pushing an initiative only because top management requested it. Walk through the process of presenting an initiative persuasively, ensuring he can *own* the message—not just deliver it.

Focusing on the big picture. Many rookie managers let fire fighting eclipse strategic initiatives. Fire fighting *feels* productive—but it doesn't teach teams to handle challenges themselves or think strategically.

How to help:

- Explain that strategic thinking will constitute more of your rookie's work as his career advances.
- Help him focus on the long-term, big picture. Ask strategic questions; e.g., "What marketplace trends are you seeing that could affect you in six months?"
- Request written plans documenting strategic goals as well as concrete, supporting actions.

Giving constructive feedback. Most rookies dread correcting staffers' inadequate performance. But avoidance costs managers their credibility.

How to help:

- Explain that constructive feedback strengthens staffers' skills.
- Role-play giving feedback about behaviors, not personalities.

After clarifying how your rookie manager's role has changed, you can move on to tactics. Perhaps it goes without saying, but you should lead by example. You have the responsibility to empower the rookie who works for you and do what you can to help him overcome his insecurities about his value to the organization. You can then assist him in looking for opportunities to empower and engage his team.

One young manager I worked with desperately needed to find time to train and supervise new employees. His firm had been recently acquired, and

he had to deal with high staff turnover and new industrywide rules and regulations. The most senior person on his staff—a woman who had worked for the acquiring company—was about to return from an extended family leave, and he was convinced that he couldn't ask her for help. After all, she had a part-time schedule, and she'd asked to be assigned to the company's largest client. To complicate matters, he suspected that she resented his promotion. As we evaluated the situation, the manager was able to see that the senior staffer's number one priority was reestablishing herself as an important part of the team. Once he realized this, he asked her to take on critical supervisory responsibilities, balanced with a smaller client load, and she eagerly agreed. Indeed, she returned from leave excited about partnering with her manager to develop the team.

When a new manager grumbles about mounting workloads, seize the opportunity to discuss delegation. Encourage him to take small risks initially, playing to the obvious strengths of his staff members. Asking his super-organized, reliable assistant to take the lead in handling the logistics of a new product launch, for example, is much less risky than asking a star salesperson, unaccustomed to this sort of detailed work, to do it. Early successes will build the manager's confidence and willingness to take progressively larger risks in stretching each team member's capabilities. Reinforce to him that delegation does not mean abdication. Breaking a complex project into manageable chunks, each with clearly defined milestones, makes effective follow-up easier. It's also important to schedule regular meetings before the project even begins in order to ensure that the manager stays abreast of progress and that staff members feel accountable.

Getting Support from Above

Most first-time managers see their relationship with their boss more as one of servitude than of partnership. They will wait for you to initiate meetings, ask for reports, and question results. You may welcome this restraint, but generally it's a bad sign. For one thing, it puts undue pressure on you to keep the flow of communication going. Even more important, it prevents new managers from looking to you as a critical source of support. If they don't see you that way, it's unlikely that they will see themselves that way for their own people. The problem isn't only that your position intimidates them; it's also that they fear being vulnerable. A newly promoted manager doesn't want you to see weaknesses, lest you think you made a mistake in promoting her. When I ask rookie managers about their relationships with their bosses, they often admit that they are trying to "stay under the boss's radar" and are "careful about what [they] say to the boss."

Some inexperienced managers will not seek your help even when they start to founder. Seemingly capable rookie managers often try to cover up a failing project or relationship—just until they can get it back under control. For example, one manager I worked with at a technology company hired a professional 20 years her senior. The transition was rocky, and, despite her best efforts, the individual wasn't acclimating to the organization. (The company, like many in the technology sector, was very youth oriented.) Rather than reaching out to her boss for help, the manager continued to grapple with the situation alone. The staff member ultimately resigned at the busiest time of the year, and the young manager suffered the dual punishment of being understaffed at the worst possible moment and having it known that she had lost a potentially important contributor.

What's the boss of a rookie manager to do? You can begin by clarifying expectations. Explain the connection between the rookie's success and your success, so that she understands that open communication is necessary for you to achieve your goals. Explain that you don't expect her to have all the answers. Introduce her to other managers within the company who may be

helpful, and encourage her to contact them as needed. Let her know that mistakes happen but that the cover-up is always worse than the crime. Let her know that you like to receive occasional lunch invitations as much as you like to extend them.

Lunch and drop-by meetings are important, but they usually aren't enough. Consider meeting regularly with a new manager—perhaps weekly in the early stages of a new assignment, moving to biweekly or monthly as her confidence builds. These meetings will develop rapport, provide you with insight into how the person is approaching the job, and make the new manager organize her thoughts on a regular basis. Be clear that the meetings are her time and that it's up to her to plan the agenda. You're there to ask and answer questions and to offer advice. The message you send is that the individual's work is important to you and that you're a committed business partner. More subtly, you're modeling how to simultaneously empower and guide direct reports.

Projecting Confidence

Looking confident when you don't feel confident—it's a challenge we all face, and as senior managers we're usually conscious of the need when it arises. Rookie managers are often so internally focused that they are unaware of this need or the image they project. They are so focused on substance that they forget that form counts, too. The first weeks and months on the job are a critical time for new leaders to reach out to staff. If they don't project confidence, they are unlikely to inspire and energize their teams.

I routinely work with new managers who are unaware that their everyday demeanor is hurting their organizations. In one rapidly growing technology company, the service manager, Linda, faced high levels of stress. Service outages were all too common, and they were beyond her control. Customers were exacting, and they too were under great pressure. Her rapidly growing staff was generally inexperienced. Distraught customers and employees had her tied up in knots almost daily. She consistently appeared breathless, rushed, and fearful that the other shoe was about to drop. The challenge was perhaps too big for a first-time manager, but that's what happens in rapidly growing companies. On one level, Linda was doing an excellent job keeping the operation going. The client base was growing and retention was certainly high—largely as a result of her energy and resourcefulness. But on another level, she was doing a lot of damage.

Linda's frantic demeanor had two critical repercussions. First, she had unwittingly defined the standard for acceptable conduct in her department, and her inexperienced staff began to display the same behaviors. Before long, other departments were reluctant to communicate with Linda or her team, for fear of bothering them or eliciting an emotional reaction. But for the company to arrive at real solutions to the service problems, departments needed to openly exchange information, and that wasn't happening. Second, Linda was not portraying herself to senior managers as promotion material. They were pleased with her troubleshooting abilities, but they did not see a confident, thoughtful senior manager in the making. The image Linda was

projecting would ultimately hold back both her career and her department.

Not all rookie managers display the problems that Linda did. Some appear excessively arrogant. Others wear their self-doubt on their sleeves. Whether your managers appear overwhelmed, arrogant, or insecure, honest feedback is your best tool. You can help rookie managers by telling them that it's always safe to let out their feelings—in your office, behind closed doors. Reinforce just how long a shadow they cast once they assume leadership positions. Their staff members watch them closely, and if they see professionalism and optimism, they are likely to demonstrate those characteristics as well. Preach the gospel of conscious comportment—a constant awareness of the image one is projecting to the world. If you observe a manager projecting a less-than-positive image, tell that person right away.

You should also be alert to new managers who undermine their own authority. Linda made another classic rookie mistake when she attempted to get her staff members to implement an initiative that her boss had come up with. In presenting the initiative, she let her team know it was important to implement because it had come from the division's senior vice president. While her intentions were good—rallying the team to perform—her words encouraged the group to focus attention above her rather than on her. There is no quicker way for a rookie manager to lose credibility with her staff than to appear to be a mouthpiece for senior management. Pointing out that senior management will be checking up on the initiative certainly won't hurt, but the rookie manager must take care never to be perceived simply as the messenger.

Just-in-time coaching is often the most effective method for showing rookie managers how to project confidence. For instance, the first time you ask a new manager to carry out an initiative, take a little extra time to walk her through the process. Impress upon her the cardinal rule of management: Your staff members don't necessarily have to like you, but they do need to trust you. Ensure that the new manager owns the message she's delivering.

Layoffs are a classic example of a message the rookie manager will struggle with. Don't allow a rookie to proceed half-prepared. Share as much information as you can. Make sure she's ready for all the likely questions and reactions by asking her to do an informal dry run with you. You might be surprised by how poorly she conveys the message in her first few attempts. A little practice may preserve the image of your manager and your company.

Focusing on the Big Picture

Rookie managers have a real knack for allowing immediate tasks to overshadow overarching initiatives. This is particularly true for those promoted from within, because they've just come from the front lines where they're accustomed to constant fire fighting. As a recent individual contributor armed with plenty of technical know-how, the rookie manager instinctively runs to the immediate rescue of any client or staff member in need. The sense of accomplishment rookies get from such rescues is seductive and far more exhilarating than rooting out the cause of all the fire fighting. And what could be better for team spirit than having the boss jump into the trenches and fight the good fight?

Of course, a leader shows great team spirit if he joins the troops in emergencies. But are all those emergencies true emergencies? Are newer staff members being empowered to handle complex challenges? And if the rookie manager is busy fighting fires, who is thinking strategically for the department? If you're the senior manager and these questions are popping into your head, you may well have a rookie manager who doesn't fully understand his role or is afraid to seize it.

I recently worked with a young manager who had become so accustomed to responding to a steady flow of problems that he was reluctant to block off any time to work on the strategic initiatives we had identified. When I probed, he revealed that he felt a critical part of his role was to wait for crises to arise. "What if I schedule this time and something urgent comes up and I disappoint someone?" he asked. When I pointed out that he could always postpone his strategy sessions if a true emergency arose, he seemed relieved. But he saw the concept of making time to think about the business as self-indulgent—this, despite the fact that his group was going to be asked to raise productivity significantly in the following fiscal year, and he'd done nothing to prepare for that reality.

Senior managers can help rookies by explaining to them that strategic thinking is a necessary skill for career advancement: For first-time managers,

10% of the work might be strategic and 90% tactical. As executives climb the corporate ladder, however, those percentages will flip-flop. To be successful at the next level, managers must demonstrate that they can think and act strategically. You can use your regularly scheduled meetings to help your managers focus on the big picture. Don't allow them to simply review the latest results and move on. Ask probing questions about those results. For example, "What trends are you seeing in the marketplace that could affect you in two quarters? Tell me how your competition is responding to those same trends." Don't let them regale you with the wonderful training their staffs have been getting without asking, "What additional skills do we need to build in the staff to increase productivity by 25% next year?" If you aren't satisfied with your managers' responses, let them know that you expect them to think this way—not to have all the answers, but to be fully engaged in the strategic thought process.

Rookie managers commonly focus on activities rather than on goals. That's because activities can be accomplished quickly (for example, conducting a seminar to improve the sales staff's presentation skills), whereas achieving goals generally takes more time (for example, actually enhancing the sales staff's effectiveness). The senior manager can help the rookie manager think strategically by asking for written goals that clearly distinguish between the goals and their supporting activities. Insisting on a goal-setting discipline will help your new (and not-so-new) managers to organize their strategic game plans. Critical but soft goals, such as staff development, are often overlooked because they are difficult to measure. Putting such goals in print with clear action steps makes them concrete, rendering a sense of accomplishment when they are achieved and a greater likelihood that they will be rewarded. Managers with clear goals will be less tempted to become full-time tacticians. Just as important, the process will help you ensure that they are thinking about the right issues and deploying their teams effectively.

Giving Constructive Feedback

It's human nature to avoid confrontations, and most people feel awkward when they have to correct others' behavior or actions. Rookie managers are no exception, and they often avoid addressing important issues with their staff. The typical scenario goes something like this: A staff member is struggling to meet performance goals or is acting inappropriately in meetings. The manager sits back, watches, and hopes that things will magically improve. Other staff members observe the situation and become frustrated by the manager's inaction. The manager's own frustration builds, as she can't believe the subordinate doesn't get it. The straightforward performance issue has now evolved into a credibility problem. When the manager finally addresses the problem, she personalizes it, lets her frustration seep into the discussion with her staff member, and finds the recipient rushing to defend himself from attack.

Most inexperienced managers wait far too long to talk with staff about performance problems. The senior manager can help by creating an environment in which constructive feedback is perceived not as criticism but as a source of empowerment. This begins with the feedback you offer to your managers about their own development. It can be as simple as getting them to tell you where their weaknesses are before they become problematic. After a good performance review, for example, you might say to your new manager, "By all accounts, you have a bright future here, so it's important that we talk about what you *don't* want me to know. What are you feeling least confident about? How can we address those areas so that you're ready for any opportunity that arises?" You'll probably be surprised by how attuned most high performers are to their own development needs. But they are not likely to do much about them unless you put those needs on the table.

More than likely, the feedback your managers have to offer their staffs will not always be so positive or easy to deliver. The key is to foster in them the desire to help their reports achieve their goals. Under those circumstances, even loathsome personal issues become approachable.

One of my clients managed a high-performing senior staff member who was notably unhelpful to others in the department and who resented her own lack of advancement. Instead of avoiding the issue because he didn't want to tell the staff member that she had a bad attitude, the senior manager took a more productive approach. He leveraged his knowledge of her personal goals to introduce the feedback. "I know that you're anxious for your first management role, and one of my goals is to help you attain that. I can't do that unless I'm completely honest with you. A big part of management is developing stronger skills in your staff. You aren't demonstrating that you enjoy that role. How can we can work together on that?" No guilt, no admonishment—just an offer to help her get what she wanted. Yet the message was received loud and clear.

A brainstorming session this client and I had about ways to offer critical feedback led to that approach. Often, brainstorming sessions can help rookie managers see that sticky personal issues can be broken down into straightforward business issues. In the case of the unhelpful senior staff member, her attitude didn't really need to enter the discussion; her actions did. Recommending a change in action is much easier than recommending a change in attitude. Never forget the old saw: You can't ask people to change their personalities, but you can ask them to change their behaviors.

Indeed, senior managers should share their own techniques for dealing with difficult conversations. One manager I worked with became defensive whenever a staff member questioned her judgment. She didn't really need me to tell her that her behavior was undermining her image and effectiveness. She did need me to offer her some techniques that would enable her to respond differently in the heat of the moment. She trained herself to respond quickly and earnestly with a small repertoire of questions like, "Can you tell me more about what you mean by that?" This simple technique bought her the time she needed to gather her thoughts and engage in an interchange that was productive rather than defensive. She was too close to the situation to come up with the technique herself.

Delegating, thinking strategically, communicating—you may think this all sounds like Management 101. And you're right. The most basic elements of management are often what trip up managers early in their careers. And

because they are the basics, the bosses of rookie managers often take them for granted. They shouldn't—an extraordinary number of people fail to develop these skills. I've maintained an illusion throughout this article—that only rookie managers suffer because they haven't mastered these core skills. But the truth is, managers at all levels make these mistakes. An organization that supports its new managers by helping them to develop these skills will have surprising advantages over the competition.

Originally published in April 2002. Reprint R0204H.

What Great Managers Do

by Marcus Buckingham

“THE BEST BOSS I EVER HAD.” That’s a phrase most of us have said or heard at some point, but what does it mean? What sets the great boss apart from the average boss? The literature is rife with provocative writing about the qualities of managers and leaders and whether the two differ, but little has been said about what happens in the thousands of daily interactions and decisions that allows managers to get the best out of their people and win their devotion. What do great managers actually *do*?

In my research, beginning with a survey of 80,000 managers conducted by the Gallup Organization and continuing during the past two years with in-depth studies of a few top performers, I’ve found that while there are as many styles of management as there are managers, there is one quality that sets truly great managers apart from the rest: They discover what is unique about each person and then capitalize on it. Average managers play checkers, while great managers play chess. The difference? In checkers, all the pieces are uniform and move in the same way; they are interchangeable. You need to plan and coordinate their movements, certainly, but they all move at the same pace, on parallel paths. In chess, each type of piece moves in a different way, and you can’t play if you don’t know how each piece moves. More important, you won’t win if you don’t think carefully about how you move the pieces. Great managers know and value the unique abilities and even the eccentricities of their employees, and they learn how best to integrate them into a coordinated plan of attack.

This is the exact opposite of what great leaders do. Great leaders discover

what is universal and capitalize on it. Their job is to rally people toward a better future. Leaders can succeed in this only when they can cut through differences of race, sex, age, nationality, and personality and, using stories and celebrating heroes, tap into those very few needs we all share. The job of a manager, meanwhile, is to turn one person's particular talent into performance. Managers will succeed only when they can identify and deploy the differences among people, challenging each employee to excel in his or her own way. This doesn't mean a leader can't be a manager or vice versa. But to excel at one or both, you must be aware of the very different skills each role requires.

The Game of Chess

What does the chess game look like in action? When I visited Michelle Miller, the manager who opened Walgreens' 4,000th store, I found the wall of her back office papered with work schedules. Michelle's store in Redondo Beach, California, employs people with sharply different skills and potentially disruptive differences in personality. A critical part of her job, therefore, is to put people into roles and shifts that will allow them to shine—and to avoid putting clashing personalities together. At the same time, she needs to find ways for individuals to grow.

There's Jeffrey, for example, a "goth rocker" whose hair is shaved on one side and long enough on the other side to cover his face. Michelle almost didn't hire him because he couldn't quite look her in the eye during his interview, but he wanted the hard-to-cover night shift, so she decided to give him a chance. After a couple of months, she noticed that when she gave Jeffrey a vague assignment, such as "Straighten up the merchandise in every aisle," what should have been a two-hour job would take him all night—and wouldn't be done very well. But if she gave him a more specific task, such as "Put up all the risers for Christmas," all the risers would be symmetrical, with the right merchandise on each one, perfectly priced, labeled, and "faced" (turned toward the customer). Give Jeffrey a generic task, and he would struggle. Give him one that forced him to be accurate and analytical, and he would excel. This, Michelle concluded, was Jeffrey's forte. So, as any good manager would do, she told him what she had deduced about him and praised him for his good work.

Idea in Brief

You've spent months coaching that employee to treat customers better, work more independently, or get organized—all to no avail.

How to make better use of your precious time? Do what great managers do: Instead of trying to change your employees, identify their unique abilities (and even their eccentricities)—then help them use those qualities to excel in their own way.

You'll need these three tactics:

- **Continuously tweak roles to capitalize on individual strengths.** One Walgreens store manager put a laconic but highly organized employee in charge of restocking aisles—freeing up more sociable employees to serve customers.
- **Pull the triggers that activate employees' strengths.** Offer incentives such as time spent with you, opportunities to work independently, and recognition in forms each employee values most.
- **Tailor coaching to unique learning styles.** Give “analyzers” the information they need before starting a task. Start “doers” off with simple tasks, then gradually raise the bar. Let “watchers” ride shotgun with your most experienced performers.

The payoff for capitalizing on employees' unique strengths? You save time. Your people take ownership for improving their skills. And you teach employees to value differences—building a powerful sense of team.

And a good manager would have left it at that. But Michelle knew she could get more out of Jeffrey. So she devised a scheme to reassign responsibilities across the entire store to capitalize on his unique strengths. In every Walgreens, there is a responsibility called “resets and revisions.” A reset involves stocking an aisle with new merchandise, a task that usually coincides with a predictable change in customer buying patterns (at the end of summer, for example, the stores will replace sun creams and lip balms with allergy medicines). A revision is a less time-consuming but more frequent version of the same thing: Replace these cartons of toothpaste with this new and improved variety. Display this new line of detergent at this end of the row. Each aisle requires some form of revision at least once a week.

Idea in Practice

A closer look at the three tactics:

Capitalize on Employees' Strengths

First identify each employee's unique strengths: Walk around, observing people's reactions to events. Note activities each employee is drawn to. Ask "What was the best day at work you've had in the past three months?" Listen for activities people find intrinsically satisfying.

Watch for weaknesses, too, but downplay them in your communications with employees. Offer training to help employees overcome shortcomings stemming from lack of skills or knowledge. Otherwise, apply these strategies:

- **Find the employee a partner with complementary talents.** A merchandising manager who couldn't start tasks without exhaustive information performed superbly once her supervisor (the VP) began acting as her "information partner." The VP committed to leaving the manager a brief voicemail update daily and arranging two "touch base" conversations weekly.
- **Reconfigure work to neutralize weaknesses.** Use your creativity to envision more effective work arrangements, and be courageous about adopting unconventional job designs.

Activate Employees' Strengths

The ultimate trigger for activating an employee's strengths is recognition. But each employee plays to a different audience. So tailor your praise

accordingly.

If an employee values recognition from. . .	Praise him by. . .
His peers	• Publicly celebrating his achievement in front of coworkers
You	• Telling him privately but vividly why he's such a valuable team member
Others with similar expertise	• Giving him a professional or technical award
Customers	• Posting a photo of him and his best customer in the office

Tailor Coaching to Learning Style

Adapt your coaching efforts to each employee's unique learning style:

If an employee is . . .	Coach him by. . .
An "analyzer" —he requires extensive information before taking on a task, and he hates making mistakes	• Giving him ample classroom time • Role-playing with him • Giving him time to prepare for challenges
A "doer" —he uses trial and error to enhance his skills while grappling with tasks	• Assigning him a simple task, explaining the desired outcomes, and getting out of his way • Gradually increasing a task's complexity until he masters his role
A "watcher" —he hones his skills by watching other people in action	• Having him "shadow" top performers.

In most Walgreens stores, each employee "owns" one aisle, where she is responsible not only for serving customers but also for facing the merchandise, keeping the aisle clean and orderly, tagging items with a Telxon gun, and conducting all resets and revisions. This arrangement is simple and efficient, and it affords each employee a sense of personal responsibility. But Michelle decided that since Jeffrey was so good at resets and revisions—and didn't enjoy interacting with customers—this should be his full-time job, in every single aisle.

It was a challenge. One week's worth of revisions requires a binder three

inches thick. But Michelle reasoned that not only would Jeffrey be excited by the challenge and get better and better with practice, but other employees would be freed from what they considered a chore and have more time to greet and serve customers. The store's performance proved her right. After the reorganization, Michelle saw not only increases in sales and profit but also in that most critical performance metric, customer satisfaction. In the subsequent four months, her store netted perfect scores in Walgreens' mystery shopper program.

So far, so very good. Sadly, it didn't last. This "perfect" arrangement depended on Jeffrey remaining content, and he didn't. With his success at doing resets and revisions, his confidence grew, and six months into the job, he wanted to move into management. Michelle wasn't disappointed by this, however; she was intrigued. She had watched Jeffrey's progress closely and had already decided that he might do well as a manager, though he wouldn't be a particularly emotive one. Besides, like any good chess player, she had been thinking a couple of moves ahead.

Over in the cosmetics aisle worked an employee named Genoa. Michelle saw Genoa as something of a double threat. Not only was she adept at putting customers at ease—she remembered their names, asked good questions, was welcoming yet professional when answering the phone—but she was also a neatnik. The cosmetics department was always perfectly faced, every product remained aligned, and everything was arranged just so. Her aisle was sexy: It made you want to reach out and touch the merchandise.

To capitalize on these twin talents, and to accommodate Jeffrey's desire for promotion, Michelle shuffled the roles within the store once again. She split Jeffrey's reset and revision job in two and gave the "revision" part of it to Genoa so that the whole store could now benefit from her ability to arrange merchandise attractively. But Michelle didn't want the store to miss out on Genoa's gift for customer service, so Michelle asked her to focus on the revision role only between 8:30 AM and 11 AM, and after that, when the store began to fill with customers on their lunch breaks, Genoa should shift her focus over to them.

She kept the reset role with Jeffrey. Assistant managers don't usually have an ongoing responsibility in the store, but, Michelle reasoned, he was now so good and so fast at tearing an aisle apart and rebuilding it that he could easily finish a major reset during a five-hour stint, so he could handle resets along with his managerial responsibilities.

By the time you read this, the Jeffrey–Genoa configuration has probably outlived its usefulness, and Michelle has moved on to design other effective and inventive configurations. The ability to keep tweaking roles to capitalize on the uniqueness of each person is the essence of great management.

A manager's approach to capitalizing on differences can vary tremendously from place to place. Walk into the back office at another Walgreens, this one in San Jose, California, managed by Jim Kawashima, and you won't see a single work schedule. Instead, the walls are covered with sales figures and statistics, the best of them circled with red felt-tip pen, and dozens of photographs of sales contest winners, most featuring a customer service representative named Manjit.

Manjit outperforms her peers consistently. When I first heard about her, she had just won a competition in Walgreens' suggestive selling program to sell the most units of Gillette deodorant in a month. The national average was 300; Manjit had sold 1,600. Disposable cameras, toothpaste, batteries—you name it, she could sell it. And Manjit won contest after contest despite working the graveyard shift, from 12:30 AM to 8:30 AM, during which she met significantly fewer customers than did her peers.

Manjit hadn't always been such an exceptional performer. She became stunningly successful only when Jim, who has made a habit of resuscitating troubled stores, came on board. What did Jim do to initiate the change in Manjit? He quickly picked up on her idiosyncrasies and figured out how to translate them into outstanding performance. For example, back in India, Manjit was an athlete—a runner and a weight lifter—and had always thrilled to the challenge of measured performance. When I interviewed her, one of the first things out of her mouth was, "On Saturday, I sold 343 low-carb candy bars. On Sunday, I sold 367. Yesterday, 110, and today, 105." I asked if she always knows how well she's doing. "Oh yes," she replied. "Every day I check Mr. K's charts. Even on my day off, I make a point to come in and check my numbers."

The Research

TO GATHER THE RAW MATERIAL for my book *The One Thing You Need to Know: About Great Managing, Great Leading, and Sustained Individual Success*, from which this article has been adapted, I chose an approach that is rather different from the one I used for my previous books. For 17 years, I had the good fortune to work with the Gallup Organization, one of the most respected research firms in the world. During that time, I was given the opportunity to interview some of the world's best leaders, managers, teachers, salespeople, stockbrokers, lawyers, and public servants. These interviews were a part of large-scale studies that involved surveying groups of people in the hopes of finding broad patterns in the data. For my book, I used this foundation as the jumping-off point for deeper, more individualized research.

In each of the three areas targeted in the book—managing, leading, and sustained individual success—I first identified one or two people in various roles and fields who had measurably, consistently, and dramatically outperformed their peers. These individuals included Myrtle Potter, president of commercial operations for Genentech, who transformed a failing drug into the highest selling prescription drug in the world; Sir Terry Leahy, the president of the European retailing giant Tesco; Manjit, the customer service representative from Jim Kawashima's top-performing Walgreens store in San Jose, California, who sold more than 1,600 units of Gillette deodorant in one month; and David Koepp, the prolific screenwriter who penned such blockbusters as *Jurassic Park*, *Mission: Impossible*, and *Spider-Man*.

What interested me about these high achievers was the practical, seemingly banal details of their actions and their choices. Why did Myrtle Potter repeatedly turn down promotions before taking on the challenge of turning around that failing drug? Why did Terry Leahy rely more on the memories of his working-class upbringing to define his company's strategy than on the results of customer surveys or focus groups? Manjit works the night shift, and one of her hobbies is weight lifting. Are those factors relevant to her

performance? What were these special people doing that made them so very good at their roles?

Once these many details were duly noted and recorded, they slowly came together to reveal the “one thing” at the core of great managing, great leading, and sustained individual success.

Manjit loves to win and revels in public recognition. Hence, Jim’s walls are covered with charts and figures, Manjit’s scores are always highlighted in red, and there are photos documenting her success. Another manager might have asked Manjit to curb her enthusiasm for the limelight and give someone else a chance. Jim found a way to capitalize on it.

But what about Jim’s other staff members? Instead of being resentful of Manjit’s public recognition, the other employees came to understand that Jim took the time to see them as individuals and evaluate them based on their personal strengths. They also knew that Manjit’s success spoke well of the entire store, so her success galvanized the team. In fact, before long, the pictures of Manjit began to include other employees from the store, too. After a few months, the San Jose location was ranked number one out of 4,000 in Walgreens’ suggestive selling program.

Great Managers Are Romantics

Think back to Michelle. Her creative choreography may sound like a last resort, an attempt to make the best of a bad hire. It's not. Jeffrey and Genoa are not mediocre employees, and capitalizing on each person's uniqueness is a tremendously powerful tool.

First, identifying and capitalizing on each person's uniqueness saves time. No employee, however talented, is perfectly well-rounded. Michelle could have spent untold hours coaching Jeffrey and cajoling him into smiling at, making friends with, and remembering the names of customers, but she probably would have seen little result for her efforts. Her time was much better spent carving out a role that took advantage of Jeffrey's natural abilities.

The Elusive “One Thing”

IT'S BOLD TO CHARACTERIZE ANYTHING as *the* explanation or solution, so it's a risky move to make such definitive assertions as “this is the one thing all great managers do.” But with enough research and focus, it is possible to identify that elusive “one thing.”

I like to think of the concept of “one thing” as a “controlling insight.” Controlling insights don't explain all outcomes or events; they serve as the best explanation of the greatest number of events. Such insights help you know which of your actions will have the most far-reaching influence in virtually every situation.

For a concept to emerge as the single controlling insight, it must pass three tests. First, it must be applicable across a wide range of situations. Take leadership as an example. Lately, much has been made of the notion that there is no one best way to lead and that instead, the most effective leadership style depends on the circumstance. While there is no doubt that different situations require different actions from a leader, that doesn't mean the most insightful thing you can say about leadership is that it's situational. With enough focus, you can identify the one thing that underpins successful leadership across all situations and all styles.

Second, a controlling insight must serve as a multiplier. In any equation, some factors will have only an additive value: When you focus your actions on these factors, you see some incremental improvement. The controlling insight should be more powerful. It should show you how to get exponential improvement. For example, good managing is the result of a combination of many actions—selecting talented employees, setting clear expectations, catching people doing things right, and so on—but none of these factors qualifies as the “one thing” that great managers do, because even when done well, these actions merely prevent managers from chasing their best employees away.

Finally, the controlling insight must guide action. It must point to precise things that can be done to create better outcomes more consistently. Insights that managers can act on—rather than simply ruminate over—are the ones that can make all the difference.

Second, capitalizing on uniqueness makes each person more accountable. Michelle didn't just praise Jeffrey for his ability to execute specific assignments. She challenged him to make this ability the cornerstone of his contribution to the store, to take ownership for this ability, to practice it, and to refine it.

Third, capitalizing on what is unique about each person builds a stronger sense of team, because it creates interdependency. It helps people appreciate one another's particular skills and learn that their coworkers can fill in where they are lacking. In short, it makes people need one another. The old cliché is that there's no "I" in "team." But as Michael Jordan once said, "There may be no 'I' in 'team,' but there is in 'win.'"

Finally, when you capitalize on what is unique about each person, you introduce a healthy degree of disruption into your world. You shuffle existing hierarchies: If Jeffrey is in charge of all resets and revisions in the store, should he now command more or less respect than an assistant manager? You also shuffle existing assumptions about who is allowed to do what: If Jeffrey devises new methods of resetting an aisle, does he have to ask permission to try these out, or can he experiment on his own? And you shuffle existing beliefs about where the true expertise lies: If Genoa comes up with a way of arranging new merchandise that she thinks is more appealing than the method suggested by the "planogram" sent down from Walgreens headquarters, does her expertise trump the planners back at corporate? These questions will challenge Walgreens' orthodoxies and thus will help the company become more inquisitive, more intelligent, more vital, and, despite its size, more able to duck and weave into the future.

All that said, the reason great managers focus on uniqueness isn't just because it makes good business sense. They do it because they can't help it. Like Shelley and Keats, the nineteenth-century Romantic poets, great managers are fascinated with individuality for its own sake. Fine shadings of personality, though they may be invisible to some and frustrating to others, are crystal clear to and highly valued by great managers. They could no more

ignore these subtleties than ignore their own needs and desires. Figuring out what makes people tick is simply in their nature.

The Three Levers

Although the Romantics were mesmerized by differences, at some point, managers need to rein in their inquisitiveness, gather up what they know about a person, and put the employee's idiosyncrasies to use. To that end, there are three things you must know about someone to manage her well: her strengths, the triggers that activate those strengths, and how she learns.

Make the most of strengths

It takes time and effort to gain a full appreciation of an employee's strengths and weaknesses. The great manager spends a good deal of time outside the office walking around, watching each person's reactions to events, listening, and taking mental notes about what each individual is drawn to and what each person struggles with. There's no substitute for this kind of observation, but you can obtain a lot of information about a person by asking a few simple, open-ended questions and listening carefully to the answers. Two queries in particular have proven most revealing when it comes to identifying strengths and weaknesses, and I recommend asking them of all new hires—and revisiting the questions periodically.

To identify a person's strengths, first ask, "What was the best day at work you've had in the past three months?" Find out what the person was doing and why he enjoyed it so much. Remember: A strength is not merely something you are good at. In fact, it might be something you aren't good at yet. It might be just a predilection, something you find so intrinsically satisfying that you look forward to doing it again and again and getting better at it over time. This question will prompt your employee to start thinking about his interests and abilities from this perspective.

To identify a person's weaknesses, just invert the question: "What was the worst day you've had at work in the past three months?" And then probe for details about what he was doing and why it grated on him so much. As with a strength, a weakness is not merely something you are bad at (in fact, you might be quite competent at it). It is something that drains you of energy, an activity that you never look forward to doing and that when you are doing it, all you can think about is stopping.

What You Need to Know About Each of Your Direct Reports

- ☐ What are his or her strengths?
- ☐ What are the triggers that activate those strengths?
- ☐ What is his or her learning style?

Although you're keeping an eye out for both the strengths and weaknesses of your employees, your focus should be on their strengths. Conventional wisdom holds that self-awareness is a good thing and that it's the job of the manager to identify weaknesses and create a plan for overcoming them. But research by Albert Bandura, the father of social learning theory, has shown that self-assurance (labeled "self-efficacy" by cognitive psychologists), not self-awareness, is the strongest predictor of a person's ability to set high goals, to persist in the face of obstacles, to bounce back when reversals occur, and, ultimately, to achieve the goals they set. By contrast, self-awareness has not been shown to be a predictor of any of these outcomes, and in some cases, it appears to retard them.

Great managers seem to understand this instinctively. They know that their job is not to arm each employee with a dispassionately accurate understanding of the limits of her strengths and the liabilities of her weaknesses but to reinforce her self-assurance. That's why great managers focus on strengths. When a person succeeds, the great manager doesn't praise her hard work. Even if there's some exaggeration in the statement, he tells her that she succeeded because she has become so good at deploying her

specific strengths. This, the manager knows, will strengthen the employee's self-assurance and make her more optimistic and more resilient in the face of challenges to come.

The focus-on-strengths approach might create in the employee a modicum of overconfidence, but great managers mitigate this by emphasizing the size and the difficulty of the employee's goals. They know that their primary objective is to create in each employee a specific state of mind: one that includes a realistic assessment of the difficulty of the obstacle ahead but an unrealistically optimistic belief in her ability to overcome it.

And what if the employee fails? Assuming the failure is not attributable to factors beyond her control, always explain failure as a lack of effort, even if this is only partially accurate. This will obscure self-doubt and give her something to work on as she faces up to the next challenge.

Repeated failure, of course, may indicate weakness where a role requires strength. In such cases, there are four approaches for overcoming weaknesses. If the problem amounts to a lack of skill or knowledge, that's easy to solve: Simply offer the relevant training, allow some time for the employee to incorporate the new skills, and look for signs of improvement. If her performance doesn't get better, you'll know that the reason she's struggling is because she is missing certain talents, a deficit no amount of skill or knowledge training is likely to fix. You'll have to find a way to manage around this weakness and neutralize it.

Which brings us to the second strategy for overcoming an employee weakness. Can you find her a partner, someone whose talents are strong in precisely the areas where hers are weak? Here's how this strategy can look in action. As vice president of merchandising for the women's clothing retailer Ann Taylor, Judi Langley found that tensions were rising between her and one of her merchandising managers, Claudia (not her real name), whose analytical mind and intense nature created an overpowering "need to know." If Claudia learned of something before Judi had a chance to review it with her, she would become deeply frustrated. Given the speed with which decisions were made, and given Judi's busy schedule, this happened frequently. Judi was concerned that Claudia's irritation was unsettling the whole product team, not to mention earning the employee a reputation as a malcontent.

An average manager might have identified this behavior as a weakness and lectured Claudia on how to control her need for information. Judi,

however, realized that this “weakness” was an aspect of Claudia’s greatest strength: her analytical mind. Claudia would never be able to rein it in, at least not for long. So Judi looked for a strategy that would honor and support Claudia’s need to know, while channeling it more productively. Judi decided to act as Claudia’s information partner, and she committed to leaving Claudia a voice mail at the end of each day with a brief update. To make sure nothing fell through the cracks, they set up two live “touch base” conversations per week. This solution managed Claudia’s expectations and assured her that she would get the information she needed, if not exactly when she wanted it, then at least at frequent and predictable intervals. Giving Claudia a partner neutralized the negative manifestations of her strength, allowing her to focus her analytical mind on her work. (Of course, in most cases, the partner would need to be someone other than a manager.)

Should the perfect partner prove hard to find, try this third strategy: Insert into the employee’s world a technique that helps accomplish through discipline what the person can’t accomplish through instinct. I met one very successful screenwriter and director who had struggled with telling other professionals, such as composers and directors of photography, that their work was not up to snuff. So he devised a mental trick: He now imagines what the “god of art” would want and uses this imaginary entity as a source of strength. In his mind, he no longer imposes his own opinion on his colleagues but rather tells himself (and them) that an authoritative third party has weighed in.

If training produces no improvement, if complementary partnering proves impractical, and if no nifty discipline technique can be found, you are going to have to try the fourth and final strategy, which is to rearrange the employee’s working world to render his weakness irrelevant, as Michelle Miller did with Jeffrey. This strategy will require of you, first, the creativity to envision a more effective arrangement and, second, the courage to make that arrangement work. But as Michelle’s experience revealed, the payoff that may come in the form of increased employee productivity and engagement is well worth it.

Trigger good performance

A person's strengths aren't always on display. Sometimes they require precise triggering to turn them on. Squeeze the right trigger, and a person will push himself harder and persevere in the face of resistance. Squeeze the wrong one, and the person may well shut down. This can be tricky because triggers come in myriad and mysterious forms. One employee's trigger might be tied to the time of day (he is a night owl, and his strengths only kick in after 3 PM). Another employee's trigger might be tied to time with you, the boss (even though he's worked with you for more than five years, he still needs you to check in with him every day, or he feels he's being ignored). Another worker's trigger might be just the opposite—independence (she's only worked for you for six months, but if you check in with her even once a week, she feels micromanaged).

The most powerful trigger by far is recognition, not money. If you're not convinced of this, start ignoring one of your highly paid stars, and watch what happens. Most managers are aware that employees respond well to recognition. Great managers refine and extend this insight. They realize that each employee plays to a slightly different audience. To excel as a manager, you must be able to match the employee to the audience he values most. One employee's audience might be his peers; the best way to praise him would be to stand him up in front of his coworkers and publicly celebrate his achievement. Another's favorite audience might be you; the most powerful recognition would be a one-on-one conversation where you tell him quietly but vividly why he is such a valuable member of the team. Still another employee might define himself by his expertise; his most prized form of recognition would be some type of professional or technical award. Yet another might value feedback only from customers, in which case a picture of the employee with her best customer or a letter to her from the customer would be the best form of recognition.

Given how much personal attention it requires, tailoring praise to fit the person is mostly a manager's responsibility. But organizations can take a cue from this, too. There's no reason why a large company can't take this

individualized approach to recognition and apply it to every employee. Of all the companies I've encountered, the North American division of HSBC, a London-based bank, has done the best job of this. Each year it presents its top individual consumer-lending performers with its Dream Awards. Each winner receives a unique prize. During the year, managers ask employees to identify what they would like to receive should they win. The prize value is capped at \$10,000, and it cannot be redeemed as cash, but beyond those two restrictions, each employee is free to pick the prize he wants. At the end of the year, the company holds a Dream Awards gala, during which it shows a video about the winning employee and why he selected his particular prize.

You can imagine the impact these personalized prizes have on HSBC employees. It's one thing to be brought up on stage and given yet another plaque. It's another thing when, in addition to public recognition of your performance, you receive a college tuition fund for your child, or the Harley-Davidson motorcycle you've always dreamed of, or—the prize everyone at the company still talks about—the airline tickets to fly you and your family back to Mexico to visit the grandmother you haven't seen in ten years.

Tailor to learning styles

Although there are many learning styles, a careful review of adult learning theory reveals that three styles predominate. These three are not mutually exclusive; certain employees may rely on a combination of two or perhaps all three. Nonetheless, staying attuned to each employee's style or styles will help focus your coaching.

First, there's analyzing. Claudia from Ann Taylor is an analyzer. She understands a task by taking it apart, examining its elements, and reconstructing it piece by piece. Because every single component of a task is important in her eyes, she craves information. She needs to absorb all there is to know about a subject before she can begin to feel comfortable with it. If she doesn't feel she has enough information, she will dig and push until she gets it. She will read the assigned reading. She will attend the required classes. She will take good notes. She will study. And she will still want more.

The best way to teach an analyzer is to give her ample time in the classroom. Role-play with her. Do postmortem exercises with her. Break her performance down into its component parts so she can carefully build it back up. Always allow her time to prepare. The analyzer hates mistakes. A commonly held view is that mistakes fuel learning, but for the analyzer, this just isn't true. In fact, the reason she prepares so diligently is to minimize the possibility of mistakes. So don't expect to teach her much by throwing her into a new situation and telling her to wing it.

The opposite is true for the second dominant learning style, doing. While the most powerful learning moments for the analyzer occur prior to the performance, the doer's most powerful moments occur *during* the performance. Trial and error are integral to this learning process. Jeffrey, from Michelle Miller's store, is a doer. He learns the most while he's in the act of figuring things out for himself. For him, preparation is a dry, uninspiring activity. So rather than role-play with someone like Jeffrey, pick a specific task within his role that is simple but real, give him a brief overview of the outcomes you want, and get out of his way. Then gradually

increase the degree of each task's complexity until he has mastered every aspect of his role. He may make a few mistakes along the way, but for the doer, mistakes are the raw material for learning.

Finally, there's watching. Watchers won't learn much through role-playing. They won't learn by doing, either. Since most formal training programs incorporate both of these elements, watchers are often viewed as rather poor students. That may be true, but they aren't necessarily poor learners.

Watchers can learn a great deal when they are given the chance to see the total performance. Studying the individual parts of a task is about as meaningful for them as studying the individual pixels of a digital photograph. What's important for this type of learner is the content of each pixel, its position relative to all the others. Watchers are only able to see this when they view the complete picture.

As it happens, this is the way I learn. Years ago, when I first began interviewing, I struggled to learn the skill of creating a report on a person after I had interviewed him. I understood all the required steps, but I couldn't seem to put them together. Some of my colleagues could knock out a report in an hour; for me, it would take the better part of a day. Then one afternoon, as I was staring morosely into my Dictaphone, I overheard the voice of the analyst next door. He was talking so rapidly that I initially thought he was on the phone. Only after a few minutes did I realize that he was dictating a report. This was the first time I had heard someone "in the act." I'd seen the finished results countless times, since reading the reports of others was the way we were supposed to learn, but I'd never actually heard another analyst in the act of creation. It was a revelation. I finally saw how everything should come together into a coherent whole. I remember picking up my Dictaphone, mimicking the cadence and even the accent of my neighbor, and feeling the words begin to flow.

If you're trying to teach a watcher, by far the most effective technique is to get her out of the classroom. Take her away from the manuals, and make her ride shotgun with one of your most experienced performers.

We've seen, in the stories of great managers like Michelle Miller and Judi Langley, that at the very heart of their success lies an appreciation for

individuality. This is not to say that managers don't need other skills. They need to be able to hire well, to set expectations, and to interact productively with their own bosses, just to name a few. But what they do—instinctively—is play chess. Mediocre managers assume (or hope) that their employees will all be motivated by the same things and driven by the same goals, that they will desire the same kinds of relationships and learn in roughly the same way. They define the behaviors they expect from people and tell them to work on behaviors that don't come naturally. They praise those who can overcome their natural styles to conform to preset ideas. In short, they believe the manager's job is to mold, or transform, each employee into the perfect version of the role.

Great managers don't try to change a person's style. They never try to push a knight to move in the same way as a bishop. They know that their employees will differ in how they think, how they build relationships, how altruistic they are, how patient they can be, how much of an expert they need to be, how prepared they need to feel, what drives them, what challenges them, and what their goals are. These differences of trait and talent are like blood types: They cut across the superficial variations of race, sex, and age and capture the essential uniqueness of each individual.

Like blood types, the majority of these differences are enduring and resistant to change. A manager's most precious resource is time, and great managers know that the most effective way to invest their time is to identify exactly how each employee is different and then to figure out how best to incorporate those enduring idiosyncrasies into the overall plan.

To excel at managing others, you must bring that insight to your actions and interactions. Always remember that great managing is about release, not transformation. It's about constantly tweaking your environment so that the unique contribution, the unique needs, and the unique style of each employee can be given free rein. Your success as a manager will depend almost entirely on your ability to do this.

Originally published in March 2005. Reprint R0503D.

Fair Process

**Managing in the Knowledge Economy. by W. Chan Kim
and Renée Mauborgne**

A LONDON POLICEMAN GAVE a woman a ticket for making an illegal turn. When the woman protested that there was no sign prohibiting the turn, the policeman pointed to one that was bent out of shape and difficult to see from the road. Furious, the woman decided to appeal by going to court. Finally, the day of her hearing arrived, and she could hardly wait to speak her piece. But she had just begun to tell her side of the story when the magistrate stopped her and summarily ruled in her favor.

How did the woman feel? Vindicated? Victorious? Satisfied?

No, she was frustrated and deeply unhappy. “I came for justice,” she complained, “but the magistrate never let me explain what happened.” In other words, although she liked the outcome, she didn’t like the process that had created it.

For the purposes of their theories, economists assume that people are maximizers of utility, driven mainly by rational calculations of their own self-interest. That is, economists assume people focus solely on outcomes. That assumption has migrated into much of management theory and practice. It has, for instance, become embedded in the tools managers traditionally use to control and motivate employees’ behavior—from incentive systems to

organizational structures. But it is an assumption that managers would do well to reexamine because we all know that in real life it doesn't always hold true. People do care about outcomes, but—like the woman in London—they also care about the processes that produce those outcomes. They want to know that they had their say—that their point of view was considered even if it was rejected. Outcomes matter, but no more than the fairness of the processes that produce them.

Never has the idea of fair process been more important for managers than it is today. Fair process turns out to be a powerful management tool for companies struggling to make the transition from a production-based to a knowledge-based economy, in which value creation depends increasingly on ideas and innovation. Fair process profoundly influences attitudes and behaviors critical to high performance. It builds trust and unlocks ideas. With it, managers can achieve even the most painful and difficult goals while gaining the voluntary cooperation of the employees affected. Without fair process, even outcomes that employees might favor can be difficult to achieve—as the experience of an elevator manufacturer we'll call Elco illustrates.

Good Outcome, Unfair Process

In the late 1980s, sales in the elevator industry headed south as overconstruction of office space left some large U.S. cities with vacancy rates as high as 20%. Faced with diminished domestic demand for its product, Elco knew it had to improve its operations. The company made the decision to replace its batch-manufacturing system with a cellular approach that would allow self-directed teams to achieve superior performance. Given the industry's collapse, top management felt the transformation had to be made in record time.

Lacking expertise in cellular manufacturing, Elco retained a consulting firm to design a master plan for the conversion. Elco asked the consultants to work quickly and with minimal disturbance to employees. The new manufacturing system would be installed first at Elco's Chester plant, where employee relations were so good that in 1983 workers had decertified their own union. Subsequently, Elco would roll the process out to its High Park plant, where a strong union would probably resist that, or any other, change.

Idea in Brief

In just months, a model workforce degenerated into a cauldron of mistrust, resistance, and plummeting performance. Why? Management launched a major change effort without inviting employees' input, without explaining the reasons for the change, and without clarifying new performance expectations.

In other words, the company ignored **fair process**—a decision-making approach that addresses our basic human need to be valued and respected. When people feel a decision affecting them was made fairly, they trust and cooperate with managers. They share ideas and willingly go beyond the call of duty. Corporate performance soars.

In knowledge-based organizations—whose lifeblood consists of employees' trust, commitment, and ideas—fair process is essential. It enables companies to channel people's energy and creativity toward organizational goals.

The benefits of fair process may seem obvious—yet most organizations don't practice it. Why? Some managers find it threatening, assuming it will diminish their power. They keep employees at arm's length to avoid challenges to their authority. Others believe employees are concerned only with what's best for themselves. But evidence shows that most people will accept outcomes not wholly in their favor—if they believe the process for arriving at those outcomes was fair.

Under the leadership of a much beloved plant manager, Chester was in all respects a model operation. Visiting customers were always impressed by the knowledge and enthusiasm of Chester's employees, so much so that the vice president of marketing saw the plant as one of Elco's best marketing tools. "Just let customers talk with Chester employees," he observed, "and they walk away convinced that buying an Elco elevator is the smart choice."

But one day in January of 1991, Chester's employees arrived at work to discover strangers at the plant. Who were these people wearing dark suits,

white dress shirts, and ties? They weren't customers. They showed up daily and spoke in low tones to one another. They didn't interact with employees. They hovered behind people's backs, taking notes and drawing fancy diagrams. The rumor circulated that after employees went home in the afternoon, these people would swarm across the plant floor, snoop around people's workstations, and have heated discussions.

Idea in Practice

Fair process isn't decision by consensus or democracy in the workplace. Its goal is to pursue the best ideas, not create harmony. Fair process consists of three principles:

- ***Engagement***—involving individuals in decisions by inviting their input and encouraging them to challenge one another's ideas. Engagement communicates management's respect for individuals and their ideas and builds collective wisdom. It generates better decisions and greater commitment from those involved in executing those decisions.
- ***Explanation***—clarifying the thinking behind a final decision. Explanation reassures people that managers have considered their opinions and made the decision with the company's overall interests at heart. Employees trust managers' intentions—even if their own ideas were rejected.
- ***Expectation clarity***—stating the new rules of the game, including performance standards, penalties for failure, and new responsibilities. By minimizing political jockeying and favoritism, expectation clarity enables employees to focus on the job at hand.

Example: Facing decreasing demand, an elevator manufacturer we'll call Elco decided to design a more efficient manufacturing system. It would introduce the system at its Chester plant, a model operation with such positive employee relations that it decertified its own union. Then it would incorporate the new system at High Park, a strongly unionized plant highly resistant to change.

Seeking minimal workforce disturbance, managers didn't involve the Chester employees in the system design process, explain why change was necessary, or clarify new performance expectations. Soon rumors about layoffs proliferated, trust and commitment deteriorated, and fights erupted on the shop floor. Quality sank.

Rattled but wiser, Elco took a different tack at their High Park site. Managers held ongoing plantwide meetings to explain the need for the new system, encouraged employees to help design the new process, and laid out new expectations. The anticipated resistance never came—and trusting employees embraced the new system.

During this period, the plant manager was increasingly absent. He was spending more time at Elco's head office in meetings with the consultants—sessions deliberately scheduled away from the plant so as not to distract the employees. But the plant manager's absence produced the opposite effect. As people grew anxious, wondering why the captain of their ship seemed to be deserting them, the rumor mill moved into high gear. Everyone became convinced that the consultants would downsize the plant. They were sure they were about to lose their jobs. The fact that the plant manager was always gone—obviously, he was avoiding them—and that no explanation was given, could only mean that management was, they thought, “trying to pull one over on us.” Trust and commitment at the Chester plant quickly deteriorated. Soon, people were bringing in newspaper clippings about other plants around the country that had been shut down with the help of consultants. Employees saw themselves as imminent victims of yet another management fad and resented it.

In fact, Elco managers had no intention of closing the plant. They wanted to cut out waste, freeing people to enhance quality and produce elevators for new international markets. But plant employees could not have known that.

The master plan

In March 1991, management gathered the Chester employees in a large room. Three months after the consultants had first appeared, they were formally introduced. At the same time, management unveiled to employees the master plan for change at the Chester plant. In a meeting that lasted only 30 minutes, employees heard how their time-honored way of working would be abolished and replaced by something called “cellular manufacturing.” No one explained why the change was needed, nor did anyone say exactly what would be expected of employees under the new approach. The managers didn’t mean to skirt the issues; they just didn’t feel they had the time to go into details.

The employees sat in stunned silence, which the managers mistook for acceptance, forgetting how many months it had taken them as leaders to get comfortable with the idea of cellular manufacturing and the changes it entailed. The managers felt good when the meeting was over, believing the employees were on board. With such a terrific staff, they thought, implementation of the new system was bound to go well.

Master plan in hand, management quickly began rearranging the plant. When employees asked what the new layout aimed to achieve, the response was “efficiency gains.” The managers didn’t have time to explain why efficiency needed to be improved and didn’t want to worry employees. But lacking an intellectual understanding of what was happening to them, some employees literally began feeling sick when they came to work.

Managers informed employees that they would no longer be judged on individual performance but rather on the performance of the cell. They said quicker or more experienced employees would have to pick up the slack for slower or less experienced colleagues. But they didn’t elaborate. How the new system was supposed to work, management didn’t make clear.

In fact, the new cell design offered tremendous benefits to employees, making vacations easier to schedule, for example, and giving them the opportunity to broaden their skills and engage in a greater variety of work. But lacking trust in the change process, employees could see only its negative side. They began taking out their fears and anger on one another. Fights

erupted on the plant floor as employees refused to help those they called “lazy people who can’t finish their own jobs” or interpreted offers of help as meddling, responding with, “This is my job. You keep to your own workstation.”

Chester’s model workforce was falling apart. For the first time in the plant manager’s career, employees refused to do as they were asked, turning down assignments “even if you fire me.” They felt they could no longer trust the once popular plant manager, so they began to go around him, taking their complaints directly to his boss at the head office.

The plant manager then announced that the new cell design would allow employees to act as self-directed teams and that the role of the supervisor would be abolished. He expected people to react with excitement to his vision of Chester as the epitome of the factory of the future, where employees are empowered as entrepreneurial agents. Instead, they were simply confused. They had no idea how to succeed in this new environment. Without supervisors, what would they do if stock ran short or machines broke down? Did empowerment mean that the teams could self-authorize overtime, address quality problems such as rework, or purchase new machine tools? Unclear about how to succeed, employees felt set up to fail.

Time out

By the summer of 1991, both cost and quality performance were in a free fall. Employees were talking about bringing the union back. Finally, in despair, the plant manager phoned Elco's industrial psychologist. "I need your help," he said. "I have lost control."

The psychologist conducted an employee opinion survey to learn what had gone wrong. Employees complained, "Management doesn't care about our ideas or our input." They felt that the company had scant respect for them as individuals, treating them as if they were not worthy of knowing about business conditions: "They don't bother to tell us where we are going and what this means to us." And they were deeply confused and mistrustful: "We don't know exactly what management expects of us in this new cell."

What Is Fair Process?

The theme of justice has preoccupied writers and philosophers throughout the ages, but the systematic study of fair process emerged only in the mid-1970s, when two social scientists, John W. Thibaut and Laurens Walker, combined their interest in the psychology of justice with the study of process. Focusing their attention on legal settings, they sought to understand what makes people trust a legal system so that they will comply with laws without being coerced into doing so. Their research established that people care as much about the fairness of the process through which an outcome is produced as they do about the outcome itself. Subsequent researchers such as Tom R. Tyler and E. Allan Lind demonstrated the power of fair process across diverse cultures and social settings.

Making Sense of Irrational Behavior at VW and Siemens-Nixdorf

Economic theories do a good job of explaining the rational side of human behavior, but they fall short in explaining why people can act negatively in the face of positive outcomes. Fair process offers managers a theory of behavior that explains—or might help predict—what would otherwise appear to be bewilderingly noneconomic, or irrational, behavior.

Consider what happened to Volkswagen. In 1992, the German carmaker was in the midst of expanding its manufacturing facility in Puebla, Mexico, its only production site in North America. The appreciation of the deutsche mark against the U.S. dollar was pricing Volkswagen out of the U.S. market. But after the North American Free Trade Agreement (NAFTA) became law in 1992, Volkswagen's cost-efficient Mexican facility was well positioned to reconquer the large North American market.

In the summer of 1992, a new labor agreement had to be hammered out. The accord VW signed with the union's secretary-general included a generous 20% pay raise for employees. VW thought the workers would be pleased.

But the union's leaders had not involved the employees in discussions about the contract's terms; they did a poor job of communicating what the new agreement would mean to employees and why a number of work-rule changes were necessary. Workers did not understand the basis for the decisions their leaders had taken. They felt betrayed.

VW's management was completely caught off guard when, on July 21, the employees started a massive walkout that cost the company as much as an estimated \$10 million per day. On August 21, about 300 protesters were attacked by police dogs. The government was forced to step in to end the violence. Volkswagen's plans for the U.S. market were in disarray, and its performance was devastated.

In contrast, consider the turnaround of Siemens-Nixdorf Informationssysteme (SNI), the largest European supplier of information technology. Created in 1990 when Siemens acquired the troubled Nixdorf Computer Company, SNI had cut head count from 52,000 to 35,000 by 1994. Anxiety and fear were rampant at the company.

In 1994, Gerhard Schulmeyer, the newly appointed CEO, went out to talk to as many employees as he could. In a series of meetings large and small with a total of more than 11,000 people, Schulmeyer shared his crusading mission to engage everyone in turning the company around. He began by painting a bleakly honest picture of SNI's situation: The company was losing money despite recent efforts to slash costs. Deeper cuts were needed, and every business would have to demonstrate its viability or be eliminated. Schulmeyer set clear but tough rules about how decisions would be made. He then asked for volunteers to come up with ideas.

Within three months, the initial group of 30 volunteers grew to encompass an additional 75 SNI executives and 300 employees. These 405 change agents soon turned into 1,000, then 3,000, then 9,000, as they progressively recruited others to help save the company. Throughout the process, ideas were solicited from managers and employees alike concerning decisions that affected them, and they all understood how decisions would be made. Ideas would be auctioned off to executives willing to champion and finance them. If no executive bought a proposal on its merits, the idea would not be pursued. Although 20% to 30% of their proposals were rejected, employees thought the process was fair.

People voluntarily pitched in—mostly after business hours, often until midnight. In just over two years, SNI has achieved a transformation notable in European corporate history. Despite accumulated losses of DM 2 billion, by 1995 SNI was already operating in the black. In the same period, employee satisfaction almost doubled, despite the radical and difficult changes under way.

Why did employees of Volkswagen revolt, despite their upbeat economic circumstances? How, in the face of such demoralizing economic conditions, could SNI turn around its performance? What is at issue is not *what* the two companies did but *how* they did it. The cases illustrate the tremendous power

of fair process—fairness in the process of making and executing decisions. Fair process profoundly influences attitudes and behavior critical to high performance.

We discovered the managerial relevance of fair process more than a decade ago, during a study of strategic decision making in multinational corporations. Many top executives in those corporations were frustrated—and baffled—by the way the senior managers of their local subsidiaries behaved. Why did those managers so often fail to share information and ideas with the executives? Why did they sabotage the execution of plans they had agreed to carry out? In the 19 companies we studied, we found a direct link between processes, attitudes, and behavior. Managers who believed the company's processes were fair displayed a high level of trust and commitment, which, in turn, engendered active cooperation. Conversely, when managers felt fair process was absent, they hoarded ideas and dragged their feet.

In subsequent field research, we explored the relevance of fair process in other business contexts—for example, in companies in the midst of transformations, in teams engaged in product innovation, and in company-supplier partnerships. (See the sidebar “Making Sense of Irrational Behavior at VW and Siemens-Nixdorf.”) For companies seeking to harness the energy and creativity of committed managers and employees, the central idea that emerges from our fair-process research is this: Individuals are most likely to trust and cooperate freely with systems—whether they themselves win or lose by those systems—when fair process is observed.

Fair process responds to a basic human need. All of us, whatever our role in a company, want to be valued as human beings and not as “personnel” or “human assets.” We want others to respect our intelligence. We want our ideas to be taken seriously. And we want to understand the rationale behind specific decisions. People are sensitive to the signals conveyed through a company's decision-making processes. Such processes can reveal a company's willingness to trust people and seek their ideas—or they can signal the opposite.

The three principles

In all the diverse management contexts we have studied, we have asked people to identify the bedrock elements of fair process. And whether we were working with senior executives or shop floor employees, the same three mutually reinforcing principles consistently emerged: engagement, explanation, and expectation clarity.

Engagement means involving individuals in the decisions that affect them by asking for their input and allowing them to refute the merits of one another's ideas and assumptions. Engagement communicates management's respect for individuals and their ideas. Encouraging refutation sharpens everyone's thinking and builds collective wisdom. Engagement results in better decisions by management and greater commitment from all involved in executing those decisions.

Explanation means that everyone involved and affected should understand why final decisions are made as they are. An explanation of the thinking that underlies decisions makes people confident that managers have considered their opinions and have made those decisions impartially in the overall interests of the company. An explanation allows employees to trust managers' intentions even if their own ideas have been rejected. It also serves as a powerful feedback loop that enhances learning.

Expectation clarity requires that once a decision is made, managers state clearly the new rules of the game. Although the expectations may be demanding, employees should know up front by what standards they will be judged and the penalties for failure. What are the new targets and milestones? Who is responsible for what? To achieve fair process, it matters less what the new rules and policies are and more that they are clearly understood. When people clearly understand what is expected of them, political jockeying and favoritism are minimized, and they can focus on the job at hand.

Notice that fair process is not decision by consensus. Fair process does not set out to achieve harmony or to win people's support through compromises that accommodate every individual's opinions, needs, or interests. While fair process gives every idea a chance, the merit of the ideas—and not consensus

—is what drives the decision making.

Nor is fair process the same as democracy in the workplace. Achieving fair process does not mean that managers forfeit their prerogative to make decisions and establish policies and procedures. Fair process pursues the best ideas whether they are put forth by one or many.

“We really screwed up”

Elco managers violated all three basic principles of fair process at the Chester plant. They failed to engage employees in decisions that directly affected them. They didn't explain why decisions were being made the way they were and what those decisions meant to employees' careers and work methods. And they neglected to make clear what would be expected of employees under cellular manufacturing. In the absence of fair process, the employees at Chester rejected the transformation.

A week after the psychologist's survey was completed, management invited employees to meetings in groups of 20. Employees surmised that management was either going to pretend that the survey had never happened or accuse employees of disloyalty for having voiced their complaints. But to their amazement, managers kicked off the meeting by presenting the undiluted survey results and declaring, “We were wrong. We really screwed up. In our haste and ignorance, we did not go through the proper process.” Employees couldn't believe their ears. There were whispers in the back of the room, “What the devil did they say?” At more than 20 meetings over the next few weeks, managers repeated their confession. “No one was prepared to believe us at first,” one manager said. “We had screwed up too badly.”

At subsequent meetings, management shared with employees the company's dismal business forecast and the limited options available. Without cost reduction, Elco would have to raise its prices, and higher prices would further depress sales. That would mean cutting production even more, perhaps even moving manufacturing offshore. Heads nodded. Employees saw the bind the company was in. The business problem was becoming theirs, not just management's.

But still there were concerns: “If we help to cut costs and learn to produce elevators that are twice as good in half the time, will we work ourselves out of a job?” In response, the managers described their strategy to increase sales outside the United States. They also announced a new policy called *proaction time*: No one would be laid off because of any improvements made by an employee. Instead, employees could use their newly free time to attend cross-

training programs designed to give them the skills they would need to work in any area of operations. Or employees could act as consultants addressing quality issues. In addition, management agreed not to replace any departing employees with new hires until business conditions improved. At the same time, however, management made it clear that it retained the right to let people go if business conditions grew worse.

Employees may not have liked what they heard, but they understood it. They began to see that they shared responsibility with management for Elco's success. If they could improve quality and productivity, Elco could bring more value to the market and prevent further sales erosion. To give employees confidence that they were not being misled, management pledged to regularly share data on sales, costs, and market trends—a first step toward rebuilding trust and commitment.

Elco's managers could not undo past mistakes, but they could involve employees in making future decisions. Managers asked employees why they thought the new manufacturing cells weren't working and how to fix them. Employees suggested making changes in the location of materials, in the placement of machines, and in the way tasks were performed. They began to share their knowledge; as they did so, the cells were redesigned and performance steadily improved, often far exceeding the expectations originally set by the consultants. As trust and commitment were restored, talk of bringing the union back died out.

High Park's turn

Meanwhile, management worried about introducing the new work methods at Elco's High Park plant, which, unlike the Chester plant, had a history of resisting change. The union was strong at High Park, and some employees there had as much as 25 years' service. Moreover, the plant manager, a young engineer new to High Park, had never run a plant before. The odds seemed to be against him. If change had created animosity at Chester, one could only imagine how much worse the situation could become at High Park.

But management's fears went unrealized. When the consultants came to the plant, the young manager introduced them to all employees. At a series of plantwide meetings, corporate executives openly discussed business conditions and the company's declining sales and profits. They explained that they had visited other companies' plants and had seen the productivity improvements that cellular manufacturing could bring. They announced the proaction-time policy to calm employees' justifiable fears of layoffs. At the High Park plant, managers encouraged employees to help the consultants design the new manufacturing cells, and they encouraged active debate. Then, as the old performance measures were discarded, managers worked with employees to develop new ones and to establish the cell teams' new responsibilities.

Every day, the High Park plant manager waited for the anticipated meltdown, but it never came. Of course, there were some gripes, but even when people didn't like the decisions, they felt they had been treated fairly and, so, willingly participated in the plant's eventual performance turnaround.

Three years later, we revisited a popular local eatery to talk with people from both plants. Employees from both Chester and High Park now believe that the cellular approach is a better way to work. High Park employees spoke about their plant manager with admiration, and they commiserated with the difficulties Elco's managers had in making the changeover to cellular manufacturing. They concluded that it had been a necessary, worthwhile, and positive experience. But Chester employees spoke with

anger and indignation as they described their treatment by Elco's managers. (See "The Price of Unfairness.") For them, as for the London woman who had been unfairly ticketed, fair process was as important as—if not more important than—the outcome.

Fair Process in the Knowledge Economy

Fair process may sound like a soft issue, but understanding its value is crucial for managers trying to adapt their companies to the demands of the knowledge-based economy. Unlike the traditional factors of production—land, labor, and capital—knowledge is a resource locked in the human mind. Creating and sharing knowledge are intangible activities that can neither be supervised nor forced out of people. They happen only when people cooperate voluntarily. As the Nobel laureate economist Friedrich Hayek has argued, “Practically every individual...possesses unique information” that can be put to use only with “his active cooperation.” Getting that cooperation may well turn out to be one of the key managerial issues of the next few decades. (See “Fair Process Is Critical in Knowledge Work.”)

Voluntary cooperation was not what Frederick Winslow Taylor had in mind when at the turn of the century he began to develop an arsenal of tools to promote efficiency and consistency by controlling individuals’ behavior and compelling employees to comply with management dictates. Traditional management science, which is rooted in Taylor’s time-and-motion studies, encouraged a managerial preoccupation with allocating resources, creating economic incentives and rewards, monitoring and measuring performance, and manipulating organizational structures to set lines of authority. These conventional management levers still have their role to play, but they have little to do with encouraging active cooperation. Instead, they operate in the realm of outcome fairness or what social scientists call *distributive justice*, where the psychology works like this: When people get the compensation (or the resources, or the place in the organizational hierarchy) they deserve, they feel satisfied with that outcome. They will reciprocate by fulfilling to the letter their obligation to the company. The psychology of fair process, or *procedural justice*, is quite different. Fair process builds trust and commitment, trust and commitment produce voluntary cooperation, and voluntary cooperation drives performance, leading people to go beyond the call of duty by sharing their knowledge and applying their creativity. In all

the management contexts we've studied, whatever the task, we have consistently observed this dynamic at work. (See the exhibit "Two complementary paths to performance.")

The Price of Unfairness

Historically, policies designed to establish fair process in organizations arise mainly in reaction to employees' complaints and uprisings. But by then it is too late. When individuals have been so angered by the violation of fair process that they have been driven to organized protest, their demands often stretch well beyond the reasonable to a desire for what theorists call *retributive justice*: Not only do they want fair process restored, they also seek to visit punishment and vengeance upon those who have violated it in compensation for the disrespect the unfair process signals.

Lacking trust in management, employees push for policies that are laboriously detailed, inflexible, and often administratively constricting. They want to ensure that managers will never have the discretion to act unjustly again. In their indignation, they may try to roll back decisions imposed unfairly even when the decisions themselves were good ones—even when they were critical to the company's competitiveness or beneficial to the workers themselves. Such is the emotional power that unfair process can provoke.

Managers who view fair process as a nuisance or as a limit on their freedom to manage must understand that it is the violation of fair process that will wreak the most serious damage on corporate performance. Retribution can be very expensive.

Consider the transformation of Bethlehem Steel Corporation's Sparrows Point, Maryland, division, a business unit responsible for marketing, sales, production, and financial performance. Until 1993, the 106-year-old division was managed in the classic command-and-control style. People were expected to do what they were told to do—no more and no less—and management and employees saw themselves as adversaries.

That year, Bethlehem Steel introduced a management model so different at Sparrows Point that Taylor—who was, in fact, the company's consulting

engineer about 100 years ago—wouldn't have recognized it. The new model was designed to invoke in employees an active sense of responsibility for sharing their knowledge and ideas with one another and with management. It was also meant to encourage them to take the initiative for getting things done. In the words of Joe Rosel, the president of one of the division's five unions, "It's all about involvement, justification for decisions, and a clear set of expectations."

At Sparrows Point, employees are involved in making and executing decisions at three levels. At the top is a joint-leadership team, composed of senior managers and five employee representatives, that deals with companywide issues when they arise. At the department level are area teams, consisting of managers like superintendents and of employees from the different areas of the plant, such as zone committee people. Those teams deal with day-to-day operational issues such as customer service, quality, and logistics. Ad hoc problem-solving teams of employees address opportunities and obstacles as they arise on the shop floor. At each level, teammates share and debate their ideas. Thus, employees are assured a fair hearing for their points of view on decisions likely to affect them. With the exception of decisions involving major changes or resource commitments, the teams make and execute the decisions themselves.

Sparrows Point uses numerous processes and devices to ensure that all employees can understand why decisions have been made and how such decisions need to be executed. There is, for example, a bulletin board where decisions are posted and explained, allowing employees who haven't been directly involved in those decisions to understand what's going on and why. In addition, in more than 70 four-hour seminars, groups ranging in size from 50 to 250 employees have met to discuss changes occurring at the division, learn about new ideas under consideration, and find out how changes might affect employees' roles and responsibilities. A quarterly newsletter and a monthly "report card" of the division's strategic, marketing, operational, and financial performance keeps each of the unit's 5,300 employees informed. And the teams report back to their colleagues about the changes they are making, seeking help in making the ideas work.

Fair Process Is Critical in Knowledge Work

It is easy to see fair process at work on the plant floor, where its violation can produce such highly visible manifestations as strikes, slowdowns, and high defect rates. But fair process can have an even greater impact on the quality of professional and managerial work. That is because innovation is the key challenge of the knowledge-based economy, and innovation requires the exchange of ideas, which in turn depends on trust.

Executives and professionals rarely walk the picket line, but when their trust has not been won, they frequently withhold their full cooperation—and their ideas. In knowledge work, then, ignoring fair process creates high opportunity costs in the form of ideas that never see daylight and initiatives that are never seized. For example:

A multifunctional team is created to develop an important new product. Because it contains representatives from every major functional area of the company, the team *should* produce more innovative products, with less internal fighting, shortened lead times, and lower costs. The team meets, but people drag their feet. Executives at a computer maker developing a new workstation, for example, thoughtfully deploy the traditional management levers. They hammer out a good incentive scheme. They define the project scope and structure. And they allocate the right resources. Yet the trust, idea sharing, and commitment that everyone wants never materialize. Why? Early in the project, manufacturing and marketing representatives on the team propose building a prototype, but the strong design-engineering group driving the project ignores them. Subsequently, problems surface because the design is difficult to manufacture and the application software is inadequate. The team members from manufacturing and marketing are aware of these issues all along but remain passive in sharing their concerns with the powerful design engineers. Instead, they wait until the problems reveal themselves—at which time they are very expensive to fix.

Two companies create a joint venture that offers clear benefits to both

parties. But they then hold their cards so close to their chests that they ensure the alliance will create limited value for either partner. The Chinese joint-venture partner of a European engineering group, for example, withholds critical information from the field, failing to report that customers are having problems installing the partner's products and sitting on requests for new product features. Why do the Chinese fail to cooperate fully, even if it means hurting their own business?

Early in the partnership, the Chinese felt they had been shut out of key product and operating decisions. To make matters worse, the Europeans never explained the logic guiding their decisions. As the Chinese withhold critical information, the increasingly frustrated European partner responds in kind by slowing the transfer of managerial know-how, which the Chinese need badly.

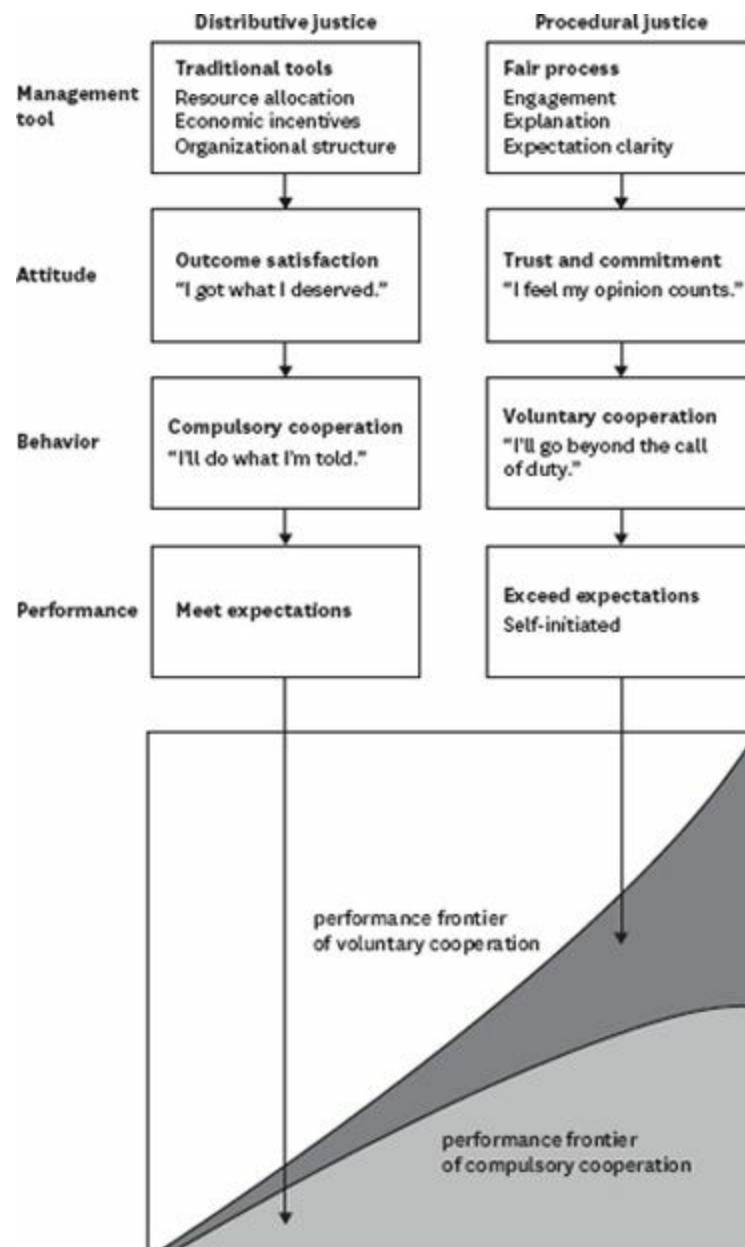
Two companies create a supplier partnership to achieve improved value at lower cost. They agree to act in a seamless fashion, as one company. But the supplier seems to spend more energy on developing other customers than on deepening the partnership. One consumer goods manufacturer, for example, keeps delaying the installation of a joint electronic consumer-response data system with a major food retailer. The system will substantially improve inventory management for both partners. But the supplier remains too wary to invest. Why? The retailer has a history of dropping some of the supplier's products without explanation. And the consumer company can't understand the retailer's ambiguous criteria for designating "preferred suppliers."

Fair process has produced significant changes in people's attitudes and behavior. Consider, for example, the tin mill unit at Sparrows Point. In 1992, the unit's performance was among the worst in the industry. But then, as one employee explains, "People started coming forward and sharing their ideas. They started caring about doing great work, not just getting by. Take the success we've had in light-gauge cable sheathing. We had let this high value-added product slip because the long throughput time required for production held up the other mills in the unit. But after we started getting everyone involved and explained why we needed to improve throughput, ideas started to flow. At first, the company was doubtful: If the product had created a

bottleneck before, why should it be different now? But people came up with the idea of using two sequential mills instead of one to eliminate the bottleneck. Did people suddenly get smarter? No. I'd say they started to care."

The object in creating this new way of working at Sparrows Point was to improve the intellectual buy-in and emotional commitment of employees. It has apparently been successful. Since 1993, Sparrows Point has turned a profit three years in a row, the first time that has happened since the late 1970s. The division is becoming a showcase demonstrating how a declining industry can be revitalized in today's knowledge economy. In the words of one Sparrows Point employee, "Since we know now everything that's going on in the company, we have more trust in management and are more committed to making things happen. People have started doing things beyond the normal call of duty."

Two complementary paths to performance



Overcoming Mental Barriers

If fair process is such a simple idea and yet so powerful, why do so few companies practice it? Most people think of themselves as fair, and managers are no exception. But if you ask them what it means to be a fair manager, most will describe how they give people the authority they deserve, or the resources they need, or the rewards they have earned. In other words, they will confuse fair process with fair outcomes. The few managers who focus on process might identify only one of the three fair-process principles (the most widely understood is engagement), and they would stop there.

But there are two more fundamental reasons, beyond this simple lack of understanding, that explain why fair process is so rare. The first involves power. Some managers continue to believe that knowledge is power and that they retain power only by keeping what they know to themselves. Their implicit strategy is to preserve their managerial discretion by deliberately leaving the rules for success and failure vague. Other managers maintain control by keeping employees at arm's length, substituting memos and forms for direct, two-way communication, thus avoiding challenges to their ideas or authority. Such styles can reflect deeply ingrained patterns of behavior, and rarely are managers conscious of how they exercise power. For them, fair process would represent a threat.

The second reason is also largely unconscious because it resides in an economic assumption that most of us have grown up taking at face value: the belief that people are concerned only with what's best for themselves. But, as we have seen, there is ample evidence to show that when the process is perceived to be fair, most people will accept outcomes that are not wholly in their favor. People realize that compromises and sacrifices are necessary on the job. They accept the need for short-term personal sacrifices in order to advance the long-term interests of the corporation. Acceptance is conditional, however, hinged as it is on fair process.

Fair process reaches into a dimension of human psychology that hasn't been fully explored in conventional management practice. Yet every

company can tap into the voluntary cooperation of its people by building trust through fair processes.

Originally published in July 1997. Reprint R0301K.

Teaching Smart People How to Learn

by Chris Argyris

ANY COMPANY THAT ASPIRES to succeed in the tougher business environment of the 1990s must first resolve a basic dilemma: success in the marketplace increasingly depends on learning, yet most people don't know how to learn. What's more, those members of the organization that many assume to be the best at learning are, in fact, not very good at it. I am talking about the well-educated, high-powered, high-commitment professionals who occupy key leadership positions in the modern corporation.

Most companies not only have tremendous difficulty addressing this learning dilemma; they aren't even aware that it exists. The reason: they misunderstand what learning is and how to bring it about. As a result, they tend to make two mistakes in their efforts to become a learning organization.

First, most people define learning too narrowly as mere "problem solving," so they focus on identifying and correcting errors in the external environment. Solving problems is important. But if learning is to persist, managers and employees must also look inward. They need to reflect critically on their own behavior, identify the ways they often inadvertently contribute to the organization's problems, and then change how they act. In particular, they must learn how the very way they go about defining and solving problems can be a source of problems in its own right.

I have coined the terms "single loop" and "double loop" learning to capture this crucial distinction. To give a simple analogy: a thermostat that automatically turns on the heat whenever the temperature in a room drops below 68 degrees is a good example of single-loop learning. A thermostat

that could ask, “Why am I set at 68 degrees?” and then explore whether or not some other temperature might more economically achieve the goal of heating the room would be engaging in double-loop learning.

Highly skilled professionals are frequently very good at single-loop learning. After all, they have spent much of their lives acquiring academic credentials, mastering one or a number of intellectual disciplines, and applying those disciplines to solve real-world problems. But ironically, this very fact helps explain why professionals are often so bad at double-loop learning.

Put simply, because many professionals are almost always successful at what they do, they rarely experience failure. And because they have rarely failed, they have never learned how to learn from failure. So whenever their single-loop learning strategies go wrong, they become defensive, screen out criticism, and put the “blame” on anyone and everyone but themselves. In short, their ability to learn shuts down precisely at the moment they need it the most.

The propensity among professionals to behave defensively helps shed light on the second mistake that companies make about learning. The common assumption is that getting people to learn is largely a matter of motivation. When people have the right attitudes and commitment, learning automatically follows. So companies focus on creating new organizational structures—compensation programs, performance reviews, corporate cultures, and the like—that are designed to create motivated and committed employees.

But effective double-loop learning is not simply a function of how people feel. It is a reflection of how they think—that is, the cognitive rules or reasoning they use to design and implement their actions. Think of these rules as a kind of “master program” stored in the brain, governing all behavior. Defensive reasoning can block learning even when the individual commitment to it is high, just as a computer program with hidden bugs can produce results exactly the opposite of what its designers had planned.

Idea in Brief

Problem solving is an example of **single-loop learning**. You identify an error and apply a particular remedy to correct it. But genuine learning involves an extra step, in which you reflect on your assumptions and test the validity of your hypotheses. Achieving this **double-loop learning** is more than a matter of motivation—you have to reflect on the way you think.

Failure forces you to reflect on your assumptions and inferences. Which is why an organization's smartest and most successful employees are often such poor learners: they haven't had the opportunity for introspection that failure affords. So when they do fail—or merely underperform—they can be surprisingly defensive. Instead of critically examining their own behavior, they cast blame outward—on anyone or anything they can.

Companies can learn how to resolve the learning dilemma. What it takes is to make the ways managers and employees reason about their behavior a focus of organizational learning and continuous improvement programs. Teaching people how to reason about their behavior in new and more effective ways breaks down the defenses that block learning.

All of the examples that follow involve a particular kind of professional: fast-track consultants at major management consulting companies. But the implications of my argument go far beyond this specific occupational group. The fact is, more and more jobs—no matter what the title—are taking on the contours of “knowledge work.” People at all levels of the organization must combine the mastery of some highly specialized technical expertise with the ability to work effectively in teams, form productive relationships with clients and customers, and critically reflect on and then change their own organizational practices. And the nuts and bolts of management—whether of high-powered consultants or service representatives, senior managers or factory technicians—increasingly consists of guiding and integrating the autonomous but interconnected work of highly skilled people.

Idea in Practice

People often profess to be open to critique and new learning, but their actions suggest a very different set of governing values or theories-in-use:

- the desire to remain in unilateral control
- the goal of maximizing “winning” while minimizing “losing”
- the belief that negative feelings should be suppressed
- the desire to appear as rational as possible.

Taken together, these values betray a profoundly defensive posture: a need to avoid embarrassment, threat, or feelings of vulnerability and incompetence. This **closed-loop reasoning** explains why the mere encouragement of open inquiry can be intimidating to some. And it’s especially relevant to the behavior of many of the most highly skilled and best-trained employees. Behind their high aspirations are an equally high fear of failure and a tendency to be ashamed when they don’t live up to their high standards. Consequently, they become brittle and despondent in situations in which they don’t excel immediately.

Fortunately, it *is* possible for individuals and organizations to develop more productive patterns of behavior. Two suggestions for how to make this happen:

1. **Apply the same kind of “tough reasoning” you use to conduct**

strategic analysis. Collect the most objective data you can find. Make your inferences explicit and test them constantly. Submit your conclusions to the toughest tests of all: make sure they aren't self-serving or impossible for others to verify.

2. **Senior managers must model the desired changes first.** When the leadership demonstrates its willingness to examine critically its own theories-in-use, changing them as indicated, everyone will find it easier to do the same.

Example: The CEO of an organizational-development firm created a case study to address real problems caused by the intense competition among his direct reports. In a paragraph, he described a meeting he intended to have with his subordinates. Then he wrote down what he planned to say, how he thought his subordinates would respond, as well any thoughts or feelings he thought he might have but not express for fear of derailing the conversation. Instead of actually holding the meeting, he analyzed the scenario he had developed *with* his direct reports. The result was an illuminating conversation in which the CEO and his subordinates were able to circumvent the closed-loop reasoning that had characterized so many prior discussions.

How Professionals Avoid Learning

For 15 years, I have been conducting in-depth studies of management consultants. I decided to study consultants for a few simple reasons. First, they are the epitome of the highly educated professionals who play an increasingly central role in all organizations. Almost all of the consultants I've studied have MBAs from the top three or four U.S. business schools. They are also highly committed to their work. For instance, at one company, more than 90% of the consultants responded in a survey that they were "highly satisfied" with their jobs and with the company.

I also assumed that such professional consultants would be good at learning. After all, the essence of their job is to teach others how to do things differently. I found, however, that these consultants embodied the learning dilemma. The most enthusiastic about continuous improvement in their own organizations, they were also often the biggest obstacle to its complete success.

As long as efforts at learning and change focused on external organizational factors—job redesign, compensation programs, performance reviews, and leadership training—the professionals were enthusiastic participants. Indeed, creating new systems and structures was precisely the kind of challenge that well-educated, highly motivated professionals thrived on.

And yet the moment the quest for continuous improvement turned to the professionals' *own* performance, something went wrong. It wasn't a matter of bad attitude. The professionals' commitment to excellence was genuine, and the vision of the company was clear. Nevertheless, continuous improvement did not persist. And the longer the continuous improvement efforts continued, the greater the likelihood that they would produce ever-diminishing returns.

What happened? The professionals began to feel embarrassed. They were threatened by the prospect of critically examining their own role in the organization. Indeed, because they were so well paid (and generally believed that their employers were supportive and fair), the idea that their performance

might not be at its best made them feel guilty.

Far from being a catalyst for real change, such feelings caused most to react defensively. They projected the blame for any problems away from themselves and onto what they said were unclear goals, insensitive and unfair leaders, and stupid clients.

Consider this example. At a premier management consulting company, the manager of a case team called a meeting to examine the team's performance on a recent consulting project. The client was largely satisfied and had given the team relatively high marks, but the manager believed the team had not created the value added that it was capable of and that the consulting company had promised. In the spirit of continuous improvement, he felt that the team could do better. Indeed, so did some of the team members.

The manager knew how difficult it was for people to reflect critically on their own work performance, especially in the presence of their manager, so he took a number of steps to make possible a frank and open discussion. He invited to the meeting an outside consultant whom team members knew and trusted—"just to keep me honest," he said. He also agreed to have the entire meeting tape-recorded. That way, any subsequent confusions or disagreements about what went on at the meeting could be checked against the transcript. Finally, the manager opened the meeting by emphasizing that no subject was off limits—including his own behavior.

"I realize that you may believe you cannot confront me," the manager said. "But I encourage you to challenge me. You have a responsibility to tell me where you think the leadership made mistakes, just as I have the responsibility to identify any I believe you made. And all of us must acknowledge our own mistakes. If we do not have an open dialogue, we will not learn."

The professionals took the manager up on the first half of his invitation but quietly ignored the second. When asked to pinpoint the key problems in the experience with the client, they looked entirely outside themselves. The clients were uncooperative and arrogant. "They didn't think we could help them." The team's own managers were unavailable and poorly prepared. "At times, our managers were not up to speed before they walked into the client meetings." In effect, the professionals asserted that they were helpless to act differently—not because of any limitations of their own but because of the limitations of others.

The manager listened carefully to the team members and tried to respond to their criticisms. He talked about the mistakes that he had made during the consulting process. For example, one professional objected to the way the manager had run the project meetings. “I see that the way I asked questions closed down discussions,” responded the manager. “I didn’t mean to do that, but I can see how you might have believed that I had already made up my mind.” Another team member complained that the manager had caved in to pressure from his superior to produce the project report far too quickly, considering the team’s heavy work load. “I think that it was my responsibility to have said no,” admitted the manager. “It was clear that we all had an immense amount of work.”

Finally, after some three hours of discussion about his own behavior, the manager began to ask the team members if there were any errors *they* might have made. “After all,” he said, “this client was not different from many others. How can we be more effective in the future?”

The professionals repeated that it was really the clients’ and their own managers’ fault. As one put it, “They have to be open to change and want to learn.” The more the manager tried to get the team to examine its own responsibility for the outcome, the more the professionals bypassed his concerns. The best one team member could suggest was for the case team to “promise less”—implying that there was really no way for the group to improve its performance.

The case team members were reacting defensively to protect themselves, even though their manager was not acting in ways that an outsider would consider threatening. Even if there were some truth to their charges—the clients may well have been arrogant and closed, their own managers distant—the way they presented these claims was guaranteed to stop learning. With few exceptions, the professionals made attributions about the behavior of the clients and the managers but never publicly tested their claims. For instance, they said that the clients weren’t motivated to learn but never really presented any evidence supporting that assertion. When their lack of concrete evidence was pointed out to them, they simply repeated their criticisms more vehemently.

If the professionals had felt so strongly about these issues, why had they never mentioned them during the project? According to the professionals, even this was the fault of others. “We didn’t want to alienate the client,” argued one. “We didn’t want to be seen as whining,” said another.

The professionals were using their criticisms of others to protect themselves from the potential embarrassment of having to admit that perhaps they too had contributed to the team's less-than-perfect performance. What's more, the fact that they kept repeating their defensive actions in the face of the manager's efforts to turn the group's attention to its own role shows that this defensiveness had become a reflexive routine. From the professionals' perspective, they weren't resisting; they were focusing on the "real" causes. Indeed, they were to be respected, if not congratulated, for working as well as they did under such difficult conditions.

The end result was an unproductive parallel conversation. Both the manager and the professionals were candid; they expressed their views forcefully. But they talked past each other, never finding a common language to describe what had happened with the client. The professionals kept insisting that the fault lay with others. The manager kept trying, unsuccessfully, to get the professionals to see how they contributed to the state of affairs they were criticizing. The dialogue of this parallel conversation looks like this:

Professionals: "The clients have to be open. They must want to change."

Manager: "It's our task to help them see that change is in their interest."

Professionals: "But the clients didn't agree with our analyses."

Manager: "If they didn't think our ideas were right, how might we have convinced them?"

Professionals: "Maybe we need to have more meetings with the client."

Manager: "If we aren't adequately prepared and if the clients don't think we're credible, how will more meetings help?"

Professionals: "There should be better communication between case team members and management."

Manager: "I agree. But professionals should take the initiative to educate the manager about the problems they are experiencing."

Professionals: “Our leaders are unavailable and distant.”

Manager: “How do you expect us to know that if you don’t tell us?”

Conversations such as this one dramatically illustrate the learning dilemma. The problem with the professionals’ claims is not that they are wrong but that they aren’t useful. By constantly turning the focus away from their own behavior to that of others, the professionals bring learning to a grinding halt. The manager understands the trap but does not know how to get out of it. To learn how to do that requires going deeper into the dynamics of defensive reasoning—and into the special causes that make professionals so prone to it.

Defensive Reasoning and the Doom Loop

What explains the professionals' defensiveness? Not their attitudes about change or commitment to continuous improvement; they really wanted to work more effectively. Rather, the key factor is the way they reasoned about their behavior and that of others.

It is impossible to reason anew in every situation. If we had to think through all the possible responses every time someone asked, "How are you?" the world would pass us by. Therefore, everyone develops a theory of action—a set of rules that individuals use to design and implement their own behavior as well as to understand the behavior of others. Usually, these theories of actions become so taken for granted that people don't even realize they are using them.

One of the paradoxes of human behavior, however, is that the master program people actually use is rarely the one they think they use. Ask people in an interview or questionnaire to articulate the rules they use to govern their actions, and they will give you what I call their "espoused" theory of action. But observe these same people's behavior, and you will quickly see that this espoused theory has very little to do with how they actually behave. For example, the professionals on the case team said they believed in continuous improvement, and yet they consistently acted in ways that made improvement impossible.

When you observe people's behavior and try to come up with rules that would make sense of it, you discover a very different theory of action—what I call the individual's "theory-in-use." Put simply, people consistently act inconsistently, unaware of the contradiction between their espoused theory and their theory-in-use, between the way they think they are acting and the way they really act.

What's more, most theories-in-use rest on the same set of governing values. There seems to be a universal human tendency to design one's actions consistently according to four basic values:

1. To remain in unilateral control;
2. To maximize “winning” and minimize “losing”;
3. To suppress negative feelings; and
4. To be as “rational” as possible—by which people mean defining clear objectives and evaluating their behavior in terms of whether or not they have achieved them.

The purpose of all these values is to avoid embarrassment or threat, feeling vulnerable or incompetent. In this respect, the master program that most people use is profoundly defensive. Defensive reasoning encourages individuals to keep private the premises, inferences, and conclusions that shape their behavior and to avoid testing them in a truly independent, objective fashion.

Because the attributions that go into defensive reasoning are never really tested, it is a closed loop, remarkably impervious to conflicting points of view. The inevitable response to the observation that somebody is reasoning defensively is yet more defensive reasoning. With the case team, for example, whenever anyone pointed out the professionals’ defensive behavior to them, their initial reaction was to look for the cause in somebody else—clients who were so sensitive that they would have been alienated if the consultants had criticized them or a manager so weak that he couldn’t have taken it had the consultants raised their concerns with him. In other words, the case team members once again denied their own responsibility by externalizing the problem and putting it on someone else.

In such situations, the simple act of encouraging more open inquiry is often attacked by others as “intimidating.” Those who do the attacking deal with their feelings about possibly being wrong by blaming the more open individual for arousing these feelings and upsetting them.

Needless to say, such a master program inevitably short-circuits learning. And for a number of reasons unique to their psychology, well-educated professionals are especially susceptible to this.

Nearly all the consultants I have studied have stellar academic records. Ironically, their very success at education helps explain the problems they have with learning. Before they enter the world of work, their lives are primarily full of successes, so they have rarely experienced the embarrassment and sense of threat that comes with failure. As a result, their defensive reasoning has rarely been activated. People who rarely experience failure, however, end up not knowing how to deal with it effectively. And this serves to reinforce the normal human tendency to reason defensively.

In a survey of several hundred young consultants at the organizations I have been studying, these professionals describe themselves as driven internally by an unrealistically high ideal of performance: “Pressure on the job is self-imposed.” “I must not only do a good job; I must also be the best.” “People around here are very bright and hardworking; they are highly motivated to do an outstanding job.” “Most of us want not only to succeed but also to do so at maximum speed.”

These consultants are always comparing themselves with the best around them and constantly trying to better their own performance. And yet they do not appreciate being required to compete openly with each other. They feel it is somehow inhumane. They prefer to be the individual contributor—what might be termed a “productive loner.”

Behind this high aspiration for success is an equally high fear of failure and a propensity to feel shame and guilt when they do fail to meet their high standards. “You must avoid mistakes,” said one. “I hate making them. Many of us fear failure, whether we admit it or not.”

To the extent that these consultants have experienced success in their lives, they have not had to be concerned about failure and the attendant feelings of shame and guilt. But to exactly the same extent, they also have never developed the tolerance for feelings of failure or the skills to deal with these feelings. This in turn has led them not only to fear failure but also to fear the fear of failure itself. For they know that they will not cope with it superlatively—their usual level of aspiration.

The consultants use two intriguing metaphors to describe this phenomenon. They talk about the “doom loop” and “doom zoom.” Often, consultants will perform well on the case team, but because they don’t do the jobs perfectly or receive accolades from their managers, they go into a doom loop of despair. And they don’t ease into the doom loop, they zoom into it.

As a result, many professionals have extremely “brittle” personalities.

When suddenly faced with a situation they cannot immediately handle, they tend to fall apart. They cover up their distress in front of the client. They talk about it constantly with their fellow case team members. Interestingly, these conversations commonly take the form of bad-mouthing clients.

Such brittleness leads to an inappropriately high sense of despondency or even despair when people don't achieve the high levels of performance they aspire to. Such despondency is rarely psychologically devastating, but when combined with defensive reasoning, it can result in a formidable predisposition against learning.

There is no better example of how this brittleness can disrupt an organization than performance evaluations. Because it represents the one moment when a professional must measure his or her own behavior against some formal standard, a performance evaluation is almost tailor-made to push a professional into the doom loop. Indeed, a poor evaluation can reverberate far beyond the particular individual involved to spark defensive reasoning throughout an entire organization.

At one consulting company, management established a new performance-evaluation process that was designed to make evaluations both more objective and more useful to those being evaluated. The consultants participated in the design of the new system and in general were enthusiastic because it corresponded to their espoused values of objectivity and fairness. A brief two years into the new process, however, it had become the object of dissatisfaction. The catalyst for this about-face was the first unsatisfactory rating.

Senior managers had identified six consultants whose performance they considered below standard. In keeping with the new evaluation process, they did all they could to communicate their concerns to the six and to help them improve. Managers met with each individual separately for as long and as often as the professional requested to explain the reasons behind the rating and to discuss what needed to be done to improve—but to no avail. Performance continued at the same low level and, eventually, the six were let go.

When word of the dismissal spread through the company, people responded with confusion and anxiety. After about a dozen consultants angrily complained to management, the CEO held two lengthy meetings where employees could air their concerns.

At the meetings, the professionals made a variety of claims. Some said the

performance-evaluation process was unfair because judgments were subjective and biased and the criteria for minimum performance unclear. Others suspected that the real cause for the dismissals was economic and that the performance-evaluation procedure was just a fig leaf to hide the fact that the company was in trouble. Still others argued that the evaluation process was antilearning. If the company were truly a learning organization, as it claimed, then people performing below the minimum standard should be taught how to reach it. As one professional put it: “We were told that the company did not have an up-or-out policy. Up-or-out is inconsistent with learning. You misled us.”

The CEO tried to explain the logic behind management’s decision by grounding it in the facts of the case and by asking the professionals for any evidence that might contradict these facts.

Is there subjectivity and bias in the evaluation process? Yes, responded the CEO, but “we strive hard to reduce them. We are constantly trying to improve the process. If you have any ideas, please tell us. If you know of someone treated unfairly, please bring it up. If any of you feel that you have been treated unfairly, let’s discuss it now or, if you wish, privately.”

Is the level of minimum competence too vague? “We are working to define minimum competence more clearly,” he answered. “In the case of the six, however, their performance was so poor that it wasn’t difficult to reach a decision.” Most of the six had received timely feedback about their problems. And in the two cases where people had not, the reason was that they had never taken the responsibility to seek out evaluations—and, indeed, had actively avoided them. “If you have any data to the contrary,” the CEO added, “let’s talk about it.”

Were the six asked to leave for economic reasons? No, said the CEO. “We have more work than we can do, and letting professionals go is extremely costly for us. Do any of you have any information to the contrary?”

As to the company being antilearning, in fact, the entire evaluation process was designed to encourage learning. When a professional is performing below the minimum level, the CEO explained, “we jointly design remedial experiences with the individual. Then we look for signs of improvement. In these cases, either the professionals were reluctant to take on such assignments or they repeatedly failed when they did. Again, if you have information or evidence to the contrary, I’d like to hear about it.”

The CEO concluded: “It’s regrettable, but sometimes we make mistakes

and hire the wrong people. If individuals don't produce and repeatedly prove themselves unable to improve, we don't know what else to do except dismiss them. It's just not fair to keep poorly performing individuals in the company. They earn an unfair share of the financial rewards."

Instead of responding with data of their own, the professionals simply repeated their accusations but in ways that consistently contradicted their claims. They said that a genuinely fair evaluation process would contain clear and documentable data about performance—but they were unable to provide firsthand examples of the unfairness that they implied colored the evaluation of the six dismissed employees. They argued that people shouldn't be judged by inferences unconnected to their actual performance—but they judged management in precisely this way. They insisted that management define clear, objective, and unambiguous performance standards—but they argued that any humane system would take into account that the performance of a professional cannot be precisely measured. Finally, they presented themselves as champions of learning—but they never proposed any criteria for assessing whether an individual might be unable to learn.

In short, the professionals seemed to hold management to a different level of performance than they held themselves. In their conversation at the meetings, they used many of the features of ineffective evaluation that they condemned—the absence of concrete data, for example, and the dependence on a circular logic of "heads we win, tails you lose." It is as if they were saying, "Here are the features of a fair performance-evaluation system. You should abide by them. But we don't have to when we are evaluating you."

Indeed, if we were to explain the professionals' behavior by articulating rules that would have to be in their heads in order for them to act the way they did, the rules would look something like this:

1. When criticizing the company, state your criticism in ways that you believe are valid—but also in ways that prevent others from deciding for themselves whether your claim to validity is correct.
2. When asked to illustrate your criticisms, don't include any data that others could use to decide for themselves whether the illustrations are valid.

3. State your conclusions in ways that disguise their logical implications. If others point out those implications to you, deny them.

Of course, when such rules were described to the professionals, they found them abhorrent. It was inconceivable that these rules might explain their actions. And yet in defending themselves against this observation, they almost always inadvertently confirmed the rules.

Learning How to Reason Productively

If defensive reasoning is as widespread as I believe, then focusing on an individual's attitudes or commitment is never enough to produce real change. And as the previous example illustrates, neither is creating new organizational structures or systems. The problem is that even when people are genuinely committed to improving their performance and management has changed its structures in order to encourage the "right" kind of behavior, people still remain locked in defensive reasoning. Either they remain unaware of this fact, or if they do become aware of it, they blame others.

There is, however, reason to believe that organizations can break out of this vicious circle. Despite the strength of defensive reasoning, people genuinely strive to produce what they intend. They value acting competently. Their self-esteem is intimately tied up with behaving consistently and performing effectively. Companies can use these universal human tendencies to teach people how to reason in a new way—in effect, to change the master programs in their heads and thus reshape their behavior.

People can be taught how to recognize the reasoning they use when they design and implement their actions. They can begin to identify the inconsistencies between their espoused and actual theories of action. They can face up to the fact that they unconsciously design and implement actions that they do not intend. Finally, people can learn how to identify what individuals and groups do to create organizational defenses and how these defenses contribute to an organization's problems.

Once companies embark on this learning process, they will discover that the kind of reasoning necessary to reduce and overcome organizational defenses is the same kind of "tough reasoning" that underlies the effective use of ideas in strategy, finance, marketing, manufacturing, and other management disciplines. Any sophisticated strategic analysis, for example, depends on collecting valid data, analyzing it carefully, and constantly testing the inferences drawn from the data. The toughest tests are reserved for the conclusions. Good strategists make sure that their conclusions can withstand

all kinds of critical questioning.

So too with productive reasoning about human behavior. The standard of analysis is just as high. Human resource programs no longer need to be based on “soft” reasoning but should be as analytical and as data-driven as any other management discipline.

Of course, that is not the kind of reasoning the consultants used when they encountered problems that were embarrassing or threatening. The data they collected was hardly objective. The inferences they made rarely became explicit. The conclusions they reached were largely self-serving, impossible for others to test, and as a result, “self-sealing,” impervious to change.

How can an organization begin to turn this situation around, to teach its members how to reason productively? The first step is for managers at the top to examine critically and change their own theories-in-use. Until senior managers become aware of how they reason defensively and the counterproductive consequences that result, there will be little real progress. Any change activity is likely to be just a fad.

Change has to start at the top because otherwise defensive senior managers are likely to disown any transformation in reasoning patterns coming from below. If professionals or middle managers begin to change the way they reason and act, such changes are likely to appear strange—if not actually dangerous—to those at the top. The result is an unstable situation where senior managers still believe that it is a sign of caring and sensitivity to bypass and cover up difficult issues, while their subordinates see the very same actions as defensive.

The key to any educational experience designed to teach senior managers how to reason productively is to connect the program to real business problems. The best demonstration of the usefulness of productive reasoning is for busy managers to see how it can make a direct difference in their own performance and in that of the organization. This will not happen overnight. Managers need plenty of opportunity to practice the new skills. But once they grasp the powerful impact that productive reasoning can have on actual performance, they will have a strong incentive to reason productively not just in a training session but in all their work relationships.

One simple approach I have used to get this process started is to have participants produce a kind of rudimentary case study. The subject is a real business problem that the manager either wants to deal with or has tried unsuccessfully to address in the past. Writing the actual case usually takes

less than an hour. But then the case becomes the focal point of an extended analysis.

For example, a CEO at a large organizational-development consulting company was preoccupied with the problems caused by the intense competition among the various business functions represented by his four direct reports. Not only was he tired of having the problems dumped in his lap, but he was also worried about the impact the interfunctional conflicts were having on the organization's flexibility. He had even calculated that the money being spent to iron out disagreements amounted to hundreds of thousands of dollars every year. And the more fights there were, the more defensive people became, which only increased the costs to the organization.

In a paragraph or so, the CEO described a meeting he intended to have with his direct reports to address the problem. Next, he divided the paper in half, and on the right-hand side of the page, he wrote a scenario for the meeting—much like the script for a movie or play—describing what he would say and how his subordinates would likely respond. On the left-hand side of the page, he wrote down any thoughts and feelings that he would be likely to have during the meeting but that he wouldn't express for fear they would derail the discussion.

But instead of holding the meeting, the CEO analyzed this scenario *with* his direct reports. The case became the catalyst for a discussion in which the CEO learned several things about the way he acted with his management team.

He discovered that his four direct reports often perceived his conversations as counterproductive. In the guise of being “diplomatic,” he would pretend that a consensus about the problem existed, when in fact none existed. The unintended result: instead of feeling reassured, his subordinates felt wary and tried to figure out “what is he *really* getting at.”

The CEO also realized that the way he dealt with the competitiveness among department heads was completely contradictory. On the one hand, he kept urging them to “think of the organization as a whole.” On the other, he kept calling for actions—department budget cuts, for example—that placed them directly in competition with each other.

Finally, the CEO discovered that many of the tacit evaluations and attributions he had listed turned out to be wrong. Since he had never expressed these assumptions, he had never found out just how wrong they were. What's more, he learned that much of what he thought he was hiding

came through to his subordinates anyway—but with the added message that the boss was covering up.

The CEO's colleagues also learned about their own ineffective behavior. They learned by examining their own behavior as they tried to help the CEO analyze his case. They also learned by writing and analyzing cases of their own. They began to see that they too tended to bypass and cover up the real issues and that the CEO was often aware of it but did not say so. They too made inaccurate attributions and evaluations that they did not express. Moreover, the belief that they had to hide important ideas and feelings from the CEO and from each other in order not to upset anyone turned out to be mistaken. In the context of the case discussions, the entire senior management team was quite willing to discuss what had always been undiscussable.

In effect, the case study exercise legitimizes talking about issues that people have never been able to address before. Such a discussion can be emotional—even painful. But for managers with the courage to persist, the payoff is great: management teams and entire organizations work more openly and more effectively and have greater options for behaving flexibly and adapting to particular situations.

When senior managers are trained in new reasoning skills, they can have a big impact on the performance of the entire organization—even when other employees are still reasoning defensively. The CEO who led the meetings on the performance-evaluation procedure was able to defuse dissatisfaction because he didn't respond to professionals' criticisms in kind but instead gave a clear presentation of relevant data. Indeed, most participants took the CEO's behavior to be a sign that the company really acted on the values of participation and employee involvement that it espoused.

Of course, the ideal is for all the members of an organization to learn how to reason productively. This has happened at the company where the case team meeting took place. Consultants and their managers are now able to confront some of the most difficult issues of the consultant-client relationship. To get a sense of the difference productive reasoning can make, imagine how the original conversation between the manager and case team might have gone had everyone engaged in effective reasoning. (The following dialogue is based on actual sessions I have attended with other case teams at the same company since the training has been completed.)

First, the consultants would have demonstrated their commitment to

continuous improvement by being willing to examine their own role in the difficulties that arose during the consulting project. No doubt they would have identified their managers and the clients as part of the problem, but they would have gone on to admit that they had contributed to it as well. More important, they would have agreed with the manager that as they explored the various roles of clients, managers, and professionals, they would make sure to test any evaluations or attributions they might make against the data. Each individual would have encouraged the others to question his or her reasoning. Indeed, they would have insisted on it. And in turn, everyone would have understood that act of questioning not as a sign of mistrust or an invasion of privacy but as a valuable opportunity for learning.

The conversation about the manager's unwillingness to say no might look something like this:

Professional #1: "One of the biggest problems I had with the way you managed this case was that you seemed to be unable to say no when either the client or your superior made unfair demands." [Gives an example.]

Professional #2: "I have another example to add. [Describes a second example.] But I'd also like to say that we never really told you how we felt about this. Behind your back we were bad-mouthing you—you know, 'he's being such a wimp'—but we never came right out and said it."

Manager: "It certainly would have been helpful if you had said something. Was there anything I said or did that gave you the idea that you had better not raise this with me?"

Professional #3: "Not really. I think we didn't want to sound like we were whining."

Manager: "Well, I certainly don't think you sound like you're whining. But two thoughts come to mind. If I understand you correctly, you *were* complaining, but the complaining about me and my inability to say no was covered up. Second, if we had discussed this, I might have gotten the data I needed to be able to say no."

Notice that when the second professional describes how the consultants had covered up their complaints, the manager doesn't criticize her. Rather, he rewards her for being open by responding in kind. He focuses on the ways that he too may have contributed to the cover-up. Reflecting undefensively about his own role in the problem then makes it possible for the professionals to talk about their fears of appearing to be whining. The manager then agrees with the professionals that they shouldn't become complainers. At the same time, he points out the counterproductive consequences of covering up their complaints.

Another unresolved issue in the case team meeting concerned the supposed arrogance of the clients. A more productive conversation about that problem might go like this:

Manager: "You said that the clients were arrogant and uncooperative. What did they say and do?"

Professional #1: "One asked me if I had ever met a payroll. Another asked how long I've been out of school."

Professional #2: "One even asked me how old I was!"

Professional #3: "That's nothing. The worst is when they say that all we do is interview people, write a report based on what they tell us, and then collect our fees."

Manager: "The fact that we tend to be so young is a real problem for many of our clients. They get very defensive about it. But I'd like to explore whether there is a way for them to freely express their views without our getting defensive..."

"What troubled me about your original responses was that you assumed you were right in calling the clients stupid. One thing I've noticed about consultants—in this company and others—is that we tend to defend ourselves by bad-mouthing the client."

Professional #1: “Right. After all, if they are genuinely stupid, then it’s obviously not our fault that they aren’t getting it!”

Professional #2: “Of course, that stance is antilearning and overprotective. By assuming that they can’t learn, we absolve ourselves from having to.”

Professional #3: “And the more we all go along with the bad-mouthing, the more we reinforce each other’s defensiveness.”

Manager: “So what’s the alternative? How can we encourage our clients to express their defensiveness and at the same time constructively build on it?”

Professional #1: “We all know that the real issue isn’t our age; it’s whether or not we are able to add value to the client’s organization. They should judge us by what we produce. And if we aren’t adding value, they should get rid of us—no matter how young or old we happen to be.”

Manager: “Perhaps that is exactly what we should tell them.”

In both these examples, the consultants and their manager are doing real work. They are learning about their own group dynamics and addressing some generic problems in client-consultant relationships. The insights they gain will allow them to act more effectively in the future—both as individuals and as a team. They are not just solving problems but developing a far deeper and more textured understanding of their role as members of the organization. They are laying the groundwork for continuous improvement that is truly continuous. They are learning how to learn.

Originally published in May 1991. Reprint 4304.

How (Un)ethical Are You?

by Mahzarin R. Banaji, Max H. Bazerman, and Dolly Chugh

ANSWER TRUE OR FALSE: “I am an ethical manager.”

If you answered “true,” here’s an uncomfortable fact: You’re probably not. Most of us believe that we are ethical and unbiased. We imagine we’re good decision makers, able to objectively size up a job candidate or a venture deal and reach a fair and rational conclusion that’s in our, and our organization’s, best interests. But more than two decades of research confirms that, in reality, most of us fall woefully short of our inflated self-perception. We’re deluded by what Yale psychologist David Armor calls the illusion of objectivity, the notion that we’re free of the very biases we’re so quick to recognize in others. What’s more, these unconscious, or implicit, biases can be contrary to our consciously held, explicit beliefs. We may believe with confidence and conviction that a job candidate’s race has no bearing on our hiring decisions or that we’re immune to conflicts of interest. But psychological research routinely exposes counterintentional, unconscious biases. The prevalence of these biases suggests that even the most well-meaning person unwittingly allows unconscious thoughts and feelings to influence seemingly objective decisions. These flawed judgments are ethically problematic and undermine managers’ fundamental work—to recruit and retain superior talent, boost the performance of individuals and teams, and collaborate effectively with partners.

This article explores four related sources of unintentional unethical decision making: implicit forms of prejudice, bias that favors one’s own group, conflict of interest, and a tendency to overclaim credit. Because we are

not consciously aware of these sources of bias, they often cannot be addressed by penalizing people for their bad decisions. Nor are they likely to be corrected through conventional ethics training. Rather, managers must bring a new type of vigilance to bear. To begin, this requires letting go of the notion that our conscious attitudes always represent what we think they do. It also demands that we abandon our faith in our own objectivity and our ability to be fair. In the following pages, we will offer strategies that can help managers recognize these pervasive, corrosive, unconscious biases and reduce their impact.

Implicit Prejudice: Bias That Emerges from Unconscious Beliefs

Most fair-minded people strive to judge others according to their merits, but our research shows how often people instead judge according to unconscious stereotypes and attitudes, or “implicit prejudice.” What makes implicit prejudice so common and persistent is that it is rooted in the fundamental mechanics of thought. Early on, we learn to associate things that commonly go together and expect them to inevitably coexist: thunder and rain, for instance, or gray hair and old age. This skill—to perceive and learn from associations—often serves us well.

But, of course, our associations only reflect approximations of the truth; they are rarely applicable to every encounter. Rain doesn’t always accompany thunder, and the young can also go gray. Nonetheless, because we automatically make such associations to help us organize our world, we grow to trust them, and they can blind us to those instances in which the associations are not accurate—when they don’t align with our expectations.

Because implicit prejudice arises from the ordinary and unconscious tendency to make associations, it is distinct from conscious forms of prejudice, such as overt racism or sexism. This distinction explains why people who are free from conscious prejudice may still harbor biases and act accordingly. Exposed to images that juxtapose black men and violence, portray women as sex objects, imply that the physically disabled are mentally weak and the poor are lazy, even the most consciously unbiased person is bound to make biased associations. These associations play out in the workplace just as they do anywhere else.

Idea in Brief

Are you an ethical manager? Most would probably say, “Of course!” The truth is, most of us are not.

Most of us believe that we’re ethical and unbiased. We assume that we objectively size up job candidates or venture deals and reach fair and rational conclusions that are in our organization’s best interests.

But the truth is, we harbor many unconscious—and unethical—biases that derail our decisions and undermine our work as managers. Hidden biases prevent us from recognizing high-potential workers and retaining talented managers. They stop us from collaborating effectively with partners. They erode our teams’ performance. They can also lead to costly lawsuits.

But how can we root out these biases if they’re unconscious? Fortunately, as a manager, you can take deliberate actions to counteract their pull. **Regularly audit your decisions.** Have you, for example, hired a disproportionate number of people of your own race? **Expose yourself to non-stereotypical environments** that challenge your biases. If your department is led by men, spend time in one with women in leadership positions. And **consider counterintuitive options** when making decisions. Don’t rely on a mental short-list of candidates for a new assignment; consider every employee with relevant qualifications.

In the mid-1990s, Tony Greenwald, a professor of psychology at the University of Washington, developed an experimental tool called the Implicit Association Test (IAT) to study unconscious bias. A computerized version of the test requires subjects to rapidly classify words and images as “good” or “bad.” Using a keyboard, test takers must make split-second “good/bad” distinctions between words like “love,” “joy,” “pain,” and “sorrow” and at the same time sort images of faces that are (depending on the bias in question) black or white, young or old, fat or thin, and so on. The test exposes implicit biases by detecting subtle shifts in reaction time that can occur when

test takers are required to pair different sets of words and faces. Subjects who consciously believe that they have no negative feelings toward, say, black Americans or the elderly are nevertheless likely to be slower to associate elderly or black faces with the “good” words than they are to associate youthful or white faces with “good” words.

Idea in Practice

Unconscious Biases

Are the following unconscious biases levying what amounts to a “stereotype tax” on your company?

Implicit prejudice Judging according to unconscious stereotypes rather than merit exacts a high business cost. Exposed to images that juxtapose physical disabilities with mental weakness or portray poor people as lazy, even the most consciously unbiased person is bound to make biased associations. As a result, we routinely overlook highly qualified candidates for assignments.

In-group favoritism Granting favors to people with your same background—your nationality or alma mater—effectively discriminates against those who are different from you. Consider the potential cost of offering bonuses to employees who refer their friends for job openings: hires who may not have made the grade *without* in-group favoritism.

Overclaiming credit Most of us consider ourselves above average. But when every member of a team thinks he’s making the biggest contribution, each starts to think the others aren’t pulling their weight. That jeopardizes future collaborations. It also frustrates talented workers who may resign because they feel underappreciated.

Counteract Biases

To keep yourself from making similarly skewed calls, consider these guidelines:

Gather better data Expose your own implicit biases. Take the Implicit

Association Test (at <http://implicit.harvard.edu>). If you discover gender or racial biases, examine your hiring and promotion decisions in that new light. When working with others, have team members estimate their colleagues' contributions *before* they claim their own credit.

Rid your workplace of stereotypical cues Think about the biased associations your workplace may foster. Do your company's advertising and marketing materials frequently include sports metaphors or high-tech jargon? Make a conscious effort to curb such "insider" language—making your products more appealing to a diverse customer base. And if your department invariably promotes the same type of manager—highly analytic, for instance—shadow a department that values a different—perhaps more conceptual—skill-set.

Broaden your mind-set when making decisions Apply the "veil of ignorance" to your next managerial decision. Suppose you're considering a new policy that would give more vacation time to all employees but eliminate the flextime that has allowed new parents to keep working. How would your opinion differ if you were a parent or childless? Male or female? Healthy or unhealthy? You'll learn how strongly implicit biases influence you.

Since 1998, when Greenwald, Brian Nosek, and Mahzarin Banaji put the IAT online, people from around the world have taken over 2.5 million tests, confirming and extending the findings of more traditional laboratory experiments. Both show implicit biases to be strong and pervasive. (For more information on the IAT, see "Are You Biased?".)

Biases are also likely to be costly. In controlled experiments, psychologists Laurie Rudman at Rutgers and Peter Glick at Lawrence University have studied how implicit biases may work to exclude qualified people from certain roles. One set of experiments examined the relationship between participants' implicit gender stereotypes and their hiring decisions. Those holding stronger implicit biases were less likely to select a qualified woman who exhibited stereotypically "masculine" personality qualities, such as ambition or independence, for a job requiring stereotypically "feminine" qualities, such as interpersonal skills. Yet they would select a qualified man

exhibiting these same qualities. The hirers' biased perception was that the woman was less likely to be socially skilled than the man, though their qualifications were in fact the same. These results suggest that implicit biases may exact costs by subtly excluding qualified people from the very organizations that seek their talents.

Legal cases also reveal the real costs of implicit biases, both economic and social. Consider *Price Waterhouse v. Hopkins*. Despite logging more billable hours than her peers, bringing in \$25 million to the company, and earning the praise of her clients, Ann Hopkins was turned down for partner, and she sued. The details of the case reveal that her evaluators were explicitly prejudiced in their attitudes. For example, they had commented that Ann "overcompensated for being a woman" and needed a "course at charm school." But perhaps more damning from a legal standpoint was blunt testimony from experimental research. Testifying as an expert witness for the defense, psychology professor Susan Fiske, now at Princeton University, argued that the potential for biased decision making is *inherent* in a system in which a person has "solo" status—that is, a system in which the person is the only one of a kind (the only woman, the only African-American, the only person with a disability, and the like). Judge Gerhard Gesell concluded that "a far more subtle process [than the usual discriminatory intent] is involved" in the assessments made of Ann Hopkins, and she won both in a lower court and in the Supreme Court in what is now a landmark case in discrimination law.

Likewise, the 1999 case of *Thomas v. Kodak* demonstrates that implicit biases can be the basis for rulings. Here, the court posed the question of "whether the employer consciously intended to base the evaluations on race or simply did so because of unthinking stereotypes or bias." The court concluded that plaintiffs can indeed challenge "subjective evaluations which could easily mask covert or unconscious race discrimination." Although courts are careful not to assign responsibility easily for unintentional biases, these cases demonstrate the potential for corporate liability that such patterns of behavior could unwittingly create.

In-Group Favoritism: Bias That Favors Your Group

Think about some of the favors you have done in recent years, whether for a friend, a relative, or a colleague. Have you helped someone get a useful introduction, admission to a school, or a job? Most of us are glad to help out with such favors. Not surprisingly, we tend to do more favors for those we know, and those we know tend to be like ourselves: people who share our nationality, social class, and perhaps religion, race, employer, or alma mater. This all sounds rather innocent. What's wrong with asking your neighbor, the university dean, to meet with a coworker's son? Isn't it just being helpful to recommend a former sorority sister for a job or to talk to your banker cousin when a friend from church gets turned down for a home loan?

Few people set out to exclude anyone through such acts of kindness. But when those in the majority or those in power allocate scarce resources (such as jobs, promotions, and mortgages) to people just like them, they effectively discriminate against those who are different from them. Such "in-group favoritism" amounts to giving extra credit for group membership. Yet while discriminating against those who are different is considered unethical, helping people close to us is often viewed favorably. Think about the number of companies that explicitly encourage this by offering hiring bonuses to employees who refer their friends for job opportunities.

But consider the finding that banks in the United States are more likely to deny a mortgage application from a black person than from a white person, even when the applicants are equally qualified. The common view has been that banks are hostile to African-Americans. While this may be true of some banks and some loan officers, social psychologist David Messick has argued that in-group favoritism is more likely to be at the root of such discriminatory lending. A white loan officer may feel hopeful or lenient toward an unqualified white applicant while following the bank's lending standards strictly with an unqualified black applicant. In denying the black applicant's mortgage, the loan officer may not be expressing hostility toward blacks so much as favoritism toward whites. It's a subtle but crucial distinction.

The ethical cost is clear and should be reason enough to address the problem. But such inadvertent bias produces an additional effect: It erodes the bottom line. Lenders who discriminate in this way, for example, incur bad-debt costs they could have avoided if their lending decisions were more objective. They also may find themselves exposed to damaging publicity or discrimination lawsuits if the skewed lending pattern is publicly revealed. In a different context, companies may pay a real cost for marginal hires who wouldn't have made the grade but for the sympathetic hiring manager swayed by in-group favoritism.

Are You Biased?

ARE YOU WILLING TO bet that you feel the same way toward European-Americans as you do toward African-Americans? How about women versus men? Or older people versus younger ones? Think twice before you take that bet. Visit implicit.harvard.edu or www.tolerance.org/hidden_bias to examine your unconscious attitudes.

The Implicit Association Tests available on these sites reveal unconscious beliefs by asking takers to make split-second associations between words with positive or negative connotations and images representing different types of people. The various tests on these sites expose the differences—or the alignment—between test takers' conscious and unconscious attitudes toward people of different races, sexual orientation, or physical characteristics. Data gathered from over 2.5 million online tests and further research tells us that unconscious biases are:

- **widely prevalent.** At least 75% of test takers show an implicit bias favoring the young, the rich, and whites.
- **robust.** The mere conscious desire not to be biased does not eliminate implicit bias.
- **contrary to conscious intention.** Although people tend to report little or no *conscious* bias against African-Americans, Arabs, Arab-Americans, Jews, gay men, lesbians, or the poor, they show substantial biases on implicit measures.
- **different in degree depending on group status.** Minority group members tend to show less implicit preference for their own group than majority group members show for theirs. For example, African-Americans report strong preference for their group on explicit measures

but show relatively less implicit preference in the tests. Conversely, white Americans report a low explicit bias for their group but a higher implicit bias.

- **consequential.** Those who show higher levels of bias on the IAT are also likely to behave in ways that are more biased in face-to-face interactions with members of the group they are biased against and in the choices they make, such as hiring decisions.
- **costly.** Research currently under way in our lab suggests that implicit bias generates a “stereotype tax”—negotiators leave money on the table because biases cause them to miss opportunities to learn about their opponent and thus create additional value through mutually beneficial trade-offs.

In-group favoritism is tenacious when membership confers clear advantages, as it does, for instance, among whites and other dominant social groups. (It may be weaker or absent among people whose group membership offers little societal advantage.) Thus for a wide array of managerial tasks—from hiring, firing, and promoting to contracting services and forming partnerships—qualified minority candidates are subtly and unconsciously discriminated against, sometimes simply because they are in the minority: There are not enough of them to counter the propensity for in-group favoritism in the majority.

Overclaiming Credit: Bias That Favors You

It's only natural for successful people to hold positive views about themselves. But many studies show that the majority of people consider themselves above average on a host of measures, from intelligence to driving ability. Business executives are no exception. We tend to overrate our individual contribution to groups, which, bluntly put, tends to lead to an overblown sense of entitlement. We become the unabashed, repeated beneficiaries of this unconscious bias, and the more we think only of our own contributions, the less fairly we judge others with whom we work.

Lab research demonstrates this most personal of biases. At Harvard, Eugene Caruso, Nick Epley, and Max Bazerman recently asked MBA students in study groups to estimate what portion of their group's work each had done. The sum of the contribution by all members, of course, must add up to 100%. But the researchers found that the totals for each study group averaged 139%. In a related study, Caruso and his colleagues uncovered rampant overestimates by academic authors of their contribution to shared research projects. Sadly, but not surprisingly, the more the sum of the total estimated group effort exceeded 100% (in other words, the more credit each person claimed), the less the parties wanted to collaborate in the future.

Likewise in business, claiming too much credit can destabilize alliances. When each party in a strategic partnership claims too much credit for its own contribution and becomes skeptical about whether the other is doing its fair share, they both tend to reduce their contributions to compensate. This has obvious repercussions for the joint venture's performance.

Unconscious overclaiming can be expected to reduce the performance and longevity of groups within organizations, just as it diminished the academic authors' willingness to collaborate. It can also take a toll on employee commitment. Think about how employees perceive raises. Most are not so different from the children at Lake Wobegon, believing that they, too, rank in the upper half of their peer group. But many necessarily get pay increases that are below the average. If an employee learns of a colleague's greater

compensation—while honestly believing that he himself is more deserving—resentment may be natural. At best, his resentment might translate into reduced commitment and performance. At worst, he may leave the organization that, it seems, doesn't appreciate his contribution.

Conflict of Interest: Bias That Favors Those Who Can Benefit You

Everyone knows that conflict of interest can lead to intentionally corrupt behavior. But numerous psychological experiments show how powerfully such conflicts can unintentionally skew decision making. (For an examination of the evidence in one business arena, see Max Bazerman, George Loewenstein, and Don Moore's November 2002 HBR article, "Why Good Accountants Do Bad Audits.") These experiments suggest that the work world is rife with situations in which such conflicts lead honest, ethical professionals to unconsciously make unsound and unethical recommendations.

Physicians, for instance, face conflicts of interest when they accept payment for referring patients into clinical trials. While, surely, most physicians consciously believe that their referrals are the patient's best clinical option, how do they know that the promise of payment did not skew their decisions? Similarly, many lawyers earn fees based on their clients' awards or settlements. Since going to trial is expensive and uncertain, settling out of court is often an attractive option for the lawyer. Attorneys may consciously believe that settling is in their clients' best interests. But how can they be objective, unbiased judges under these circumstances?

Research done with brokerage house analysts demonstrates how conflict of interest can unconsciously distort decision making. A survey of analysts conducted by the financial research service First Call showed that during a period in 2000 when the Nasdaq dropped 60%, fully 99% of brokerage analysts' client recommendations remained "strong buy," "buy," or "hold." What accounts for this discrepancy between what was happening and what was recommended? The answer may lie in a system that fosters conflicts of interest. A portion of analysts' pay is based on brokerage firm revenues. Some firms even tie analysts' compensation to the amount of business the analysts bring in from clients, giving analysts an obvious incentive to prolong and extend their relationships with clients. But to assume that during this

Nasdaq free fall all brokerage house analysts were consciously corrupt, milking their clients to exploit this incentive system, defies common sense. Surely there were some bad apples. But how much more likely it is that most of these analysts believed their recommendations were sound and in their clients' best interests. What many didn't appreciate was that the built-in conflict of interest in their compensation incentives made it impossible for them to see the implicit bias in their own flawed recommendations.

Trying Harder Isn't Enough

As companies keep collapsing into financial scandal and ruin, corporations are responding with ethics-training programs for managers, and many of the world's leading business schools have created new courses and chaired professorships in ethics. Many of these efforts focus on teaching broad principles of moral philosophy to help managers understand the ethical challenges they face.

We applaud these efforts, but we doubt that a well-intentioned, just-try-harder approach will fundamentally improve the quality of executives' decision making. To do that, ethics training must be broadened to include what is now known about how our minds work and must expose managers directly to the unconscious mechanisms that underlie biased decision making. And it must provide managers with exercises and interventions that can root out the biases that lead to bad decisions.

Managers can make wiser, more ethical decisions if they become mindful of their unconscious biases. But how can we get at something outside our conscious awareness? By bringing the conscious mind to bear. Just as the driver of a misaligned car deliberately counteracts its pull, so can managers develop conscious strategies to counteract the pull of their unconscious biases. What's required is vigilance—continual awareness of the forces that can cause decision making to veer from its intended course and continual adjustments to counteract them. Those adjustments fall into three general categories: collecting data, shaping the environment, and broadening the decision-making process.

Collect data

The first step to reducing unconscious bias is to collect data to reveal its presence. Often, the data will be counterintuitive. Consider many people's surprise to learn of their own gender and racial biases on the IAT. Why the surprise? Because most of us trust the "statistics" our intuition provides. Better data are easily, but rarely, collected. One way to get those data is to examine our decisions in a systematic way.

Remember the MBA study groups whose participants overestimated their individual contributions to the group effort so that the totals averaged 139%? When the researchers asked group members to estimate what each of the other members' contributions were *before* claiming their own, the total fell to 121%. The tendency to claim too much credit still persisted, but this strategy of "unpacking" the work reduced the magnitude of the bias. In environments characterized by "I deserve more than you're giving me" claims, merely asking team members to unpack the contributions of others before claiming their own share of the pot usually aligns claims more closely with what's actually deserved. As this example demonstrates, such systematic audits of both individual and group decision-making processes can occur even as the decisions are being made.

Unpacking is a simple strategy that managers should routinely use to evaluate the fairness of their own claims within the organization. But they can also apply it in any situation where team members or subordinates may be overclaiming. For example, in explaining a raise that an employee feels is inadequate, a manager should ask the subordinate not what he thinks he alone deserves but what he considers an appropriate raise after taking into account each coworker's contribution and the pool available for pay increases. Similarly, when an individual feels she's doing more than her fair share of a team's work, asking her to consider other people's efforts before estimating her own can help align her perception with reality, restore her commitment, and reduce a skewed sense of entitlement.

Taking the IAT is another valuable strategy for collecting data. We recommend that you and others in your organization use the test to expose

your own implicit biases. But one word of warning: Because the test is an educational and research tool, not a selection or evaluation tool, it is critical that you consider your results and others' to be private information. Simply knowing the magnitude and pervasiveness of your own biases can help direct your attention to areas of decision making that are in need of careful examination and reconsideration. For example, a manager whose testing reveals a bias toward certain groups ought to examine her hiring practices to see if she has indeed been disproportionately favoring those groups. But because so many people harbor such biases, they can also be generally acknowledged, and that knowledge can be used as the basis for changing the way decisions are made. It is important to guard against using pervasiveness to justify complacency and inaction: Pervasiveness of bias is not a mark of its appropriateness any more than poor eyesight is considered so ordinary a condition that it does not require corrective lenses.

Shape your environment

Research shows that implicit attitudes can be shaped by external cues in the environment. For example, Curtis Hardin and colleagues at UCLA used the IAT to study whether subjects' implicit race bias would be affected if the test was administered by a black investigator. One group of students took the test under the guidance of a white experimenter; another group took the test with a black experimenter. The mere presence of a black experimenter, Hardin found, reduced the level of subjects' implicit antiblack bias on the IAT. Numerous similar studies have shown similar effects with other social groups. What accounts for such shifts? We can speculate that experimenters in classrooms are assumed to be competent, in charge, and authoritative. Subjects guided by a black experimenter attribute these positive characteristics to that person, and then perhaps to the group as a whole. These findings suggest that one remedy for implicit bias is to expose oneself to images and social environments that challenge stereotypes.

We know of a judge whose court is located in a predominantly African-American neighborhood. Because of the crime and arrest patterns in the community, most people the judge sentences are black. The judge confronted a paradox. On the one hand, she took a judicial oath to be objective and egalitarian, and indeed she consciously believed that her decisions were unbiased. On the other hand, every day she was exposed to an environment that reinforced the association between black men and crime. Although she consciously rejected racial stereotypes, she suspected that she harbored unconscious prejudices merely from working in a segregated world. Immersed in this environment each day, she wondered if it was possible to give the defendants a fair hearing.

Rather than allow her environment to reinforce a bias, the judge created an alternative environment. She spent a vacation week sitting in a fellow judge's court in a neighborhood where the criminals being tried were predominantly white. Case after case challenged the stereotype of blacks as criminal and whites as law abiding and so challenged any bias against blacks that she might have harbored.

Think about the possibly biased associations your workplace fosters. Is there, perhaps, a “wall of fame” with pictures of high achievers all cast from the same mold? Are certain types of managers invariably promoted? Do people overuse certain analogies drawn from stereotypical or narrow domains of knowledge (sports metaphors, for instance, or cooking terms)? Managers can audit their organization to uncover such patterns or cues that unwittingly lead to stereotypical associations.

If an audit reveals that the environment may be promoting unconscious biased or unethical behavior, consider creating countervailing experiences, as the judge did. For example, if your department reinforces the stereotype of men as naturally dominant in a hierarchy (most managers are male, and most assistants are female), find a department with women in leadership positions and set up a shadow program. Both groups will benefit from the exchange of best practices, and your group will be quietly exposed to counterstereotypical cues. Managers sending people out to spend time in clients’ organizations as a way to improve service should take care to select organizations likely to counter stereotypes reinforced in your own company.

Broaden your decision making

Imagine that you are making a decision in a meeting about an important company policy that will benefit some groups of employees more than others. A policy might, for example, provide extra vacation time for all employees but eliminate the flex time that has allowed many new parents to balance work with their family responsibilities. Another policy might lower the mandatory retirement age, eliminating some older workers but creating advancement opportunities for younger ones. Now pretend that, as you make your decisions, you don't know which group you belong to. That is, you don't know whether you are senior or junior, married or single, gay or straight, a parent or childless, male or female, healthy or unhealthy. You will eventually find out, but not until after the decision has been made. In this hypothetical scenario, what decision would you make? Would you be willing to risk being in the group disadvantaged by your own decision? How would your decisions differ if you could make them wearing various identities not your own?

This thought experiment is a version of philosopher John Rawls's concept of the "veil of ignorance," which posits that only a person ignorant of his own identity is capable of a truly ethical decision. Few of us can assume the veil completely, which is precisely why hidden biases, even when identified, are so difficult to correct. Still, applying the veil of ignorance to your next important managerial decision may offer some insight into how strongly implicit biases influence you.

Just as managers can expose bias by collecting data before acting on intuition, they can take other preemptive steps. What list of names do you start with when considering whom to send to a training program, recommend for a new assignment, or nominate for a fast-track position? Most of us can quickly and with little concentration come up with such a list. But keep in mind that your intuition is prone to implicit prejudice (which will strongly favor dominant and well-liked groups), in-group favoritism (which will favor people in your own group), overclaiming (which will favor you), and conflict of interest (which will favor people whose interests affect your own). Instead

of relying on a mental short list when making personnel decisions, start with a full list of names of employees who have relevant qualifications.

Using a broad list of names has several advantages. The most obvious is that talent may surface that might otherwise be overlooked. Less obvious but equally important, the very act of considering a counterstereotypical choice at the conscious level can reduce implicit bias. In fact, merely thinking about hypothetical, counterstereotypical scenarios—such as what it would be like to trust a complex presentation to a female colleague or to receive a promotion from an African-American boss—can prompt less-biased and more ethical decision making. Similarly, consciously considering counterintuitive options in the face of conflicts of interest, or when there's an opportunity to overclaim, can promote more objective and ethical decisions.

The Vigilant Manager

If you answered “true” to the question at the start of this article, you felt with some confidence that you are an ethical decision maker. How would you answer it now? It’s clear that neither simple conviction nor sincere intention is enough to ensure that you are the ethical practitioner you imagine yourself to be. Managers who aspire to be ethical must challenge the assumption that they’re always unbiased and acknowledge that vigilance, even more than good intention, is a defining characteristic of an ethical manager. They must actively collect data, shape their environments, and broaden their decision making. What’s more, an obvious redress is available. Managers should seek every opportunity to implement affirmative action policies—not because of past wrongs done to one group or another but because of the everyday wrongs that we can now document are inherent in the ordinary, everyday behavior of good, well-intentioned people. Ironically, only those who understand their own potential for unethical behavior can become the ethical decision makers that they aspire to be.

Originally published in December 2003. Reprint 5526.

The Discipline of Teams

by Jon R. Katzenbach and Douglas K. Smith

EARLY IN THE 1980S, Bill Greenwood and a small band of rebel railroaders took on most of the top management of Burlington Northern and created a multibillion-dollar business in “piggybacking” rail services despite widespread resistance, even resentment, within the company. The Medical Products Group at Hewlett-Packard owes most of its leading performance to the remarkable efforts of Dean Morton, Lew Platt, Ben Holmes, Dick Alberding, and a handful of their colleagues who revitalized a health care business that most others had written off. At Knight Ridder, Jim Batten’s “customer obsession” vision took root at the *Tallahassee Democrat* when 14 frontline enthusiasts turned a charter to eliminate errors into a mission of major change and took the entire paper along with them.

Such are the stories and the work of teams—real teams that perform, not amorphous groups that we call teams because we think that the label is motivating and energizing. The difference between teams that perform and other groups that don’t is a subject to which most of us pay far too little attention. Part of the problem is that “team” is a word and concept so familiar to everyone. (See “Not All Groups Are Teams: How to Tell the Difference.”)

Or at least that’s what we thought when we set out to do research for our book *The Wisdom of Teams* (HarperBusiness, 1993). We wanted to discover what differentiates various levels of team performance, where and how teams work best, and what top management can do to enhance their effectiveness. We talked with hundreds of people on more than 50 different teams in 30 companies and beyond, from Motorola and Hewlett-Packard to Operation

Desert Storm and the Girl Scouts.

We found that there is a basic discipline that makes teams work. We also found that teams and good performance are inseparable: You cannot have one without the other. But people use the word “team” so loosely that it gets in the way of learning and applying the discipline that leads to good performance. For managers to make better decisions about whether, when, or how to encourage and use teams, it is important to be more precise about what a team is and what it isn’t.

Most executives advocate teamwork. And they should. Teamwork represents a set of values that encourage listening and responding constructively to views expressed by others, giving others the benefit of the doubt, providing support, and recognizing the interests and achievements of others. Such values help teams perform, and they also promote individual performance as well as the performance of an entire organization. But teamwork values by themselves are not exclusive to teams, nor are they enough to ensure team performance. (See “Building Team Performance.”)

Nor is a team just any group working together. Committees, councils, and task forces are not necessarily teams. Groups do not become teams simply because that is what someone calls them. The entire workforce of any large and complex organization is *never* a team, but think about how often that platitude is offered up.

To understand how teams deliver extra performance, we must distinguish between teams and other forms of working groups. That distinction turns on performance results. A working group’s performance is a function of what its members do as individuals. A team’s performance includes both individual results and what we call “collective work products.” A collective work product is what two or more members must work on together, such as interviews, surveys, or experiments. Whatever it is, a collective work product reflects the joint, real contribution of team members.

Idea in Brief

The word *team* gets bandied about so loosely that many managers are oblivious to its real meaning—or its true potential. With a run-of-the-mill working group, performance is a function of what the members do as individuals. A team's performance, by contrast, calls for both individual and mutual accountability.

Though it may not seem like anything special, mutual accountability can lead to astonishing results. It enables a team to achieve performance levels that are far greater than the individual bests of the team's members. To achieve these benefits, team members must do more than listen, respond constructively, and provide support to one another. In addition to sharing these team-building values, they must share an essential *discipline*.

Working groups are both prevalent and effective in large organizations where individual accountability is most important. The best working groups come together to share information, perspectives, and insights; to make decisions that help each person do his or her job better; and to reinforce individual performance standards. But the focus is always on individual goals and accountabilities. Working-group members don't take responsibility for results other than their own. Nor do they try to develop incremental performance contributions requiring the combined work of two or more members.

Teams differ fundamentally from working groups because they require both individual and mutual accountability. Teams rely on more than group discussion, debate, and decision, on more than sharing information and best-practice performance standards. Teams produce discrete work products through the joint contributions of their members. This is what makes possible performance levels greater than the sum of all the individual bests of team members. Simply stated, a team is more than the sum of its parts.

The first step in developing a disciplined approach to team management is to think about teams as discrete units of performance and not just as positive sets of values. Having observed and worked with scores of teams in action,

both successes and failures, we offer the following. Think of it as a working definition or, better still, an essential discipline that real teams share: *A team is a small number of people with complementary skills who are committed to a common purpose, set of performance goals, and approach for which they hold themselves mutually accountable.*

Idea in Practice

A team's essential discipline comprises five characteristics:

1. **A meaningful common purpose that the team has helped shape.** Most teams are responding to an initial mandate from outside the team. But to be successful, the team must “own” this purpose, develop its own spin on it.
2. **Specific performance goals that flow from the common purpose.** For example, getting a new product to market in less than half the normal time. Compelling goals inspire and challenge a team, give it a sense of urgency. They also have a leveling effect, requiring members to focus on the collective effort necessary rather than any differences in title or status.
3. **A mix of complementary skills.** These include technical or functional expertise, problem-solving and decision-making skills, and interpersonal skills. Successful teams rarely have all the needed skills at the outset—they develop them as they learn what the challenge requires.
4. **A strong commitment to how the work gets done.** Teams must agree on who will do what jobs, how schedules will be established and honored, and how decisions will be made and modified. On a genuine team, each member does equivalent amounts of real work; all members, the leader included, contribute in concrete ways to the team's collective work-products.
5. **Mutual accountability.** Trust and commitment cannot be coerced. The process of agreeing upon appropriate goals serves as the crucible in which members forge their accountability to each other—not just to the leader.

Once the essential discipline has been established, a team is free to concentrate on the critical challenges it faces:

- For a team whose purpose is to make recommendations, that means making a fast and constructive start and providing a clean handoff to those who will implement the recommendations.
- For a team that makes or does things, it's keeping the specific performance goals in sharp focus.
- For a team that runs things, the primary task is distinguishing the challenges that require a real team approach from those that don't.

If a task doesn't demand joint work-products, a working group can be the more effective option. Team opportunities are usually those in which hierarchy or organizational boundaries inhibit the skills and perspectives needed for optimal results. Little wonder, then, that teams have become the primary units of productivity in high-performance organizations.

The essence of a team is common commitment. Without it, groups perform as individuals; with it, they become a powerful unit of collective performance. This kind of commitment requires a purpose in which team members can believe. Whether the purpose is to "transform the contributions of suppliers into the satisfaction of customers," to "make our company one we can be proud of again," or to "prove that all children can learn," credible team purposes have an element related to winning, being first, revolutionizing, or being on the cutting edge.

Teams develop direction, momentum, and commitment by working to shape a meaningful purpose. Building ownership and commitment to team purpose, however, is not incompatible with taking initial direction from outside the team. The often-asserted assumption that a team cannot "own" its

purpose unless management leaves it alone actually confuses more potential teams than it helps. In fact, it is the exceptional case—for example, entrepreneurial situations—when a team creates a purpose entirely on its own.

Most successful teams shape their purposes in response to a demand or opportunity put in their path, usually by higher management. This helps teams get started by broadly framing the company's performance expectation. Management is responsible for clarifying the charter, rationale, and performance challenge for the team, but management must also leave enough flexibility for the team to develop commitment around its own spin on that purpose, set of specific goals, timing, and approach.

The best teams invest a tremendous amount of time and effort exploring, shaping, and agreeing on a purpose that belongs to them both collectively and individually. This “purposing” activity continues throughout the life of the team. By contrast, failed teams rarely develop a common purpose. For whatever reason—an insufficient focus on performance, lack of effort, poor leadership—they do not coalesce around a challenging aspiration.

The best teams also translate their common purpose into specific performance goals, such as reducing the reject rate from suppliers by 50% or increasing the math scores of graduates from 40% to 95%. Indeed, if a team fails to establish specific performance goals or if those goals do not relate directly to the team's overall purpose, team members become confused, pull apart, and revert to mediocre performance. By contrast, when purposes and goals build on one another and are combined with team commitment, they become a powerful engine of performance.

Transforming broad directives into specific and measurable performance goals is the surest first step for a team trying to shape a purpose meaningful to its members. Specific goals, such as getting a new product to market in less than half the normal time, responding to all customers within 24 hours, or achieving a zero-defect rate while simultaneously cutting costs by 40%, all provide firm footholds for teams. There are several reasons:

- Specific team-performance goals help define a set of work products that are different both from an organization-wide mission and from individual job objectives. As a result, such work products require the

collective effort of team members to make something specific happen that, in and of itself, adds real value to results. By contrast, simply gathering from time to time to make decisions will not sustain team performance.

- The specificity of performance objectives facilitates clear communication and constructive conflict within the team. When a plant-level team, for example, sets a goal of reducing average machine changeover time to two hours, the clarity of the goal forces the team to concentrate on what it would take either to achieve or to reconsider the goal. When such goals are clear, discussions can focus on how to pursue them or whether to change them; when goals are ambiguous or nonexistent, such discussions are much less productive.
- The attainability of specific goals helps teams maintain their focus on getting results. A product-development team at Eli Lilly's Peripheral Systems Division set definite yardsticks for the market introduction of an ultrasonic probe to help doctors locate deep veins and arteries.

The probe had to have an audible signal through a specified depth of tissue, be capable of being manufactured at a rate of 100 per day, and have a unit cost less than a preestablished amount. Because the team could measure its progress against each of these specific objectives, the team knew throughout the development process where it stood. Either it had achieved its goals or not.

- As Outward Bound and other team-building programs illustrate, specific objectives have a leveling effect conducive to team behavior. When a small group of people challenge themselves to get over a wall or to reduce cycle time by 50%, their respective titles, perks, and other stripes fade into the background. The teams that succeed evaluate what and how each individual can best contribute to the team's goal and, more important, do so in terms of the performance objective itself rather than a person's status or personality.
- Specific goals allow a team to achieve small wins as it pursues its broader purpose. These small wins are invaluable to building commitment and overcoming the inevitable obstacles that get in the way

of a long-term purpose. For example, the Knight Ridder team mentioned at the outset turned a narrow goal to eliminate errors into a compelling customer service purpose.

- Performance goals are compelling. They are symbols of accomplishment that motivate and energize. They challenge the people on a team to commit themselves, as a team, to make a difference. Drama, urgency, and a healthy fear of failure combine to drive teams that have their collective eye on an attainable, but challenging, goal. Nobody but the team can make it happen. It's their challenge.

The combination of purpose and specific goals is essential to performance. Each depends on the other to remain relevant and vital. Clear performance goals help a team keep track of progress and hold itself accountable; the broader, even nobler, aspirations in a team's purpose supply both meaning and emotional energy.

Virtually all effective teams we have met, read or heard about, or been members of have ranged between two and 25 people. For example, the Burlington Northern piggybacking team had seven members, and the Knight Ridder newspaper team had 14. The majority of them have numbered less than ten. Small size is admittedly more of a pragmatic guide than an absolute necessity for success. A large number of people, say 50 or more, can theoretically become a team. But groups of such size are more likely to break into subteams rather than function as a single unit.

Why? Large numbers of people have trouble interacting constructively as a group, much less doing real work together. Ten people are far more likely than 50 to work through their individual, functional, and hierarchical differences toward a common plan and to hold themselves jointly accountable for the results.

Large groups also face logistical issues, such as finding enough physical space and time to meet. And they confront more complex constraints, like crowd or herd behaviors, which prevent the intense sharing of viewpoints needed to build a team. As a result, when they try to develop a common purpose, they usually produce only superficial "missions" and well-meaning intentions that cannot be translated into concrete objectives. They tend fairly quickly to reach a point when meetings become a chore, a clear sign that

most of the people in the group are uncertain why they have gathered, beyond some notion of getting along better. Anyone who has been through one of these exercises understands how frustrating it can be. This kind of failure tends to foster cynicism, which gets in the way of future team efforts.

In addition to finding the right size, teams must develop the right mix of skills; that is, each of the complementary skills necessary to do the team's job. As obvious as it sounds, it is a common failing in potential teams. Skill requirements fall into three fairly self-evident categories.

Technical or functional expertise

It would make little sense for a group of doctors to litigate an employment discrimination case in a court of law. Yet teams of doctors and lawyers often try medical malpractice or personal injury cases. Similarly, product development groups that include only marketers or engineers are less likely to succeed than those with the complementary skills of both.

Problem-solving and decision-making skills

Teams must be able to identify the problems and opportunities they face, evaluate the options they have for moving forward, and then make necessary trade-offs and decisions about how to proceed. Most teams need some members with these skills to begin with, although many will develop them best on the job.

Interpersonal skills

Common understanding and purpose cannot arise without effective communication and constructive conflict, which in turn depend on interpersonal skills. These skills include risk taking, helpful criticism, objectivity, active listening, giving the benefit of the doubt, and recognizing the interests and achievements of others.

Obviously, a team cannot get started without some minimum complement of skills, especially technical and functional ones. Still, think about how often you've been part of a team whose members were chosen primarily on the basis of personal compatibility or formal position in the organization, and in which the skill mix of its members wasn't given much thought.

Not All Groups Are Teams: How to Tell the Difference

Working Group

- Strong, clearly focused leader
- Individual accountability
- The group's purpose is the same as the broader organizational mission
- Individual work products
- Runs efficient meetings
- Measures its effectiveness indirectly by its influence on others (such as financial performance of the business)
- Discusses, decides, and delegates

Team

- Shared leadership roles
- Individual and mutual accountability
- Specific team purpose that the team itself delivers

- Collective work products
- Encourages open-ended discussion and active problem-solving meetings
- Measures performance directly by assessing collective work products
- Discusses, decides, and does real work together

It is equally common to overemphasize skills in team selection. Yet in all the successful teams we've encountered, not one had all the needed skills at the outset. The Burlington Northern team, for example, initially had no members who were skilled marketers despite the fact that their performance challenge was a marketing one. In fact, we discovered that teams are powerful vehicles for developing the skills needed to meet the team's performance challenge. Accordingly, team member selection ought to ride as much on skill potential as on skills already proven.

Effective teams develop strong commitment to a common approach; that is, to how they will work together to accomplish their purpose. Team members must agree on who will do particular jobs, how schedules will be set and adhered to, what skills need to be developed, how continuing membership in the team is to be earned, and how the group will make and modify decisions. This element of commitment is as important to team performance as the team's commitment to its purpose and goals.

Agreeing on the specifics of work and how they fit together to integrate individual skills and advance team performance lies at the heart of shaping a common approach. It is perhaps self-evident that an approach that delegates all the real work to a few members (or staff outsiders) and thus relies on reviews and meetings for its only "work together" aspects, cannot sustain a real team. Every member of a successful team does equivalent amounts of real work; all members, including the team leader, contribute in concrete ways to the team's work product. This is a very important element of the emotional logic that drives team performance.

When individuals approach a team situation, especially in a business setting, each has preexisting job assignments as well as strengths and

weaknesses reflecting a variety of talents, backgrounds, personalities, and prejudices. Only through the mutual discovery and understanding of how to apply all its human resources to a common purpose can a team develop and agree on the best approach to achieve its goals. At the heart of such long and, at times, difficult interactions lies a commitment-building process in which the team candidly explores who is best suited to each task as well as how individual roles will come together. In effect, the team establishes a social contract among members that relates to their purpose and guides and obligates how they must work together.

No group ever becomes a team until it can hold itself accountable as a team. Like common purpose and approach, mutual accountability is a stiff test. Think, for example, about the subtle but critical difference between “the boss holds me accountable” and “we hold ourselves accountable.” The first case can lead to the second, but without the second, there can be no team.

Companies like Hewlett-Packard and Motorola have an ingrained performance ethic that enables teams to form organically whenever there is a clear performance challenge requiring collective rather than individual effort. In these companies, the factor of mutual accountability is commonplace. “Being in the boat together” is how their performance game is played.

At its core, team accountability is about the sincere promises we make to ourselves and others, promises that underpin two critical aspects of effective teams: commitment and trust. Most of us enter a potential team situation cautiously because ingrained individualism and experience discourage us from putting our fates in the hands of others or accepting responsibility for others. Teams do not succeed by ignoring or wishing away such behavior.

Mutual accountability cannot be coerced any more than people can be made to trust one another. But when a team shares a common purpose, goals, and approach, mutual accountability grows as a natural counterpart. Accountability arises from and reinforces the time, energy, and action invested in figuring out what the team is trying to accomplish and how best to get it done.

When people work together toward a common objective, trust and commitment follow. Consequently, teams enjoying a strong common purpose and approach inevitably hold themselves responsible, both as individuals and as a team, for the team’s performance. This sense of mutual accountability also produces the rich rewards of mutual achievement in which all members share. What we heard over and over from members of effective teams is that

they found the experience energizing and motivating in ways that their “normal” jobs never could match.

On the other hand, groups established primarily for the sake of becoming a team or for job enhancement, communication, organizational effectiveness, or excellence rarely become effective teams, as demonstrated by the bad feelings left in many companies after experimenting with quality circles that never translated “quality” into specific goals. Only when appropriate performance goals are set does the process of discussing the goals and the approaches to them give team members a clearer and clearer choice: They can disagree with a goal and the path that the team selects and, in effect, opt out, or they can pitch in and become accountable with and to their teammates.

The discipline of teams we’ve outlined is critical to the success of all teams. Yet it is also useful to go one step further. Most teams can be classified in one of three ways: teams that recommend things, teams that make or do things, and teams that run things. In our experience, each type faces a characteristic set of challenges.

Teams that recommend things

These teams include task forces; project groups; and audit, quality, or safety groups asked to study and solve particular problems. Teams that recommend things almost always have predetermined completion dates. Two critical issues are unique to such teams: getting off to a fast and constructive start and dealing with the ultimate handoff that's required to get recommendations implemented.

The key to the first issue lies in the clarity of the team's charter and the composition of its membership. In addition to wanting to know why and how their efforts are important, task forces need a clear definition of whom management expects to participate and the time commitment required. Management can help by ensuring that the team includes people with the skills and influence necessary for crafting practical recommendations that will carry weight throughout the organization. Moreover, management can help the team get the necessary cooperation by opening doors and dealing with political obstacles.

Missing the handoff is almost always the problem that stymies teams that recommend things. To avoid this, the transfer of responsibility for recommendations to those who must implement them demands top management's time and attention. The more top managers assume that recommendations will "just happen," the less likely it is that they will. The more involvement task force members have in implementing their recommendations, the more likely they are to get implemented.

To the extent that people outside the task force will have to carry the ball, it is critical to involve them in the process early and often, certainly well before recommendations are finalized. Such involvement may take many forms, including participating in interviews, helping with analyses, contributing and critiquing ideas, and conducting experiments and trials. At a minimum, anyone responsible for implementation should receive a briefing on the task force's purpose, approach, and objectives at the beginning of the effort as well as regular reviews of progress.

Teams that make or do things

These teams include people at or near the front lines who are responsible for doing the basic manufacturing, development, operations, marketing, sales, service, and other value-adding activities of a business. With some exceptions, such as new-product development or process design teams, teams that make or do things tend to have no set completion dates because their activities are ongoing.

In deciding where team performance might have the greatest impact, top management should concentrate on what we call the company's "critical delivery points"—that is, places in the organization where the cost and value of the company's products and services are most directly determined. Such critical delivery points might include where accounts get managed, customer service performed, products designed, and productivity determined. If performance at critical delivery points depends on combining multiple skills, perspectives, and judgments in real time, then the team option is the smartest one.

When an organization does require a significant number of teams at these points, the sheer challenge of maximizing the performance of so many groups will demand a carefully constructed and performance-focused set of management processes. The issue here for top management is how to build the necessary systems and process supports without falling into the trap of appearing to promote teams for their own sake.

The imperative here, returning to our earlier discussion of the basic discipline of teams, is a relentless focus on performance. If management fails to pay persistent attention to the link between teams and performance, the organization becomes convinced that "this year, we are doing 'teams'." Top management can help by instituting processes like pay schemes and training for teams responsive to their real time needs, but more than anything else, top management must make clear and compelling demands on the teams themselves and then pay constant attention to their progress with respect to both team basics and performance results. This means focusing on specific teams and specific performance challenges. Otherwise "performance," like

“team,” will become a cliché.

Teams that run things

Despite the fact that many leaders refer to the group reporting to them as a team, few groups really are. And groups that become real teams seldom think of themselves as a team because they are so focused on performance results. Yet the opportunity for such teams includes groups from the top of the enterprise down through the divisional or functional level. Whether it is in charge of thousands of people or just a handful, as long as the group oversees some business, ongoing program, or significant functional activity, it is a team that runs things.

The main issue these teams face is determining whether a real team approach is the right one. Many groups that run things can be more effective as working groups than as teams. The key judgment is whether the sum of individual bests will suffice for the performance challenge at hand or whether the group must deliver substantial incremental performance requiring real joint work products. Although the team option promises greater performance, it also brings more risk, and managers must be brutally honest in assessing the trade-offs.

Members may have to overcome a natural reluctance to trust their fate to others. The price of faking the team approach is high: At best, members get diverted from their individual goals, costs outweigh benefits, and people resent the imposition on their time and priorities. At worst, serious animosities develop that undercut even the potential personal bests of the working-group approach.

Working groups present fewer risks. Effective working groups need little time to shape their purpose, since the leader usually establishes it. Meetings are run against well-prioritized agendas. And decisions are implemented through specific individual assignments and accountabilities. Most of the time, therefore, if performance aspirations can be met through individuals doing their respective jobs well, the working-group approach is more comfortable, less risky, and less disruptive than trying for more elusive team performance levels. Indeed, if there is no performance need for the team approach, efforts spent to improve the effectiveness of the working group

make much more sense than floundering around trying to become a team.

Having said that, we believe the extra level of performance teams can achieve is becoming critical for a growing number of companies, especially as they move through major changes during which company performance depends on broad-based behavioral change. When top management uses teams to run things, it should make sure the team succeeds in identifying specific purposes and goals.

This is a second major issue for teams that run things. Too often, such teams confuse the broad mission of the total organization with the specific purpose of their small group at the top. The discipline of teams tells us that for a real team to form, there must be a team purpose that is distinctive and specific to the small group and that requires its members to roll up their sleeves and accomplish something beyond individual end products. If a group of managers looks only at the economic performance of the part of the organization it runs to assess overall effectiveness, the group will not have any team performance goals of its own.

While the basic discipline of teams does not differ for them, teams at the top are certainly the most difficult. The complexities of long-term challenges, heavy demands on executive time, and the deep-seated individualism of senior people conspire against teams at the top. At the same time, teams at the top are the most powerful. At first we thought such teams were nearly impossible. That is because we were looking at the teams as defined by the formal organizational structure; that is, the leader and all his or her direct reports equals the team. Then we discovered that real teams at the top were often smaller and less formalized: Whitehead and Weinberg at Goldman Sachs; Hewlett and Packard at HP; Krasnoff, Pall, and Hardy at Pall Corporation; Kendall, Pearson, and Calloway at Pepsi; Haas and Haas at Levi Strauss; Batten and Ridder at Knight Ridder. They were mostly twos and threes, with an occasional fourth.

Nonetheless, real teams at the top of large, complex organizations are still few and far between. Far too many groups at the top of large corporations needlessly constrain themselves from achieving real team levels of performance because they assume that all direct reports must be on the team, that team goals must be identical to corporate goals, that the team members' positions rather than skills determine their respective roles, that a team must be a team all the time, and that the team leader is above doing real work.

As understandable as these assumptions may be, most of them are

unwarranted. They do not apply to the teams at the top we have observed, and when replaced with more realistic and flexible assumptions that permit the team discipline to be applied, real team performance at the top can and does occur. Moreover, as more and more companies are confronted with the need to manage major change across their organizations, we will see more real teams at the top.

We believe that teams will become the primary unit of performance in high-performance organizations. But that does not mean that teams will crowd out individual opportunity or formal hierarchy and process. Rather, teams will enhance existing structures without replacing them. A team opportunity exists anywhere hierarchy or organizational boundaries inhibit the skills and perspectives needed for optimal results. Thus, new-product innovation requires preserving functional excellence through structure while eradicating functional bias through teams. And frontline productivity requires preserving direction and guidance through hierarchy while drawing on energy and flexibility through self-managing teams.

We are convinced that every company faces specific performance challenges for which teams are the most practical and powerful vehicle at top management's disposal. The critical role for senior managers, therefore, is to worry about company performance and the kinds of teams that can deliver it. This means top management must recognize a team's unique potential to deliver results, deploy teams strategically when they are the best tool for the job, and foster the basic discipline of teams that will make them effective. By doing so, top management creates the kind of environment that enables team as well as individual and organizational performance.

Building Team Performance

Although there is no guaranteed how-to recipe for building team performance, we observed a number of approaches shared by many successful teams.

Establish urgency, demanding performance standards, and direction

All team members need to believe the team has urgent and worthwhile purposes, and they want to know what the expectations are. Indeed, the more urgent and meaningful the rationale, the more likely it is that the team will live up to its performance potential, as was the case for a customer-service team that was told that further growth for the entire company would be impossible without major improvements in that area. Teams work best in a compelling context. That is why companies with strong performance ethics usually form teams readily.

Select members for skill and skill potential, not personality

No team succeeds without all the skills needed to meet its purpose and performance goals. Yet most teams figure out the skills they will need after they are formed. The wise manager will choose people for their existing skills and their potential to improve existing skills and learn new ones.

Pay particular attention to first meetings and actions. Initial impressions always mean a great deal

When potential teams first gather, everyone monitors the signals given by others to confirm, suspend, or dispel assumptions and concerns. They pay particular attention to those in authority: the team leader and any executives who set up, oversee, or otherwise influence the team. And, as always, what such leaders do is more important than what they say. If a senior executive leaves the team kickoff to take a phone call ten minutes after the session has begun and he never returns, people get the message.

Set some clear rules of behavior

All effective teams develop rules of conduct at the outset to help them achieve their purpose and performance goals. The most critical initial rules pertain to attendance (for example, “no interruptions to take phone calls”), discussion (“no sacred cows”), confidentiality (“the only things to leave this room are what we agree on”), analytic approach (“facts are friendly”), end-product orientation (“everyone gets assignments and does them”), constructive confrontation (“no finger pointing”), and, often the most important, contributions (“everyone does real work”).

Set and seize upon a few immediate performance-oriented tasks and goals

Most effective teams trace their advancement to key performance-oriented events. Such events can be set in motion by immediately establishing a few challenging goals that can be reached early on. There is no such thing as a real team without performance results, so the sooner such results occur, the sooner the team congeals.

Challenge the group regularly with fresh facts and information

New information causes a team to redefine and enrich its understanding of the performance challenge, thereby helping the team shape a common purpose, set clearer goals, and improve its common approach. A plant quality improvement team knew the cost of poor quality was high, but it wasn't until they researched the different types of defects and put a price tag on each one that they knew where to go next. Conversely, teams err when they assume that all the information needed exists in the collective experience and knowledge of their members.

Spend lots of time together

Common sense tells us that team members must spend a lot of time together, scheduled and unscheduled, especially in the beginning. Indeed, creative insights as well as personal bonding require impromptu and casual interactions just as much as analyzing spreadsheets and interviewing customers. Busy executives and managers too often intentionally minimize

the time they spend together. The successful teams we've observed all gave themselves the time to learn to be a team. This time need not always be spent together physically; electronic, fax, and phone time can also count as time spent together.

Exploit the power of positive feedback, recognition, and reward

Positive reinforcement works as well in a team context as elsewhere. Giving out "gold stars" helps shape new behaviors critical to team performance. If people in the group, for example, are alert to a shy person's initial efforts to speak up and contribute, they can give the honest positive reinforcement that encourages continued contributions. There are many ways to recognize and reward team performance beyond direct compensation, from having a senior executive speak directly to the team about the urgency of its mission to using awards to recognize contributions. Ultimately, however, the satisfaction shared by a team in its own performance becomes the most cherished reward.

Originally published in March 1993. Reprint R0507P.

Managing Your Boss

by John J. Gabarro and John P. Kotter

TO MANY PEOPLE, THE PHRASE “managing your boss” may sound unusual or suspicious. Because of the traditional top-down emphasis in most organizations, it is not obvious why you need to manage relationships upward—unless, of course, you would do so for personal or political reasons. But we are not referring to political maneuvering or to apple polishing. We are using the term to mean the process of consciously working with your superior to obtain the best possible results for you, your boss, and the company.

Recent studies suggest that effective managers take time and effort to manage not only relationships with their subordinates but also those with their bosses. These studies also show that this essential aspect of management is sometimes ignored by otherwise talented and aggressive managers. Indeed, some managers who actively and effectively supervise subordinates, products, markets, and technologies assume an almost passively reactive stance vis-à-vis their bosses. Such a stance almost always hurts them and their companies.

If you doubt the importance of managing your relationship with your boss or how difficult it is to do so effectively, consider for a moment the following sad but telling story:

Frank Gibbons was an acknowledged manufacturing genius in his industry and, by any profitability standard, a very effective executive. In 1973, his strengths propelled him into the position of vice president of manufacturing for the second largest and most profitable company in its industry. Gibbons was not, however, a good manager of people. He knew

this, as did others in his company and his industry. Recognizing this weakness, the president made sure that those who reported to Gibbons were good at working with people and could compensate for his limitations. The arrangement worked well.

In 1975, Philip Bonnevie was promoted into a position reporting to Gibbons. In keeping with the previous pattern, the president selected Bonnevie because he had an excellent track record and a reputation for being good with people. In making that selection, however, the president neglected to notice that, in his rapid rise through the organization, Bonnevie had always had good-to-excellent bosses. He had never been forced to manage a relationship with a difficult boss. In retrospect, Bonnevie admits he had never thought that managing his boss was a part of his job.

Fourteen months after he started working for Gibbons, Bonnevie was fired. During that same quarter, the company reported a net loss for the first time in seven years. Many of those who were close to these events say that they don't really understand what happened. This much is known, however: While the company was bringing out a major new product—a process that required sales, engineering, and manufacturing groups to coordinate decisions very carefully—a whole series of misunderstandings and bad feelings developed between Gibbons and Bonnevie.

For example, Bonnevie claims Gibbons was aware of and had accepted Bonnevie's decision to use a new type of machinery to make the new product; Gibbons swears he did not. Furthermore, Gibbons claims he made it clear to Bonnevie that the introduction of the product was too important to the company in the short run to take any major risks.

As a result of such misunderstandings, planning went awry: A new manufacturing plant was built that could not produce the new product designed by engineering, in the volume desired by sales, at a cost agreed on by the executive committee. Gibbons blamed Bonnevie for the mistake. Bonnevie blamed Gibbons.

Idea in Brief

Managing our *bosses*? Isn't that merely manipulation? Corporate cozying up? Out-and-out apple polishing? In fact, we manage our bosses for very good reasons: to get resources to do the best job, not only for ourselves, but for our bosses and our companies as well. We actively pursue a healthy and productive working relationship based on mutual respect and understanding—understanding our own and our bosses' strengths, weaknesses, goals, work styles, and needs. Here's what can happen when we don't:

Example: A new president with a formal work style replaced someone who'd been looser, more intuitive. The new president preferred written reports and structured meetings. One of his managers found this too controlling. He seldom sent background information, and was often blindsided by unanticipated questions. His boss found their meetings inefficient and frustrating. The manager had to resign.

In contrast, here's how another manager's sensitivity to this same boss's style really paid off:

Example: This manager identified the kinds and frequency of information the president wanted. He sent ahead background reports and discussion agendas. The result? Highly productive meetings and even more innovative problem solving than with his previous boss.

Managers often don't realize how much their bosses depend on them. They need cooperation, reliability, and honesty from their direct reports. Many managers also don't realize how much *they* depend on their bosses—for links to the rest of the organization, for setting priorities, and for obtaining critical resources.

Recognizing this mutual dependence, effective managers seek out information about the boss's concerns and are sensitive to his work style. They also understand how their own attitudes toward authority can sabotage the relationship. Some see the boss as the enemy and fight him at every turn;

others are overly compliant, viewing the boss as an all-wise parent.

Of course, one could argue that the problem here was caused by Gibbons's inability to manage his subordinates. But one can make just as strong a case that the problem was related to Bonnevie's inability to manage his boss. Remember, Gibbons was not having difficulty with any other subordinates. Moreover, given the personal price paid by Bonnevie (being fired and having his reputation within the industry severely tarnished), there was little consolation in saying the problem was that Gibbons was poor at managing subordinates. Everyone already knew that.

Idea in Practice

You can benefit from this mutual dependence and develop a very productive relationship with your boss by focusing on:

- **compatible work styles.** Bosses process information differently. “Listeners” prefer to be briefed in person so they can ask questions. “Readers” want to process written information first, and then meet to discuss.

Decision-making styles also vary. Some bosses are highly involved. Touch base with them frequently. Others prefer to delegate. Inform them about important decisions you’ve already made.

- **mutual expectations.** Don’t passively assume you know what the boss expects. Find out. With some bosses, write detailed outlines of your work for their approval. With others, carefully planned discussions are key.

Also, communicate *your* expectations to find out if they are realistic. Persuade the boss to accept the most important ones.

- **information flow.** Managers typically underestimate what their bosses

need to know—and what they *do* know. Keep the boss informed through processes that fit his style. Be forthright about both good and bad news.

- dependability and honesty. Trustworthy subordinates only make promises they can keep and don't shade the truth or play down difficult issues.
- good use of time and resources. Don't waste your boss's time with trivial issues. Selectively draw on his time and resources to meet the most important goals—yours, his, and the company's.

We believe that the situation could have turned out differently had Bonnevie been more adept at understanding Gibbons and at managing his relationship with him. In this case, an inability to manage upward was unusually costly. The company lost \$2 million to \$5 million, and Bonnevie's career was, at least temporarily, disrupted. Many less costly cases similar to this probably occur regularly in all major corporations, and the cumulative effect can be very destructive.

Misreading the Boss–Subordinate Relationship

People often dismiss stories like the one we just related as being merely cases of personality conflict. Because two people can on occasion be psychologically or temperamentally incapable of working together, this can be an apt description. But more often, we have found, a personality conflict is only a part of the problem—sometimes a very small part.

Bonnevie did not just have a different personality from Gibbons, he also made or had unrealistic assumptions and expectations about the very nature of boss–subordinate relationships. Specifically, he did not recognize that his relationship to Gibbons involved *mutual dependence* between two *fallible* human beings. Failing to recognize this, a manager typically either avoids trying to manage his or her relationship with a boss or manages it ineffectively.

Some people behave as if their bosses were not very dependent on them. They fail to see how much the boss needs their help and cooperation to do his or her job effectively. These people refuse to acknowledge that the boss can be severely hurt by their actions and needs cooperation, dependability, and honesty from them.

Some people see themselves as not very dependent on their bosses. They gloss over how much help and information they need from the boss in order to perform their own jobs well. This superficial view is particularly damaging when a manager's job and decisions affect other parts of the organization, as was the case in Bonnevie's situation. A manager's immediate boss can play a critical role in linking the manager to the rest of the organization, making sure the manager's priorities are consistent with organizational needs, and in securing the resources the manager needs to perform well. Yet some managers need to see themselves as practically self-sufficient, as not needing the critical information and resources a boss can supply.

Many managers, like Bonnevie, assume that the boss will magically know what information or help their subordinates need and provide it to them. Certainly, some bosses do an excellent job of caring for their subordinates in

this way, but for a manager to expect that from all bosses is dangerously unrealistic. A more reasonable expectation for managers to have is that modest help will be forthcoming. After all, bosses are only human. Most really effective managers accept this fact and assume primary responsibility for their own careers and development. They make a point of seeking the information and help they need to do a job instead of waiting for their bosses to provide it.

In light of the foregoing, it seems to us that managing a situation of mutual dependence among fallible human beings requires the following:

1. You have a good understanding of the other person and yourself, especially regarding strengths, weaknesses, work styles, and needs.
2. You use this information to develop and manage a healthy working relationship—one that is compatible with both people's work styles and assets, is characterized by mutual expectations, and meets the most critical needs of the other person.

This combination is essentially what we have found highly effective managers doing.

Understanding the Boss

Managing your boss requires that you gain an understanding of the boss and his or her context, as well as your own situation. All managers do this to some degree, but many are not thorough enough.

At a minimum, you need to appreciate your boss's goals and pressures, his or her strengths and weaknesses. What are your boss's organizational and personal objectives, and what are his or her pressures, especially those from his or her own boss and others at the same level? What are your boss's long suits and blind spots? What is the preferred style of working? Does your boss like to get information through memos, formal meetings, or phone calls? Does he or she thrive on conflict or try to minimize it? Without this information, a manager is flying blind when dealing with the boss, and unnecessary conflicts, misunderstandings, and problems are inevitable.

In one situation we studied, a top-notch marketing manager with a superior performance record was hired into a company as a vice president "to straighten out the marketing and sales problems." The company, which was having financial difficulties, had recently been acquired by a larger corporation. The president was eager to turn it around and gave the new marketing vice president free rein—at least initially. Based on his previous experience, the new vice president correctly diagnosed that greater market share was needed for the company and that strong product management was required to bring that about. Following that logic, he made a number of pricing decisions aimed at increasing high-volume business.

When margins declined and the financial situation did not improve, however, the president increased pressure on the new vice president. Believing that the situation would eventually correct itself as the company gained back market share, the vice president resisted the pressure.

When by the second quarter, margins and profits had still failed to improve, the president took direct control over all pricing decisions and put all items on a set level of margin, regardless of volume. The new vice president began to find himself shut out by the president, and their

relationship deteriorated. In fact, the vice president found the president's behavior bizarre. Unfortunately, the president's new pricing scheme also failed to increase margins, and by the fourth quarter, both the president and the vice president were fired.

What the new vice president had not known until it was too late was that improving marketing and sales had been only *one* of the president's goals. His most immediate goal had been to make the company more profitable—quickly.

Nor had the new vice president known that his boss was invested in this short-term priority for personal as well as business reasons. The president had been a strong advocate of the acquisition within the parent company, and his personal credibility was at stake.

The vice president made three basic errors. He took information supplied to him at face value, he made assumptions in areas where he had no information, and—what was most damaging—he never actively tried to clarify what his boss's objectives were. As a result, he ended up taking actions that were actually at odds with the president's priorities and objectives.

Managers who work effectively with their bosses do not behave this way. They seek out information about the boss's goals and problems and pressures. They are alert for opportunities to question the boss and others around him or her to test their assumptions. They pay attention to clues in the boss's behavior. Although it is imperative that they do this especially when they begin working with a new boss, effective managers also do this on an ongoing basis because they recognize that priorities and concerns change.

Being sensitive to a boss's work style can be crucial, especially when the boss is new. For example, a new president who was organized and formal in his approach replaced a man who was informal and intuitive. The new president worked best when he had written reports. He also preferred formal meetings with set agendas.

One of his division managers realized this need and worked with the new president to identify the kinds and frequency of information and reports that the president wanted. This manager also made a point of sending background information and brief agendas ahead of time for their discussions. He found that with this type of preparation their meetings were very useful. Another interesting result was, he found that with adequate preparation his new boss was even more effective at brainstorming problems than his more informal

and intuitive predecessor had been.

In contrast, another division manager never fully understood how the new boss's work style differed from that of his predecessor. To the degree that he did sense it, he experienced it as too much control. As a result, he seldom sent the new president the background information he needed, and the president never felt fully prepared for meetings with the manager. In fact, the president spent much of the time when they met trying to get information that he felt he should have had earlier. The boss experienced these meetings as frustrating and inefficient, and the subordinate often found himself thrown off guard by the questions that the president asked. Ultimately, this division manager resigned.

The difference between the two division managers just described was not so much one of ability or even adaptability. Rather, one of the men was more sensitive to his boss's work style and to the implications of his boss's needs than the other was.

Understanding Yourself

The boss is only one-half of the relationship. You are the other half, as well as the part over which you have more direct control. Developing an effective working relationship requires, then, that you know your own needs, strengths and weaknesses, and personal style.

You are not going to change either your basic personality structure or that of your boss. But you can become aware of what it is about you that impedes or facilitates working with your boss and, with that awareness, take actions that make the relationship more effective.

For example, in one case we observed, a manager and his superior ran into problems whenever they disagreed. The boss's typical response was to harden his position and overstate it. The manager's reaction was then to raise the ante and intensify the forcefulness of his argument. In doing this, he channeled his anger into sharpening his attacks on the logical fallacies he saw in his boss's assumptions. His boss in turn would become even more adamant about holding his original position. Predictably, this escalating cycle resulted in the subordinate avoiding whenever possible any topic of potential conflict with his boss.

In discussing this problem with his peers, the manager discovered that his reaction to the boss was typical of how he generally reacted to counterarguments—but with a difference. His response would overwhelm his peers but not his boss. Because his attempts to discuss this problem with his boss were unsuccessful, he concluded that the only way to change the situation was to deal with his own instinctive reactions. Whenever the two reached an impasse, he would check his own impatience and suggest that they break up and think about it before getting together again. Usually when they renewed their discussion, they had digested their differences and were more able to work them through.

Gaining this level of self-awareness and acting on it are difficult but not impossible. For example, by reflecting over his past experiences, a young manager learned that he was not very good at dealing with difficult and

emotional issues where people were involved. Because he disliked those issues and realized that his instinctive responses to them were seldom very good, he developed a habit of touching base with his boss whenever such a problem arose. Their discussions always surfaced ideas and approaches the manager had not considered. In many cases, they also identified specific actions the boss could take to help.

Although a superior-subordinate relationship is one of mutual dependence, it is also one in which the subordinate is typically more dependent on the boss than the other way around. This dependence inevitably results in the subordinate feeling a certain degree of frustration, sometimes anger, when his actions or options are constrained by his boss's decisions. This is a normal part of life and occurs in the best of relationships. The way in which a manager handles these frustrations largely depends on his or her predisposition toward dependence on authority figures.

Some people's instinctive reaction under these circumstances is to resent the boss's authority and to rebel against the boss's decisions. Sometimes a person will escalate a conflict beyond what is appropriate. Seeing the boss almost as an institutional enemy, this type of manager will often, without being conscious of it, fight with the boss just for the sake of fighting. The subordinate's reactions to being constrained are usually strong and sometimes impulsive. He or she sees the boss as someone who, by virtue of the role, is a hindrance to progress, an obstacle to be circumvented or at best tolerated.

Psychologists call this pattern of reactions counterdependent behavior. Although a counterdependent person is difficult for most superiors to manage and usually has a history of strained relationships with superiors, this sort of manager is apt to have even more trouble with a boss who tends to be directive or authoritarian. When the manager acts on his or her negative feelings, often in subtle and nonverbal ways, the boss sometimes does become the enemy. Sensing the subordinate's latent hostility, the boss will lose trust in the subordinate or his or her judgment and then behave even less openly.

Paradoxically, a manager with this type of predisposition is often a good manager of his or her own people. He or she will many times go out of the way to get support for them and will not hesitate to go to bat for them.

At the other extreme are managers who swallow their anger and behave in a very compliant fashion when the boss makes what they know to be a poor decision. These managers will agree with the boss even when a disagreement

might be welcome or when the boss would easily alter a decision if given more information. Because they bear no relationship to the specific situation at hand, their responses are as much an overreaction as those of counterdependent managers. Instead of seeing the boss as an enemy, these people deny their anger—the other extreme—and tend to see the boss as if he or she were an all-wise parent who should know best, should take responsibility for their careers, train them in all they need to know, and protect them from overly ambitious peers.

Both counterdependence and overdependence lead managers to hold unrealistic views of what a boss is. Both views ignore that bosses, like everyone else, are imperfect and fallible. They don't have unlimited time, encyclopedic knowledge, or extrasensory perception; nor are they evil enemies. They have their own pressures and concerns that are sometimes at odds with the wishes of the subordinate—and often for good reason.

Altering predispositions toward authority, especially at the extremes, is almost impossible without intensive psychotherapy (psychoanalytic theory and research suggest that such predispositions are deeply rooted in a person's personality and upbringing). However, an awareness of these extremes and the range between them can be very useful in understanding where your own predispositions fall and what the implications are for how you tend to behave in relation to your boss.

If you believe, on the one hand, that you have some tendencies toward counterdependence, you can understand and even predict what your reactions and overreactions are likely to be. If, on the other hand, you believe you have some tendencies toward overdependence, you might question the extent to which your overcompliance or inability to confront real differences may be making both you and your boss less effective.

Developing and Managing the Relationship

With a clear understanding of both your boss and yourself, you can *usually* establish a way of working together that fits both of you, that is characterized by unambiguous mutual expectations, and that helps you both be more productive and effective. The “Checklist for managing your boss” summarizes some things such a relationship consists of. Following are a few more.

Checklist for Managing Your Boss

Make sure you understand your boss and his or her context, including:

- ☐ Goals and objectives
- ☐ Pressures
- ☐ Strengths, weaknesses, blind spots
- ☐ Preferred work style

Assess yourself and your needs, including:

- ☐ Strengths and weaknesses
- ☐ Personal style
- ☐ Predisposition toward dependence on authority figures

Develop and maintain a relationship that:

- ☐ Fits both your needs and styles
 - ☐ Is characterized by mutual expectations
 - ☐ Keeps your boss informed
 - ☐ Is based on dependability and honesty
 - ☐ Selectively uses your boss's time and resources
-

Compatible work styles

Above all else, a good working relationship with a boss accommodates differences in work style. For example, in one situation we studied, a manager (who had a relatively good relationship with his superior) realized that during meetings his boss would often become inattentive and sometimes brusque. The subordinate's own style tended to be discursive and exploratory. He would often digress from the topic at hand to deal with background factors, alternative approaches, and so forth. His boss preferred to discuss problems with a minimum of background detail and became impatient and distracted whenever his subordinate digressed from the immediate issue.

Recognizing this difference in style, the manager became terser and more direct during meetings with his boss. To help himself do this, before meetings, he would develop brief agendas that he used as a guide. Whenever he felt that a digression was needed, he explained why. This small shift in his own style made these meetings more effective and far less frustrating for both of them.

Subordinates can adjust their styles in response to their bosses' preferred method for receiving information. Peter Drucker divides bosses into "listeners" and "readers." Some bosses like to get information in report form so they can read and study it. Others work better with information and reports presented in person so they can ask questions. As Drucker points out, the implications are obvious. If your boss is a listener, you brief him or her in person, *then* follow it up with a memo. If your boss is a reader, you cover important items or proposals in a memo or report, *then* discuss them.

Other adjustments can be made according to a boss's decision-making style. Some bosses prefer to be involved in decisions and problems as they arise. These are high-involvement managers who like to keep their hands on the pulse of the operation. Usually their needs (and your own) are best satisfied if you touch base with them on an ad hoc basis. A boss who has a need to be involved will become involved one way or another, so there are advantages to including him or her at your initiative. Other bosses prefer to

delegate—they don't want to be involved. They expect you to come to them with major problems and inform them about any important changes.

Creating a compatible relationship also involves drawing on each other's strengths and making up for each other's weaknesses. Because he knew that the boss—the vice president of engineering—was not very good at monitoring his employees' problems, one manager we studied made a point of doing it himself. The stakes were high: The engineers and technicians were all union members, the company worked on a customer-contract basis, and the company had recently experienced a serious strike.

The manager worked closely with his boss, along with people in the scheduling department and the personnel office, to make sure that potential problems were avoided. He also developed an informal arrangement through which his boss would review with him any proposed changes in personnel or assignment policies before taking action. The boss valued his advice and credited his subordinate for improving both the performance of the division and the labor-management climate.

Mutual expectations

The subordinate who passively assumes that he or she knows what the boss expects is in for trouble. Of course, some superiors will spell out their expectations very explicitly and in great detail. But most do not. And although many corporations have systems that provide a basis for communicating expectations (such as formal planning processes, career planning reviews, and performance appraisal reviews), these systems never work perfectly. Also, between these formal reviews, expectations invariably change.

Ultimately, the burden falls on the subordinate to find out what the boss's expectations are. They can be both broad (such as what kinds of problems the boss wishes to be informed about and when) as well as very specific (such things as when a particular project should be completed and what kinds of information the boss needs in the interim).

Getting a boss who tends to be vague or not explicit to express expectations can be difficult. But effective managers find ways to get that information. Some will draft a detailed memo covering key aspects of their work and then send it to their boss for approval. They then follow this up with a face-to-face discussion in which they go over each item in the memo. A discussion like this will often surface virtually all of the boss's expectations.

Other effective managers will deal with an inexplicit boss by initiating an ongoing series of informal discussions about "good management" and "our objectives." Still others find useful information more indirectly through those who used to work for the boss and through the formal planning systems in which the boss makes commitments to his or her own superior. Which approach you choose, of course, should depend on your understanding of your boss's style.

Developing a workable set of mutual expectations also requires that you communicate your own expectations to the boss, find out if they are realistic, and influence the boss to accept the ones that are important to you. Being able to influence the boss to value your expectations can be particularly

important if the boss is an overachiever. Such a boss will often set unrealistically high standards that need to be brought into line with reality.

A flow of information

How much information a boss needs about what a subordinate is doing will vary significantly depending on the boss's style, the situation he or she is in, and the confidence the boss has in the subordinate. But it is not uncommon for a boss to need more information than the subordinate would naturally supply or for the subordinate to think the boss knows more than he or she really does. Effective managers recognize that they probably underestimate what their bosses need to know and make sure they find ways to keep them informed through processes that fit their styles.

Managing the flow of information upward is particularly difficult if the boss does not like to hear about problems. Although many people would deny it, bosses often give off signals that they want to hear only good news. They show great displeasure—usually nonverbally—when someone tells them about a problem. Ignoring individual achievement, they may even evaluate more favorably subordinates who do not bring problems to them.

Nevertheless, for the good of the organization, the boss, and the subordinate, a superior needs to hear about failures as well as successes. Some subordinates deal with a good-news-only boss by finding indirect ways to get the necessary information to him or her, such as a management information system. Others see to it that potential problems, whether in the form of good surprises or bad news, are communicated immediately.

Dependability and honesty

Few things are more disabling to a boss than a subordinate on whom he cannot depend, whose work he cannot trust. Almost no one is intentionally undependable, but many managers are inadvertently so because of oversight or uncertainty about the boss's priorities. A commitment to an optimistic delivery date may please a superior in the short term but become a source of displeasure if not honored. It's difficult for a boss to rely on a subordinate who repeatedly slips deadlines. As one president (describing a subordinate) put it: "I'd rather he be more consistent even if he delivered fewer peak successes—at least I could rely on him."

Nor are many managers intentionally dishonest with their bosses. But it is easy to shade the truth and play down issues. Current concerns often become future surprise problems. It's almost impossible for bosses to work effectively if they cannot rely on a fairly accurate reading from their subordinates. Because it undermines credibility, dishonesty is perhaps the most troubling trait a subordinate can have. Without a basic level of trust, a boss feels compelled to check all of a subordinate's decisions, which makes it difficult to delegate.

Good use of time and resources

Your boss is probably as limited in his or her store of time, energy, and influence as you are. Every request you make of your boss uses up some of these resources, so it's wise to draw on these resources selectively. This may sound obvious, but many managers use up their boss's time (and some of their own credibility) over relatively trivial issues.

One vice president went to great lengths to get his boss to fire a meddlesome secretary in another department. His boss had to use considerable influence to do it. Understandably, the head of the other department was not pleased. Later, when the vice president wanted to tackle more important problems, he ran into trouble. By using up blue chips on a relatively trivial issue, he had made it difficult for him and his boss to meet more important goals.

No doubt, some subordinates will resent that on top of all their other duties, they also need to take time and energy to manage their relationships with their bosses. Such managers fail to realize the importance of this activity and how it can simplify their jobs by eliminating potentially severe problems. Effective managers recognize that this part of their work is legitimate. Seeing themselves as ultimately responsible for what they achieve in an organization, they know they need to establish and manage relationships with everyone on whom they depend—and that includes the boss.

Originally published in January 1980. Reprint R0501J.

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First eBook Edition: January 2011

ISBN: 978-1-4221-5797-8

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What Makes a Leader?

by Daniel Goleman

EVERY BUSINESSPERSON KNOWS a story about a highly intelligent, highly skilled executive who was promoted into a leadership position only to fail at the job. And they also know a story about someone with solid—but not extraordinary—intellectual abilities and technical skills who was promoted into a similar position and then soared.

Such anecdotes support the widespread belief that identifying individuals with the “right stuff” to be leaders is more art than science. After all, the personal styles of superb leaders vary: Some leaders are subdued and analytical; others shout their manifestos from the mountaintops. And just as important, different situations call for different types of leadership. Most mergers need a sensitive negotiator at the helm, whereas many turnarounds require a more forceful authority.

I have found, however, that the most effective leaders are alike in one crucial way: They all have a high degree of what has come to be known as *emotional intelligence*. It’s not that IQ and technical skills are irrelevant. They do matter, but mainly as “threshold capabilities”; that is, they are the entry-level requirements for executive positions. But my research, along with other recent studies, clearly shows that emotional intelligence is the sine qua non of leadership. Without it, a person can have the best training in the world, an incisive, analytical mind, and an endless supply of smart ideas, but he still won’t make a great leader.

In the course of the past year, my colleagues and I have focused on how emotional intelligence operates at work. We have examined the relationship

between emotional intelligence and effective performance, especially in leaders. And we have observed how emotional intelligence shows itself on the job. How can you tell if someone has high emotional intelligence, for example, and how can you recognize it in yourself? In the following pages, we'll explore these questions, taking each of the components of emotional intelligence—self-awareness, self-regulation, motivation, empathy, and social skill—in turn.

Evaluating Emotional Intelligence

Most large companies today have employed trained psychologists to develop what are known as “competency models” to aid them in identifying, training, and promoting likely stars in the leadership firmament. The psychologists have also developed such models for lower-level positions. And in recent years, I have analyzed competency models from 188 companies, most of which were large and global and included the likes of Lucent Technologies, British Airways, and Credit Suisse.

In carrying out this work, my objective was to determine which personal capabilities drove outstanding performance within these organizations, and to what degree they did so. I grouped capabilities into three categories: purely technical skills like accounting and business planning; cognitive abilities like analytical reasoning; and competencies demonstrating emotional intelligence, such as the ability to work with others and effectiveness in leading change.

To create some of the competency models, psychologists asked senior managers at the companies to identify the capabilities that typified the organization’s most outstanding leaders. To create other models, the psychologists used objective criteria, such as a division’s profitability, to differentiate the star performers at senior levels within their organizations from the average ones. Those individuals were then extensively interviewed and tested, and their capabilities were compared. This process resulted in the creation of lists of ingredients for highly effective leaders. The lists ranged in length from seven to 15 items and included such ingredients as initiative and strategic vision.

Idea in Brief

What distinguishes great leaders from merely good ones? It isn't IQ or technical skills, says Daniel Goleman. It's **emotional intelligence**: a group of five skills that enable the best leaders to maximize their own *and* their followers' performance. When senior managers at one company had a critical mass of EI capabilities, their divisions outperformed yearly earnings goals by 20%.

The EI skills are:

- *Self-awareness*—knowing one's strengths, weaknesses, drives, values, and impact on others
- *Self-regulation*—controlling or redirecting disruptive impulses and moods
- *Motivation*—relishing achievement for its own sake
- *Empathy*—understanding other people's emotional makeup
- *Social skill*—building rapport with others to move them in desired directions

We're each born with certain levels of EI skills. But we can strengthen these abilities through persistence, practice, and feedback from colleagues or coaches.

When I analyzed all this data, I found dramatic results. To be sure, intellect was a driver of outstanding performance. Cognitive skills such as big-picture thinking and long-term vision were particularly important. But when I calculated the ratio of technical skills, IQ, and emotional intelligence as ingredients of excellent performance, emotional intelligence proved to be twice as important as the others for jobs at all levels.

Moreover, my analysis showed that emotional intelligence played an increasingly important role at the highest levels of the company, where differences in technical skills are of negligible importance. In other words,

the higher the rank of a person considered to be a star performer, the more emotional intelligence capabilities showed up as the reason for his or her effectiveness. When I compared star performers with average ones in senior leadership positions, nearly 90% of the difference in their profiles was attributable to emotional intelligence factors rather than cognitive abilities.

Idea in Practice

Understanding EI'S Components

El Component	Definition	Hallmarks	Example
Self-awareness	Knowing one's emotions, strengths, weaknesses, drives, values, and goals—and their impact on others	• Self-confidence • Realistic self-assessment • Self-deprecating sense of humor • Thirst for constructive criticism	A manager knows tight deadlines bring out the worst in him. So he plans his time to get work done well in advance.
Self-regulation	Controlling or redirecting disruptive emotions and impulses	• Trustworthiness • Integrity • Comfort with ambiguity and change	When a team botches a presentation, its leader resists the urge to scream. Instead, she considers possible reasons for the failure, explains the consequences to her team, and explores solutions with them.
Motivation	Being driven to achieve for the sake of achievement	• A passion for the work itself and for new challenges • Unflagging energy to improve • Optimism in the face of failure	A portfolio manager at an investment company sees his fund tumble for three consecutive quarters. Major clients defect. Instead of blaming external circumstances, she decides to learn from the experience—and engineers a turnaround.

Empathy	Considering others' feelings, especially when making decisions	• Expertise in attracting and retaining talent • Ability to develop others • Sensitivity to cross-cultural differences	An American consultant and her team pitch a project to a potential client in Japan. Her team interprets the client's silence as disapproval, and prepares to leave. The consultant reads the client's body language and senses interest. She continues the meeting, and her team gets the job.
Social Skill	Managing relationships to move people in desired directions	• Effectiveness in leading change • Persuasiveness • Extensive networking • Expertise in building and leading teams	A manager wants his company to adopt a better Internet strategy. He finds kindred spirits and assembles a de facto team to create a prototype Web site. He persuades allies in other divisions to fund the company's participation in a relevant convention. His company forms an Internet division—and puts him in charge of it.

Strengthening Your EI

Use practice and feedback from others to strengthen specific EI skills.

Example: An executive learned from others that she lacked empathy, especially the ability to listen. She wanted to fix the problem, so she asked a coach to tell her when she exhibited poor listening skills. She then role-played incidents to practice giving better responses; for example, not interrupting. She also began observing executives skilled at listening—and imitated their behavior.

The five components of emotional intelligence at work

	Definition	Hallmarks
Self-awareness	The ability to recognize and understand your moods, emotions, and drives, as well as their effect on others	Self-confidence Realistic self-assessment Self-deprecating sense of humor
Self-Regulation	The ability to control or redirect disruptive impulses and moods The propensity to suspend judgment—to think before acting	Trustworthiness and integrity Comfort with ambiguity Openness to change
Motivation	A passion to work for reasons that go beyond money or status A propensity to pursue goals with energy and persistence	Strong drive to achieve Optimism, even in the face of failure Organizational commitment
Empathy	The ability to understand the emotional makeup of other people Skill in treating people according to their emotional reactions	Expertise in building and retaining talent Cross-cultural sensitivity Service to clients and customers
Social Skill	Proficiency in managing relationships and building networks An ability to find common ground and build rapport	Effectiveness in leading change Persuasiveness Expertise in building and leading teams

Other researchers have confirmed that emotional intelligence not only distinguishes outstanding leaders but can also be linked to strong performance. The findings of the late David McClelland, the renowned researcher in human and organizational behavior, are a good example. In a 1996 study of a global food and beverage company, McClelland found that when senior managers had a critical mass of emotional intelligence capabilities, their divisions outperformed yearly earnings goals by 20%. Meanwhile, division leaders without that critical mass underperformed by almost the same amount. McClelland's findings, interestingly, held as true in the company's U.S. divisions as in its divisions in Asia and Europe.

In short, the numbers are beginning to tell us a persuasive story about the link between a company's success and the emotional intelligence of its leaders. And just as important, research is also demonstrating that people can, if they take the right approach, develop their emotional intelligence. (See the

sidebar “Can Emotional Intelligence Be Learned?”)

Self-Awareness

Self-awareness is the first component of emotional intelligence—which makes sense when one considers that the Delphic oracle gave the advice to “know thyself” thousands of years ago. Self-awareness means having a deep understanding of one’s emotions, strengths, weaknesses, needs, and drives. People with strong self-awareness are neither overly critical nor unrealistically hopeful. Rather, they are honest—with themselves and with others.

People who have a high degree of self-awareness recognize how their feelings affect them, other people, and their job performance. Thus, a self-aware person who knows that tight deadlines bring out the worst in him plans his time carefully and gets his work done well in advance. Another person with high self-awareness will be able to work with a demanding client. She will understand the client’s impact on her moods and the deeper reasons for her frustration. “Their trivial demands take us away from the real work that needs to be done,” she might explain. And she will go one step further and turn her anger into something constructive.

Can Emotional Intelligence Be Learned?

FOR AGES, PEOPLE HAVE DEBATED if leaders are born or made. So too goes the debate about emotional intelligence. Are people born with certain levels of empathy, for example, or do they acquire empathy as a result of life's experiences? The answer is both. Scientific inquiry strongly suggests that there is a genetic component to emotional intelligence. Psychological and developmental research indicates that nurture plays a role as well. How much of each perhaps will never be known, but research and practice clearly demonstrate that emotional intelligence can be learned.

One thing is certain: Emotional intelligence increases with age. There is an old-fashioned word for the phenomenon: maturity. Yet even with maturity, some people still need training to enhance their emotional intelligence. Unfortunately, far too many training programs that intend to build leadership skills—including emotional intelligence—are a waste of time and money. The problem is simple: They focus on the wrong part of the brain.

Emotional intelligence is born largely in the neurotransmitters of the brain's limbic system, which governs feelings, impulses, and drives. Research indicates that the limbic system learns best through motivation, extended practice, and feedback. Compare this with the kind of learning that goes on in the neocortex, which governs analytical and technical ability. The neocortex grasps concepts and logic. It is the part of the brain that figures out how to use a computer or make a sales call by reading a book. Not surprisingly—but mistakenly—it is also the part of the brain targeted by most training programs aimed at enhancing emotional intelligence. When such programs take, in effect, a neocortical approach, my research with the Consortium for Research on Emotional Intelligence in Organizations has shown they can even have a *negative* impact on people's job performance.

To enhance emotional intelligence, organizations must refocus their training to include the limbic system. They must help people break old behavioral habits and establish new ones. That not only takes much more time than conventional training programs, it also requires an individualized approach.

Imagine an executive who is thought to be low on empathy by her colleagues. Part of that deficit shows itself as an inability to listen; she interrupts people and doesn't pay close attention to what they're saying. To fix the problem, the executive needs to be motivated to change, and then she needs practice and feedback from others in the company. A colleague or coach could be tapped to let the executive know when she has been observed failing to listen. She would then have to replay the incident and give a better response; that is, demonstrate her ability to absorb what others are saying. And the executive could be directed to observe certain executives who listen well and to mimic their behavior.

With persistence and practice, such a process can lead to lasting results. I know one Wall Street executive who sought to improve his empathy—specifically his ability to read people's reactions and see their perspectives. Before beginning his quest, the executive's subordinates were terrified of working with him. People even went so far as to hide bad news from him. Naturally, he was shocked when finally confronted with these facts. He went home and told his family—but they only confirmed what he had heard at work. When their opinions on any given subject did not mesh with his, they, too, were frightened of him.

Enlisting the help of a coach, the executive went to work to heighten his empathy through practice and feedback. His first step was to take a vacation to a foreign country where he did not speak the language. While there, he monitored his reactions to the unfamiliar and his openness to people who were different from him. When he returned home, humbled by his week abroad, the executive asked his coach to

shadow him for parts of the day, several times a week, to critique how he treated people with new or different perspectives. At the same time, he consciously used on-the-job interactions as opportunities to practice “hearing” ideas that differed from his. Finally, the executive had himself videotaped in meetings and asked those who worked for and with him to critique his ability to acknowledge and understand the feelings of others. It took several months, but the executive’s emotional intelligence did ultimately rise, and the improvement was reflected in his overall performance on the job.

It’s important to emphasize that building one’s emotional intelligence cannot—will not—happen without sincere desire and concerted effort. A brief seminar won’t help; nor can one buy a how-to manual. It is much harder to learn to empathize—to internalize empathy as a natural response to people—than it is to become adept at regression analysis. But it can be done. “Nothing great was ever achieved without enthusiasm,” wrote Ralph Waldo Emerson. If your goal is to become a real leader, these words can serve as a guidepost in your efforts to develop high emotional intelligence.

Self-awareness extends to a person’s understanding of his or her values and goals. Someone who is highly self-aware knows where he is headed and why; so, for example, he will be able to be firm in turning down a job offer that is tempting financially but does not fit with his principles or long-term goals. A person who lacks self-awareness is apt to make decisions that bring on inner turmoil by treading on buried values. “The money looked good so I signed on,” someone might say two years into a job, “but the work means so little to me that I’m constantly bored.” The decisions of self-aware people mesh with their values; consequently, they often find work to be energizing.

How can one recognize self-awareness? First and foremost, it shows itself as candor and an ability to assess oneself realistically. People with high self-awareness are able to speak accurately and openly—although not necessarily effusively or confessionally—about their emotions and the impact they have on their work. For instance, one manager I know of was skeptical about a new personal-shopper service that her company, a major department-store

chain, was about to introduce. Without prompting from her team or her boss, she offered them an explanation: “It’s hard for me to get behind the rollout of this service,” she admitted, “because I really wanted to run the project, but I wasn’t selected. Bear with me while I deal with that.” The manager did indeed examine her feelings; a week later, she was supporting the project fully.

Such self-knowledge often shows itself in the hiring process. Ask a candidate to describe a time he got carried away by his feelings and did something he later regretted. Self-aware candidates will be frank in admitting to failure—and will often tell their tales with a smile. One of the hallmarks of self-awareness is a self-deprecating sense of humor.

Self-awareness can also be identified during performance reviews. Self-aware people know—and are comfortable talking about—their limitations and strengths, and they often demonstrate a thirst for constructive criticism. By contrast, people with low self-awareness interpret the message that they need to improve as a threat or a sign of failure.

Self-aware people can also be recognized by their self-confidence. They have a firm grasp of their capabilities and are less likely to set themselves up to fail by, for example, overstretching on assignments. They know, too, when to ask for help. And the risks they take on the job are calculated. They won’t ask for a challenge that they know they can’t handle alone. They’ll play to their strengths.

Consider the actions of a midlevel employee who was invited to sit in on a strategy meeting with her company’s top executives. Although she was the most junior person in the room, she did not sit there quietly, listening in awestruck or fearful silence. She knew she had a head for clear logic and the skill to present ideas persuasively, and she offered cogent suggestions about the company’s strategy. At the same time, her self-awareness stopped her from wandering into territory where she knew she was weak.

Despite the value of having self-aware people in the workplace, my research indicates that senior executives don’t often give self-awareness the credit it deserves when they look for potential leaders. Many executives mistake candor about feelings for “wimpiness” and fail to give due respect to employees who openly acknowledge their shortcomings. Such people are too readily dismissed as “not tough enough” to lead others.

In fact, the opposite is true. In the first place, people generally admire and respect candor. Furthermore, leaders are constantly required to make

judgment calls that require a candid assessment of capabilities—their own and those of others. Do we have the management expertise to acquire a competitor? Can we launch a new product within six months? People who assess themselves honestly—that is, self-aware people—are well suited to do the same for the organizations they run.

Self-Regulation

Biological impulses drive our emotions. We cannot do away with them—but we can do much to manage them. Self-regulation, which is like an ongoing inner conversation, is the component of emotional intelligence that frees us from being prisoners of our feelings. People engaged in such a conversation feel bad moods and emotional impulses just as everyone else does, but they find ways to control them and even to channel them in useful ways.

Imagine an executive who has just watched a team of his employees present a botched analysis to the company's board of directors. In the gloom that follows, the executive might find himself tempted to pound on the table in anger or kick over a chair. He could leap up and scream at the group. Or he might maintain a grim silence, glaring at everyone before stalking off.

But if he had a gift for self-regulation, he would choose a different approach. He would pick his words carefully, acknowledging the team's poor performance without rushing to any hasty judgment. He would then step back to consider the reasons for the failure. Are they personal—a lack of effort? Are there any mitigating factors? What was his role in the debacle? After considering these questions, he would call the team together, lay out the incident's consequences, and offer his feelings about it. He would then present his analysis of the problem and a well-considered solution.

Why does self-regulation matter so much for leaders? First of all, people who are in control of their feelings and impulses—that is, people who are reasonable—are able to create an environment of trust and fairness. In such an environment, politics and infighting are sharply reduced and productivity is high. Talented people flock to the organization and aren't tempted to leave. And self-regulation has a trickle-down effect. No one wants to be known as a hothead when the boss is known for her calm approach. Fewer bad moods at the top mean fewer throughout the organization.

Second, self-regulation is important for competitive reasons. Everyone knows that business today is rife with ambiguity and change. Companies merge and break apart regularly. Technology transforms work at a dizzying

pace. People who have mastered their emotions are able to roll with the changes. When a new program is announced, they don't panic; instead, they are able to suspend judgment, seek out information, and listen to the executives as they explain the new program. As the initiative moves forward, these people are able to move with it.

Sometimes they even lead the way. Consider the case of a manager at a large manufacturing company. Like her colleagues, she had used a certain software program for five years. The program drove how she collected and reported data and how she thought about the company's strategy. One day, senior executives announced that a new program was to be installed that would radically change how information was gathered and assessed within the organization. While many people in the company complained bitterly about how disruptive the change would be, the manager mulled over the reasons for the new program and was convinced of its potential to improve performance. She eagerly attended training sessions—some of her colleagues refused to do so—and was eventually promoted to run several divisions, in part because she used the new technology so effectively.

I want to push the importance of self-regulation to leadership even further and make the case that it enhances integrity, which is not only a personal virtue but also an organizational strength. Many of the bad things that happen in companies are a function of impulsive behavior. People rarely plan to exaggerate profits, pad expense accounts, dip into the till, or abuse power for selfish ends. Instead, an opportunity presents itself, and people with low impulse control just say yes.

By contrast, consider the behavior of the senior executive at a large food company. The executive was scrupulously honest in his negotiations with local distributors. He would routinely lay out his cost structure in detail, thereby giving the distributors a realistic understanding of the company's pricing. This approach meant the executive couldn't always drive a hard bargain. Now, on occasion, he felt the urge to increase profits by withholding information about the company's costs. But he challenged that impulse—he saw that it made more sense in the long run to counteract it. His emotional self-regulation paid off in strong, lasting relationships with distributors that benefited the company more than any short-term financial gains would have.

The signs of emotional self-regulation, therefore, are easy to see: a propensity for reflection and thoughtfulness; comfort with ambiguity and change; and integrity—an ability to say no to impulsive urges.

Like self-awareness, self-regulation often does not get its due. People who can master their emotions are sometimes seen as cold fish—their considered responses are taken as a lack of passion. People with fiery temperaments are frequently thought of as “classic” leaders—their outbursts are considered hallmarks of charisma and power. But when such people make it to the top, their impulsiveness often works against them. In my research, extreme displays of negative emotion have never emerged as a driver of good leadership.

Motivation

If there is one trait that virtually all effective leaders have, it is motivation. They are driven to achieve beyond expectations—their own and everyone else's. The key word here is *achieve*. Plenty of people are motivated by external factors, such as a big salary or the status that comes from having an impressive title or being part of a prestigious company. By contrast, those with leadership potential are motivated by a deeply embedded desire to achieve for the sake of achievement.

If you are looking for leaders, how can you identify people who are motivated by the drive to achieve rather than by external rewards? The first sign is a passion for the work itself—such people seek out creative challenges, love to learn, and take great pride in a job well done. They also display an unflagging energy to do things better. People with such energy often seem restless with the status quo. They are persistent with their questions about why things are done one way rather than another; they are eager to explore new approaches to their work.

A cosmetics company manager, for example, was frustrated that he had to wait two weeks to get sales results from people in the field. He finally tracked down an automated phone system that would beep each of his salespeople at 5 pm every day. An automated message then prompted them to punch in their numbers—how many calls and sales they had made that day. The system shortened the feedback time on sales results from weeks to hours.

That story illustrates two other common traits of people who are driven to achieve. They are forever raising the performance bar, and they like to keep score. Take the performance bar first. During performance reviews, people with high levels of motivation might ask to be “stretched” by their superiors. Of course, an employee who combines self-awareness with internal motivation will recognize her limits—but she won't settle for objectives that seem too easy to fulfill.

And it follows naturally that people who are driven to do better also want a way of tracking progress—their own, their team's, and their company's.

Whereas people with low achievement motivation are often fuzzy about results, those with high achievement motivation often keep score by tracking such hard measures as profitability or market share. I know of a money manager who starts and ends his day on the Internet, gauging the performance of his stock fund against four industry-set benchmarks.

Interestingly, people with high motivation remain optimistic even when the score is against them. In such cases, self-regulation combines with achievement motivation to overcome the frustration and depression that come after a setback or failure. Take the case of another portfolio manager at a large investment company. After several successful years, her fund tumbled for three consecutive quarters, leading three large institutional clients to shift their business elsewhere.

Some executives would have blamed the nosedive on circumstances outside their control; others might have seen the setback as evidence of personal failure. This portfolio manager, however, saw an opportunity to prove she could lead a turnaround. Two years later, when she was promoted to a very senior level in the company, she described the experience as “the best thing that ever happened to me; I learned so much from it.”

Executives trying to recognize high levels of achievement motivation in their people can look for one last piece of evidence: commitment to the organization. When people love their jobs for the work itself, they often feel committed to the organizations that make that work possible. Committed employees are likely to stay with an organization even when they are pursued by headhunters waving money.

It's not difficult to understand how and why a motivation to achieve translates into strong leadership. If you set the performance bar high for yourself, you will do the same for the organization when you are in a position to do so. Likewise, a drive to surpass goals and an interest in keeping score can be contagious. Leaders with these traits can often build a team of managers around them with the same traits. And of course, optimism and organizational commitment are fundamental to leadership—just try to imagine running a company without them.

Empathy

Of all the dimensions of emotional intelligence, empathy is the most easily recognized. We have all felt the empathy of a sensitive teacher or friend; we have all been struck by its absence in an unfeeling coach or boss. But when it comes to business, we rarely hear people praised, let alone rewarded, for their empathy. The very word seems unbusinesslike, out of place amid the tough realities of the marketplace.

But empathy doesn't mean a kind of "I'm OK, you're OK" mushiness. For a leader, that is, it doesn't mean adopting other people's emotions as one's own and trying to please everybody. That would be a nightmare—it would make action impossible. Rather, empathy means thoughtfully considering employees' feelings—along with other factors—in the process of making intelligent decisions.

For an example of empathy in action, consider what happened when two giant brokerage companies merged, creating redundant jobs in all their divisions. One division manager called his people together and gave a gloomy speech that emphasized the number of people who would soon be fired. The manager of another division gave his people a different kind of speech. He was up-front about his own worry and confusion, and he promised to keep people informed and to treat everyone fairly.

The difference between these two managers was empathy. The first manager was too worried about his own fate to consider the feelings of his anxiety-stricken colleagues. The second knew intuitively what his people were feeling, and he acknowledged their fears with his words. Is it any surprise that the first manager saw his division sink as many demoralized people, especially the most talented, departed? By contrast, the second manager continued to be a strong leader, his best people stayed, and his division remained as productive as ever.

Empathy is particularly important today as a component of leadership for at least three reasons: the increasing use of teams; the rapid pace of globalization; and the growing need to retain talent.

Consider the challenge of leading a team. As anyone who has ever been a part of one can attest, teams are cauldrons of bubbling emotions. They are often charged with reaching a consensus—which is hard enough with two people and much more difficult as the numbers increase. Even in groups with as few as four or five members, alliances form and clashing agendas get set. A team's leader must be able to sense and understand the viewpoints of everyone around the table.

That's exactly what a marketing manager at a large information technology company was able to do when she was appointed to lead a troubled team. The group was in turmoil, overloaded by work and missing deadlines. Tensions were high among the members. Tinkering with procedures was not enough to bring the group together and make it an effective part of the company.

So the manager took several steps. In a series of one-on-one sessions, she took the time to listen to everyone in the group—what was frustrating them, how they rated their colleagues, whether they felt they had been ignored. And then she directed the team in a way that brought it together: She encouraged people to speak more openly about their frustrations, and she helped people raise constructive complaints during meetings. In short, her empathy allowed her to understand her team's emotional makeup. The result was not just heightened collaboration among members but also added business, as the team was called on for help by a wider range of internal clients.

Globalization is another reason for the rising importance of empathy for business leaders. Cross-cultural dialogue can easily lead to miscues and misunderstandings. Empathy is an antidote. People who have it are attuned to subtleties in body language; they can hear the message beneath the words being spoken. Beyond that, they have a deep understanding of both the existence and the importance of cultural and ethnic differences.

Consider the case of an American consultant whose team had just pitched a project to a potential Japanese client. In its dealings with Americans, the team was accustomed to being bombarded with questions after such a proposal, but this time it was greeted with a long silence. Other members of the team, taking the silence as disapproval, were ready to pack and leave. The lead consultant gestured them to stop. Although he was not particularly familiar with Japanese culture, he read the client's face and posture and sensed not rejection but interest—even deep consideration. He was right: When the client finally spoke, it was to give the consulting firm the job.

Finally, empathy plays a key role in the retention of talent, particularly in today's information economy. Leaders have always needed empathy to develop and keep good people, but today the stakes are higher. When good people leave, they take the company's knowledge with them.

That's where coaching and mentoring come in. It has repeatedly been shown that coaching and mentoring pay off not just in better performance but also in increased job satisfaction and decreased turnover. But what makes coaching and mentoring work best is the nature of the relationship. Outstanding coaches and mentors get inside the heads of the people they are helping. They sense how to give effective feedback. They know when to push for better performance and when to hold back. In the way they motivate their protégés, they demonstrate empathy in action.

In what is probably sounding like a refrain, let me repeat that empathy doesn't get much respect in business. People wonder how leaders can make hard decisions if they are "feeling" for all the people who will be affected. But leaders with empathy do more than sympathize with people around them: They use their knowledge to improve their companies in subtle but important ways.

Social Skill

The first three components of emotional intelligence are self- management skills. The last two, empathy and social skill, concern a person's ability to manage relationships with others. As a component of emotional intelligence, social skill is not as simple as it sounds. It's not just a matter of friendliness, although people with high levels of social skill are rarely mean-spirited. Social skill, rather, is friendliness with a purpose: moving people in the direction you desire, whether that's agreement on a new marketing strategy or enthusiasm about a new product.

Socially skilled people tend to have a wide circle of acquaintances, and they have a knack for finding common ground with people of all kinds—a knack for building rapport. That doesn't mean they socialize continually; it means they work according to the assumption that nothing important gets done alone. Such people have a network in place when the time for action comes.

Social skill is the culmination of the other dimensions of emotional intelligence. People tend to be very effective at managing relationships when they can understand and control their own emotions and can empathize with the feelings of others. Even motivation contributes to social skill. Remember that people who are driven to achieve tend to be optimistic, even in the face of setbacks or failure. When people are upbeat, their “glow” is cast upon conversations and other social encounters. They are popular, and for good reason.

Because it is the outcome of the other dimensions of emotional intelligence, social skill is recognizable on the job in many ways that will by now sound familiar. Socially skilled people, for instance, are adept at managing teams—that's their empathy at work. Likewise, they are expert persuaders—a manifestation of self-awareness, self-regulation, and empathy combined. Given those skills, good persuaders know when to make an emotional plea, for instance, and when an appeal to reason will work better. And motivation, when publicly visible, makes such people excellent

collaborators; their passion for the work spreads to others, and they are driven to find solutions.

But sometimes social skill shows itself in ways the other emotional intelligence components do not. For instance, socially skilled people may at times appear not to be working while at work. They seem to be idly schmoozing—chatting in the hallways with colleagues or joking around with people who are not even connected to their “real” jobs. Socially skilled people, however, don’t think it makes sense to arbitrarily limit the scope of their relationships. They build bonds widely because they know that in these fluid times, they may need help someday from people they are just getting to know today.

For example, consider the case of an executive in the strategy department of a global computer manufacturer. By 1993, he was convinced that the company’s future lay with the Internet. Over the course of the next year, he found kindred spirits and used his social skill to stitch together a virtual community that cut across levels, divisions, and nations. He then used this de facto team to put up a corporate Web site, among the first by a major company. And, on his own initiative, with no budget or formal status, he signed up the company to participate in an annual Internet industry convention. Calling on his allies and persuading various divisions to donate funds, he recruited more than 50 people from a dozen different units to represent the company at the convention.

Management took notice: Within a year of the conference, the executive’s team formed the basis for the company’s first Internet division, and he was formally put in charge of it. To get there, the executive had ignored conventional boundaries, forging and maintaining connections with people in every corner of the organization.

Is social skill considered a key leadership capability in most companies? The answer is yes, especially when compared with the other components of emotional intelligence. People seem to know intuitively that leaders need to manage relationships effectively; no leader is an island. After all, the leader’s task is to get work done through other people, and social skill makes that possible. A leader who cannot express her empathy may as well not have it at all. And a leader’s motivation will be useless if he cannot communicate his passion to the organization. Social skill allows leaders to put their emotional intelligence to work.

It would be foolish to assert that good-old-fashioned IQ and technical

ability are not important ingredients in strong leadership. But the recipe would not be complete without emotional intelligence. It was once thought that the components of emotional intelligence were “nice to have” in business leaders. But now we know that, for the sake of performance, these are ingredients that leaders “need to have.”

It is fortunate, then, that emotional intelligence can be learned. The process is not easy. It takes time and, most of all, commitment. But the benefits that come from having a well-developed emotional intelligence, both for the individual and for the organization, make it worth the effort.

Originally published in June 1996. Reprint R0401H

What Makes an Effective Executive

by Peter F. Drucker

AN EFFECTIVE EXECUTIVE DOES NOT need to be a leader in the sense that the term is now most commonly used. Harry Truman did not have one ounce of charisma, for example, yet he was among the most effective chief executives in U.S. history. Similarly, some of the best business and nonprofit CEOs I've worked with over a 65-year consulting career were not stereotypical leaders. They were all over the map in terms of their personalities, attitudes, values, strengths, and weaknesses. They ranged from extroverted to nearly reclusive, from easygoing to controlling, from generous to parsimonious.

What made them all effective is that they followed the same eight practices:

- They asked, "What needs to be done?"
- They asked, "What is right for the enterprise?"
- They developed action plans.
- They took responsibility for decisions.
- They took responsibility for communicating.
- They were focused on opportunities rather than problems.
- They ran productive meetings.
- They thought and said "we" rather than "I."

The first two practices gave them the knowledge they needed. The next four helped them convert this knowledge into effective action. The last two ensured that the whole organization felt responsible and accountable.

Get the Knowledge You Need

The first practice is to ask what needs to be done. Note that the question is not “What do I want to do?” Asking what has to be done, and taking the question seriously, is crucial for managerial success. Failure to ask this question will render even the ablest executive ineffectual.

When Truman became president in 1945, he knew exactly what he wanted to do: complete the economic and social reforms of Roosevelt’s New Deal, which had been deferred by World War II. As soon as he asked what needed to be done, though, Truman realized that foreign affairs had absolute priority. He organized his working day so that it began with tutorials on foreign policy by the secretaries of state and defense. As a result, he became the most effective president in foreign affairs the United States has ever known. He contained Communism in both Europe and Asia and, with the Marshall Plan, triggered 50 years of worldwide economic growth.

Similarly, Jack Welch realized that what needed to be done at General Electric when he took over as chief executive was not the overseas expansion he wanted to launch. It was getting rid of GE businesses that, no matter how profitable, could not be number one or number two in their industries.

The answer to the question “What needs to be done?” almost always contains more than one urgent task. But effective executives do not splinter themselves. They concentrate on one task if at all possible. If they are among those people—a sizable minority—who work best with a change of pace in their working day, they pick two tasks. I have never encountered an executive who remains effective while tackling more than two tasks at a time. Hence, after asking what needs to be done, the effective executive sets priorities and sticks to them. For a CEO, the priority task might be redefining the company’s mission. For a unit head, it might be redefining the unit’s relationship with headquarters. Other tasks, no matter how important or appealing, are postponed. However, after completing the original top-priority task, the executive resets priorities rather than moving on to number two from the original list. He asks, “What must be done now?” This generally results in

new and different priorities.



Idea in Brief

Worried that you're not a born leader? That you lack charisma, the right talents, or some other secret ingredient? No need: leadership isn't about personality or talent. In fact, the best leaders exhibit wildly different personalities, attitudes, values, and strengths—they're extroverted or reclusive, easygoing or controlling, generous or parsimonious, numbers or vision oriented.

So what do effective leaders have in common? They get the right things done, in the right ways—by following eight simple rules:

- Ask what needs to be done.
- Ask what's right for the enterprise.
- Develop action plans.
- Take responsibility for decisions.
- Take responsibility for communicating.
- Focus on opportunities, not problems.
- Run productive meetings.
- Think and say "We," not "I."

Using discipline to apply these rules, you gain the knowledge you need to make smart decisions, convert that knowledge into effective action, and ensure accountability throughout your organization.

To refer again to America's best-known CEO: Every five years, according to his autobiography, Jack Welch asked himself, "What needs to be done *now*?" And every time, he came up with a new and different priority.

But Welch also thought through another issue before deciding where to concentrate his efforts for the next five years. He asked himself which of the two or three tasks at the top of the list he himself was best suited to undertake. Then he concentrated on that task; the others he delegated. Effective executives try to focus on jobs they'll do especially well. They

know that enterprises perform if top management performs—and don't if it doesn't.



Idea in Practice

Get the Knowledge You Need

Ask what needs to be done. When Jack Welch asked this question while taking over as CEO at General Electric, he realized that dropping GE businesses that couldn't be first or second in their industries was essential—not the overseas expansion he had wanted to launch. Once you know what must be done, identify tasks you're best at, concentrating on one at a time. After completing a task, reset priorities based on new realities.

Ask what's right for the enterprise. Don't agonize over what's best for owners, investors, employees, or customers. Decisions that are right for your *enterprise* are ultimately right for all stakeholders.

Convert Your Knowledge into Action **Develop action plans.** Devise plans that specify *desired results* and *constraints* (Is the course of action legal and compatible with the company's mission, values, and policies?). Include *check-in points* and *implications for how you'll spend your time*. And *revise* plans to reflect new opportunities.

Take responsibility for decisions. Ensure that each decision specifies who's accountable for carrying it out, when it must be implemented, who'll be affected by it, and who must be informed. Regularly review decisions, especially hires and promotions. This enables you to correct poor decisions before doing real damage.

Take responsibility for communicating. Get input from superiors,

subordinates, and peers on your action plans. Let each know what information you need to get the job done. Pay equal attention to peers' and superiors' information needs.

Focus on opportunities, not problems. You get results by exploiting opportunities, not solving problems. Identify changes inside and outside your organization (new technologies, product innovations, new market structures), asking "How can we exploit this change to benefit our enterprise?" Then match your best people with the best opportunities.

Ensure Companywide Accountability Run productive meetings. Articulate each meeting's purpose (Making an announcement? Delivering a report?). Terminate the meeting once the purpose is accomplished. Follow up with short communications summarizing the discussion, spelling out new work assignments and deadlines for completing them. General Motors CEO Alfred Sloan's legendary mastery of meeting follow-up helped secure GM's industry dominance in the mid-twentieth century.

Think and say "We," not "I." Your authority comes from your organization's trust in you. To get the best results, always consider your organization's needs and opportunities before your own.

Effective executives' second practice—fully as important as the first—is to ask, "Is this the right thing for the enterprise?" They do not ask if it's right for the owners, the stock price, the employees, or the executives. Of course they know that shareholders, employees, and executives are important constituencies who have to support a decision, or at least acquiesce in it, if the choice is to be effective. They know that the share price is important not only for the shareholders but also for the enterprise, since the price/earnings ratio sets the cost of capital. But they also know that a decision that isn't right for the enterprise will ultimately not be right for any of the stakeholders.

This second practice is especially important for executives at family owned or family run businesses—the majority of businesses in every country

—particularly when they’re making decisions about people. In the successful family company, a relative is promoted only if he or she is measurably superior to all nonrelatives on the same level. At DuPont, for instance, all top managers (except the controller and lawyer) were family members in the early years when the firm was run as a family business. All male descendants of the founders were entitled to entry-level jobs at the company. Beyond the entrance level, a family member got a promotion only if a panel composed primarily of nonfamily managers judged the person to be superior in ability and performance to all other employees at the same level. The same rule was observed for a century in the highly successful British family business J. Lyons & Company (now part of a major conglomerate) when it dominated the British food-service and hotel industries.

Asking “What is right for the enterprise?” does not guarantee that the right decision will be made. Even the most brilliant executive is human and thus prone to mistakes and prejudices. But failure to ask the question virtually guarantees the *wrong* decision.

Write an Action Plan

Executives are doers; they execute. Knowledge is useless to executives until it has been translated into deeds. But before springing into action, the executive needs to plan his course. He needs to think about desired results, probable restraints, future revisions, check-in points, and implications for how he'll spend his time.

First, the executive defines desired results by asking: "What contributions should the enterprise expect from me over the next 18 months to two years? What results will I commit to? With what deadlines?" Then he considers the restraints on action: "Is this course of action ethical? Is it acceptable within the organization? Is it legal? Is it compatible with the mission, values, and policies of the organization?" Affirmative answers don't guarantee that the action will be effective. But violating these restraints is certain to make it both wrong and ineffectual.

The action plan is a statement of intentions rather than a commitment. It must not become a straitjacket. It should be revised often, because every success creates new opportunities. So does every failure. The same is true for changes in the business environment, in the market, and especially in people within the enterprise—all these changes demand that the plan be revised. A written plan should anticipate the need for flexibility.

In addition, the action plan needs to create a system for checking the results against the expectations. Effective executives usually build two such checks into their action plans. The first check comes halfway through the plan's time period; for example, at nine months. The second occurs at the end, before the next action plan is drawn up.

Finally, the action plan has to become the basis for the executive's time management. Time is an executive's scarcest and most precious resource. And organizations—whether government agencies, businesses, or nonprofits—are inherently time wasters. The action plan will prove useless unless it's allowed to determine how the executive spends his or her time.

Napoleon allegedly said that no successful battle ever followed its plan.

Yet Napoleon also planned every one of his battles, far more meticulously than any earlier general had done. Without an action plan, the executive becomes a prisoner of events. And without check-ins to reexamine the plan as events unfold, the executive has no way of knowing which events really matter and which are only noise.

Act

When they translate plans into action, executives need to pay particular attention to decision making, communication, opportunities (as opposed to problems), and meetings. I'll consider these one at a time.

Take responsibility for decisions

A decision has not been made until people know:

- the name of the person accountable for carrying it out;
- the deadline;
- the names of the people who will be affected by the decision and therefore have to know about, understand, and approve it—or at least not be strongly opposed to it—and
- the names of the people who have to be informed of the decision, even if they are not directly affected by it.

An extraordinary number of organizational decisions run into trouble because these bases aren't covered. One of my clients, 30 years ago, lost its leadership position in the fast-growing Japanese market because the company, after deciding to enter into a joint venture with a new Japanese partner, never made clear who was to inform the purchasing agents that the partner defined its specifications in meters and kilograms rather than feet and pounds—and nobody ever did relay that information.

It's just as important to review decisions periodically—at a time that's been agreed on in advance—as it is to make them carefully in the first place. That way, a poor decision can be corrected before it does real damage. These reviews can cover anything from the results to the assumptions underlying the decision.

Such a review is especially important for the most crucial and most difficult of all decisions, the ones about hiring or promoting people. Studies of decisions about people show that only one-third of such choices turn out to be truly successful. One-third are likely to be draws—neither successes nor outright failures. And one-third are failures, pure and simple. Effective executives know this and check up (six to nine months later) on the results of their people decisions. If they find that a decision has not had the desired

results, they don't conclude that the person has not performed. They conclude, instead, that they themselves made a mistake. In a well-managed enterprise, it is understood that people who fail in a new job, especially after a promotion, may not be the ones to blame.

Executives also owe it to the organization and to their fellow workers not to tolerate nonperforming individuals in important jobs. It may not be the employees' fault that they are underperforming, but even so, they have to be removed. People who have failed in a new job should be given the choice to go back to a job at their former level and salary. This option is rarely exercised; such people, as a rule, leave voluntarily, at least when their employers are U.S. firms. But the very existence of the option can have a powerful effect, encouraging people to leave safe, comfortable jobs and take risky new assignments. The organization's performance depends on employees' willingness to take such chances.

A systematic decision review can be a powerful tool for self-development, too. Checking the results of a decision against its expectations shows executives what their strengths are, where they need to improve, and where they lack knowledge or information. It shows them their biases. Very often it shows them that their decisions didn't produce results because they didn't put the right people on the job. Allocating the best people to the right positions is a crucial, tough job that many executives slight, in part because the best people are already too busy. Systematic decision review also shows executives their own weaknesses, particularly the areas in which they are simply incompetent. In these areas, smart executives don't make decisions or take actions. They delegate. Everyone has such areas; there's no such thing as a universal executive genius.

Most discussions of decision making assume that only senior executives make decisions or that only senior executives' decisions matter. This is a dangerous mistake. Decisions are made at every level of the organization, beginning with individual professional contributors and frontline supervisors. These apparently low-level decisions are extremely important in a knowledge-based organization. Knowledge workers are supposed to know more about their areas of specialization—for example, tax accounting—than anybody else, so their decisions are likely to have an impact throughout the company. Making good decisions is a crucial skill at every level. It needs to be taught explicitly to everyone in organizations that are based on knowledge.

Take responsibility for communicating

Effective executives make sure that both their action plans and their information needs are understood. Specifically, this means that they share their plans with and ask for comments from all their colleagues—superiors, subordinates, and peers. At the same time, they let each person know what information they'll need to get the job done. The information flow from subordinate to boss is usually what gets the most attention. But executives need to pay equal attention to peers' and superiors' information needs.

We all know, thanks to Chester Barnard's 1938 classic *The Functions of the Executive*, that organizations are held together by information rather than by ownership or command. Still, far too many executives behave as if information and its flow were the job of the information specialist—for example, the accountant. As a result, they get an enormous amount of data they do not need and cannot use, but little of the information they do need. The best way around this problem is for each executive to identify the information he needs, ask for it, and keep pushing until he gets it.

Focus on opportunities

Good executives focus on opportunities rather than problems. Problems have to be taken care of, of course; they must not be swept under the rug. But problem solving, however necessary, does not produce results. It prevents damage. Exploiting opportunities produces results.

Above all, effective executives treat change as an opportunity rather than a threat. They systematically look at changes, inside and outside the corporation, and ask, “How can we exploit this change as an opportunity for our enterprise?” Specifically, executives scan these seven situations for opportunities:

- an unexpected success or failure in their own enterprise, in a competing enterprise, or in the industry;
- a gap between what is and what could be in a market, process, product, or service (for example, in the nineteenth century, the paper industry concentrated on the 10% of each tree that became wood pulp and totally neglected the possibilities in the remaining 90%, which became waste);
- innovation in a process, product, or service, whether inside or outside the enterprise or its industry;
- changes in industry structure and market structure;
- demographics;
- changes in mind-set, values, perception, mood, or meaning; and
- new knowledge or a new technology.

Effective executives also make sure that problems do not overwhelm opportunities. In most companies, the first page of the monthly management report lists key problems. It’s far wiser to list opportunities on the first page and leave problems for the second page. Unless there is a true catastrophe, problems are not discussed in management meetings until opportunities have been analyzed and properly dealt with.

Staffing is another important aspect of being opportunity focused. Effective executives put their best people on opportunities rather than on problems. One way to staff for opportunities is to ask each member of the management group to prepare two lists every six months—a list of opportunities for the entire enterprise and a list of the best-performing people throughout the enterprise. These are discussed, then melded into two master lists, and the best people are matched with the best opportunities. In Japan, by the way, this matchup is considered a major HR task in a big corporation or government department; that practice is one of the key strengths of Japanese business.

Make meetings productive

The most visible, powerful, and, arguably, effective nongovernmental executive in the America of World War II and the years thereafter was not a businessman. It was Francis Cardinal Spellman, the head of the Roman Catholic Archdiocese of New York and adviser to several U.S. presidents. When Spellman took over, the diocese was bankrupt and totally demoralized. His successor inherited the leadership position in the American Catholic church. Spellman often said that during his waking hours he was alone only twice each day, for 25 minutes each time: when he said Mass in his private chapel after getting up in the morning and when he said his evening prayers before going to bed. Otherwise he was always with people in a meeting, starting at breakfast with one Catholic organization and ending at dinner with another.

Top executives aren't quite as imprisoned as the archbishop of a major Catholic diocese. But every study of the executive workday has found that even junior executives and professionals are with other people—that is, in a meeting of some sort—more than half of every business day. The only exceptions are a few senior researchers. Even a conversation with only one other person is a meeting. Hence, if they are to be effective, executives must make meetings productive. They must make sure that meetings are work sessions rather than bull sessions.

The key to running an effective meeting is to decide in advance what kind of meeting it will be. Different kinds of meetings require different forms of preparation and different results.

A meeting to prepare a statement, an announcement, or a press release. For this to be productive, one member has to prepare a draft beforehand. At the meeting's end, a preappointed member has to take responsibility for disseminating the final text.

A meeting to make an announcement—for example, an organizational change. This meeting should be confined to the

announcement and a discussion about it.

A meeting in which one member reports. Nothing but the report should be discussed.

A meeting in which several or all members report. Either there should be no discussion at all or the discussion should be limited to questions for clarification. Alternatively, for each report there could be a short discussion in which all participants may ask questions. If this is the format, the reports should be distributed to all participants well before the meeting. At this kind of meeting, each report should be limited to a preset time—for example, 15 minutes.

A meeting to inform the convening executive. The executive should listen and ask questions. He or she should sum up but not make a presentation.

A meeting whose only function is to allow the participants to be in the executive's presence. Cardinal Spellman's breakfast and dinner meetings were of that kind. There is no way to make these meetings productive. They are the penalties of rank. Senior executives are effective to the extent to which they can prevent such meetings from encroaching on their workdays. Spellman, for instance, was effective in large part because he confined such meetings to breakfast and dinner and kept the rest of his working day free of them.

Making a meeting productive takes a good deal of self-discipline. It requires that executives determine what kind of meeting is appropriate and then stick to that format. It's also necessary to terminate the meeting as soon as its specific purpose has been accomplished. Good executives don't raise another matter for discussion. They sum up and adjourn.

Good follow-up is just as important as the meeting itself. The great master of follow-up was Alfred Sloan, the most effective business executive I have ever known. Sloan, who headed General Motors from the 1920s until the 1950s, spent most of his six working days a week in meetings—three days a week in formal committee meetings with a set membership, the other three days in ad hoc meetings with individual GM executives or with a small group

of executives. At the beginning of a formal meeting, Sloan announced the meeting's purpose. He then listened. He never took notes and he rarely spoke except to clarify a confusing point. At the end he summed up, thanked the participants, and left. Then he immediately wrote a short memo addressed to one attendee of the meeting. In that note, he summarized the discussion and its conclusions and spelled out any work assignment decided upon in the meeting (including a decision to hold another meeting on the subject or to study an issue). He specified the deadline and the executive who was to be accountable for the assignment. He sent a copy of the memo to everyone who'd been present at the meeting. It was through these memos—each a small masterpiece—that Sloan made himself into an outstandingly effective executive.

Effective executives know that any given meeting is either productive or a total waste of time.

Think and Say “We”

The final practice is this: Don’t think or say “I.” Think and say “we.” Effective executives know that they have ultimate responsibility, which can be neither shared nor delegated. But they have authority only because they have the trust of the organization. This means that they think of the needs and the opportunities of the organization before they think of their own needs and opportunities. This one may sound simple; it isn’t, but it needs to be strictly observed.

We’ve just reviewed eight practices of effective executives. I’m going to throw in one final, bonus practice. This one’s so important that I’ll elevate it to the level of a rule: *Listen first, speak last.*

Effective executives differ widely in their personalities, strengths, weaknesses, values, and beliefs. All they have in common is that they get the right things done. Some are born effective. But the demand is much too great to be satisfied by extraordinary talent. Effectiveness is a discipline. And, like every discipline, effectiveness *can* be learned and *must* be earned.

Originally published in June 2004. Reprint R0406C

What Leaders Really Do

by John P. Kotter

LEADERSHIP IS DIFFERENT FROM MANAGEMENT, but not for the reasons most people think. Leadership isn't mystical and mysterious. It has nothing to do with having "charisma" or other exotic personality traits. It is not the province of a chosen few. Nor is leadership necessarily better than management or a replacement for it.

Rather, leadership and management are two distinctive and complementary systems of action. Each has its own function and characteristic activities. Both are necessary for success in an increasingly complex and volatile business environment.

Most U.S. corporations today are over-managed and underled. They need to develop their capacity to exercise leadership. Successful corporations don't wait for leaders to come along. They actively seek out people with leadership potential and expose them to career experiences designed to develop that potential. Indeed, with careful selection, nurturing, and encouragement, dozens of people can play important leadership roles in a business organization.

But while improving their ability to lead, companies should remember that strong leadership with weak management is no better, and is sometimes actually worse, than the reverse. The real challenge is to combine strong leadership and strong management and use each to balance the other.

Of course, not everyone can be good at both leading and managing. Some people have the capacity to become excellent managers but not strong leaders. Others have great leadership potential but, for a variety of reasons,

have great difficulty becoming strong managers. Smart companies value both kinds of people and work hard to make them a part of the team.

But when it comes to preparing people for executive jobs, such companies rightly ignore the recent literature that says people cannot manage *and* lead. They try to develop leader-managers. Once companies understand the fundamental difference between leadership and management, they can begin to groom their top people to provide both.

The Difference Between Management and Leadership

Management is about coping with complexity. Its practices and procedures are largely a response to one of the most significant developments of the twentieth century: the emergence of large organizations. Without good management, complex enterprises tend to become chaotic in ways that threaten their very existence. Good management brings a degree of order and consistency to key dimensions like the quality and profitability of products.

Leadership, by contrast, is about coping with change. Part of the reason it has become so important in recent years is that the business world has become more competitive and more volatile. Faster technological change, greater international competition, the deregulation of markets, overcapacity in capital-intensive industries, an unstable oil cartel, raiders with junk bonds, and the changing demographics of the work-force are among the many factors that have contributed to this shift. The net result is that doing what was done yesterday, or doing it 5% better, is no longer a formula for success. Major changes are more and more necessary to survive and compete effectively in this new environment. More change always demands more leadership.

Consider a simple military analogy: A peacetime army can usually survive with good administration and management up and down the hierarchy, coupled with good leadership concentrated at the very top. A wartime army, however, needs competent leadership at all levels. No one yet has figured out how to manage people effectively into battle; they must be led.

Idea in Brief

The most pernicious half-truth about leadership is that it's just a matter of charisma and vision—you either have it or you don't. The fact of the matter is that leadership skills are not innate. They can be acquired, and honed. But first you have to appreciate how they differ from management skills.

Management is about coping with *complexity*; it brings order and predictability to a situation. But that's no longer enough—to succeed, companies must be able to adapt to change. Leadership, then, is about learning how to cope with rapid *change*.

How does this distinction play out?

- Management involves planning and budgeting. Leadership involves setting direction.
- Management involves organizing and staffing. Leadership involves aligning people.
- Management provides control and solves problems. Leadership provides motivation.

These two different functions—coping with complexity and coping with change—shape the characteristic activities of management and leadership. Each system of action involves deciding what needs to be done, creating networks of people and relationships that can accomplish an agenda, and then trying to ensure that those people actually do the job. But each accomplishes these three tasks in different ways.

Companies manage complexity first by *planning and budgeting*—setting

targets or goals for the future (typically for the next month or year), establishing detailed steps for achieving those targets, and then allocating resources to accomplish those plans. By contrast, leading an organization to constructive change begins by *setting a direction*—developing a vision of the future (often the distant future) along with strategies for producing the changes needed to achieve that vision.

Management develops the capacity to achieve its plan by *organizing and staffing*—creating an organizational structure and set of jobs for accomplishing plan requirements, staffing the jobs with qualified individuals, communicating the plan to those people, delegating responsibility for carrying out the plan, and devising systems to monitor implementation. The equivalent leadership activity, however, is *aligning people*. This means communicating the new direction to those who can create coalitions that understand the vision and are committed to its achievement.

Idea in Practice

Management and leadership both involve deciding what needs to be done, creating networks of people to accomplish the agenda, and ensuring that the work actually gets done. Their work is complementary, but each system of action goes about the tasks in different ways.

1. Planning and budgeting versus setting direction. The aim of management is predictability—orderly results. Leadership’s function is to produce change. Setting the direction of that change, therefore, is essential work. There’s nothing mystical about this work, but it is more inductive than planning and budgeting. It involves the search for patterns and relationships. And it doesn’t produce detailed plans; instead, direction-setting results in visions and the overarching strategies for realizing them.

Example: In mature industries, increased competition usually dampens growth. But at American Express, Lou Gerstner bucked this trend, successfully crafting a vision of a dynamic enterprise.

The new direction he set wasn’t a mere attention-grabbing scheme—it was the result of asking fundamental questions about market and competitive forces.

2. Organizing and staffing versus aligning people. Managers look for the right fit between people and jobs. This is essentially a design problem: setting up systems to ensure that plans are implemented precisely and efficiently. Leaders, however, look for the right fit between people and the vision. This is more of a communication problem. It involves getting a large number of people, inside and outside the company, first to believe in an alternative future—and then to take initiative based on that shared vision.

3. Controlling activities and solving problems versus motivating and inspiring. Management strives to make it easy for people to complete routine jobs day after day. But since high energy is essential to overcoming the barriers to change, leaders attempt to touch people at their deepest levels—by stirring in them a sense of belonging, idealism, and self-esteem.

Example: At Procter & Gamble’s paper products division, Richard Nicolosi underscored the message that “each of us is a leader” by pushing responsibility down to newly formed teams. An entrepreneurial attitude took root, and profits rebounded.

Finally, management ensures plan accomplishment by *controlling and problem solving*—monitoring results versus the plan in some detail, both formally and informally, by means of reports, meetings, and other tools; identifying deviations; and then planning and organizing to solve the problems. But for leadership, achieving a vision requires *motivating and inspiring*—keeping people moving in the right direction, despite major obstacles to change, by appealing to basic but often untapped human needs, values, and emotions.

A closer examination of each of these activities will help clarify the skills leaders need.

Setting a Direction Versus Planning and Budgeting

Since the function of leadership is to produce change, setting the direction of that change is fundamental to leadership. Setting direction is never the same as planning or even long-term planning, although people often confuse the two. Planning is a management process, deductive in nature and designed to produce orderly results, not change. Setting a direction is more inductive. Leaders gather a broad range of data and look for patterns, relationships, and linkages that help explain things. What's more, the direction-setting aspect of leadership does not produce plans; it creates vision and strategies. These describe a business, technology, or corporate culture in terms of what it should become over the long term and articulate a feasible way of achieving this goal.

Most discussions of vision have a tendency to degenerate into the mystical. The implication is that a vision is something mysterious that mere mortals, even talented ones, could never hope to have. But developing good business direction isn't magic. It is a tough, sometimes exhausting process of gathering and analyzing information. People who articulate such visions aren't magicians but broad-based strategic thinkers who are willing to take risks.

Aligning People: Chuck Trowbridge and Bob Crandall at Eastman Kodak

EASTMAN KODAK ENTERED THE copy business in the early 1970s, concentrating on technically sophisticated machines that sold, on average, for about \$60,000 each. Over the next decade, this business grew to nearly \$1 billion in revenues. But costs were high, profits were hard to find, and problems were nearly everywhere. In 1984, Kodak had to write off \$40 million in inventory. Most people at the company knew there were problems, but they couldn't agree on how to solve them. So in his first two months as general manager of the new copy products group, established in 1984, Chuck Trowbridge met with nearly every key person inside his group, as well as with people elsewhere at Kodak who could be important to the copier business. An especially crucial area was the engineering and manufacturing organization, headed by Bob Crandall.

Trowbridge and Crandall's vision for engineering and manufacturing was simple: to become a world-class manufacturing operation and to create a less bureaucratic and more decentralized organization. Still, this message was difficult to convey because it was such a radical departure from previous communications, not only in the copy products group but throughout most of Kodak. So Crandall set up dozens of vehicles to emphasize the new direction and align people to it: weekly meetings with his own 12 direct reports; monthly "copy product forums" in which a different employee from each of his departments would meet with him as a group; discussions of recent improvements and new projects to achieve still better results; and quarterly "State of the Department" meetings, where his managers met with everybody in their own departments.

Once a month, Crandall and all those who reported to him would also

meet with 80 to 100 people from some area of his organization to discuss anything they wanted. To align his biggest supplier—the Kodak Apparatus Division, which supplied one-third of the parts used in design and manufacturing—he and his managers met with the top management of that group over lunch every Thursday. Later, he created a format called “business meetings,” where his managers meet with 12 to 20 people on a specific topic, such as inventory or master scheduling. The goal: to get all of his 1,500 employees in at least one of these focused business meetings each year.

Trowbridge and Crandall also enlisted written communication in their cause. A four- to eight-page “Copy Products Journal” was sent to employees once a month. A program called “Dialog Letters” gave employees the opportunity to anonymously ask questions of Crandall and his top managers and be guaranteed a reply. But the most visible and powerful written communications were the charts. In a main hallway near the cafeteria, these huge charts vividly reported the quality, cost, and delivery results for each product, measured against difficult targets. A hundred smaller versions of these charts were scattered throughout the manufacturing area, reporting quality levels and costs for specific work groups.

Results of this intensive alignment process began to appear within six months, and still more surfaced after a year. These successes made the message more credible and helped get more people on board. Between 1984 and 1988, quality on one of the main product lines increased nearly 100-fold. Defects per unit went from 30 to 0.3. Over a three-year period, costs on another product line went down nearly 24%. Deliveries on schedule increased from 82% in 1985 to 95% in 1987. Inventory levels dropped by over 50% between 1984 and 1988, even though the volume of products was increasing. And productivity, measured in units per manufacturing employee, more than doubled between 1985 and 1988.

Nor do visions and strategies have to be brilliantly innovative; in fact,

some of the best are not. Effective business visions regularly have an almost mundane quality, usually consisting of ideas that are already well known. The particular combination or patterning of the ideas may be new, but sometimes even that is not the case.

For example, when CEO Jan Carlzon articulated his vision to make Scandinavian Airlines System (SAS) the best airline in the world for the frequent business traveler, he was not saying anything that everyone in the airline industry didn't already know. Business travelers fly more consistently than other market segments and are generally willing to pay higher fares. Thus, focusing on business customers offers an airline the possibility of high margins, steady business, and considerable growth. But in an industry known more for bureaucracy than vision, no company had ever put these simple ideas together and dedicated itself to implementing them. SAS did, and it worked.

Setting a Direction: Lou Gerstner at American Express

WHEN LOU GERSTNER BECAME PRESIDENT of the Travel Related Services (TRS) arm at American Express in 1979, the unit was facing one of its biggest challenges in AmEx's 130-year history. Hundreds of banks offering or planning to introduce credit cards through Visa and MasterCard that would compete with the American Express card. And more than two dozen financial service firms were coming into the traveler's checks business. In a mature marketplace, this increase in competition usually reduces margins and prohibits growth.

But that was not how Gerstner saw the business. Before joining American Express, he had spent five years as a consultant to TRS, analyzing the money-losing travel division and the increasingly competitive card operation. Gerstner and his team asked fundamental questions about the economics, market, and competition and developed a deep understanding of the business. In the process, he began to craft a vision of TRS that looked nothing like a 130-year-old company in a mature industry.

Gerstner thought TRS had the potential to become a dynamic and growing enterprise, despite the onslaught of Visa and MasterCard competition from thousands of banks. The key was to focus on the global marketplace and, specifically, on the relatively affluent customer American Express had been traditionally serving with top-of-the-line products. By further segmenting this market, aggressively developing a broad range of new products and services, and investing to increase productivity and to lower costs, TRS could provide the best service possible to customers who had enough discretionary income to buy many more services from TRS than they had in the past.

Within a week of his appointment, Gerstner brought together the people running the card organization and questioned all the principles by which they conducted their business. In particular, he challenged two widely shared beliefs—that the division should have only one product, the green card, and that this product was limited in potential for growth and innovation.

Gerstner also moved quickly to develop a more entrepreneurial culture, to hire and train people who would thrive in it, and to clearly communicate to them the overall direction. He and other top managers rewarded intelligent risk taking. To make entrepreneurship easier, they discouraged unnecessary bureaucracy. They also upgraded hiring standards and created the TRS Graduate Management Program, which offered high-potential young people special training, an enriched set of experiences, and an unusual degree of exposure to people in top management. To encourage risk taking among all TRS employees, Gerstner also established something called the Great Performers program to recognize and reward truly exceptional customer service, a central tenet in the organization's vision.

These incentives led quickly to new markets, products, and services. TRS expanded its overseas presence dramatically. By 1988, AmEx cards were issued in 29 currencies (as opposed to only 11 a decade earlier). The unit also focused aggressively on two market segments that had historically received little attention: college students and women. In 1981, TRS combined its card and travel-service capabilities to offer corporate clients a unified system to monitor and control travel expenses. And by 1988, AmEx had grown to become the fifth largest direct-mail merchant in the United States.

Other new products and services included 90-day insurance on all purchases made with the AmEx card, a Platinum American Express card, and a revolving credit card known as Optima. In 1988, the company also switched to image-processing technology for billing, producing a more convenient monthly statement for customers and

reducing billing costs by 25%.

As a result of these innovations, TRS's net income increased a phenomenal 500% between 1978 and 1987—a compounded annual rate of about 18%. The business outperformed many so-called high-tech/high-growth companies. With a 1988 return on equity of 28%, it also outperformed most low-growth but high-profit businesses.

What's crucial about a vision is not its originality but how well it serves the interests of important constituencies—customers, stockholders, employees—and how easily it can be translated into a realistic competitive strategy. Bad visions tend to ignore the legitimate needs and rights of important constituencies—favoring, say, employees over customers or stockholders. Or they are strategically unsound. When a company that has never been better than a weak competitor in an industry suddenly starts talking about becoming number one, that is a pipe dream, not a vision.

One of the most frequent mistakes that overmanaged and underled corporations make is to embrace long-term planning as a panacea for their lack of direction and inability to adapt to an increasingly competitive and dynamic business environment. But such an approach misinterprets the nature of direction setting and can never work.

Long-term planning is always time consuming. Whenever something unexpected happens, plans have to be redone. In a dynamic business environment, the unexpected often becomes the norm, and long-term planning can become an extraordinarily burdensome activity. That is why most successful corporations limit the time frame of their planning activities. Indeed, some even consider “long-term planning” a contradiction in terms.

In a company without direction, even short-term planning can become a black hole capable of absorbing an infinite amount of time and energy. With no vision and strategy to provide constraints around the planning process or to guide it, every eventuality deserves a plan. Under these circumstances, contingency planning can go on forever, draining time and attention from far more essential activities, yet without ever providing the clear sense of direction that a company desperately needs. After awhile, managers inevitably become cynical, and the planning process can degenerate into a

highly politicized game.

Planning works best not as a substitute for direction setting but as a complement to it. A competent planning process serves as a useful reality check on direction-setting activities. Likewise, a competent direction-setting process provides a focus in which planning can then be realistically carried out. It helps clarify what kind of planning is essential and what kind is irrelevant.

Aligning People Versus Organizing and Staffing

A central feature of modern organizations is interdependence, where no one has complete autonomy, where most employees are tied to many others by their work, technology, management systems, and hierarchy. These linkages present a special challenge when organizations attempt to change. Unless many individuals line up and move together in the same direction, people will tend to fall all over one another. To executives who are overeducated in management and undereducated in leadership, the idea of getting people moving in the same direction appears to be an organizational problem. What executives need to do, however, is not organize people but align them.

Managers “organize” to create human systems that can implement plans as precisely and efficiently as possible. Typically, this requires a number of potentially complex decisions. A company must choose a structure of jobs and reporting relationships, staff it with individuals suited to the jobs, provide training for those who need it, communicate plans to the workforce, and decide how much authority to delegate and to whom. Economic incentives also need to be constructed to accomplish the plan, as well as systems to monitor its implementation. These organizational judgments are much like architectural decisions. It’s a question of fit within a particular context.

Aligning is different. It is more of a communications challenge than a design problem. Aligning invariably involves talking to many more individuals than organizing does. The target population can involve not only a manager’s subordinates but also bosses, peers, staff in other parts of the organization, as well as suppliers, government officials, and even customers. Anyone who can help implement the vision and strategies or who can block implementation is relevant.

Trying to get people to comprehend a vision of an alternative future is also a communications challenge of a completely different magnitude from organizing them to fulfill a short-term plan. It’s much like the difference between a football quarterback attempting to describe to his team the next two or three plays versus his trying to explain to them a totally new approach

to the game to be used in the second half of the season.

Whether delivered with many words or a few carefully chosen symbols, such messages are not necessarily accepted just because they are understood. Another big challenge in leadership efforts is credibility—getting people to believe the message. Many things contribute to credibility: the track record of the person delivering the message, the content of the message itself, the communicator's reputation for integrity and trustworthiness, and the consistency between words and deeds.

Finally, aligning leads to empowerment in a way that organizing rarely does. One of the reasons some organizations have difficulty adjusting to rapid changes in markets or technology is that so many people in those companies feel relatively powerless. They have learned from experience that even if they correctly perceive important external changes and then initiate appropriate actions, they are vulnerable to someone higher up who does not like what they have done. Reprimands can take many different forms: "That's against policy," or "We can't afford it," or "Shut up and do as you're told."

Alignment helps overcome this problem by empowering people in at least two ways. First, when a clear sense of direction has been communicated throughout an organization, lower-level employees can initiate actions without the same degree of vulnerability. As long as their behavior is consistent with the vision, superiors will have more difficulty reprimanding them. Second, because everyone is aiming at the same target, the probability is less that one person's initiative will be stalled when it comes into conflict with someone else's.

Motivating People Versus Controlling and Problem Solving

Since change is the function of leadership, being able to generate highly energized behavior is important for coping with the inevitable barriers to change. Just as direction setting identifies an appropriate path for movement and just as effective alignment gets people moving down that path, successful motivation ensures that they will have the energy to overcome obstacles.

According to the logic of management, control mechanisms compare system behavior with the plan and take action when a deviation is detected. In a well-managed factory, for example, this means the planning process establishes sensible quality targets, the organizing process builds an organization that can achieve those targets, and a control process makes sure that quality lapses are spotted immediately, not in 30 or 60 days, and corrected.

For some of the same reasons that control is so central to management, highly motivated or inspired behavior is almost irrelevant. Managerial processes must be as close as possible to fail-safe and risk free. That means they cannot be dependent on the unusual or hard to obtain. The whole purpose of systems and structures is to help normal people who behave in normal ways to complete routine jobs successfully, day after day. It's not exciting or glamorous. But that's management.

Leadership is different. Achieving grand visions always requires a burst of energy. Motivation and inspiration energize people, not by pushing them in the right direction as control mechanisms do but by satisfying basic human needs for achievement, a sense of belonging, recognition, self-esteem, a feeling of control over one's life, and the ability to live up to one's ideals. Such feelings touch us deeply and elicit a powerful response.

Good leaders motivate people in a variety of ways. First, they always articulate the organization's vision in a manner that stresses the values of the audience they are addressing. This makes the work important to those individuals. Leaders also regularly involve people in deciding how to achieve

the organization's vision (or the part most relevant to a particular individual). This gives people a sense of control. Another important motivational technique is to support employee efforts to realize the vision by providing coaching, feedback, and role modeling, thereby helping people grow professionally and enhancing their self-esteem. Finally, good leaders recognize and reward success, which not only gives people a sense of accomplishment but also makes them feel like they belong to an organization that cares about them. When all this is done, the work itself becomes intrinsically motivating.

The more that change characterizes the business environment, the more that leaders must motivate people to provide leadership as well. When this works, it tends to reproduce leadership across the entire organization, with people occupying multiple leadership roles throughout the hierarchy. This is highly valuable, because coping with change in any complex business demands initiatives from a multitude of people. Nothing less will work.

Motivating People: Richard Nicolosi at Procter and Gamble

FOR ABOUT 20 YEARS AFTER ITS FOUNDING in 1956, Procter & Gamble's paper products division had experienced little competition for its high-quality, reasonably priced, and well-marketed consumer goods. By the late 1970s, however, the market position of the division had changed. New competitive thrusts hurt P&G badly. For example, industry analysts estimate that the company's market share for disposable diapers fell from 75% in the mid-1970s to 52% in 1984.

That year, Richard Nicolosi came to paper products as the associate general manager, after three years in P&G's smaller and faster moving soft-drink business. He found a heavily bureaucratic and centralized organization that was overly preoccupied with internal functional goals and projects. Almost all information about customers came through highly quantitative market research. The technical people were rewarded for cost savings, the commercial people focused on volume and share, and the two groups were nearly at war with each other.

During the late summer of 1984, top management announced that Nicolosi would become the head of paper products in October, and by August he was unofficially running the division. Immediately he began to stress the need for the division to become more creative and market driven, instead of just trying to be a low-cost producer. "I had to make it very clear," Nicolosi later reported, "that the rules of the game had changed."

The new direction included a much greater stress on teamwork and multiple leadership roles. Nicolosi pushed a strategy of using groups

to manage the division and its specific products. In October, he and his team designated themselves as the paper division “board” and began meeting first monthly and then weekly. In November, they established “category teams” to manage their major brand groups (like diapers, tissues, towels) and started pushing responsibility down to these teams. “Shun the incremental,” Nicolosi stressed, “and go for the leap.”

In December, Nicolosi selectively involved himself in more detail in certain activities. He met with the advertising agency and got to know key creative people. He asked the marketing manager of diapers to report directly to him, eliminating a layer in the hierarchy. He talked more to the people who were working on new product development projects.

In January 1985, the board announced a new organizational structure that included not only category teams but also new-brand business teams. By the spring, the board was ready to plan an important motivational event to communicate the new paper products vision to as many people as possible. On June 4, 1985, all the Cincinnati-based personnel in paper plus sales district managers and paper plant managers—several thousand people in all—met in the local Masonic Temple. Nicolosi and other board members described their vision of an organization where “each of us is a leader.” The event was videotaped, and an edited version was sent to all sales offices and plants for everyone to see.

All these activities helped create an entrepreneurial environment where large numbers of people were motivated to realize the new vision. Most innovations came from people dealing with new products. Ultra Pampers, first introduced in February 1985, took the market share of the entire Pampers product line from 40% to 58% and profitability from break-even to positive. And within only a few months of the introduction of Luvs Delux in May 1987, market share for the overall brand grew by 150%.

Other employee initiatives were oriented more toward a functional area, and some came from the bottom of the hierarchy. In the spring of 1986, a few of the division's secretaries, feeling empowered by the new culture, developed a secretaries network. This association established subcommittees on training, on rewards and recognition, and on the "secretary of the future." Echoing the sentiments of many of her peers, one paper products secretary said: "I don't see why we, too, can't contribute to the division's new direction."

By the end of 1988, revenues at the paper products division were up 40% over a four-year period. Profits were up 68%. And this happened despite the fact that the competition continued to get tougher.

Of course, leadership from many sources does not necessarily converge. To the contrary, it can easily conflict. For multiple leadership roles to work together, people's actions must be carefully coordinated by mechanisms that differ from those coordinating traditional management roles.

Strong networks of informal relationships—the kind found in companies with healthy cultures—help coordinate leadership activities in much the same way that formal structure coordinates managerial activities. The key difference is that informal networks can deal with the greater demands for coordination associated with nonroutine activities and change. The multitude of communication channels and the trust among the individuals connected by those channels allow for an ongoing process of accommodation and adaptation. When conflicts arise among roles, those same relationships help resolve the conflicts. Perhaps most important, this process of dialogue and accommodation can produce visions that are linked and compatible instead of remote and competitive. All this requires a great deal more communication than is needed to coordinate managerial roles, but unlike formal structure, strong informal networks can handle it.

Informal relations of some sort exist in all corporations. But too often these networks are either very weak—some people are well connected but most are not—or they are highly fragmented—a strong network exists inside the marketing group and inside R&D but not across the two departments. Such networks do not support multiple leadership initiatives well. In fact,

extensive informal networks are so important that if they do not exist, creating them has to be the focus of activity early in a major leadership initiative.

Creating a Culture of Leadership

Despite the increasing importance of leadership to business success, the on-the-job experiences of most people actually seem to undermine the development of the attributes needed for leadership. Nevertheless, some companies have consistently demonstrated an ability to develop people into outstanding leader-managers. Recruiting people with leadership potential is only the first step. Equally important is managing their career patterns. Individuals who are effective in large leadership roles often share a number of career experiences.

Perhaps the most typical and most important is significant challenge early in a career. Leaders almost always have had opportunities during their twenties and thirties to actually try to lead, to take a risk, and to learn from both triumphs and failures. Such learning seems essential in developing a wide range of leadership skills and perspectives. These opportunities also teach people something about both the difficulty of leadership and its potential for producing change.

Later in their careers, something equally important happens that has to do with broadening. People who provide effective leadership in important jobs always have a chance, before they get into those jobs, to grow beyond the narrow base that characterizes most managerial careers. This is usually the result of lateral career moves or of early promotions to unusually broad job assignments. Sometimes other vehicles help, like special task-force assignments or a lengthy general management course. Whatever the case, the breadth of knowledge developed in this way seems to be helpful in all aspects of leadership. So does the network of relationships that is often acquired both inside and outside the company. When enough people get opportunities like this, the relationships that are built also help create the strong informal networks needed to support multiple leadership initiatives.

Corporations that do a better-than-average job of developing leaders put an emphasis on creating challenging opportunities for relatively young employees. In many businesses, decentralization is the key. By definition, it

pushes responsibility lower in an organization and in the process creates more challenging jobs at lower levels. Johnson & Johnson, 3M, Hewlett-Packard, General Electric, and many other well-known companies have used that approach quite successfully. Some of those same companies also create as many small units as possible so there are a lot of challenging lower-level general management jobs available.

Sometimes these businesses develop additional challenging opportunities by stressing growth through new products or services. Over the years, 3M has had a policy that at least 25% of its revenue should come from products introduced within the last five years. That encourages small new ventures, which in turn offer hundreds of opportunities to test and stretch young people with leadership potential.

Such practices can, almost by themselves, prepare people for small- and medium-sized leadership jobs. But developing people for important leadership positions requires more work on the part of senior executives, often over a long period of time. That work begins with efforts to spot people with great leadership potential early in their careers and to identify what will be needed to stretch and develop them.

Again, there is nothing magic about this process. The methods successful companies use are surprisingly straightforward. They go out of their way to make young employees and people at lower levels in their organizations visible to senior management. Senior managers then judge for themselves who has potential and what the development needs of those people are. Executives also discuss their tentative conclusions among themselves to draw more accurate judgments.

Armed with a clear sense of who has considerable leadership potential and what skills they need to develop, executives in these companies then spend time planning for that development. Sometimes that is done as part of a formal succession planning or high-potential development process; often it is more informal. In either case, the key ingredient appears to be an intelligent assessment of what feasible development opportunities fit each candidate's needs.

To encourage managers to participate in these activities, well-led businesses tend to recognize and reward people who successfully develop leaders. This is rarely done as part of a formal compensation or bonus formula, simply because it is so difficult to measure such achievements with precision. But it does become a factor in decisions about promotion,

especially to the most senior levels, and that seems to make a big difference. When told that future promotions will depend to some degree on their ability to nurture leaders, even people who say that leadership cannot be developed somehow find ways to do it.

Such strategies help create a corporate culture where people value strong leadership and strive to create it. Just as we need more people to provide leadership in the complex organizations that dominate our world today, we also need more people to develop the cultures that will create that leadership. Institutionalizing a leadership-centered culture is the ultimate act of leadership.

Originally published May 1990. Reprint R0111F

The Work of Leadership

by Ronald A. Heifetz and Donald L. Laurie

TO STAY ALIVE, JACK PRITCHARD had to change his life. Triple bypass surgery and medication could help, the heart surgeon told him, but no technical fix could release Pritchard from his own responsibility for changing the habits of a lifetime. He had to stop smoking, improve his diet, get some exercise, and take time to relax, remembering to breathe more deeply each day. Pritchard's doctor could provide sustaining technical expertise and take supportive action, but only Pritchard could adapt his ingrained habits to improve his long-term health. The doctor faced the leadership task of mobilizing the patient to make critical behavioral changes; Jack Pritchard faced the adaptive work of figuring out which specific changes to make and how to incorporate them into his daily life.

Companies today face challenges similar to the ones that confronted Pritchard and his doctor. They face adaptive challenges. Changes in societies, markets, customers, competition, and technology around the globe are forcing organizations to clarify their values, develop new strategies, and learn new ways of operating. Often the toughest task for leaders in effecting change is mobilizing people throughout the organization to do adaptive work.

Adaptive work is required when our deeply held beliefs are challenged, when the values that made us successful become less relevant, and when legitimate yet competing perspectives emerge. We see adaptive challenges every day at every level of the workplace—when companies restructure or reengineer, develop or implement strategy, or merge businesses. We see adaptive challenges when marketing has difficulty working with operations,

when cross-functional teams don't work well, or when senior executives complain, "We don't seem to be able to execute effectively." Adaptive problems are often systemic problems with no ready answers.

Mobilizing an organization to adapt its behaviors in order to thrive in new business environments is critical. Without such change, any company today would falter. Indeed, getting people to do adaptive work is the mark of leadership in a competitive world. Yet for most senior executives, providing leadership and not just authoritative expertise is extremely difficult. Why? We see two reasons. First, in order to make change happen, executives have to break a longstanding behavior pattern of their own: providing leadership in the form of solutions. This tendency is quite natural because many executives reach their positions of authority by virtue of their competence in taking responsibility and solving problems. But the locus of responsibility for problem solving when a company faces an adaptive challenge must shift to its people. Solutions to adaptive challenges reside not in the executive suite but in the collective intelligence of employees at all levels, who need to use one another as resources, often across boundaries, and learn their way to those solutions.

Second, adaptive change is distressing for the people going through it. They need to take on new roles, new relationships, new values, new behaviors, and new approaches to work. Many employees are ambivalent about the efforts and sacrifices required of them. They often look to the senior executive to take problems off their shoulders. But those expectations have to be unlearned. Rather than fulfilling the expectation that they will provide answers, leaders have to ask tough questions. Rather than protecting people from outside threats, leaders should allow them to feel the pinch of reality in order to stimulate them to adapt. Instead of orienting people to their current roles, leaders must disorient them so that new relationships can develop. Instead of quelling conflict, leaders have to draw the issues out. Instead of maintaining norms, leaders have to challenge "the way we do business" and help others distinguish immutable values from historical practices that must go.

Idea in Brief

What presents your company with its toughest challenges? Shifting markets? Stiffening competition? Emerging technologies? When such challenges intensify, you may need to reclarify corporate values, redesign strategies, merge or dissolve businesses, or manage cross-functional strife.

These **adaptive challenges** are murky, systemic problems with no easy answers. Perhaps even more vexing, the solutions to adaptive challenges *don't* reside in the executive suite. Solving them requires the involvement of people *throughout* your organization.

Adaptive work is tough on everyone. For *leaders*, it's counterintuitive. Rather than providing solutions, you must ask tough questions and leverage employees' collective intelligence. Instead of maintaining norms, you must challenge the "way we do business." And rather than quelling conflict, you need to draw issues out and let people feel the sting of reality.

For your *employees*, adaptive work is painful—requiring unfamiliar roles, responsibilities, values, and ways of working. No wonder employees often try to lob adaptive work back to their leaders.

How to ensure that you *and* your employees embrace the challenges of adaptive work? Applying the following six principles will help.

Drawing on our experience with managers from around the world, we offer six principles for leading adaptive work: "getting on the balcony," identifying the adaptive challenge, regulating distress, maintaining disciplined attention, giving the work back to people, and protecting voices of

leadership from below. We illustrate those principles with an example of adaptive change at KPMG Netherlands, a professional-services firm.

Get on the Balcony

Earvin “Magic” Johnson’s greatness in leading his basketball team came in part from his ability to play hard while keeping the whole game situation in mind, as if he stood in a press box or on a balcony above the field of play. Bobby Orr played hockey in the same way. Other players might fail to recognize the larger patterns of play that performers like Johnson and Orr quickly understand, because they are so engaged in the game that they get carried away by it. Their attention is captured by the rapid motion, the physical contact, the roar of the crowd, and the pressure to execute. In sports, most players simply may not see who is open for a pass, who is missing a block, or how the offense and defense work together. Players like Johnson and Orr watch these things and allow their observations to guide their actions.

Idea in Practice

1. Get on the balcony. Don't get swept up in the field of play. Instead, move back and forth between the "action" and the "balcony." You'll spot emerging patterns, such as power struggles or work avoidance. This high-level perspective helps you mobilize people to do adaptive work.

2. Identify your adaptive challenge.

Example: When British Airways' passengers nicknamed it "Bloody Awful," CEO Colin Marshall knew he had to infuse the company with a dedication to customers. He identified the adaptive challenge as "creating trust throughout British Airways." To diagnose the challenge further, Marshall's team mingled with employees and customers in baggage areas, reservation centers, and planes, asking which beliefs, values, and behaviors needed overhauling. They exposed value-based conflicts underlying surface-level disputes, and resolved the team's own dysfunctional conflicts that impaired companywide collaboration. By understanding themselves, their people, and the company's conflicts, the team strengthened British Airways' bid to become "the World's Favourite Airline."

3. Regulate distress. To inspire change—without disabling people—pace adaptive work:

- First, let employees debate issues and clarify assumptions behind competing views—safely.
- Then provide direction. Define *key* issues and values. Control the rate of change: Don't start too many initiatives simultaneously without stopping others.

- Maintain just enough tension, resisting pressure to restore the status quo. Raise tough questions without succumbing to anxiety yourself. Communicate presence and poise.

4. Maintain disciplined attention. Encourage managers to grapple with divisive issues, rather than indulging in scapegoating or denial. Deepen the debate to unlock polarized, superficial conflict. Demonstrate collaboration to solve problems.

5. Give the work back to employees. To instill collective self-confidence—versus dependence on you—support rather than control people. Encourage risk-taking and responsibility—then back people up if they err. Help them recognize they contain the solutions.

6. Protect leadership voices from below. Don't silence whistleblowers, creative deviants, and others exposing contradictions within your company. Their perspectives can provoke fresh thinking. Ask, "What is this guy *really* talking about? Have we missed something?"

Business leaders have to be able to view patterns as if they were on a balcony. It does them no good to be swept up in the field of action. Leaders have to see a context for change or create one. They should give employees a strong sense of the history of the enterprise and what's good about its past, as well as an idea of the market forces at work today and the responsibility people must take in shaping the future. Leaders must be able to identify struggles over values and power, recognize patterns of work avoidance, and watch for the many other functional and dysfunctional reactions to change.

Without the capacity to move back and forth between the field of action and the balcony, to reflect day to day, moment to moment, on the many ways in which an organization's habits can sabotage adaptive work, a leader easily and unwittingly becomes a prisoner of the system. The dynamics of adaptive

change are far too complex to keep track of, let alone influence, if leaders stay only on the field of play.

We have encountered several leaders, some of whom we discuss in this article, who manage to spend much of their precious time on the balcony as they guide their organizations through change. Without that perspective, they probably would have been unable to mobilize people to do adaptive work. Getting on the balcony is thus a prerequisite for following the next five principles.

Identify the Adaptive Challenge

When a leopard threatens a band of chimpanzees, the leopard rarely succeeds in picking off a stray. Chimps know how to respond to this kind of threat. But when a man with an automatic rifle comes near, the routine responses fail. Chimps risk extinction in a world of poachers unless they figure out how to disarm the new threat. Similarly, when businesses cannot learn quickly to adapt to new challenges, they are likely to face their own form of extinction.

Consider the well-known case of British Airways. Having observed the revolutionary changes in the airline industry during the 1980s, then chief executive Colin Marshall clearly recognized the need to transform an airline nicknamed Bloody Awful by its own passengers into an exemplar of customer service. He also understood that this ambition would require more than anything else changes in values, practices, and relationships throughout the company. An organization whose people clung to functional silos and valued pleasing their bosses more than pleasing customers could not become “the world’s favorite airline.” Marshall needed an organization dedicated to serving people, acting on trust, respecting the individual, and making teamwork happen across boundaries. Values had to change throughout British Airways. People had to learn to collaborate and to develop a collective sense of responsibility for the direction and performance of the airline. Marshall identified the essential adaptive challenge: creating trust throughout the organization. He is one of the first executives we have known to make “creating trust” a priority.

To lead British Airways, Marshall had to get his executive team to understand the nature of the threat created by dissatisfied customers: Did it represent a technical challenge or an adaptive challenge? Would expert advice and technical adjustments within basic routines suffice, or would people throughout the company have to learn different ways of doing business, develop new competencies, and begin to work collectively?

Marshall and his team set out to diagnose in more detail the organization’s challenges. They looked in three places. First, they listened to the ideas and

concerns of people inside and outside the organization—meeting with crews on flights, showing up in the 350-person reservations center in New York, wandering around the baggage-handling area in Tokyo, or visiting the passenger lounge in whatever airport they happened to be in. Their primary questions were, Whose values, beliefs, attitudes, or behaviors would have to change in order for progress to take place? What shifts in priorities, resources, and power were necessary? What sacrifices would have to be made and by whom?

Second, Marshall and his team saw conflicts as clues—symptoms of adaptive challenges. The way conflicts across functions were being expressed were mere surface phenomena; the underlying conflicts had to be diagnosed. Disputes over seemingly technical issues such as procedures, schedules, and lines of authority were in fact proxies for underlying conflicts about values and norms.

Third, Marshall and his team held a mirror up to themselves, recognizing that they embodied the adaptive challenges facing the organization. Early in the transformation of British Airways, competing values and norms were played out on the executive team in dysfunctional ways that impaired the capacity of the rest of the company to collaborate across functions and units and make the necessary trade-offs. No executive can hide from the fact that his or her team reflects the best and the worst of the company's values and norms, and therefore provides a case in point for insight into the nature of the adaptive work ahead.

Thus, identifying its adaptive challenge was crucial in British Airways' bid to become the world's favorite airline. For the strategy to succeed, the company's leaders needed to understand themselves, their people, and the potential sources of conflict. Marshall recognized that strategy development itself requires adaptive work.

Regulate Distress

Adaptive work generates distress. Before putting people to work on challenges for which there are no ready solutions, a leader must realize that people can learn only so much so fast. At the same time, they must feel the need to change as reality brings new challenges. They cannot learn new ways when they are overwhelmed, but eliminating stress altogether removes the impetus for doing adaptive work. Because a leader must strike a delicate balance between having people feel the need to change and having them feel overwhelmed by change, leadership is a razor's edge.

A leader must attend to three fundamental tasks in order to help maintain a productive level of tension. Adhering to these tasks will allow him or her to motivate people without disabling them. First, a leader must create what can be called a *holding environment*. To use the analogy of a pressure cooker, a leader needs to regulate the pressure by turning up the heat while also allowing some steam to escape. If the pressure exceeds the cooker's capacity, the cooker can blow up. However, nothing cooks without some heat.

In the early stages of a corporate change, the holding environment can be a temporary "place" in which a leader creates the conditions for diverse groups to talk to one another about the challenges facing them, to frame and debate issues, and to clarify the assumptions behind competing perspectives and values. Over time, more issues can be phased in as they become ripe. At British Airways, for example, the shift from an internal focus to a customer focus took place over four or five years and dealt with important issues in succession: building a credible executive team, communicating with a highly fragmented organization, defining new measures of performance and compensation, and developing sophisticated information systems. During that time, employees at all levels learned to identify what and how they needed to change.

Thus, a leader must sequence and pace the work. Too often, senior managers convey that everything is important. They start new initiatives without stopping other activities, or they start too many initiatives at the same

time. They overwhelm and disorient the very people who need to take responsibility for the work.

Second, a leader is responsible for direction, protection, orientation, managing conflict, and shaping norms. (See the exhibit “Adaptive Work Calls for Leadership.”) Fulfilling these responsibilities is also important for a manager in technical or routine situations. But a leader engaged in adaptive work uses his authority to fulfill them differently. A leader provides direction by identifying the organization’s adaptive challenge and framing the key questions and issues. A leader protects people by managing the rate of change. A leader orients people to new roles and responsibilities by clarifying business realities and key values. A leader helps expose conflict, viewing it as the engine of creativity and learning. Finally, a leader helps the organization maintain those norms that must endure and challenge those that need to change.

Adaptive work calls for leadership

In the course of regulating people's distress, a leader faces several key responsibilities and may have to use his or her authority differently depending on the type of work situation.

Leader's responsibilities	Type of situation	
	Technical or routine	Adaptive
Direction	Define problems and provide solutions	Identify the adaptive challenge and frame key questions and issues
Protection	Shield the organization from external threats	Let the organization feel external pressures within a range it can stand
Orientation	Clarify roles and responsibilities	Challenge current roles and resist pressure to define new roles quickly
Managing conflict	Restore order	Expose conflict or let it emerge
Shaping norms	Maintain norms	Challenge unproductive norms

Third, a leader must have presence and poise; regulating distress is perhaps a leader's most difficult job. The pressures to restore equilibrium are enormous. Just as molecules bang hard against the walls of a pressure cooker, people bang up against leaders who are trying to sustain the pressures of tough, conflict-filled work. Although leadership demands a deep understanding of the pain of change—the fears and sacrifices associated with major readjustment—it also requires the ability to hold steady and maintain the tension. Otherwise, the pressure escapes and the stimulus for learning and change is lost.

A leader has to have the emotional capacity to tolerate uncertainty, frustration, and pain. He has to be able to raise tough questions without getting too anxious himself. Employees as well as colleagues and customers will carefully observe verbal and nonverbal cues to a leader's ability to hold steady. He needs to communicate confidence that he and they can tackle the

tasks ahead.

Maintain Disciplined Attention

Different people within the same organization bring different experiences, assumptions, values, beliefs, and habits to their work. This diversity is valuable because innovation and learning are the products of differences. No one learns anything without being open to contrasting points of view. Yet managers at all levels are often unwilling—or unable—to address their competing perspectives collectively. They frequently avoid paying attention to issues that disturb them. They restore equilibrium quickly, often with work avoidance maneuvers. A leader must get employees to confront tough trade-offs in values, procedures, operating styles, and power.

That is as true at the top of the organization as it is in the middle or on the front line. Indeed, if the executive team cannot model adaptive work, the organization will languish. If senior managers can't draw out and deal with divisive issues, how will people elsewhere in the organization change their behaviors and rework their relationships? As Jan Carlzon, the legendary CEO of Scandinavian Airlines System (SAS), told us, "One of the most interesting missions of leadership is getting people on the executive team to listen to and learn from one another. Held in debate, people can learn their way to collective solutions when they understand one another's assumptions. The work of the leader is to get conflict out into the open and use it as a source of creativity."

Because work avoidance is rampant in organizations, a leader has to counteract distractions that prevent people from dealing with adaptive issues. Scapegoating, denial, focusing only on today's technical issues, or attacking individuals rather than the perspectives they represent—all forms of work avoidance—are to be expected when an organization undertakes adaptive work. Distractions have to be identified when they occur so that people will regain focus.

When sterile conflict takes the place of dialogue, a leader has to step in and put the team to work on reframing the issues. She has to deepen the debate with questions, unbundling the issues into their parts rather than

letting conflict remain polarized and superficial. When people preoccupy themselves with blaming external forces, higher management, or a heavy workload, a leader has to sharpen the team's sense of responsibility for carving out the time to press forward. When the team fragments and individuals resort to protecting their own turf, leaders have to demonstrate the need for collaboration. People have to discover the value of consulting with one another and using one another as resources in the problem-solving process. For example, one CEO we know uses executive meetings, even those that focus on operational and technical issues, as opportunities to teach the team how to work collectively on adaptive problems.

Of course, only the rare manager intends to avoid adaptive work. In general, people feel ambivalent about it. Although they want to make progress on hard problems or live up to their renewed and clarified values, people also want to avoid the associated distress. Just as millions of U.S. citizens want to reduce the federal budget deficit, but not by giving up their tax dollars or benefits or jobs, so, too, managers may consider adaptive work a priority but have difficulty sacrificing their familiar ways of doing business. People need leadership to help them maintain their focus on the tough questions. Disciplined attention is the currency of leadership.

Give the Work Back to People

Everyone in the organization has special access to information that comes from his or her particular vantage point. Everyone may see different needs and opportunities. People who sense early changes in the marketplace are often at the periphery, but the organization will thrive if it can bring that information to bear on tactical and strategic decisions. When people do not act on their special knowledge, businesses fail to adapt.

All too often, people look up the chain of command, expecting senior management to meet market challenges for which they themselves are responsible. Indeed, the greater and more persistent distresses that accompany adaptive work make such dependence worse. People tend to become passive, and senior managers who pride themselves on being problem solvers take decisive action. That behavior restores equilibrium in the short term but ultimately leads to complacency and habits of work avoidance that shield people from responsibility, pain, and the need to change.

Getting people to assume greater responsibility is not easy. Not only are many lower-level employees comfortable being told what to do, but many managers are accustomed to treating subordinates like machinery that requires control. Letting people take the initiative in defining and solving problems means that management needs to learn to support rather than control. Workers, for their part, need to learn to take responsibility.

Jan Carlzon encouraged responsibility taking at SAS by trusting others and decentralizing authority. A leader has to let people bear the weight of responsibility. “The key is to let them discover the problem,” he said. “You won’t be successful if people aren’t carrying the recognition of the problem and the solution within themselves.” To that end, Carlzon sought widespread engagement.

For example, in his first two years at SAS, Carlzon spent up to 50% of his time communicating directly in large meetings and indirectly in a host of innovative ways: through workshops, brainstorming sessions, learning

exercises, newsletters, brochures, and exposure in the public media. He demonstrated through a variety of symbolic acts—for example, by eliminating the pretentious executive dining room and burning thousands of pages of manuals and handbooks—the extent to which rules had come to dominate the company. He made himself a pervasive presence, meeting with and listening to people both inside and outside the organization. He even wrote a book, *Moments of Truth* (HarperCollins, 1989), to explain his values, philosophy, and strategy. As Carlzon noted, “If no one else read it, at least my people would.”

A leader also must develop collective self-confidence. Again, Carlzon said it well: “People aren’t born with self-confidence. Even the most self-confident people can be broken. Self-confidence comes from success, experience, and the organization’s environment. The leader’s most important role is to instill confidence in people. They must dare to take risks and responsibility. You must back them up if they make mistakes.”

Protect Voices of Leadership from Below

Giving a voice to all people is the foundation of an organization that is willing to experiment and learn. But, in fact, whistle-blowers, creative deviants, and other such original voices routinely get smashed and silenced in organizational life. They generate disequilibrium, and the easiest way for an organization to restore equilibrium is to neutralize those voices, sometimes in the name of teamwork and “alignment.”

The voices from below are usually not as articulate as one would wish. People speaking beyond their authority usually feel self-conscious and sometimes have to generate “too much” passion to get themselves geared up for speaking out. Of course, that often makes it harder for them to communicate effectively. They pick the wrong time and place, and often bypass proper channels of communication and lines of authority. But buried inside a poorly packaged interjection may lie an important intuition that needs to be teased out and considered. To toss it out for its bad timing, lack of clarity, or seeming unreasonableness is to lose potentially valuable information and discourage a potential leader in the organization.

That is what happened to David, a manager in a large manufacturing company. He had listened when his superiors encouraged people to look for problems, speak openly, and take responsibility. So he raised an issue about one of the CEO’s pet projects—an issue that was deemed “too hot to handle” and had been swept under the carpet for years. Everyone understood that it was not open to discussion, but David knew that proceeding with the project could damage or derail key elements of the company’s overall strategy. He raised the issue directly in a meeting with his boss and the CEO. He provided a clear description of the problem, a rundown of competing perspectives, and a summary of the consequences of continuing to pursue the project.

The CEO angrily squelched the discussion and reinforced the positive aspects of his pet project. When David and his boss left the room, his boss exploded: “Who do you think you are, with your holier-than-thou attitude?” He insinuated that David had never liked the CEO’s pet project because

David hadn't come up with the idea himself. The subject was closed.

David had greater expertise in the area of the project than either his boss or the CEO. But his two superiors demonstrated no curiosity, no effort to investigate David's reasoning, no awareness that he was behaving responsibly with the interests of the company at heart. It rapidly became clear to David that it was more important to understand what mattered to the boss than to focus on real issues. The CEO and David's boss together squashed the viewpoint of a leader from below and thereby killed his potential for leadership in the organization. He would either leave the company or never go against the grain again.

Leaders must rely on others within the business to raise questions that may indicate an impending adaptive challenge. They have to provide cover to people who point to the internal contradictions of the enterprise. Those individuals often have the perspective to provoke rethinking that people in authority do not. Thus, as a rule of thumb, when authority figures feel the reflexive urge to glare at or otherwise silence someone, they should resist. The urge to restore social equilibrium is quite powerful, and it comes on fast. One has to get accustomed to getting on the balcony, delaying the impulse, and asking, What is this guy really talking about? Is there something we're missing?

Doing Adaptive Work at KPMG Netherlands

The highly successful KPMG Netherlands provides a good example of how a company can engage in adaptive work. In 1994, Ruud Koedijk, the firm's chairman, recognized a strategic challenge. Although the auditing, consulting, and tax-preparation partnership was the industry leader in the Netherlands and was highly profitable, growth opportunities in the segments it served were limited. Margins in the auditing business were being squeezed as the market became more saturated, and competition in the consulting business was increasing as well. Koedijk knew that the firm needed to move into more profitable growth areas, but he didn't know what they were or how KPMG might identify them.

Koedijk and his board were confident that they had the tools to do the analytical strategy work: analyze trends and discontinuities, understand core competencies, assess their competitive position, and map potential opportunities. They were considerably less certain that they could commit to implementing the strategy that would emerge from their work. Historically, the partnership had resisted attempts to change, basically because the partners were content with the way things were. They had been successful for a long time, so they saw no reason to learn new ways of doing business, either from their fellow partners or from anyone lower down in the organization. Overturning the partners' attitude and its deep impact on the organization's culture posed an enormous adaptive challenge for KPMG.

Koedijk could see from the balcony that the very structure of KPMG inhibited change. In truth, KPMG was less a partnership than a collection of small fiefdoms in which each partner was a lord. The firm's success was the cumulative accomplishment of each of the individual partners, not the unified result of 300 colleagues pulling together toward a shared ambition. Success was measured solely in terms of the profitability of individual units. As one partner described it, "If the bottom line was correct, you were a 'good fellow.'" As a result, one partner would not trespass on another's turf, and learning from others was a rare event. Because independence was so highly

valued, confrontations were rare and conflict was camouflaged. If partners wanted to resist firmwide change, they did not kill the issue directly. “Say yes, do no” was the operative phrase.

Koedijk also knew that this sense of autonomy got in the way of developing new talent at KPMG. Directors rewarded their subordinates for two things: not making mistakes and delivering a high number of billable hours per week. The emphasis was not on creativity or innovation. Partners were looking for errors when they reviewed their subordinates’ work, not for new understanding or fresh insight. Although Koedijk could see the broad outlines of the adaptive challenges facing his organization, he knew that he could not mandate behavioral change. What he could do was create the conditions for people to discover for themselves how they needed to change. He set a process in motion to make that happen.

To start, Koedijk held a meeting of all 300 partners and focused their attention on the history of KPMG, the current business reality, and the business issues they could expect to face. He then raised the question of how they would go about changing as a firm and asked for their perspectives on the issues. By launching the strategic initiative through dialogue rather than edict, he built trust within the partner ranks. Based on this emerging trust and his own credibility, Koedijk persuaded the partners to release 100 partners and nonpartners from their day-to-day responsibilities to work on the strategic challenges. They would devote 60% of their time for nearly four months to that work.

Koedijk and his colleagues established a strategic integration team of 12 senior partners to work with the 100 professionals (called “the 100”) from different levels and disciplines. Engaging people below the rank of partner in a major strategic initiative was unheard of and signaled a new approach from the start: Many of these people’s opinions had never before been valued or sought by authority figures in the firm. Divided into 14 task forces, the 100 were to work in three areas: gauging future trends and discontinuities, defining core competencies, and grappling with the adaptive challenges facing the organization. They were housed on a separate floor with their own support staff, and they were unfettered by traditional rules and regulations. Hennie Both, KPMG’s director of marketing and communications, signed on as project manager.

As the strategy work got under way, the task forces had to confront the existing KPMG culture. Why? Because they literally could not do their new

work within the old rules. They could not work when strong respect for the individual came at the expense of effective teamwork, when deeply held individual beliefs got in the way of genuine discussion, and when unit loyalties formed a barrier to cross-functional problem solving. Worst of all, task force members found themselves avoiding conflict and unable to discuss those problems. A number of the task forces became dysfunctional and unable to do their strategy work.

To focus their attention on what needed to change, Both helped the task forces map the culture they desired against the current culture. They discovered very little overlap. The top descriptors of the current culture were: develop opposing views, demand perfection, and avoid conflict. The top characteristics of the desired culture were: create the opportunity for self-fulfillment, develop a caring environment, and maintain trusting relations with colleagues. Articulating this gap made tangible for the group the adaptive challenge that Koedijk saw facing KPMG. In other words, the people who needed to do the changing had finally framed the adaptive challenge for themselves: How could KPMG succeed at a competence-based strategy that depended on cooperation across multiple units and layers if its people couldn't succeed in these task forces? Armed with that understanding, the task force members could become emissaries to the rest of the firm.

On a more personal level, each member was asked to identify his or her individual adaptive challenge. What attitudes, behaviors, or habits did each one need to change, and what specific actions would he or she take? Who else needed to be involved for individual change to take root? Acting as coaches and consultants, the task force members gave one another supportive feedback and suggestions. They had learned to confide, to listen, and to advise with genuine care.

Progress on these issues raised the level of trust dramatically, and task force members began to understand what adapting their behavior meant in everyday terms. They understood how to identify an adaptive issue and developed a language with which to discuss what they needed to do to improve their collective ability to solve problems. They talked about dialogue, work avoidance, and using the collective intelligence of the group. They knew how to call one another on dysfunctional behavior. They had begun to develop the culture required to implement the new business strategy.

Despite the critical breakthroughs toward developing a collective

understanding of the adaptive challenge, regulating the level of distress was a constant preoccupation for Koedijk, the board, and Both. The nature of the work was distressing. Strategy work means broad assignments with limited instructions; at KPMG, people were accustomed to highly structured assignments. Strategy work also means being creative. At one breakfast meeting, a board member stood on a table to challenge the group to be more creative and toss aside old rules. This radical and unexpected behavior further raised the distress level: No one had ever seen a partner behave this way before. People realized that their work experience had prepared them only for performing routine tasks with people “like them” from their own units.

The process allowed for conflict and focused people’s attention on the hot issues in order to help them learn how to work with conflict in a constructive manner. But the heat was kept within a tolerable range in some of the following ways:

- On one occasion when tensions were unusually high, the 100 were brought together to voice their concerns to the board in an Oprah Winfrey–style meeting. The board sat in the center of an auditorium and took pointed questions from the surrounding group.
- The group devised sanctions to discourage unwanted behavior. In the soccer-crazy Netherlands, all participants in the process were issued the yellow cards that soccer referees use to indicate “foul” to offending players. They used the cards to stop the action when someone started arguing his or her point without listening to or understanding the assumptions and competing perspectives of other participants.
- The group created symbols. They compared the old KPMG to a hippopotamus that was large and cumbersome, liked to sleep a lot, and became aggressive when its normal habits were disturbed. They aspired to be dolphins, which they characterized as playful, eager to learn, and happily willing to go the extra mile for the team. They even paid attention to the statement that clothes make: It surprised some clients to see managers wandering through the KPMG offices that summer in Bermuda shorts and T-shirts.
- The group made a deliberate point of having fun. “Playtime” could mean long bicycle rides or laser-gun games at a local amusement center. In one spontaneous moment at the KPMG offices, a discussion of the

power of people mobilized toward a common goal led the group to go outside and use their collective leverage to move a seemingly immovable concrete block.

- The group attended frequent two- and three-day off-site meetings to help bring closure to parts of the work.

These actions, taken as a whole, altered attitudes and behaviors. Curiosity became more valued than obedience to rules. People no longer deferred to the senior authority figure in the room; genuine dialogue neutralized hierarchical power in the battle over ideas. The tendency for each individual to promote his or her pet solution gave way to understanding other perspectives. A confidence in the ability of people in different units to work together and work things out emerged. The people with the most curious minds and interesting questions soon became the most respected.

As a result of confronting strategic and adaptive challenges, KPMG as a whole will move from auditing to assurance, from operations consulting to shaping corporate vision, from business-process reengineering to developing organizational capabilities, and from teaching traditional skills to its own clients to creating learning organizations. The task forces identified \$50 million to \$60 million worth of new business opportunities.

Many senior partners who had believed that a firm dominated by the auditing mentality could not contain creative people were surprised when the process unlocked creativity, passion, imagination, and a willingness to take risks. Two stories illustrate the fundamental changes that took place in the firm's mind-set.

We saw one middle manager develop the confidence to create a new business. He spotted the opportunity to provide KPMG services to virtual organizations and strategic alliances. He traveled the world, visiting the leaders of 65 virtual organizations. The results of his innovative research served as a resource to KPMG in entering this growing market. Moreover, he represented the new KPMG by giving a keynote address discussing his findings at a world forum. We also saw a 28-year-old female auditor skillfully guide a group of older, male senior partners through a complex day of looking at opportunities associated with implementing the firm's new strategies. That could not have occurred the year before. The senior partners

never would have listened to such a voice from below.

Leadership as Learning

Many efforts to transform organizations through mergers and acquisitions, restructuring, reengineering, and strategy work falter because managers fail to grasp the requirements of adaptive work. They make the classic error of treating adaptive challenges like technical problems that can be solved by tough-minded senior executives.

The implications of that error go to the heart of the work of leaders in organizations today. Leaders crafting strategy have access to the technical expertise and the tools they need to calculate the benefits of a merger or restructuring, understand future trends and discontinuities, identify opportunities, map existing competencies, and identify the steering mechanisms to support their strategic direction. These tools and techniques are readily available both within organizations and from a variety of consulting firms, and they are very useful. In many cases, however, seemingly good strategies fail to be implemented. And often the failure is misdiagnosed: “We had a good strategy, but we couldn’t execute it effectively.”

In fact, the strategy itself is often deficient because too many perspectives were ignored during its formulation. The failure to do the necessary adaptive work during the strategy development process is a symptom of senior managers’ technical orientation. Managers frequently derive their solution to a problem and then try to sell it to some colleagues and bypass or sandbag others in the commitment-building process. Too often, leaders, their team, and consultants fail to identify and tackle the adaptive dimensions of the challenge and to ask themselves, Who needs to learn what in order to develop, understand, commit to, and implement the strategy?

The same technical orientation entraps business-process-reengineering and restructuring initiatives, in which consultants and managers have the know-how to do the technical work of framing the objectives, designing a new work flow, documenting and communicating results, and identifying the activities to be performed by people in the organization. In many instances,

reengineering falls short of the mark because it treats process redesign as a technical problem: Managers neglect to identify the adaptive work and involve the people who have to do the changing. Senior executives fail to invest their time and their souls in understanding these issues and guiding people through the transition. Indeed, engineering is itself the wrong metaphor.

In short, the prevailing notion that leadership consists of having a vision and aligning people with that vision is bankrupt because it continues to treat adaptive situations as if they were technical: The authority figure is supposed to divine where the company is going, and people are supposed to follow. Leadership is reduced to a combination of grand knowing and salesmanship. Such a perspective reveals a basic misconception about the way businesses succeed in addressing adaptive challenges. Adaptive situations are hard to define and resolve precisely because they demand the work and responsibility of managers and people throughout the organization. They are not amenable to solutions provided by leaders; adaptive solutions require members of the organization to take responsibility for the problematic situations that face them.

Leadership has to take place every day. It cannot be the responsibility of the few, a rare event, or a once-in-a-lifetime opportunity. In our world, in our businesses, we face adaptive challenges all the time. When an executive is asked to square conflicting aspirations, he and his people face an adaptive challenge. When a manager sees a solution to a problem—technical in many respects except that it requires a change in the attitudes and habits of subordinates—he faces an adaptive challenge. When an employee close to the front line sees a gap between the organization's purpose and the objectives he is asked to achieve, he faces both an adaptive challenge and the risks and opportunity of leading from below.

Leadership, as seen in this light, requires a learning strategy. A leader, from above or below, with or without authority, has to engage people in confronting the challenge, adjusting their values, changing perspectives, and learning new habits. To an authoritative person who prides himself on his ability to tackle hard problems, this shift may come as a rude awakening. But it also should ease the burden of having to know all the answers and bear all the load. To the person who waits to receive either the coach's call or "the vision" to lead, this change may also seem a mixture of good news and bad news. The adaptive demands of our time require leaders who take

responsibility without waiting for revelation or request. One can lead with no more than a question in hand.

Originally published in January 1997. Reprint R0111K

Why Should Anyone Be Led by You?

by Robert Goffee and Gareth Jones

IF YOU WANT TO SILENCE a room of executives, try this small trick. Ask them, “Why would anyone want to be led by you?” We’ve asked just that question for the past ten years while consulting for dozens of companies in Europe and the United States. Without fail, the response is a sudden, stunned hush. All you can hear are knees knocking.

Executives have good reason to be scared. You can’t do anything in business without followers, and followers in these “empowered” times are hard to find. So executives had better know what it takes to lead effectively—they must find ways to engage people and rouse their commitment to company goals. But most don’t know how, and who can blame them? There’s simply too much advice out there. Last year alone, more than 2,000 books on leadership were published, some of them even repackaging Moses and Shakespeare as leadership gurus.

We’ve yet to hear advice that tells the whole truth about leadership. Yes, everyone agrees that leaders need vision, energy, authority, and strategic direction. That goes without saying. But we’ve discovered that inspirational leaders also share four unexpected qualities:

- **They selectively show their weaknesses.** By exposing some vulnerability, they reveal their approachability and humanity.
- **They rely heavily on intuition to gauge the appropriate timing and course of their actions.** Their ability to collect and interpret soft data

helps them know just when and how to act.

- **They manage employees with something we call tough empathy.** Inspirational leaders empathize passionately—and realistically—with people, and they care intensely about the work employees do.
- **They reveal their differences.** They capitalize on what's unique about themselves. You may find yourself in a top position without these qualities, but few people will want to be led by you.

Our theory about the four essential qualities of leadership, it should be noted, is not about results per se. While many of the leaders we have studied and use as examples do in fact post superior financial returns, the focus of our research has been on leaders who excel at inspiring people—in capturing hearts, minds, and souls. This ability is not everything in business, but any experienced leader will tell you it is worth quite a lot. Indeed, great results may be impossible without it.

Our research into leadership began some 25 years ago and has followed three streams since then. First, as academics, we ransacked the prominent leadership theories of the past century to develop our own working model of effective leadership. (For more on the history of leadership thinking, see the sidebar “Leadership: A Small History of a Big Topic.”) Second, as consultants, we have tested our theory with thousands of executives in workshops worldwide and through observations with dozens of clients. And third, as executives ourselves, we have vetted our theories in our own organizations.

Reveal Your Weaknesses

When leaders reveal their weaknesses, they show us who they are—warts and all. This may mean admitting that they're irritable on Monday mornings, that they are somewhat disorganized, or even rather shy. Such admissions work because people need to see leaders own up to some flaw before they participate willingly in an endeavor. Exposing a weakness establishes trust and thus helps get folks on board. Indeed, if executives try to communicate that they're perfect at everything, there will be no need for anyone to help them with anything. They won't need followers. They'll signal that they can do it all themselves.

Idea in Brief

The question “Why should anyone be led by you?” strikes fear in the hearts of most executives. With good reason. You can’t get anything done without followers, and in these “empowered” times, followers are hard to find—*except* by leaders who excel at capturing people’s hearts, minds, and spirits.

How do you do that? Of course, you need vision, energy, authority, and strategic direction—and these four additional qualities:

- Show you’re human, selectively revealing weaknesses.
- Be a “sensor,” collecting soft people data that lets you rely on intuition.
- Manage employees with “tough empathy.” Care passionately about them and their work, while giving them only what they *need* to achieve their best.
- Dare to be different, capitalizing on your uniqueness.

Mix and match these qualities to find the right style for the right moment.

Without all four qualities, you might climb to the top. But few people will want to follow you, and your company won’t achieve its best results.

Beyond creating trust and a collaborative atmosphere, communicating a weakness also builds solidarity between followers and leaders. Consider a

senior executive we know at a global management consultancy. He agreed to give a major presentation despite being badly afflicted by physical shaking caused by a medical condition. The otherwise highly critical audience greeted this courageous display of weakness with a standing ovation. By giving the talk, he had dared to say, “I am just like you—imperfect.” Sharing an imperfection is so effective because it underscores a human being’s authenticity. Richard Branson, the founder of Virgin, is a brilliant businessman and a hero in the United Kingdom. (Indeed, the Virgin brand is so linked to him personally that succession is a significant issue.) Branson is particularly effective at communicating his vulnerability. He is ill at ease and fumbles incessantly when interviewed in public. It’s a weakness, but it’s Richard Branson. That’s what revealing a weakness is all about: showing your followers that you are genuine and approachable—human and humane.

Idea in Practice

Reveal Your Weaknesses

Nobody wants to work with a perfect leader—he doesn't appear to need help. So show you're human—warts and all. You'll build collaboration and solidarity between you and your followers, and underscore your approachability.

Tips:

- Don't expose a weakness that others see as fatal. (A new finance director shouldn't reveal his ignorance of discounted cash flow!) Choose a tangential weakness instead.
- Pick a flaw that others consider a strength, e.g., workaholism.

Become a Sensor

Hone your ability to collect and interpret subtle interpersonal cues, detecting what's going on without others' spelling it out.

Example: Franz Humer, highly successful CEO of Roche, a health-care research company, senses underlying currents of opinion, gauges unexpressed feelings, and accurately judges relationships' quality.

Tips:

- Test your perceptions: Validate them with a trusted advisor or

inner-team member.

Practice Tough Empathy

Real leaders empathize fiercely with their followers and care intensely about their people's work. They're also empathetically "tough." This means giving people not necessarily what they *want*, but what they *need* to achieve their best.

Example: BBC CEO Greg Dyke knew that to survive in a digital world, the company had to spend more on programs and less on people. He restructured the organization, but only after explaining this openly and directly to the staff. Though many employees lost jobs, Dyke kept people's commitment.

Dare to Be Different

Capitalizing on what's unique about yourself lets you signal your separateness as a leader, and motivates others to perform better. Followers push themselves more if their leader is just a little aloof.

Tips:

- Don't overdifferentiate yourself—you could lose contact with followers. Robert Horton, former CEO of British Petroleum, conspicuously displayed his formidable intelligence. Followers saw him as arrogant, and detached themselves from him. He was dismissed after three years.
- Distinguish yourself through qualities like imagination, expertise, and adventuresomeness.

Another advantage to exposing a weakness is that it offers a leader valuable protection. Human nature being what it is, if you don't show some weakness, then observers may invent one for you. Celebrities and politicians have always known this. Often, they deliberately give the public something to talk about, knowing full well that if they don't, the newspapers will invent something even worse. Princess Diana may have aired her eating disorder in public, but she died with her reputation intact, indeed even enhanced.

That said, the most effective leaders know that exposing a weakness must be done carefully. They own up to *selective* weaknesses. Knowing which weakness to disclose is a highly honed art. The golden rule is never to expose a weakness that will be seen as a fatal flaw—by which we mean a flaw that jeopardizes central aspects of your professional role. Consider the new finance director of a major corporation. He can't suddenly confess that he's never understood discounted cash flow. A leader should reveal only a tangential flaw—and perhaps even several of them. Paradoxically, this admission will help divert attention away from major weaknesses.

Another well-known strategy is to pick a weakness that can in some ways be considered a strength, such as being a workaholic. When leaders expose these limited flaws, people won't see much of anything and little harm will come to them. There is an important caveat, however: if the leader's vulnerability is not perceived to be genuine, he won't gain anyone's support. Instead he will open himself up to derision and scorn. One scenario we saw repeatedly in our research was one in which a CEO feigns absentmindedness to conceal his inconsistency or even dishonesty. This is a sure way to alienate followers who will remember accurately what happened or what was said.

Leadership: A Small History of a Big Topic

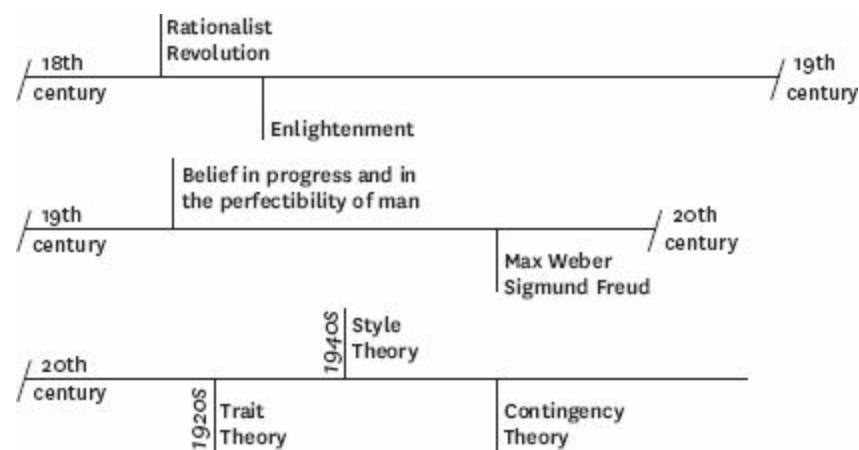
PEOPLE HAVE BEEN TALKING about leadership since the time of Plato. But in organizations all over the world—in dinosaur conglomerates and new-economy startups alike—the same complaint emerges: we don't have enough leadership. We have to ask ourselves, Why are we so obsessed with leadership?

One answer is that there is a crisis of belief in the modern world that has its roots in the rationalist revolution of the eighteenth century. During the Enlightenment, philosophers such as Voltaire claimed that through the application of reason alone, people could control their destiny. This marked an incredibly optimistic turn in world history. In the nineteenth century, two beliefs stemmed from this rationalist notion: a belief in progress and a belief in the perfectibility of man. This produced an even rosier world view than before. It wasn't until the end of the nineteenth century, with the writings first of Sigmund Freud and later of Max Weber, that the chinks in the armor appeared. These two thinkers destroyed Western man's belief in rationality and progress. The current quest for leadership is a direct consequence of their work.

The founder of psychoanalysis, Freud theorized that beneath the surface of the rational mind was the unconscious. He supposed that the unconscious was responsible for a fair proportion of human behavior. Weber, the leading critic of Marx and a brilliant sociologist, also explored the limits of reason. Indeed, for him, the most destructive force operating in institutions was something he called technical rationality—that is, rationality without morality.

For Weber, technical rationality was embodied in one particular organizational form—the bureaucracy. Bureaucracies, he said, were frightening not for their inefficiencies but for their efficiencies and

their capacity to dehumanize people. The tragic novels of Franz Kafka bear stark testimony to the debilitating effects of bureaucracy. Even more chilling was the testimony of Hitler's lieutenant Adolf Eichmann that "I was just a good bureaucrat." Weber believed that the only power that could resist bureaucratization was charismatic leadership. But even this has a very mixed record in the twentieth century. Although there have been inspirational and transformational wartime leaders, there have also been charismatic leaders like Hitler, Stalin, and Mao Tse-tung who committed horrendous atrocities.



By the twentieth century, there was much skepticism about the power of reason and man's ability to progress continuously. Thus, for both pragmatic and philosophic reasons, an intense interest in the concept of leadership began to develop. And indeed, in the 1920s, the first serious research started. The first leadership theory—trait theory—attempted to identify the common characteristics of effective leaders. To that end, leaders were weighed and measured and subjected to a battery of psychological tests. But no one could identify what effective leaders had in common. Trait theory fell into disfavor soon after expensive studies concluded that effective leaders were either above-average height or below.

Trait theory was replaced by style theory in the 1940s, primarily in

the United States. One particular style of leadership was singled out as having the most potential. It was a hail-fellow-well-met democratic style of leadership, and thousands of American executives were sent to training courses to learn how to behave this way. There was only one drawback. The theory was essentially capturing the spirit of FDR's America—open, democratic, and meritocratic. And so when McCarthyism and the Cold War surpassed the New Deal, a completely new style was required. Suddenly, everyone was encouraged to behave like a Cold War warrior! The poor executive was completely confused.

Recent leadership thinking is dominated by contingency theory, which says that leadership is dependent on a particular situation. That's fundamentally true, but given that there are endless contingencies in life, there are endless varieties of leadership. Once again, the beleaguered executive looking for a model to help him is hopelessly lost.

For this article, we ransacked all the leadership theories to come up with the four essential leadership qualities. Like Weber, we look at leadership that is primarily antibureaucratic and charismatic. From trait theory, we derived the qualities of weaknesses and differences. Unlike the original trait theorists, however, we do not believe that all leaders have the same weaknesses; our research only showed that all leaders expose some flaws. Tough empathy grew out of style theory, which looked at different kinds of relationships between leaders and their followers. Finally, context theory set the stage for needing to know what skills to use in various circumstances.

Become a Sensor

Inspirational leaders rely heavily on their instincts to know when to reveal a weakness or a difference. We call them good situation sensors, and by that we mean that they can collect and interpret soft data. They can sniff out the signals in the environment and sense what's going on without having anything spelled out for them.

Franz Humer, the CEO of Roche, is a classic sensor. He is highly accomplished in detecting shifts in climate and ambience; he can read subtle cues and sense underlying currents of opinion that elude less perceptive people. Humer says he developed this skill as a tour guide in his mid-twenties when he was responsible for groups of 100 or more. "There was no salary, only tips," he explains. "Pretty soon, I knew how to hone in on particular groups. Eventually, I could predict within 10% how much I could earn from any particular group." Indeed, great sensors can easily gauge unexpressed feelings; they can very accurately judge whether relationships are working or not. The process is complex, and as anyone who has ever encountered it knows, the results are impressive.

Consider a human resources executive we worked with in a multinational entertainment company. One day he got news of a distribution problem in Italy that had the potential to affect the company's worldwide operations. As he was thinking about how to hide the information temporarily from the Paris-based CEO while he worked on a solution, the phone rang. It was the CEO saying, "Tell me, Roberto, what the hell's going on in Milan?" The CEO was already aware that something was wrong. How? He had his networks, of course. But in large part, he was gifted at detecting information that wasn't aimed at him. He could read the silences and pick up on nonverbal cues in the organization.

Not surprisingly, the most impressive business leaders we have worked with are all very refined sensors. Ray van Schaik, the chairman of Heineken in the early 1990s, is a good example. Conservative and urbane, van Schaik's genius lay in his ability to read signals he received from colleagues and from

Freddie Heineken, the third-generation family member who was “always there without being there.” While some senior managers spent a lot of time second-guessing the major shareholder, van Schaik developed an ability to “just know” what Heineken wanted. This ability was based on many years of working with him on the Heineken board, but it was more than that—van Schaik could read Heineken even though they had very different personalities and didn’t work together directly.

Success stories like van Schaik’s come with a word of warning. While leaders must be great sensors, sensing can create problems. That’s because in making fine judgments about how far they can go, leaders risk losing their followers. The political situation in Northern Ireland is a powerful example. Over the past two years, several leaders—David Trimble, Gerry Adams, and Tony Blair, together with George Mitchell—have taken unprecedented initiatives toward peace. At every step of the way, these leaders had to sense how far they could go without losing their electorates. In business, think of mergers and acquisitions. Unless organizational leaders and negotiators can convince their followers in a timely way that the move is positive, value and goodwill quickly erode. This is the situation recently faced by Vodafone and France Telecom in the sale and purchase of Orange.

There is another danger associated with sensing skills. By definition, sensing a situation involves projection—that state of mind whereby you attribute your own ideas to other people and things. When a person “projects,” his thoughts may interfere with the truth. Imagine a radio that picks up any number of signals, many of which are weak and distorted. Situation sensing is like that; you can’t always be sure what you’re hearing because of all the static. The employee who sees her boss distracted and leaps to the conclusion that she is going to be fired is a classic example. Most skills become heightened under threat, but particularly during situation sensing. Such oversensitivity in a leader can be a recipe for disaster. For this reason, sensing capability must always be framed by reality testing. Even the most gifted sensor may need to validate his perceptions with a trusted adviser or a member of his inner team.

Practice Tough Empathy

Unfortunately, there's altogether too much hype nowadays about the idea that leaders *must* show concern for their teams. There's nothing worse than seeing a manager return from the latest interpersonal-skills training program with "concern" for others. Real leaders don't need a training program to convince their employees that they care. Real leaders empathize fiercely with the people they lead. They also care intensely about the work their employees do.

Consider Alain Levy, the former CEO of Polygram. Although he often comes across as a rather aloof intellectual, Levy is well able to close the distance between himself and his followers. On one occasion, he helped some junior record executives in Australia choose singles off albums. Picking singles is a critical task in the music business: the selection of a song can make or break the album. Levy sat down with the young people and took on the work with passion. "You bloody idiots," he added his voice to the melee, "you don't know what the hell you're talking about; we always have a dance track first!" Within 24 hours, the story spread throughout the company; it was the best PR Levy ever got. "Levy really knows how to pick singles," people said. In fact, he knew how to identify with the work, and he knew how to enter his followers' world—one where strong, colorful language is the norm—to show them that he cared.

Clearly, as the above example illustrates, we do not believe that the empathy of inspirational leaders is the soft kind described in so much of the management literature. On the contrary, we feel that real leaders manage through a unique approach we call tough empathy. Tough empathy means giving people what they need, not what they want. Organizations like the Marine Corps and consulting firms specialize in tough empathy. Recruits are pushed to be the best that they can be; "grow or go" is the motto. Chris Satterwaite, the CEO of ell Pottinger Communications and a former chief executive of several ad agencies, understands what tough empathy is all about. He adeptly handles the challenges of managing creative people while making tough decisions. "If I have to, I can be ruthless," he says. "But while

they're with me, I promise my people that they'll learn."



Four Popular Myths About Leadership

IN BOTH OUR RESEARCH AND consulting work, we have seen executives who profoundly misunderstand what makes an inspirational leader. Here are four of the most common myths:

Everyone can be a leader.

Not true. Many executives don't have the self-knowledge or the authenticity necessary for leadership. And self-knowledge and authenticity are only part of the equation. Individuals must also want to be leaders, and many talented employees are not interested in shouldering that responsibility. Others prefer to devote more time to their private lives than to their work. After all, there is more to life than work, and more to work than being the boss.

Leaders deliver business results.

Not always. If results were always a matter of good leadership, picking leaders would be easy. In every case, the best strategy would be to go after people in companies with the best results. But clearly, things are not that simple. Businesses in quasi-monopolistic industries can often do very well with competent management rather than great leadership. Equally, some well-led businesses do not necessarily produce results, particularly in the short term.

People who get to the top are leaders.

Not necessarily. One of the most persistent misperceptions is that people in leadership positions are leaders. But people who make it to the top may have done so because of political acumen, not necessarily because of true leadership quality. What's more, real leaders are found all over the organization, from the executive suite to the shop floor. By definition, leaders are simply people who have followers, and rank doesn't have much to do with that. Effective military organizations like the U.S. Navy have long realized the importance of

developing leaders throughout the organization.

Leaders are great coaches.

Rarely. A whole cottage industry has grown up around the teaching that good leaders ought to be good coaches. But that thinking assumes that a single person can both inspire the troops and impart technical skills. Of course, it's possible that great leaders may also be great coaches, but we see that only occasionally. More typical are leaders like Steve Jobs whose distinctive strengths lie in their ability to excite others through their vision rather than through their coaching talents.

At its best, tough empathy balances respect for the individual and for the task at hand. Attending to both, however, isn't easy, especially when the business is in survival mode. At such times, caring leaders have to give selflessly to the people around them and know when to pull back. Consider a situation at Unilever at a time when it was developing Persil Power, a detergent that eventually had to be removed from the market because it destroyed clothes that were laundered in it. Even though the product was showing early signs of trouble, CEO Niall FitzGerald stood by his troops. "That was the popular place to be, but I should not have been there," he says now. "I should have stood back, cool and detached, looked at the whole field, watched out for the customer." But caring with detachment is not easy, especially since, when done right, tough empathy is harder on you than on your employees. "Some theories of leadership make caring look effortless. It isn't," says Paulanne Mancuso, president and CEO of Calvin Klein Cosmetics. "You have to do things you don't want to do, and that's hard." It's tough to be tough.

Tough empathy also has the benefit of impelling leaders to take risks. When Greg Dyke took over at the BBC, his commercial competitors were able to spend substantially more on programs than the BBC could. Dyke quickly realized that in order to thrive in a digital world, the BBC needed to increase its expenditures. He explained this openly and directly to the staff. Once he had secured their buy-in, he began thoroughly restructuring the organization. Although many employees were let go, he was able to maintain people's commitment. Dyke attributed his success to his tough empathy with

employees: “Once you have the people with you, you can make the difficult decisions that need to be made.”

One final point about tough empathy: those more apt to use it are people who really care about something. And when people care deeply about something—anything—they’re more likely to show their true selves. They will not only communicate authenticity, which is the precondition for leadership, but they will show that they are doing more than just playing a role. People do not commit to executives who merely live up to the obligations of their jobs. They want more. They want someone who cares passionately about the people and the work—just as they do.

Can Female Leaders Be True to Themselves?

GENDER DIFFERENCES CAN BE used to either positive or negative effect. Women, in particular, are prone to being stereotyped according to differences—albeit usually not the ones that they would choose. Partly this is because there are fewer women than men in management positions. According to research in social psychology, if a group's representation falls below 20% in a given society, then it's going to be subjected to stereotyping whether it likes it or not. For women, this may mean being typecast as a “helper,” “nurturer,” or “seductress”—labels that may prevent them from defining their own differences.

In earlier research, we discovered that many women—particularly women in their fifties—try to avoid this dynamic by disappearing. They try to make themselves invisible. They wear clothes that disguise their bodies; they try to blend in with men by talking tough. That's certainly one way to avoid negative stereotyping, but the problem is that it reduces a woman's chances of being seen as a potential leader. She's not promoting her real self and differences.

Another response to negative stereotyping is to collectively resist it—for example, by mounting a campaign that promotes the rights, opportunities, and even the number of women in the workplace. But on a day-to-day basis, survival is often all women have time for, therefore making it impossible for them to organize themselves formally.

A third response that emerged in our research was that women play into stereotyping to personal advantage. Some women, for example, knowingly play the role of “nurturer” at work, but they do it with such wit and skill that they are able to benefit from it. The cost of such a strategy?

It furthers harmful stereotypes and continues to limit opportunities for other women to communicate their genuine personal differences.

Dare to Be Different

Another quality of inspirational leaders is that they capitalize on what's unique about themselves. In fact, using these differences to great advantage is the most important quality of the four we've mentioned. The most effective leaders deliberately use differences to keep a social distance. Even as they are drawing their followers close to them, inspirational leaders signal their separateness.

Often, a leader will show his differences by having a distinctly different dress style or physical appearance, but typically he will move on to distinguish himself through qualities like imagination, loyalty, expertise, or even a handshake. Anything can be a difference, but it is important to communicate it. Most people, however, are hesitant to communicate what's unique about themselves, and it can take years for them to be fully aware of what sets them apart. This is a serious disadvantage in a world where networking is so critical and where teams need to be formed overnight.

Some leaders know exactly how to take advantage of their differences. Take Sir John Harvey-Jones, the former CEO of ICI—what was once the largest manufacturing company in the United Kingdom. When he wrote his autobiography a few years ago, a British newspaper advertised the book with a sketch of Harvey-Jones. The profile had a moustache, long hair, and a loud tie. The drawing was in black and white, but everyone knew who it was. Of course, John Harvey-Jones didn't get to the top of ICI because of eye-catching ties and long hair. But he was very clever in developing differences that he exploited to show that he was adventurous, entrepreneurial, and unique—he was John Harvey-Jones.

There are other people who aren't as aware of their differences but still use them to great effect. For instance, Richard Surface, former managing director of the UK-based Pearl Insurance, always walked the floor and overtook people, using his own pace as a means of communicating urgency. Still other leaders are fortunate enough to have colleagues point out their differences for them. As the BBC's Greg Dyke puts it, "My partner tells me,

‘You do things instinctively that you don’t understand. What I worry about is that in the process of understanding them you could lose them!’” Indeed, what emerged in our interviews is that most leaders start off not knowing what their differences are but eventually come to know—and use—they more effectively over time. Franz Humer at Roche, for instance, now realizes that he uses his emotions to evoke reactions in others.

Most of the differences we’ve described are those that tend to be apparent, either to the leader himself or to the colleagues around him. But there are differences that are more subtle but still have very powerful effects. For instance, David Prosser, the CEO of Legal and General, one of Europe’s largest and most successful insurance companies, is an outsider. He is not a smooth city type; in fact, he comes from industrial South Wales. And though generally approachable, Prosser has a hard edge, which he uses in an understated but highly effective way. At a recent cocktail party, a rather excitable sales manager had been claiming how good the company was at cross-selling products. In a low voice, Prosser intervened: “We may be good, but we’re not good enough.” A chill swept through the room. What was Prosser’s point? Don’t feel so close you can relax! I’m the leader, and I make that call. Don’t you forget it. He even uses this edge to good effect with the top team—it keeps everyone on their toes.

Inspirational leaders use separateness to motivate others to perform better. It is not that they are being Machiavellian but that they recognize instinctively that followers will push themselves if their leader is just a little aloof. Leadership, after all, is not a popularity contest.

One danger, of course, is that executives can overdifferentiate themselves in their determination to express their separateness. Indeed, some leaders lose contact with their followers, and doing so is fatal. Once they create too much distance, they stop being good sensors, and they lose the ability to identify and care. That’s what appeared to happen during Robert Horton’s tenure as chairman and CEO of BP during the early 1990s. Horton’s conspicuous display of his considerable—indeed, daunting—intelligence sometimes led others to see him as arrogant and self-aggrandizing. That resulted in overdifferentiation, and it eventually contributed to Horton’s dismissal just three years after he was appointed to the position.

Leadership in Action

All four of the qualities described here are necessary for inspirational leadership, but they cannot be used mechanically. They must become or must already be part of an executive's personality. That's why the "recipe" business books—those that prescribe to the Lee Iaccoca or Bill Gates way—often fail. No one can just ape another leader. So the challenge facing prospective leaders is for them to be themselves, but with more skill. That can be done by making yourself increasingly aware of the four leadership qualities we describe and by manipulating these qualities to come up with a personal style that works for you. Remember, there is no universal formula, and what's needed will vary from context to context. What's more, the results are often subtle, as the following story about Sir Richard Sykes, the highly successful chairman and CEO of Glaxo Wellcome, one of the world's leading pharmaceutical companies, illustrates.

When he was running the R&D division at Glaxo, Sykes gave a year-end review to the company's top scientists. At the end of the presentation, a researcher asked him about one of the company's new compounds, and the two men engaged in a short heated debate. The question-answer session continued for another 20 minutes, at the end of which the researcher broached the subject again. "Dr. Sykes," he began in a loud voice, "you have still failed to understand the structure of the new compound." You could feel Sykes's temper rise through the soles of his feet. He marched to the back of the room and displayed his anger before the intellectual brainpower of the entire company. "All right, lad," he yelled, "let us have a look at your notes!"

The Sykes story provides the ideal framework for discussing the four leadership qualities. To some people, Sykes's irritability could have seemed like inappropriate weakness. But in this context, his show of temper demonstrated Sykes's deep belief in the discussion about basic science—a company value. Therefore, his willingness to get angry actually cemented his credibility as a leader. He also showed that he was a very good sensor. If Sykes had exploded earlier in the meeting, he would have quashed the

debate. Instead, his anger was perceived as defending the faith. The story also reveals Sykes's ability to identify with his colleagues and their work. By talking to the researcher as a fellow scientist, he was able to create an empathic bond with his audience. He really cared, though his caring was clearly tough empathy. Finally, the story indicates Sykes's own willingness to show his differences. Despite being one of the United Kingdom's most successful businessmen, he has not conformed to "standard" English. On the contrary, Sykes proudly retains his distinctive northern accent. He also doesn't show the typical British reserve and decorum; he radiates passion. Like other real leaders, he acts and communicates naturally. Indeed, if we were to sum up the entire year-end review at Glaxo Wellcome, we'd say that Sykes was being himself—with great skill.

Unraveling the Mystery

As long as business is around, we will continue to pick apart the underlying ingredients of true leadership. And there will always be as many theories as there are questions. But of all the facets of leadership that one might investigate, there are few so difficult as understanding what it takes to develop leaders. The four leadership qualities are a necessary first step. Taken together, they tell executives to be authentic. As we counsel the executives we coach: “Be yourselves—more—with skill.” There can be no advice more difficult to follow than that.

Originally published in September 2000. Reprint R00506

Crucibles of Leadership

by Warren G. Bennis and Robert J. Thomas

AS LIFELONG STUDENTS OF LEADERSHIP, we are fascinated with the notion of what makes a leader. Why is it that certain people seem to naturally inspire confidence, loyalty, and hard work, while others (who may have just as much vision and smarts) stumble, again and again? It's a timeless question, and there's no simple answer. But we have come to believe it has something to do with the different ways that people deal with adversity. Indeed, our recent research has led us to conclude that one of the most reliable indicators and predictors of true leadership is an individual's ability to find meaning in negative events and to learn from even the most trying circumstances. Put another way, the skills required to conquer adversity and emerge stronger and more committed than ever are the same ones that make for extraordinary leaders.

Take Sidney Harman. Thirty-four years ago, the then-48-year-old businessman was holding down two executive positions. He was the chief executive of Harman Kardon (now Harman International), the audio components company he had cofounded, and he was serving as president of Friends World College, now Friends World Program, an experimental Quaker school on Long Island whose essential philosophy is that students, not their teachers, are responsible for their education. Juggling the two jobs, Harman was living what he calls a "bifurcated life," changing clothes in his car and eating lunch as he drove between Harman Kardon offices and plants and the Friends World campus. One day while at the college, he was told his company's factory in Bolivar, Tennessee, was having a crisis.

He immediately rushed to the Bolivar factory, a facility that was, as Harman now recalls, “raw, ugly, and, in many ways, demeaning.” The problem, he found, had erupted in the polish and buff department, where a crew of a dozen workers, mostly African-Americans, did the dull, hard work of polishing mirrors and other parts, often under unhealthy conditions. The men on the night shift were supposed to get a coffee break at 10 PM. When the buzzer that announced the workers’ break went on the fritz, management arbitrarily decided to postpone the break for ten minutes, when another buzzer was scheduled to sound. But one worker, “an old black man with an almost biblical name, Noah B. Cross,” had “an epiphany,” as Harman describes it. “He said, literally, to his fellow workers, ‘I don’t work for no buzzer. The buzzer works for me. It’s my job to tell me when it’s ten o’clock. I got me a watch. I’m not waiting another ten minutes. I’m going on my coffee break.’ And all 12 guys took their coffee break, and, of course, all hell broke loose.”

The worker’s principled rebellion—his refusal to be cowed by management’s senseless rule—was, in turn, a revelation to Harman: “The technology is there to serve the men, not the reverse,” he remembers realizing. “I suddenly had this awakening that everything I was doing at the college had appropriate applications in business.” In the ensuing years, Harman revamped the factory and its workings, turning it into a kind of campus—offering classes on the premises, including piano lessons, and encouraging the workers to take most of the responsibility for running their workplace. Further, he created an environment where dissent was not only tolerated but also encouraged. The plant’s lively independent newspaper, the *Bolivar Mirror*, gave workers a creative and emotional outlet—and they enthusiastically skewered Harman in its pages.

Harman had, unexpectedly, become a pioneer of participative management, a movement that continues to influence the shape of workplaces around the world. The concept wasn’t a grand idea conceived in the CEO’s office and imposed on the plant, Harman says. It grew organically out of his going down to Bolivar to, in his words, “put out this fire.” Harman’s transformation was, above all, a creative one. He had connected two seemingly unrelated ideas and created a radically different approach to management that recognized both the economic and humane benefits of a more collegial workplace. Harman went on to accomplish far more during his career. In addition to founding Harman International, he served as the deputy

secretary of commerce under Jimmy Carter. But he always looked back on the incident in Bolivar as the formative event in his professional life, the moment he came into his own as a leader.

Idea in Brief

What enables one leader to inspire confidence, loyalty, and hard work, while others—with equal vision and intelligence—stumble? How individuals deal with adversity provides a clue.

Extraordinary leaders find meaning in—and learn from—the most negative events. Like phoenixes rising from the ashes, they emerge from adversity stronger, more confident in themselves and their purpose, and more committed to their work.

Such transformative events are called **crucibles**—a severe test or trial. Crucibles are intense, often traumatic—and always unplanned.

The details of Harman's story are unique, but their significance is not. In interviewing more than 40 top leaders in business and the public sector over the past three years, we were surprised to find that all of them—young and old—were able to point to intense, often traumatic, always unplanned experiences that had transformed them and had become the sources of their distinctive leadership abilities.

We came to call the experiences that shape leaders “crucibles,” after the vessels medieval alchemists used in their attempts to turn base metals into gold. For the leaders we interviewed, the crucible experience was a trial and a test, a point of deep self-reflection that forced them to question who they were and what mattered to them. It required them to examine their values, question their assumptions, hone their judgment. And, invariably, they emerged from the crucible stronger and more sure of themselves and their purpose—changed in some fundamental way.

Idea in Practice

The Crucible Experience

Crucibles force leaders into deep self-reflection, where they examine their values, question their assumptions, and hone their judgment.

Example: Sidney Harman— co-founder of audio components company Harman Kardon and president of an experimental college encouraging student-driven education— encountered his crucible when “all hell broke loose” in one of his factories. After managers postponed a scheduled break because the buzzer didn’t sound, workers rebelled. “I don’t work for no buzzer,” one proclaimed.

To Harman, this refusal to bow to management’s senseless rule suggested a surprising link between student-driven education and business. Pioneering participative management, Harman transformed his plant into a kind of campus, offering classes and encouraging dissent. He considers the rebellion the formative event in his career—the moment he became a true leader.

The Many Shapes of Crucibles

Some crucibles are violent and life-threatening (encounters with prejudice, illness); others are more positive, yet profoundly challenging (such as demanding bosses or mentors). Whatever the shape, leaders create a narrative telling how they met the challenge and became better for it.

Example: While working for former Atlanta mayor Robert F. Maddox, Vernon Jordan endured repeated racial heckling from Maddox. Rather than letting Maddox’s sadism destroy him, Jordan interpreted the behavior as a desperate lashing out by someone who knew the era of the Old South was ending. Jordan’s response empowered him to become an esteemed lawyer and presidential

advisor.

Essential Leadership Skills

Four skills enable leaders to learn from adversity:

1. **Engage others in shared meaning.** For example, Sidney Harman mobilized employees around a radical new management approach—amid a factory crisis.
2. **A distinctive, compelling voice.** With words alone, college president Jack Coleman preempted a violent clash between the football team and anti-Vietnam War demonstrators threatening to burn the American flag. Coleman's suggestion to the protestors? Lower the flag, wash it, then put it back up.
3. **Integrity.** Coleman's values prevailed during the emotionally charged face-off between antiwar demonstrators and irate football players.
4. **Adaptive capacity.** This most critical skill includes the *ability to grasp context*, and *hardiness*. Grasping context requires weighing many factors (e.g., how different people will interpret a gesture). Without this quality, leaders can't connect with constituents.

Hardiness provides the perseverance and toughness needed to remain hopeful despite disaster. For instance, Michael Klein made millions in real estate during his teens, lost it all by age 20—then built several more businesses, including transforming a tiny software company into a Hewlett-Packard acquisition.

Leadership crucibles can take many forms. Some are violent, life-threatening events. Others are more prosaic episodes of self-doubt. But whatever the crucible's nature, the people we spoke with were able, like Harman, to create a narrative around it, a story of how they were challenged, met the challenge, and became better leaders. As we studied these stories, we found that they not only told us how individual leaders are shaped but also

pointed to some characteristics that seem common to all leaders—characteristics that were formed, or at least exposed, in the crucible.

Learning from Difference

A crucible is, by definition, a transformative experience through which an individual comes to a new or an altered sense of identity. It is perhaps not surprising then that one of the most common types of crucibles we documented involves the experience of prejudice. Being a victim of prejudice is particularly traumatic because it forces an individual to confront a distorted picture of him- or herself, and it often unleashes profound feelings of anger, bewilderment, and even withdrawal. For all its trauma, however, the experience of prejudice is for some a clarifying event. Through it, they gain a clearer vision of who they are, the role they play, and their place in the world.

Consider, for example, Liz Altman, now a Motorola vice president, who was transformed by the year she spent at a Sony camcorder factory in rural Japan, where she faced both estrangement and sexism. It was, says Altman, “by far, the hardest thing I’ve ever done.” The foreign culture—particularly its emphasis on groups over individuals—was both a shock and a challenge to a young American woman. It wasn’t just that she felt lonely in an alien world. She had to face the daunting prospect of carving out a place for herself as the only woman engineer in a plant, and nation, where women usually serve as low-level assistants and clerks known as “office ladies.”

Another woman who had come to Japan under similar circumstances had warned Altman that the only way to win the men’s respect was to avoid becoming allied with the office ladies. But on her very first morning, when the bell rang for a coffee break, the men headed in one direction and the women in another—and the women saved her a place at their table, while the men ignored her. Instinct told Altman to ignore the warning rather than insult the women by rebuffing their invitation.

Over the next few days, she continued to join the women during breaks, a choice that gave her a comfortable haven from which to observe the unfamiliar office culture. But it didn’t take her long to notice that some of the men spent the break at their desks reading magazines, and Altman determined that she could do the same on occasion. Finally, after paying

close attention to the conversations around her, she learned that several of the men were interested in mountain biking. Because Altman wanted to buy a mountain bike, she approached them for advice. Thus, over time, she established herself as something of a free agent, sometimes sitting with the women and other times engaging with the men.

And as it happened, one of the women she'd sat with on her very first day, the department secretary, was married to one of the engineers. The secretary took it upon herself to include Altman in social gatherings, a turn of events that probably wouldn't have occurred if Altman had alienated her female coworkers on that first day. "Had I just gone to try to break in with [the men] and not had her as an ally, it would never have happened," she says.

Looking back, Altman believes the experience greatly helped her gain a clearer sense of her personal strengths and capabilities, preparing her for other difficult situations. Her tenure in Japan taught her to observe closely and to avoid jumping to conclusions based on cultural assumptions—invaluable skills in her current position at Motorola, where she leads efforts to smooth alliances with other corporate cultures, including those of Motorola's different regional operations.

Altman has come to believe that she wouldn't have been as able to do the Motorola job if she hadn't lived in a foreign country and experienced the dissonance of cultures: ". . . even if you're sitting in the same room, ostensibly agreeing . . . unless you understand the frame of reference, you're probably missing a bunch of what's going on." Altman also credits her crucible with building her confidence—she feels that she can cope with just about anything that comes her way.

People can feel the stigma of cultural differences much closer to home, as well. Muriel ("Mickie") Siebert, the first woman to own a seat on the New York Stock Exchange, found her crucible on the Wall Street of the 1950s and 1960s, an arena so sexist that she couldn't get a job as a stockbroker until she took her first name off her résumé and substituted a genderless initial. Other than the secretaries and the occasional analyst, women were few and far between. That she was Jewish was another strike against her at a time, she points out, when most of big business was "not nice" to either women or Jews. But Siebert wasn't broken or defeated. Instead, she emerged stronger, more focused, and more determined to change the status quo that excluded her.

When we interviewed Siebert, she described her way of addressing anti-

Semitism—a technique that quieted the offensive comments of her peers without destroying the relationships she needed to do her job effectively. According to Siebert, at the time it was part of doing business to have a few drinks at lunch. She remembers, “Give somebody a couple of drinks, and they would talk about the Jews.” She had a greeting card she used for those occasions that went like this:

*Roses are reddish,
Violets are bluish,
In case you don’t know,
I am Jewish.*

Siebert would have the card hand-delivered to the person who had made the anti-Semitic remarks, and on the card she had written, “Enjoyed lunch.” As she recounts, “They got that card in the afternoon, and I never had to take any of that nonsense again. And I never embarrassed anyone, either.” It was because she was unable to get credit for the business she was bringing in at any of the large Wall Street firms that she bought a seat on the New York Stock Exchange and started working for herself.

In subsequent years, she went on to found Muriel Siebert & Company (now Siebert Financial Corporation) and has dedicated herself to helping other people avoid some of the difficulties she faced as a young professional. A prominent advocate for women in business and a leader in developing financial products directed at women, she’s also devoted to educating children about financial opportunities and responsibility.

We didn’t interview lawyer and presidential adviser Vernon Jordan for this article, but he, too, offers a powerful reminder of how prejudice can prove transformational rather than debilitating. In *Vernon Can Read! A Memoir* (Public Affairs, 2001), Jordan describes the vicious baiting he was subjected to as a young man. The man who treated him in this offensive way was his employer, Robert F. Maddox. Jordan served the racist former mayor of Atlanta at dinner, in a white jacket, with a napkin over his arm. He also functioned as Maddox’s chauffeur. Whenever Maddox could, he would derisively announce, “Vernon can read!” as if the literacy of a young African-American were a source of wonderment.

Geeks and Geezers

WE DIDN'T SET OUT TO LEARN about crucibles. Our research for this article and for our new book, *Geeks and Geezers*, was actually designed to uncover the ways that *era* influences a leader's motivation and aspirations. We interviewed 43 of today's top leaders in business and the public sector, limiting our subjects to people born in or before 1925, or in or after 1970. To our delight, we learned a lot about how age and era affect leadership style.

Our geeks and geezers (the affectionate shorthand we eventually used to describe the two groups) had very different ideas about paying your dues, work-life balance, the role of heroes, and more. But they also shared some striking similarities—among them a love of learning and strong sense of values. Most intriguing, though, both our geeks and our geezers told us again and again how certain experiences inspired them, shaped them, and, indeed, taught them to lead. And so, as the best research often does, our work turned out to be even more interesting than we thought it would be. We continued to explore the influences of era—our findings are described in our book—but at the same time we probed for stories of these crucible experiences. These are the stories we share with you here.

Subjected to this type of abuse, a lesser man might have allowed Maddox to destroy him. But in his memoir, Jordan gives his own interpretation of Maddox's sadistic heckling, a tale that empowered Jordan instead of embittering him. When he looked at Maddox through the rearview mirror, Jordan did not see a powerful member of Georgia's ruling class. He saw a desperate anachronism, a person who lashed out because he knew his time was up. As Jordan writes about Maddox, "His half-mocking, half-serious comments about my education were the death rattle of his culture. When he saw that I was . . . crafting a life for myself that would make me a man in . . . ways he thought of as being a man, he was deeply unnerved."

Maddox's cruelty was the crucible that, consciously or not, Jordan imbued with redemptive meaning. Instead of lashing out or being paralyzed with hatred, Jordan saw the fall of the Old South and imagined his own future freed of the historical shackles of racism. His ability to organize meaning around a potential crisis turned it into the crucible around which his leadership was forged.

Reinvention in the Extreme: The Power of Neoteny

ALL OF OUR INTERVIEW SUBJECTS described their crucibles as opportunities for reinvention—for taking stock of their lives and finding meaning in circumstances many people would see as daunting and potentially incapacitating. In the extreme, this capacity for reinvention comes to resemble eternal youth—a kind of vigor, openness, and an enduring capacity for wonder that is the antithesis of stereotyped old age.

We borrowed a term from biology—“neoteny,” which, according to the *American Heritage Dictionary*, means “retention of juvenile characteristics in the adults of a species”—to describe this quality, this delight in lifelong learning, which every leader we interviewed displayed, regardless of age. To a person, they were full of energy, curiosity, and confidence that the world is a place of wonders spread before them like an endless feast.

Robert Galvin, former Motorola chairman now in his late 70s, spends his weekends windsurfing. Arthur Levitt, Jr., former SEC chairman who turned 71 this year, is an avid Outward Bound trekker. And architect Frank Gehry is now a 72-year-old ice hockey player. But it’s not only an affinity for physical activity that characterizes neoteny—it’s an appetite for learning and self-development, a curiosity and passion for life.

To understand why this quality is so powerful in a leader, it might help to take a quick look at the scientific principle behind it—neoteny as an evolutionary engine. It is the winning, puppyish quality of certain ancient wolves that allowed them to evolve into dogs. Over thousands of years, humans favored wolves that were the friendliest, most approachable, and most curious. Naturally, people were most drawn to the wolves least likely to attack without warning, that readily locked eyes with them, and that seemed almost human in their eager response to

people; the ones, in short, that stayed the most like puppies. Like human infants, they have certain physical qualities that elicit a nurturing response in human adults.

When infants see an adult, they often respond with a smile that begins small and slowly grows into a radiant grin that makes the adult feel at center of the universe. Recent studies of bonding indicate that nursing and other intimate interactions with an infant cause the mother's system to be flooded with oxytocin, a calming, feel-good hormone that is a powerful antidote to cortisol, the hormone produced by stress. Oxytocin appears to be the glue that produces bonding. And the baby's distinctive look and behaviors cause oxytocin to be released in the fortunate adult. That appearance—the one that pulls an involuntary “aaah” out of us whenever we see a baby—and those oxytocin-inducing behaviors allow infants to recruit adults to be their nurturers, essential if such vulnerable and incompletely developed creatures are to survive.

The power of neoteny to recruit protectors and nurturers was vividly illustrated in the former Soviet Union. Forty years ago, a Soviet scientist decided to start breeding silver foxes for neoteny at a Siberian fur farm. The goal was to create a tamer fox that would go with less fuss to slaughter than the typical silver fox. Only the least aggressive, most approachable animals were bred.

The experiment continued for 40 years, and today, after 35 generations, the farm is home to a breed of tame foxes that look and act more like juvenile foxes and even dogs than like their wild forebears. The physical changes in the animals are remarkable (some have floppy, dog-like ears), but what is truly stunning is the change neoteny has wrought in the human response to them. Instead of taking advantage of the fact that these neotenic animals don't snap and snarl on the way to their deaths, their human keepers appear to have been recruited by their newly cute and endearing charges. The keepers and the foxes appear to have formed close bonds, so close that the keepers are trying to find ways to save the animals from slaughter.

Prevailing over Darkness

Some crucible experiences illuminate a hidden and suppressed area of the soul. These are often among the harshest of crucibles, involving, for instance, episodes of illness or violence. In the case of Sidney Rittenberg, now 79, the crucible took the form of 16 years of unjust imprisonment, in solitary confinement, in Communist China. In 1949 Rittenberg was initially jailed, without explanation, by former friends in Chairman Mao Zedong's government and spent his first year in total darkness when he wasn't being interrogated. (Rittenberg later learned that his arrest came at the behest of Communist Party officials in Moscow, who had wrongly identified him as a CIA agent.) Thrown into jail, confined to a tiny, pitch-dark cell, Rittenberg did not rail or panic. Instead, within minutes, he remembered a stanza of verse, four lines recited to him when he was a small child:

*They drew a circle that shut me out,
Heretic, rebel, a thing to flout.
But love and I had the wit to win,
We drew a circle that took them in!*

That bit of verse (adapted from "Outwitted," a poem by Edwin Markham) was the key to Rittenberg's survival. "My God," he thought, "there's my strategy." He drew the prison guards into his circle, developing relationships that would help him adapt to his confinement. Fluent in Chinese, he persuaded the guards to deliver him books and, eventually, provide a candle so that he could read. He also decided, after his first year, to devote himself to improving his mind—making it more scientific, more pure, and more dedicated to socialism. He believed that if he raised his consciousness, his captors would understand him better. And when, over time, the years in the dark began to take an intellectual toll on him and he found his reason faltering, he could still summon fairy tales and childhood stories such as *The Little Engine That Could* and take comfort from their simple messages.

By contrast, many of Rittenberg's fellow prisoners either lashed out in anger or withdrew. "They tended to go up the wall . . . They couldn't make it. And I think the reason was that they didn't understand . . . that happiness . . . is not a function of your circumstances; it's a function of your outlook on life."

Rittenberg's commitment to his ideals continued upon his release. His cell door opened suddenly in 1955, after his first six-year term in prison. He recounts, "Here was a representative of the central government telling me that I had been wronged, that the government was making a formal apology to me . . . and that they would do everything possible to make restitution." When his captors offered him money to start a new life in the United States or to travel in Europe, Rittenberg declined, choosing instead to stay in China and continue his work for the Communist Party.

And even after a second arrest, which put him into solitary confinement for ten years as retaliation for his support of open democracy during the Cultural Revolution, Rittenberg did not allow his spirit to be broken. Instead, he used his time in prison as an opportunity to question his belief system—in particular, his commitment to Marxism and Chairman Mao. "In that sense, prison emancipated me," he says.

Rittenberg studied, read, wrote, and thought, and he learned something about himself in the process: "I realized I had this great fear of being a turncoat, which . . . was so powerful that it prevented me from even looking at [my assumptions] . . . Even to question was an act of betrayal. After I got out . . . the scales fell away from my eyes and I understood that . . . the basic doctrine of arriving at democracy through dictatorship was wrong."

What's more, Rittenberg emerged from prison certain that absolutely nothing in his professional life could break him and went on to start a company with his wife. Rittenberg Associates is a consulting firm dedicated to developing business ties between the United States and China. Today, Rittenberg is as committed to his ideals—if not to his view of the best way to get there—as he was 50 years ago, when he was so severely tested.

Meeting Great Expectations

Fortunately, not all crucible experiences are traumatic. In fact, they can involve a positive, if deeply challenging, experience such as having a demanding boss or mentor. Judge Nathaniel R. Jones of the U.S. Court of Appeals for the Sixth Circuit, for instance, attributes much of his success to his interaction with a splendid mentor. That mentor was J. Maynard Dickerson, a successful attorney—the first black city prosecutor in the United States—and editor of a local African-American newspaper.

Dickerson influenced Jones at many levels. For instance, the older man brought Jones behind the scenes to witness firsthand the great civil rights struggle of the 1950s, inviting him to sit in on conversations with activists like Thurgood Marshall, Walter White, Roy Wilkins, and Robert C. Weaver. Says Jones, “I was struck by their resolve, their humor . . . and their determination not to let the system define them. Rather than just feel beaten down, they turned it around.” The experience no doubt influenced the many important opinions Judge Jones has written in regard to civil rights.

Dickerson was both model and coach. His lessons covered every aspect of Jones’s intellectual growth and presentation of self, including schooling in what we now call “emotional intelligence.” Dickerson set the highest standards for Jones, especially in the area of communication skills—a facility we’ve found essential to leadership. Dickerson edited Jones’s early attempts at writing a sports column with respectful ruthlessness, in red ink, as Jones remembers to this day—marking up the copy so that it looked, as Jones says, “like something chickens had a fight over.” But Dickerson also took the time to explain every single mistake and why it mattered.

His mentor also expected the teenage Jones to speak correctly at all times and would hiss discreetly in his direction if he stumbled. Great expectations are evidence of great respect, and as Jones learned all the complex, often subtle lessons of how to succeed, he was motivated in no small measure by his desire not to disappoint the man he still calls “Mr. Dickerson.” Dickerson gave Jones the kind of intensive mentoring that was tantamount to grooming

him for a kind of professional and moral succession—and Jones has indeed become an instrument for the profound societal change for which Dickerson fought so courageously as well. Jones found life-changing meaning in the attention Dickerson paid to him—attention fueled by a conviction that he, too, though only a teenager, had a vital role to play in society and an important destiny.

Another story of a powerful mentor came to us from Michael Klein, a young man who made millions in Southern California real estate while still in his teens, only to lose it by the time he turned 20 and then go on to start several other businesses. His mentor was his grandfather Max S. Klein, who created the paint-by-numbers fad that swept the United States in the 1950s and 1960s. Klein was only four or five years old when his grandfather approached him and offered to share his business expertise. Over the years, Michael Klein's grandfather taught him to learn from and to cope with change, and the two spoke by phone for an hour every day until shortly before Max Klein's death.

The Essentials of Leadership

In our interviews, we heard many other stories of crucible experiences. Take Jack Coleman, 78-year-old former president of Haverford College in Pennsylvania. He told us of one day, during the Vietnam War, when he heard that a group of students was planning to pull down the American flag and burn it—and that former members of the school's football team were going to make sure the students didn't succeed. Seemingly out of nowhere, Coleman had the idea to preempt the violence by suggesting that the protesting students take down the flag, wash it, and then put it back up—a crucible moment that even now elicits tremendous emotion in Coleman as he describes that day.

There's also Common Cause founder John W. Gardner, who died earlier this year at 89. He identified his arduous training as a Marine during World War II as the crucible in which his leadership abilities emerged. Architect Frank Gehry spoke of the biases he experienced as a Jew in college. Jeff Wilke, a general manager at a major manufacturer, told us of the day he learned that an employee had been killed in his plant—an experience that taught him that leadership was about much more than making quarterly numbers.

So, what allowed these people to not only cope with these difficult situations but also learn from them? We believe that great leaders possess four essential skills, and, we were surprised to learn, these happen to be the same skills that allow a person to find meaning in what could be a debilitating experience. First is the ability to engage others in shared meaning. Consider Sidney Harman, who dived into a chaotic work environment to mobilize employees around an entirely new approach to management. Second is a distinctive and compelling voice. Look at Jack Coleman's ability to defuse a potentially violent situation with only his words. Third is a sense of integrity (including a strong set of values). Here, we point again to Coleman, whose values prevailed even during the emotionally charged clash between peace demonstrators and the angry (and

strong) former football team members.

But by far the most critical skill of the four is what we call “adaptive capacity.” This is, in essence, applied creativity—an almost magical ability to transcend adversity, with all its attendant stresses, and to emerge stronger than before. It’s composed of two primary qualities: the ability to grasp context, and hardiness. The ability to grasp context implies an ability to weigh a welter of factors, ranging from how very different groups of people will interpret a gesture to being able to put a situation in perspective. Without this, leaders are utterly lost, because they cannot connect with their constituents. M. Douglas Ivester, who succeeded Roberto Goizueta at Coca-Cola, exhibited a woeful inability to grasp context, lasting just 28 months on the job. For example, he demoted his highest-ranked African-American employee even as the company was losing a \$200 million class-action suit brought by black employees—and this in Atlanta, a city with a powerful African-American majority. Contrast Ivester with Vernon Jordan. Jordan realized his boss’s time was up—not just his time in power, but the era that formed him. And so Jordan was able to see past the insults and recognize his boss’s bitterness for what it was—desperate lashing out.

Hardiness is just what it sounds like—the perseverance and toughness that enable people to emerge from devastating circumstances without losing hope. Look at Michael Klein, who experienced failure but didn’t let it defeat him. He found himself with a single asset—a tiny software company he’d acquired. Klein built it into Transoft Networks, which Hewlett-Packard acquired in 1999. Consider, too, Mickie Siebert, who used her sense of humor to curtail offensive conversations. Or Sidney Rittenberg’s strength during his imprisonment. He drew on his personal memories and inner strength to emerge from his lengthy prison term without bitterness.

It is the combination of hardiness and ability to grasp context that, above all, allows a person to not only survive an ordeal, but to learn from it, and to emerge stronger, more engaged, and more committed than ever. These attributes allow leaders to grow from their crucibles, instead of being destroyed by them—to find opportunity where others might find only despair. This is the stuff of true leadership.

Level 5 Leadership

The Triumph of Humility and Fierce Resolve.

by Jim Collins

IN 1971, A SEEMINGLY ordinary man named Darwin E. Smith was named chief executive of Kimberly-Clark, a stodgy old paper company whose stock had fallen 36% behind the general market during the previous 20 years. Smith, the company's mild-mannered in-house lawyer, wasn't so sure the board had made the right choice—a feeling that was reinforced when a Kimberly-Clark director pulled him aside and reminded him that he lacked some of the qualifications for the position. But CEO he was, and CEO he remained for 20 years.

What a 20 years it was. In that period, Smith created a stunning transformation at Kimberly-Clark, turning it into the leading consumer paper products company in the world. Under his stewardship, the company beat its rivals Scott Paper and Procter & Gamble. And in doing so, Kimberly-Clark generated cumulative stock returns that were 4.1 times greater than those of the general market, outperforming venerable companies such as Hewlett-Packard, 3M, Coca-Cola, and General Electric.

Smith's turnaround of Kimberly-Clark is one the best examples in the twentieth century of a leader taking a company from merely good to truly great. And yet few people—even ardent students of business history—have heard of Darwin Smith. He probably would have liked it that way. Smith is a classic example of a Level 5 leader—an individual who blends extreme personal humility with intense professional will. According to our five-year research study, executives who possess this paradoxical combination of traits are catalysts for the statistically rare event of transforming a good company into a great one. (The research is described in the sidebar “One Question, Five Years, 11 Companies.”)

“Level 5” refers to the highest level in a hierarchy of executive

capabilities that we identified during our research. Leaders at the other four levels in the hierarchy can produce high degrees of success but not enough to elevate companies from mediocrity to sustained excellence. (For more details about this concept, see the exhibit “The Level 5 Hierarchy.”) And while Level 5 leadership is not the only requirement for transforming a good company into a great one—other factors include getting the right people on the bus (and the wrong people off the bus) and creating a culture of discipline—our research shows it to be essential. Good-to-great transformations don’t happen without Level 5 leaders at the helm. They just don’t.

The Level 5 hierarchy

The Level 5 leader sits on top of a hierarchy of capabilities and is, according to our research, a necessary requirement for transforming an organization from good to great. But what lies beneath? Four other layers, each one appropriate in its own right but none with the power of Level 5. Individuals do not need to proceed sequentially through each level of the hierarchy to reach the top, but to be a full-fledged Level 5 requires the capabilities of all the lower levels, plus the special characteristics of Level 5.

Level 5

Executive: Builds enduring greatness through a paradoxical combination of personal humility plus professional will.

Level 4

Effective leader: Catalyzes commitment to and vigorous pursuit of a clear and compelling vision; stimulates the group to high performance standards.

Level 3

Competent manager: Organizes people and resources toward the effective and efficient pursuit of predetermined objectives.

Level 2

Contributing team member: Contributes to the achievement of

group objectives; works effectively with others in a group setting.

Level 1

Highly capable individual: Makes productive contributions through talent, knowledge, skills, and good work habits.

Idea in Brief

Out of 1,435 *Fortune* 500 companies that renowned management researcher Jim Collins studied, only 11 achieved and sustained greatness—garnering stock returns at least three times the market’s—for 15 years after a major transition period.

What did these 11 companies have in common? Each had a “Level 5” leader at the helm.

Level 5 leaders blend the paradoxical combination of **deep personal humility** with **intense professional will**. This rare combination also defies our assumptions about what makes a great leader.

Celebrities like Lee Iacocca may make headlines. But mild-mannered, steely leaders like Darwin Smith of Kimberly-Clark boost their companies to greatness—and keep them there.

Example: Darwin Smith—CEO at paper-products maker Kimberly-Clark from 1971 to 1991—epitomizes Level 5 leadership. Shy, awkward, shunning attention, he also showed iron will, determinedly redefining the firm’s core business despite Wall Street’s skepticism. The formerly lackluster Kimberly-Clark became the worldwide leader in its industry, generating stock returns 4.1 times greater than the general market’s.

Not What You Would Expect

Our discovery of Level 5 leadership is counterintuitive. Indeed, it is countercultural. People generally assume that transforming companies from good to great requires larger-than-life leaders—big personalities like Lee Iacocca, Al Dunlap, Jack Welch, and Stanley Gault, who make headlines and become celebrities.

Compared with those CEOs, Darwin Smith seems to have come from Mars. Shy, unpretentious, even awkward, Smith shunned attention. When a journalist asked him to describe his management style, Smith just stared back at the scribe from the other side of his thick black-rimmed glasses. He was dressed unfashionably, like a farm boy wearing his first J.C. Penney suit. Finally, after a long and uncomfortable silence, he said, “Eccentric.” Needless to say, the *Wall Street Journal* did not publish a splashy feature on Darwin Smith.

Idea in Practice

Humility + Will = Level 5

How do Level 5 leaders manifest humility? They routinely credit others, external factors, and good luck for their companies' success. But when results are poor, they blame themselves. They also act quietly, calmly, and determinedly—relying on inspired standards, not inspiring charisma, to motivate.

Inspired standards demonstrate Level 5 leaders' unwavering will. Utterly intolerant of mediocrity, they are stoic in their resolve to do whatever it takes to produce great results—terminating everything else. And they select superb successors, wanting their companies to become even more successful in the future.

Can You Develop Level 5 Leadership?

Level 5 leaders sit atop a hierarchy of four more common leadership levels—and possess the skills of all four. For example, Level 4 leaders catalyze commitment to and vigorous pursuit of a clear, compelling vision. Can you move from Level 4 to Level 5? Perhaps, *if* you have the Level 5 “seed” within you.

Leaders *without* the seed tend to have monumental egos they can't subjugate to something larger and more sustaining than themselves, i.e., their companies. But for leaders *with* the seed, the right conditions—such as self-reflection or a profoundly transformative event, such as a life-threatening illness—can stimulate the seed to sprout.

Growing to Level 5

Grow Level 5 seeds by practicing these good-to-great disciplines of Level 5 leaders.

First who

Attend to people first, strategy second. Get the right people on the bus and the wrong people off—*then* figure out where to drive it.

Stockdale paradox

Deal with the brutal facts of your current reality—while maintaining absolute faith that you’ll prevail.

Buildup-breakthrough flywheel

Keep pushing your organizational “flywheel.” With consistent effort, momentum increases until—bang!—the wheel hits the breakthrough point.

The hedgehog concept

Think of your company as three intersecting circles: what it can be best at, how its economics work best, and what ignites its people’s passions. Eliminate *everything* else.

But if you were to consider Smith soft or meek, you would be terribly mistaken. His lack of pretense was coupled with a fierce, even stoic, resolve toward life. Smith grew up on an Indiana farm and put himself through night school at Indiana University by working the day shift at International Harvester. One day, he lost a finger on the job. The story goes that he went to

class that evening and returned to work the very next day. Eventually, this poor but determined Indiana farm boy earned admission to Harvard Law School.

He showed the same iron will when he was at the helm of Kimberly-Clark. Indeed, two months after Smith became CEO, doctors diagnosed him with nose and throat cancer and told him he had less than a year to live. He duly informed the board of his illness but said he had no plans to die anytime soon. Smith held to his demanding work schedule while commuting weekly from Wisconsin to Houston for radiation therapy. He lived 25 more years, 20 of them as CEO.

Smith's ferocious resolve was crucial to the rebuilding of Kimberly-Clark, especially when he made the most dramatic decision in the company's history: selling the mills.

To explain: Shortly after he took over, Smith and his team had concluded that the company's traditional core business—coated paper—was doomed to mediocrity. Its economics were bad and the competition weak. But, they reasoned, if Kimberly-Clark were thrust into the fire of the consumer paper products business, better economics and world-class competition like Procter & Gamble would force it to achieve greatness or perish.

One Question, Five Years, 11 Companies

THE LEVEL 5 DISCOVERY DERIVES from a research project that began in 1996, when my research teams and I set out to answer one question: Can a good company become a great company and, if so, how? Most great companies grew up with superb parents—people like George Merck, David Packard, and Walt Disney—who instilled greatness early on. But what about the vast majority of companies that wake up partway through life and realize that they're good but not great?

To answer that question, we looked for companies that had shifted from good performance to great performance—and sustained it. We identified comparison companies that had failed to make that sustained shift. We then studied the contrast between the two groups to discover common variables that distinguished those who made and sustained a shift from those who could have but didn't.

More precisely, we searched for a specific pattern: cumulative stock returns at or below the general stock market for 15 years, punctuated by a transition point, then cumulative returns at least three times the market over the next 15 years. (See the accompanying exhibit.) We used data from the University of Chicago Center for Research in Security Prices and adjusted for stock splits and all dividends reinvested. The shift had to be distinct from the industry; if the whole industry showed the same shift, we'd drop the company. We began with 1,435 companies that appeared on the *Fortune* 500 from 1965 to 1995; we found 11 good-to-great examples. That's not a sample; that's the total number that jumped all our hurdles and passed into the study.

Those that made the cut averaged cumulative stock returns 6.9 times the general stock market for the 15 years after the point of transition.

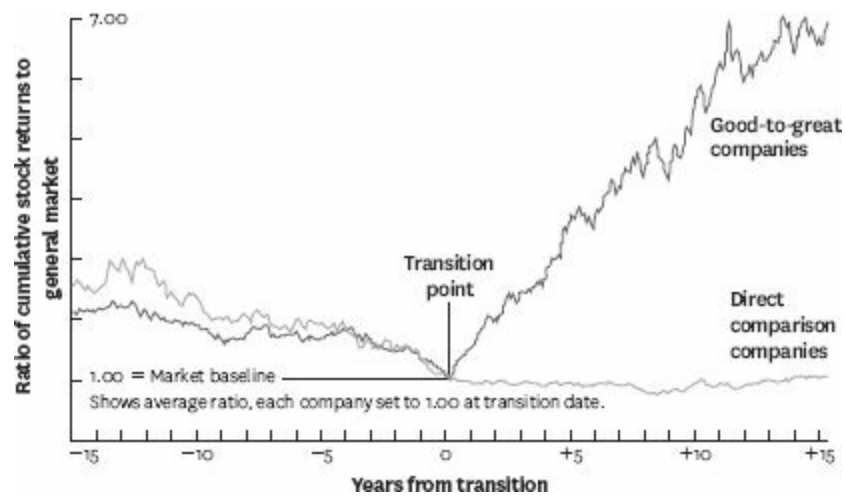
To put that in perspective, General Electric under Jack Welch outperformed the general stock market by 2.8:1 during his tenure from 1986 to 2000. One dollar invested in a mutual fund of the good-to-great companies in 1965 grew to \$470 by 2000 compared with \$56 in the general stock market. These are remarkable numbers, made all the more so by the fact that they came from previously unremarkable companies.

For each good-to-great example, we selected the best direct comparison, based on similarity of business, size, age, customers, and performance leading up to the transition. We also constructed a set of six “unsustained” comparisons (companies that showed a short-lived shift but then fell off) to address the question of sustainability. To be conservative, we consistently picked comparison companies that, if anything, were in better shape than the good-to-great companies were in the years just before the transition.

With 22 research associates working in groups of four to six at a time from 1996 to 2000, our study involved a wide range of both qualitative and quantitative analyses. On the qualitative front, we collected nearly 6,000 articles, conducted 87 interviews with key executives, analyzed companies’ internal strategy documents, and culled through analysts’ reports. On the quantitative front, we ran financial metrics, examined executive compensation, compared patterns of management turnover, quantified company layoffs and restructurings, and calculated the effect of acquisitions and divestitures on companies’ stocks. We then synthesized the results to identify the drivers of good-to-great transformations. One was Level 5 leadership. (The others are described in the sidebar “Not by Level 5 Alone.”)

Since only 11 companies qualified as good-to-great, a research finding had to meet a stiff standard before we would deem it significant. Every component in the final framework showed up in all 11 good-to-great companies during the transition era, regardless of

industry (from steel to banking), transition decade (from the 1950s to the 1990s), circumstances (from plodding along to dire crisis), or size (from tens of millions to tens of billions). Additionally, every component had to show up in less than 30% of the comparison companies during the relevant years. Level 5 easily made it into the framework as one of the strongest, most consistent contrasts between the good-to-great and the comparison companies.



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And so, like the general who burned the boats upon landing on enemy soil, leaving his troops to succeed or die, Smith announced that Kimberly-Clark would sell its mills—even the namesake mill in Kimberly, Wisconsin. All proceeds would be thrown into the consumer business, with investments in brands like Huggies diapers and Kleenex tissues. The business media called the move stupid, and Wall Street analysts downgraded the stock. But Smith never wavered. Twenty-five years later, Kimberly-Clark owned Scott Paper and beat Procter & Gamble in six of eight product categories. In retirement, Smith reflected on his exceptional performance, saying simply, “I never stopped trying to become qualified for the job.”

Not What We Expected, Either

We'll look in depth at Level 5 leadership, but first let's set an important context for our findings. We were not looking for Level 5 or anything like it. Our original question was, Can a good company become a great one and, if so, how? In fact, I gave the research teams explicit instructions to downplay the role of top executives in their analyses of this question so we wouldn't slip into the simplistic "credit the leader" or "blame the leader" thinking that is so common today.

But Level 5 found us. Over the course of the study, research teams kept saying, "We can't ignore the top executives even if we want to. There is something consistently unusual about them." I would push back, arguing, "The comparison companies also had leaders. So what's different here?" Back and forth the debate raged. Finally, as should always be the case, the data won. The executives at companies that went from good to great and sustained that performance for 15 years or more were all cut from the same cloth—one remarkably different from that which produced the executives at the comparison companies in our study. It didn't matter whether the company was in crisis or steady state, consumer or industrial, offering services or products. It didn't matter when the transition took place or how big the company. The successful organizations all had a Level 5 leader at the time of transition.

Furthermore, the absence of Level 5 leadership showed up consistently across the comparison companies. The point: Level 5 is an empirical finding, not an ideological one. And that's important to note, given how much the Level 5 finding contradicts not only conventional wisdom but much of management theory to date. (For more about our findings on good-to-great transformations, see the sidebar "Not by Level 5 Alone.")

Humility + Will = Level 5

Level 5 leaders are a study in duality: modest and willful, shy and fearless. To grasp this concept, consider Abraham Lincoln, who never let his ego get in the way of his ambition to create an enduring great nation. Author Henry Adams called him “a quiet, peaceful, shy figure.” But those who thought Lincoln’s understated manner signaled weakness in the man found themselves terribly mistaken—to the scale of 250,000 Confederate and 360,000 Union lives, including Lincoln’s own.

It might be a stretch to compare the 11 Level 5 CEOs in our research to Lincoln, but they did display the same kind of duality. Take Colman M. Mockler, CEO of Gillette from 1975 to 1991. Mockler, who faced down three takeover attempts, was a reserved, gracious man with a gentle, almost patrician manner. Despite epic battles with raiders—he took on Ronald Perelman twice and the former Coniston Partners once—he never lost his shy, courteous style. At the height of crisis, he maintained a calm business-as-usual demeanor, dispensing first with ongoing business before turning to the takeover.

And yet, those who mistook Mockler’s outward modesty as a sign of inner weakness were beaten in the end. In one proxy battle, Mockler and other senior executives called thousands of investors, one by one, to win their votes. Mockler simply would not give in. He chose to fight for the future greatness of Gillette even though he could have pocketed millions by flipping his stock.

Not by Level 5 Alone

Level 5 leadership is an essential factor for taking a company from good to great, but it's not the only one. Our research uncovered multiple factors that deliver companies to greatness. And it is the combined package—Level 5 plus these other drivers—that takes companies beyond unremarkable. There is a symbiotic relationship between Level 5 and the rest of our findings: Level 5 enables implementation of the other findings, and practicing the other findings may help you get to Level 5. We've already talked about who Level 5 leaders are; the rest of our findings describe what they do. Here is a brief look at some of the other key findings.

First Who

We expected that good-to-great leaders would start with the vision and strategy. Instead, they attended to people first, strategy second. They got the right people on the bus, moved the wrong people off, ushered the right people to the right seats—and then they figured out where to drive it.

Stockdale Paradox

This finding is named after Admiral James Stockdale, winner of the Medal of Honor, who survived seven years in a Vietcong POW camp by hanging on to two contradictory beliefs:

His life couldn't be worse at the moment, and his life would someday be better than ever. Like Stockdale, people at the good-to-great companies in our research confronted the most brutal facts of their current reality, yet simultaneously maintained absolute faith that they would prevail in the end. And they held both disciplines—faith and facts—at the same time, all the time.

Buildup-Breakthrough Flywheel

Good-to-great transformations do not happen overnight or in one big leap. Rather, the process resembles relentlessly pushing a giant, heavy flywheel in one direction. At first, pushing it gets the flywheel to turn once. With consistent effort, it goes two turns, then five, then ten, building increasing momentum until—bang!—the wheel hits the breakthrough point, and the momentum really kicks in. Our comparison companies never sustained the kind of breakthrough momentum that the good-to-great companies did; instead, they lurched back and forth with radical change programs, reactionary moves, and restructurings.

The Hedgehog Concept

In a famous essay, philosopher and scholar Isaiah Berlin described two approaches to thought and life using a simple parable: The fox knows a little about many things, but the hedgehog knows only one big thing very well. The fox is complex; the hedgehog simple. And the hedgehog wins. Our research shows that breakthroughs require a simple, hedgehog-like understanding of three intersecting circles: what a company can be the best in the world at, how its economics work best, and what best ignites the passions of its people. Breakthroughs happen when you get the hedgehog concept and become systematic and consistent with it, eliminating virtually anything that does not fit in the three circles.

Technology Accelerators

The good-to-great companies had a paradoxical relationship with technology. On the one hand, they assiduously avoided jumping on new technology bandwagons. On the other, they were pioneers in the application of carefully selected technologies, making bold, farsighted investments in those that directly linked to their hedgehog concept. Like turbochargers, these technology accelerators create an explosion in flywheel momentum.

A Culture of Discipline

When you look across the good-to-great transformations, they

consistently display three forms of discipline: disciplined people, disciplined thought, and disciplined action. When you have disciplined people, you don't need hierarchy. When you have disciplined thought, you don't need bureaucracy. When you have disciplined action, you don't need excessive controls. When you combine a culture of discipline with an ethic of entrepreneurship, you get the magical alchemy of great performance.

Consider the consequences had Mockler capitulated. If a share flipper had accepted the full 44% price premium offered by Perelman and then invested those shares in the general market for ten years, he still would have come out 64% behind a shareholder who stayed with Mockler and Gillette. If Mockler had given up the fight, it's likely that none of us would be shaving with Sensor, Lady Sensor, or the Mach III—and hundreds of millions of people would have a more painful battle with daily stubble.

Sadly, Mockler never had the chance to enjoy the full fruits of his efforts. In January 1991, Gillette received an advance copy of *Forbes*. The cover featured an artist's rendition of the publicity-shy Mockler standing on a mountaintop, holding a giant razor above his head in a triumphant pose. Walking back to his office just minutes after seeing this public acknowledgment of his 16 years of struggle, Mockler crumpled to the floor and died of a massive heart attack.

Even if Mockler had known he would die in office, he could not have changed his approach. His placid persona hid an inner intensity, a dedication to making anything he touched the best—not just because of what he would get but because he couldn't imagine doing it any other way. Mockler could not give up the company to those who would destroy it, any more than Lincoln would risk losing the chance to build an enduring great nation.

A Compelling Modesty

The Mockler story illustrates the modesty typical of Level 5 leaders. (For a summary of Level 5 traits, see the exhibit “The Yin and Yang of Level 5.”) Indeed, throughout our interviews with such executives, we were struck by the way they talked about themselves—or rather, didn’t talk about themselves. They’d go on and on about the company and the contributions of other executives, but they would instinctively deflect discussion about their own role. When pressed to talk about themselves, they’d say things like, “I hope I’m not sounding like a big shot,” or “I don’t think I can take much credit for what happened. We were blessed with marvelous people.” One Level 5 leader even asserted, “There are a lot of people in this company who could do my job better than I do.”

By contrast, consider the courtship of personal celebrity by the comparison CEOs. Scott Paper, the comparison company to Kimberly-Clark, hired Al Dunlap as CEO—a man who would tell anyone who would listen (and many who would have preferred not to) about his accomplishments. After 19 months atop Scott Paper, Dunlap said in *BusinessWeek*, “The Scott story will go down in the annals of American business history as one of the most successful, quickest turnarounds ever. It makes other turnarounds pale by comparison.” He personally accrued \$100 million for 603 days of work at Scott Paper—about \$165,000 per day—largely by slashing the workforce, halving the R&D budget, and putting the company on growth steroids in preparation for sale. After selling off the company and pocketing his quick millions, Dunlap wrote an autobiography in which he boastfully dubbed himself “Rambo in pinstripes.” It’s hard to imagine Darwin Smith thinking, “Hey, that Rambo character reminds me of me,” let alone stating it publicly.

The Yin and Yang of Level 5

Personal humility

Demonstrates a compelling modesty, shunning public adulation; never boastful.

Acts with quiet, calm determination; relies principally on inspired standards, not inspiring charisma, to motivate.

Channels ambition into the company, not the self; sets up successors for even more greatness in the next generation.

Looks in the mirror, not out the window, to apportion responsibility for poor results, never blaming other people, external factors, or bad luck.

Professional will

Creates superb results, a clear catalyst in the transition from good to great.

Demonstrates an unwavering resolve to do whatever must be done to produce the best long-term results, no matter how difficult.

Sets the standard of building an enduring great company; will settle for nothing less.

Looks out the window, not in the mirror, to apportion credit for the success of the company—to other people, external factors, and good luck.

Granted, the Scott Paper story is one of the more dramatic in our study, but it's not an isolated case. In more than two-thirds of the comparison companies, we noted the presence of a gargantuan ego that contributed to the demise or continued mediocrity of the company. We found this pattern particularly strong in the unsustained comparison companies—the companies that would show a shift in performance under a talented yet egocentric Level 4 leader, only to decline in later years.

Lee Iacocca, for example, saved Chrysler from the brink of catastrophe,

performing one of the most celebrated (and deservedly so) turnarounds in U.S. business history. The automaker's stock rose 2.9 times higher than the general market about halfway through his tenure. But then Iacocca diverted his attention to transforming himself. He appeared regularly on talk shows like the *Today Show* and *Larry King Live*, starred in more than 80 commercials, entertained the idea of running for president of the United States, and promoted his autobiography, which sold 7 million copies worldwide. Iacocca's personal stock soared, but Chrysler's stock fell 31% below the market in the second half of his tenure.

And once Iacocca had accumulated all the fame and perks, he found it difficult to leave center stage. He postponed his retirement so many times that Chrysler's insiders began to joke that Iacocca stood for "I Am Chairman of Chrysler Corporation Always." When he finally retired, he demanded that the board continue to provide a private jet and stock options. Later, he joined forces with noted takeover artist Kirk Kerkorian to launch a hostile bid for Chrysler. (It failed.) Iacocca did make one final brilliant decision: He picked a modest yet determined man—perhaps even a Level 5—as his successor. Bob Eaton rescued Chrysler from its second near-death crisis in a decade and set the foundation for a more enduring corporate transition.

An Unwavering Resolve

Besides extreme humility, Level 5 leaders also display tremendous professional will. When George Cain became CEO of Abbott Laboratories, it was a drowsy, family-controlled business sitting at the bottom quartile of the pharmaceutical industry, living off its cash cow, erythromycin. Cain was a typical Level 5 leader in his lack of pretense; he didn't have the kind of inspiring personality that would galvanize the company. But he had something much more powerful: inspired standards. He could not stand mediocrity in any form and was utterly intolerant of anyone who would accept the idea that good is good enough. For the next 14 years, he relentlessly imposed his will for greatness on Abbott Labs.

Among Cain's first tasks was to destroy one of the root causes of Abbott's middling performance: nepotism. By systematically rebuilding both the board and the executive team with the best people he could find, Cain made his statement. Family ties no longer mattered. If you couldn't become the best executive in the industry within your span of responsibility, you would lose your paycheck.

Such near-ruthless rebuilding might be expected from an outsider brought in to turn the company around, but Cain was an 18-year insider—and a part of the family, the son of a previous president. Holiday gatherings were probably tense for a few years in the Cain clan—"Sorry I had to fire you. Want another slice of turkey?"—but in the end, family members were pleased with the performance of their stock. Cain had set in motion a profitable growth machine. From its transition in 1974 to 2000, Abbott created shareholder returns that beat the market 4.5:1, outperforming industry superstars Merck and Pfizer by a factor of two.

Another good example of iron-willed Level 5 leadership comes from Charles R. "Cork" Walgreen III, who transformed dowdy Walgreens into a company that outperformed the stock market 16:1 from its transition in 1975 to 2000. After years of dialogue and debate within his executive team about what to do with Walgreens' food-service operations, this CEO sensed the

team had finally reached a watershed: The company's brightest future lay in convenient drugstores, not in food service. Dan Jorndt, who succeeded Walgreen in 1988, describes what happened next:

Cork said at one of our planning committee meetings, "Okay, now I am going to draw the line in the sand. We are going to be out of the restaurant business completely in five years." At the time we had more than 500 restaurants. You could have heard a pin drop. He said, "I want to let everybody know the clock is ticking." Six months later we were at our next planning committee meeting and someone mentioned just in passing that we had only five years to be out of the restaurant business. Cork was not a real vociferous fellow. He sort of tapped on the table and said, "Listen, you now have four-and-a-half years. I said you had five years six months ago. Now you've got four-and-a-half years." Well, that next day things really clicked into gear for winding down our restaurant business. Cork never wavered. He never doubted. He never second-guessed.

Like Darwin Smith selling the mills at Kimberly-Clark, Cork Walgreen required stoic resolve to make his decisions. Food service was not the largest part of the business, although it did add substantial profits to the bottom line. The real problem was more emotional than financial. Walgreens had, after all, invented the malted milk shake, and food service had been a long-standing family tradition dating back to Cork's grandfather. Not only that, some food-service outlets were even named after the CEO—for example, a restaurant chain named Corky's. But no matter; if Walgreen had to fly in the face of family tradition in order to refocus on the one arena in which Walgreens could be the best in the world—convenient drugstores—and terminate everything else that would not produce great results, then Cork would do it. Quietly, doggedly, simply.

One final, yet compelling, note on our findings about Level 5: Because Level 5 leaders have ambition not for themselves but for their companies, they routinely select superb successors. Level 5 leaders want to see their companies become even more successful in the next generation and are comfortable with the idea that most people won't even know that the roots of

that success trace back to them. As one Level 5 CEO said, “I want to look from my porch, see the company as one of the great companies in the world someday, and be able to say, ‘I used to work there.’” By contrast, Level 4 leaders often fail to set up the company for enduring success. After all, what better testament to your own personal greatness than that the place falls apart after you leave?

In more than three-quarters of the comparison companies, we found executives who set up their successors for failure, chose weak successors, or both. Consider the case of Rubbermaid, which grew from obscurity to become one of *Fortune*’s most admired companies—and then, just as quickly, disintegrated into such sorry shape that it had to be acquired by Newell.

The architect of this remarkable story was a charismatic and brilliant leader named Stanley C. Gault, whose name became synonymous in the late 1980s with Rubbermaid’s success. Across the 312 articles collected by our research team about the company, Gault comes through as a hard-driving, egocentric executive. In one article, he responds to the accusation of being a tyrant with the statement, “Yes, but I’m a sincere tyrant.” In another, drawn directly from his own comments on leading change, the word “I” appears 44 times, while the word “we” appears 16 times. Of course, Gault had every reason to be proud of his executive success: Rubbermaid generated 40 consecutive quarters of earnings growth under his leadership—an impressive performance, to be sure, and one that deserves respect.

But Gault did not leave behind a company that would be great without him. His chosen successor lasted a year on the job and the next in line faced a management team so shallow that he had to temporarily shoulder four jobs while scrambling to identify a new number-two executive. Gault’s successors struggled not only with a management void but also with strategic voids that would eventually bring the company to its knees.

Of course, you might say—as one *Fortune* article did—that the fact that Rubbermaid fell apart after Gault left proves his greatness as a leader. Gault was a tremendous Level 4 leader, perhaps one of the best in the last 50 years. But he was not at Level 5, and that is one crucial reason why Rubbermaid went from good to great for a brief, shining moment and then just as quickly went from great to irrelevant.

The Window and the Mirror

As part of our research, we interviewed Alan L. Wurtzel, the Level 5 leader responsible for turning Circuit City from a ramshackle company on the edge of bankruptcy into one of America's most successful electronics retailers. In the 15 years after its transition date in 1982, Circuit City outperformed the market 18.5:1.

We asked Wurtzel to list the top five factors in his company's transformation, ranked by importance. His number one factor? Luck. "We were in a great industry, with the wind at our backs," he said. But wait a minute, we retorted, Silo—your comparison company—was in the same industry, with the same wind and bigger sails. The conversation went back and forth, with Wurtzel refusing to take much credit for the transition, preferring to attribute it largely to just being in the right place at the right time. Later, when we asked him to discuss the factors that would sustain a good-to-great transformation, he said, "The first thing that comes to mind is luck. I was lucky to find the right successor."

Luck. What an odd factor to talk about. Yet the Level 5 leaders we identified invoked it frequently. We asked an executive at steel company Nucor why it had such a remarkable track record for making good decisions. His response? "I guess we were just lucky." Joseph F. Cullman III, the Level 5 CEO of Philip Morris, flat out refused to take credit for his company's success, citing his good fortune to have great colleagues, successors, and predecessors. Even the book he wrote about his career—which he penned at the urging of his colleagues and which he never intended to distribute widely outside the company—had the unusual title *I'm a Lucky Guy*.

At first, we were puzzled by the Level 5 leaders' emphasis on good luck. After all, there is no evidence that the companies that had progressed from good to great were blessed with more good luck (or more bad luck, for that matter) than the comparison companies. But then we began to notice an interesting pattern in the executives at the comparison companies: They often blamed their situations on bad luck, bemoaning the difficulties of the

environment they faced.

Compare Bethlehem Steel and Nucor, for example. Both steel companies operated with products that are hard to differentiate, and both faced a competitive challenge from cheap imported steel. Both companies paid significantly higher wages than most of their foreign competitors. And yet executives at the two companies held completely different views of the same environment.

Bethlehem Steel's CEO summed up the company's problems in 1983 by blaming the imports: "Our first, second, and third problems are imports." Meanwhile, Ken Iverson and his crew at Nucor saw the imports as a blessing: "Aren't we lucky; steel is heavy, and they have to ship it all the way across the ocean, giving us a huge advantage." Indeed, Iverson saw the first, second, and third problems facing the U.S. steel industry not in imports but in management. He even went so far as to speak out publicly against government protection against imports, telling a gathering of stunned steel executives in 1977 that the real problems facing the industry lay in the fact that management had failed to keep pace with technology.

The emphasis on luck turns out to be part of a broader pattern that we have come to call "the window and the mirror." Level 5 leaders, inherently humble, look out the window to apportion credit—even undue credit—to factors outside themselves. If they can't find a specific person or event to give credit to, they credit good luck. At the same time, they look in the mirror to assign responsibility, never citing bad luck or external factors when things go poorly. Conversely, the comparison executives frequently looked out the window for factors to blame but preened in the mirror to credit themselves when things went well.

The funny thing about the window-and-mirror concept is that it does not reflect reality. According to our research, the Level 5 leaders were responsible for their companies' transformations. But they would never admit that. We can't climb inside their heads and assess whether they deeply believed what they saw through the window and in the mirror. But it doesn't really matter, because they acted as if they believed it, and they acted with such consistency that it produced exceptional results.

Born or Bred?

Not long ago, I shared the Level 5 finding with a gathering of senior executives. A woman who had recently become chief executive of her company raised her hand. “I believe what you’ve told us about Level 5 leadership,” she said, “but I’m disturbed because I know I’m not there yet, and maybe I never will be. Part of the reason I got this job is because of my strong ego. Are you telling me that I can’t make my company great if I’m not Level 5?”

“Let me return to the data,” I responded. “Of 1,435 companies that appeared on the *Fortune* 500 since 1965, only 11 made it into our study. In those 11, all of them had Level 5 leaders in key positions, including the CEO role, at the pivotal time of transition. Now, to reiterate, we’re not saying that Level 5 is the only element required for the move from good to great, but it appears to be essential.”

She sat there, quiet for a moment, and you could guess what many people in the room were thinking. Finally, she raised her hand again. “Can you learn to become Level 5?” I still do not know the answer to that question. Our research, frankly, did not delve into how Level 5 leaders come to be, nor did we attempt to explain or codify the nature of their emotional lives. We speculated on the unique psychology of Level 5 leaders. Were they “guilty” of displacement—shifting their own raw ambition onto something other than themselves? Were they sublimating their egos for dark and complex reasons rooted in childhood trauma? Who knows? And perhaps more important, do the psychological roots of Level 5 leadership matter any more than do the roots of charisma or intelligence? The question remains: Can Level 5 be developed?

My preliminary hypothesis is that there are two categories of people: those who don’t have the Level 5 seed within them and those who do. The first category consists of people who could never in a million years bring themselves to subjugate their own needs to the greater ambition of something larger and more lasting than themselves. For those people, work will always

be first and foremost about what they get—the fame, fortune, power, adulation, and so on. Work will never be about what they build, create, and contribute. The great irony is that the animus and personal ambition that often drives people to become a Level 4 leader stands at odds with the humility required to rise to Level 5.

When you combine that irony with the fact that boards of directors frequently operate under the false belief that a larger-than-life, egocentric leader is required to make a company great, you can quickly see why Level 5 leaders rarely appear at the top of our institutions. We keep putting people in positions of power who lack the seed to become a Level 5 leader, and that is one major reason why there are so few companies that make a sustained and verifiable shift from good to great.

The second category consists of people who could evolve to Level 5; the capability resides within them, perhaps buried or ignored or simply nascent. Under the right circumstances—with self-reflection, a mentor, loving parents, a significant life experience, or other factors—the seed can begin to develop. Some of the Level 5 leaders in our study had significant life experiences that might have sparked development of the seed. Darwin Smith fully blossomed as a Level 5 after his near-death experience with cancer. Joe Cullman was profoundly affected by his World War II experiences, particularly the last-minute change of orders that took him off a doomed ship on which he surely would have died; he considered the next 60-odd years a great gift. A strong religious belief or conversion might also nurture the seed. Colman Mockler, for example, converted to evangelical Christianity while getting his MBA at Harvard, and later, according to the book *Cutting Edge* by Gordon McKibben, he became a prime mover in a group of Boston business executives that met frequently over breakfast to discuss the carryover of religious values to corporate life.

We would love to be able to give you a list of steps for getting to Level 5—other than contracting cancer, going through a religious conversion, or getting different parents—but we have no solid research data that would support a credible list. Our research exposed Level 5 as a key component inside the black box of what it takes to shift a company from good to great. Yet inside that black box is another—the inner development of a person to Level 5 leadership. We could speculate on what that inner box might hold, but it would mostly be just that: speculation.

In short, Level 5 is a very satisfying idea, a truthful idea, a powerful idea,

and, to make the move from good to great, very likely an essential idea. But to provide “ten steps to Level 5 leadership” would trivialize the concept.

My best advice, based on the research, is to practice the other good-to-great disciplines that we discovered. Since we found a tight symbiotic relationship between each of the other findings and Level 5, we suspect that conscientiously trying to lead using the other disciplines can help you move in the right direction. There is no guarantee that doing so will turn executives into full-fledged Level 5 leaders, but it gives them a tangible place to begin, especially if they have the seed within.

We cannot say for sure what percentage of people have the seed within, nor how many of those can nurture it enough to become Level 5. Even those of us on the research team who identified Level 5 do not know whether we will succeed in evolving to its heights. And yet all of us who worked on the finding have been inspired by the idea of trying to move toward Level 5. Darwin Smith, Colman Mockler, Alan Wurtzel, and all the other Level 5 leaders we learned about have become role models for us. Whether or not we make it to Level 5, it is worth trying. For like all basic truths about what is best in human beings, when we catch a glimpse of that truth, we know that our own lives and all that we touch will be the better for making the effort to get there.

Originally published in January 2001. Reprint R0507M

Seven Transformations of Leadership

by David Rooke and William R. Torbert

MOST DEVELOPMENTAL PSYCHOLOGISTS agree that what differentiates leaders is not so much their philosophy of leadership, their personality, or their style of management. Rather, it's their internal "action logic"—how they interpret their surroundings and react when their power or safety is challenged. Relatively few leaders, however, try to understand their own action logic, and fewer still have explored the possibility of changing it.

They should, because we've found that leaders who do undertake a voyage of personal understanding and development can transform not only their own capabilities but also those of their companies. In our close collaboration with psychologist Susanne Cook-Greuter—and our 25 years of extensive survey-based consulting at companies such as Deutsche Bank, Harvard Pilgrim Health Care, Hewlett-Packard, NSA, Trillium Asset Management, Aviva, and Volvo—we've worked with thousands of executives as they've tried to develop their leadership skills. The good news is that leaders who make an effort to understand their own action logic can improve their ability to lead. But to do that, it's important first to understand what kind of leader you already are.

The Seven Action Logics

Our research is based on a sentence-completion survey tool called the Leadership Development Profile. Using this tool, participants are asked to complete 36 sentences that begin with phrases such as “A good leader . . . ,” to which responses vary widely:

“. . . cracks the whip.”

“. . . realizes that it’s important to achieve good performance from subordinates.”

“. . . juggles competing forces and takes responsibility for her decisions.”

By asking participants to complete sentences of this type, it’s possible for highly trained evaluators to paint a picture of how participants interpret their own actions and the world around them; these “pictures” show which one of seven developmental action logics—Opportunist, Diplomat, Expert, Achiever, Individualist, Strategist, or Alchemist—currently functions as a leader’s dominant way of thinking. Leaders can move through these categories as their abilities grow, so taking the Leadership Development Profile again several years later can reveal whether a leader’s action logic has evolved.

Over the past 25 years, we and other researchers have administered the sentence-completion survey to thousands of managers and professionals, most between the ages of 25 and 55, at hundreds of American and European companies (as well as nonprofits and governmental agencies) in diverse industries. What we found is that the levels of corporate and individual performance vary according to action logic. Notably, we found that the three types of leaders associated with below-average corporate performance (Opportunists, Diplomats, and Experts) accounted for 55% of our sample. They were significantly less effective at implementing organizational strategies than the 30% of the sample who measured as Achievers. Moreover, only the final 15% of managers in the sample (Individualists, Strategists, and Alchemists) showed the consistent capacity to innovate and to successfully transform their organizations.

Idea in Brief

Every company needs transformational leaders—those who spearhead changes that elevate profitability, expand market share, and change the rules of the game in their industry. But few executives understand the unique strengths needed to become such a leader. Result? They miss the opportunity to develop those strengths. They and their firms lose out.

How to avoid this scenario? Recognize that great leaders are differentiated not by their personality or philosophy but by their **action logic**—how they interpret their own and others' behavior and how they maintain power or protect against threats.

Some leaders rely on action logics that hinder organizational performance. Opportunists, for example, believe in winning any way possible, and often exploit others to score personal gains. Few people follow them for long. Other types prove potent change agents. In particular, Strategists believe that every aspect of their organization is open to discussion and transformation. Their action logic enables them to challenge perceptions that constrain their organizations and to overcome resistance to change. They create compelling, shared visions and lead the pragmatic initiatives needed to realize those visions.

Though Strategists are rare, you *can* develop their defining strengths. How? Diagnose your current action logic and work to upgrade it. The payoff? You help your company execute the changes it needs to excel.

To understand how leaders fall into such distinct categories and corporate performance, let's look in more detail at each leadership style in turn, starting with the least productive (and least complex).

The Opportunist

Our most comforting finding was that only 5% of the leaders in our sample were characterized by mistrust, egocentrism, and manipulativeness. We call these leaders Opportunists, a title that reflects their tendency to focus on personal wins and see the world and other people as opportunities to be exploited. Their approach to the outside world is largely determined by their perception of control—in other words, how they will react to an event depends primarily on whether or not they think they can direct the outcome. They treat other people as objects or as competitors who are also out for themselves.

Idea in Practice

Seven Types of Action Logic

Type	Characteristics	Strengths	Weaknesses
Opportunist	<i>Wins any way possible.</i> Self-oriented; manipulative; "might makes right."	Good in emergencies and in pursuing sales.	Few people want to follow them for the long term.
Diplomat	<i>Avoids conflict.</i> Wants to belong; obeys group norms; doesn't rock the boat.	Supportive glue on teams.	Can't provide painful feedback or make the hard decisions needed to improve performance.
Expert	<i>Rules by logic and expertise.</i> Uses hard data to gain consensus and buy-in.	Good individual contributor.	Lacks emotional intelligence; lacks respect for those with less expertise.
Achiever	<i>Meets strategic goals.</i> Promotes teamwork; juggles managerial duties and responds to market demands to achieve goals.	Well suited to managerial work.	Inhibits thinking outside the box.
Individualist	<i>Operates in unconventional ways.</i> Ignores rules he/she regards as irrelevant.	Effective in venture and consulting roles.	Irritates colleagues and bosses by ignoring key organizational processes and people.
Strategist	<i>Generates organizational and personal change.</i> Highly collaborative; weaves visions with pragmatic, timely initiatives; challenges existing assumptions.	Generates transformations over the short and long term.	None
Alchemist	<i>Generates social transformations (e.g., Nelson Mandela).</i> Reinvents organizations in historically significant ways.	Leads societywide change.	None

Changing Your Action Logic Type

To change your action logic type, experiment with new interpersonal behaviors, forge new kinds of relationships, and seize advantage of work opportunities. For example:

To advance from. . .	Take these steps
Expert to Achiever	Focus more on delivering results than on perfecting your knowledge: • Become aware of differences between your assumptions and those of others. For example, practice new conversational strategies such as “You may be right, but I’d like to understand what leads you to believe that.” • Participate in training programs on topics such as effective delegation and leading high-performing teams
Achiever to Individualist	Instead of accepting goals as givens to be achieved: • Reflect on the worth of the goals themselves, with the aim of improving future goals • Use annual leadership development planning to thoughtfully set the highest-impact goals
Individualist to Strategist	Engage in peer-to-peer development: • Establish mutual mentoring with members of your professional network (board members, top managers, industry leaders) who can challenge your assumptions and practices, as well as those of your company and industry. <i>Example:</i> One CEO of a dental hygiene company envisioned introducing affordable dental hygiene in developing countries. He explored the idea with colleagues across the country, eventually proposing an educational and charitable venture that his parent company agreed to fund. He was promoted to a new vice presidency for international ventures within the parent company.

Opportunists tend to regard their bad behavior as legitimate in the cut and thrust of an eye-for-an-eye world. They reject feedback, externalize blame, and retaliate harshly. One can see this action logic in the early work of Larry Ellison (now CEO of Oracle). Ellison describes his managerial style at the start of his career as “management by ridicule.” “You’ve got to be good at intellectual intimidation and rhetorical bullying,” he once told Matthew Symonds of the *Economist*. “I’d excuse my behavior by telling myself I was just having ‘an open and honest debate.’ The fact is, I just didn’t know any

better.”

Few Opportunists remain managers for long, unless they transform to more effective action logics (as Ellison has done). Their constant firefighting, their style of self-aggrandizement, and their frequent rule breaking is the antithesis of the kind of leader people want to work with for the long term. If you have worked for an Opportunist, you will almost certainly remember it as a difficult time. By the same token, corporate environments that breed opportunism seldom endure, although Opportunists often survive longer than they should because they provide an exciting environment in which younger executives, especially, can take risks. As one ex-Enron senior staffer said, “Before the fall, those were such exciting years. We felt we could do anything, pull off everything, write our own rules. The pace was wild, and we all just rode it.” Of course, Enron’s shareholders and pensioners would reasonably feel that they were paying too heavily for that staffer’s adventure.

The Diplomat

The Diplomat makes sense of the world around him in a more benign way than the Opportunist does, but this action logic can also have extremely negative repercussions if the leader is a senior manager. Loyally serving the group, the Diplomat seeks to please higher-status colleagues while avoiding conflict. This action logic is focused on gaining control of one's own behavior—more than on gaining control of external events or other people. According to the Diplomat's action logic, a leader gains more enduring acceptance and influence by cooperating with group norms and by performing his daily roles well.

In a support role or a team context, this type of executive has much to offer. Diplomats provide social glue to their colleagues and ensure that attention is paid to the needs of others, which is probably why the great majority of Diplomats work at the most junior rungs of management, in jobs such as frontline supervisor, customer service representative, or nurse practitioner. Indeed, research into 497 managers in different industries showed that 80% of all Diplomats were at junior levels. By contrast, 80% of all Strategists were at senior levels, suggesting that managers who grow into more effective action logics—like that of the Strategist—have a greater chance of being promoted.

Diplomats are much more problematic in top leadership roles because they try to ignore conflict. They tend to be overly polite and friendly and find it virtually impossible to give challenging feedback to others. Initiating change, with its inevitable conflicts, represents a grave threat to the Diplomat, and he will avoid it if at all possible, even to the point of self-destruction.

Consider one Diplomat who became the interim CEO of an organization when his predecessor died suddenly from an aneurysm. When the board split on the selection of a permanent successor, it asked the Diplomat to carry on. Our Diplomat relished his role as a ceremonial figurehead and was a sought-after speaker at public events. Unfortunately, he found the more conflictual requirements of the job less to his liking. He failed, for instance, to replace a

number of senior managers who had serious ongoing performance issues and were resisting the change program his predecessor had initiated. Because the changes were controversial, the Diplomat avoided meetings, even planning business trips for the times when the senior team would meet. The team members were so frustrated by the Diplomat's attitude that they eventually resigned en masse. He "resolved" this crisis by thanking the team publicly for its contribution and appointing new team members. Eventually, in the face of mounting losses arising from this poor management, the board decided to demote the Diplomat to his former role as vice president.

Seven Ways of Leading

DIFFERENT LEADERS exhibit different kinds of action logic—ways in which they interpret their surroundings and react when their power or safety is challenged. In our research of thousands of leaders, we observed seven types of action logics. The least effective for organizational leadership are the Opportunist and Diplomat; the most effective, the Strategist and Alchemist. Knowing your own action logic can be the first step toward developing a more effective leadership style. If you recognize yourself as an Individualist, for example, you can work, through both formal and informal measures, to develop the strengths and characteristics of a Strategist.

Action Logic	Characteristics	Strengths	% of research sample profiling at this action logic
Opportunist	<i>Wins any way possible. Self-oriented; manipulative; "might makes right."</i>	Good in emergencies and in sales opportunities.	5%
Diplomat	<i>Avoids overt conflict. Wants to belong; obeys group norms; rarely rocks the boat.</i>	Good as supportive glue within an office; helps bring people together.	12%
Expert	<i>Rules by logic and expertise. Seeks rational efficiency.</i>	Good as an individual contributor.	38%

Achiever	Meets strategic goals. Effectively achieves goals through teams; juggles managerial duties and market demands.	Well suited to managerial roles; action and goal oriented.	30%
Individualist	Interweaves competing personal and company action logics. Creates unique structures to resolve gaps between strategy and performance.	Effective in venture and consulting roles.	10%
Strategist	Generates organizational and personal transformations. Exercises the power of mutual inquiry, vigilance, and vulnerability for both the short and long term.	Effective as a transformational leader.	4%
Alchemist	Generates social transformations. Integrates material, spiritual, and societal transformation.	Good at leading society-wide transformations.	1%

The Expert

The largest category of leader is that of Experts, who account for 38% of all professionals in our sample. In contrast to Opportunists, who focus on trying to control the world around them, and Diplomats, who concentrate on controlling their own behavior, Experts try to exercise control by perfecting their knowledge, both in their professional and personal lives. Exercising watertight thinking is extremely important to Experts. Not surprisingly, many accountants, investment analysts, marketing researchers, software engineers, and consultants operate from the Expert action logic. Secure in their expertise, they present hard data and logic in their efforts to gain consensus and buy-in for their proposals.

Experts are great individual contributors because of their pursuit of continuous improvement, efficiency, and perfection. But as managers, they can be problematic because they are so completely sure they are right. When subordinates talk about a my-way-or-the-highway type of boss, they are probably talking about someone operating from an Expert action logic. Experts tend to view collaboration as a waste of time (“Not all meetings are a waste of time—some are canceled!”), and they will frequently treat the opinions of people less expert than themselves with contempt. Emotional intelligence is neither desired nor appreciated. As Sun Microsystems’ CEO Scott McNealy put it: “I don’t do feelings; I’ll leave that to Barry Manilow.”

It comes as no surprise, then, that after unsuccessfully pleading with him to scale back in the face of growing losses during the dot-com debacle of 2001 and 2002, nearly a dozen members of McNealy’s senior management team left.

The Achiever

For those who hope someday to work for a manager who both challenges and supports them and creates a positive team and interdepartmental atmosphere, the good news is that a large proportion, 30%, of the managers in our research measured as Achievers. While these leaders create a positive work environment and focus their efforts on deliverables, the downside is that their style often inhibits thinking outside the box.

Achievers have a more complex and integrated understanding of the world than do managers who display the three previous action logics we've described. They're open to feedback and realize that many of the ambiguities and conflicts of everyday life are due to differences in interpretation and ways of relating. They know that creatively transforming or resolving clashes requires sensitivity to relationships and the ability to influence others in positive ways. Achievers can also reliably lead a team to implement new strategies over a one- to three-year period, balancing immediate and long-term objectives. One study of ophthalmologists in private practice showed that those who scored as Achievers had lower staff turnover, delegated more responsibility, and had practices that earned at least twice the gross annual revenues of those run by Experts.

Achievers often find themselves clashing with Experts. The Expert subordinate, in particular, finds the Achiever leader hard to take because he cannot deny the reality of the Achiever's success even though he feels superior. Consider Hewlett-Packard, where the research engineers tend to score as Experts and the lab managers as higher-level Achievers. At one project meeting, a lab manager—a decided Achiever—slammed her coffee cup on the table and exclaimed, “I *know* we can get 18 features into this, but the customers want delivery some time this century, and the main eight features will do.” “Philistine!” snorted one engineer, an Expert. But this kind of conflict isn't always destructive. In fact, it provides much of the fuel that has ignited—and sustained—the competitiveness of many of the country's most successful corporations.

The Individualist

The Individualist action logic recognizes that neither it nor any of the other action logics are “natural”; all are constructions of oneself and the world. This seemingly abstract idea enables the 10% of Individualist leaders to contribute unique practical value to their organizations; they put personalities and ways of relating into perspective and communicate well with people who have other action logics.

What sets Individualists apart from Achievers is their awareness of a possible conflict between their principles and their actions, or between the organization’s values and its implementation of those values. This conflict becomes the source of tension, creativity, and a growing desire for further development.

Individualists also tend to ignore rules they regard as irrelevant, which often makes them a source of irritation to both colleagues and bosses. “So, what do you think?” one of our clients asked us as he was debating whether to let go of one of his star performers, a woman who had been measured as an Individualist. Sharon (not her real name) had been asked to set up an offshore shared service function in the Czech Republic in order to provide IT support to two separate and internally competitive divisions operating there. She formed a highly cohesive team within budget and so far ahead of schedule that she quipped that she was “delivering services before Group Business Risk had delivered its report saying it can’t be done.”

The trouble was that Sharon had a reputation within the wider organization as a wild card. Although she showed great political savvy when it came to her individual projects, she put many people’s noses out of joint in the larger organization because of her unique, unconventional ways of operating. Eventually, the CEO was called in (not for the first time) to resolve a problem created by her failure to acknowledge key organizational processes and people who weren’t on her team.

Many of the dynamics created by different action logics are illustrated by this story and its outcome. The CEO, whose own action logic was that of an

Achiever, did not see how he could challenge Sharon to develop and move beyond creating such problems. Although ambivalent about her, he decided to retain her because she was delivering and because the organization had recently lost several capable, if unconventional, managers.

So Sharon stayed, but only for a while. Eventually, she left the company to set up an offshoring consultancy. When we examine in the second half of this article how to help executives transform their leadership action logics, we'll return to this story to see how both Sharon and the CEO might have succeeded in transforming theirs.

The Strategist

Strategists account for just 4% of leaders. What sets them apart from Individualists is their focus on organizational constraints and perceptions, which they treat as discussable and transformable. Whereas the Individualist masters communication with colleagues who have different action logics, the Strategist masters the second-order organizational impact of actions and agreements. The Strategist is also adept at creating shared visions across different action logics—visions that encourage both personal and organizational transformations. According to the Strategist's action logic, organizational and social change is an iterative developmental process that requires awareness and close leadership attention.

Strategists deal with conflict more comfortably than do those with other action logics, and they're better at handling people's instinctive resistance to change. As a result, Strategists are highly effective change agents. We found confirmation of this in our recent study of ten CEOs in six different industries. All of their organizations had the stated objective of transforming themselves and had engaged consultants to help with the process. Each CEO filled out a Leadership Development Profile, which showed that five of them were Strategists and the other five fell into other action logics. The Strategists succeeded in generating one or more organizational transformations over a four-year period; their companies' profitability, market share, and reputation all improved. By contrast, only two of the other five CEOs succeeded in transforming their organizations—despite help from consultants, who themselves profiled as Strategists.

Strategists are fascinated with three distinct levels of social interplay: personal relationships, organizational relations, and national and international developments. Consider Joan Bavaria, a CEO who, back in 1985, measured as a Strategist. Bavaria created one of the first socially responsible investment funds, a new subdivision of the investments industry, which by the end of 2001 managed more than \$3 trillion in funds. In 1982, Bavaria founded Trillium Asset Management, a worker-owned company, which she still

heads. She also cowrote the CERES Environmental Principles, which dozens of major companies have signed. In the late 1990s, CERES, working with the United Nations, created the Global Reporting Initiative, which supports financial, social, and environmental transparency and accountability worldwide.

Here we see the Strategist action logic at work. Bavaria saw a unique moment in which to make ethical investing a viable business, then established Trillium to execute her plan. Strategists typically have socially conscious business ideas that are carried out in a highly collaborative manner. They seek to weave together idealist visions with pragmatic, timely initiatives and principled actions. Bavaria worked beyond the boundaries of her own organization to influence the socially responsible investment industry as a whole and later made the development of social and environmental accountability standards an international endeavor by involving the United Nations. Many Achievers will use their influence to successfully promote their own companies. The Strategist works to create ethical principles and practices beyond the interests of herself or her organization.

The Alchemist

The final leadership action logic for which we have data and experience is the Alchemist. Our studies of the few leaders we have identified as Alchemists suggest that what sets them apart from Strategists is their ability to renew or even reinvent themselves and their organizations in historically significant ways. Whereas the Strategist will move from one engagement to another, the Alchemist has an extraordinary capacity to deal simultaneously with many situations at multiple levels. The Alchemist can talk with both kings and commoners. He can deal with immediate priorities yet never lose sight of long-term goals.

Alchemists constitute 1% of our sample, which indicates how rare it is to find them in business or anywhere else. Through an extensive search process, we found six Alchemists who were willing to participate in an up-close study of their daily actions. Though this is obviously a very small number that cannot statistically justify generalization, it's worth noting that all six Alchemists shared certain characteristics. On a daily basis, all were engaged in multiple organizations and found time to deal with issues raised by each. However, they were not in a constant rush—nor did they devote hours on end to a single activity. Alchemists are typically charismatic and extremely aware individuals who live by high moral standards. They focus intensely on the truth. Perhaps most important, they're able to catch unique moments in the history of their organizations, creating symbols and metaphors that speak to people's hearts and minds. In one conservative financial services company in the UK, a recently appointed CEO turned up for work in a tracksuit instead of his usual pinstripes but said nothing about it to anyone. People wondered whether this was a new dress code. Weeks later, the CEO spoke publicly about his attire and the need to be unconventional and to move with greater agility and speed.

A more celebrated example of an Alchemist is Nelson Mandela. Although we never formally profiled Mandela, he exemplifies the Alchemist action logic. In 1995, Mandela symbolized the unity of a new South Africa when he

attended the Rugby World Cup game in which the Springboks, the South African national team, were playing. Rugby had been the bastion of white supremacy, but Mandela attended the game. He walked on to the pitch wearing the Springboks' jersey so hated by black South Africans, at the same time giving the clenched fist salute of the ANC, thereby appealing, almost impossibly, both to black and white South Africans. As Tokyo Sexwale, ANC activist and premier of South Africa's Gauteng province, said of him: "Only Mandela could wear an enemy jersey. Only Mandela would go down there and be associated with the Springboks . . . All the years in the underground, in the trenches, denial, self-denial, away from home, prison, it was worth it. That's all we wanted to see."

Evolving as a Leader

The most remarkable—and encouraging—finding from our research is that leaders can transform from one action logic to another. We have, in fact, documented a number of leaders who have succeeded in transforming themselves from Experts into Achievers, from Achievers into Individualists, and from Individualists into Strategists.

Take the case of Jenny, one of our clients, who initially measured as an Expert. She became disillusioned with her role in her company's PR department and resigned in order to, as she said, "sort out what I really want to do." Six months later, she joined a different company in a similar role, and two years after that we profiled her again and she still measured as an Expert. Her decision to resign from the first company, take a "sabbatical," and then join the second company had made no difference to her action logic. At that point, Jenny chose to join a group of peer leaders committed to examining their current leadership patterns and to experimenting with new ways of acting. This group favored the Strategist perspective (and the founder of the group was profiled as an Alchemist), which in the end helped Jenny's development. She learned that her habit of consistently taking a critical position, which she considered "usefully objective," isolated her and generated distrust. As a result of the peer group's feedback, she started a series of small and private experiments, such as asking questions rather than criticizing. She realized that instead of seeing the faults in others, she had to be clear about what *she* could contribute and, in doing so, started the move from an Expert to an Achiever. Spiritually, Jenny learned that she needed an ongoing community of inquiry at the center of her life and found a spiritual home for continuing reflection in Quaker meetings, which later supported (and indeed signaled) her transition from an Achiever to an Individualist.

Two years later, Jenny left the second job to start her own company, at which point she began profiling as a Strategist. This was a highly unusual movement of three action logics in such a short time. We have had only two other instances in which a leader has transformed twice in less than four

years.

As Jenny's case illustrates, there are a number of personal changes that can support leadership transformation. Jenny experienced loss of faith in the system and feelings of boredom, irritability, burnout, depression, and even anger. She began to ask herself existential questions. But another indication of a leader's readiness to transform is an increasing attraction to the qualities she begins to intuit in people with more effective action logics. Jenny, as we saw, was drawn to and benefited hugely from her Strategist peer group as well as from a mentor who exhibited the Alchemist action logic. This search for new perspectives often manifests itself in personal transformations: The ready-to-transform leader starts developing new relationships. She may also explore new forms of spiritual practice or new forms of centering and self-expression, such as playing a musical instrument or doing tai chi.

External events can also trigger and support transformation. A promotion, for example, may give a leader the opportunity to expand his or her range of capabilities. Earlier, we cited the frustration of Expert research engineers at Hewlett-Packard with the product and delivery attitude of Achiever lab managers. Within a year of one engineer's promotion to lab manager, a role that required coordination of others and cooperation across departments, the former Expert was profiling as an Achiever. Although he initially took some heat ("Sellout!") from his former buddies, his new Achiever awareness meant that he was more focused on customers' needs and clearer about delivery schedules. For the first time, he understood the dance between engineers trying to perfect the technology and managers trying to deliver on budget and on schedule.

Changes to a manager's work practices and environment can also facilitate transformation. At one company we studied, leaders changed from Achievers to Individualists partly because of simple organizational and process changes. At the company's senior manager meetings, for example, executives other than the CEO had the chance to lead the meetings; these opportunities, which were supported by new spirit of openness, feedback, and frank debate, fostered professional growth among many of the company's leaders.

Planned and structured development interventions are another means of supporting leadership transformation. We worked with a leading oil and gas exploration company on developing the already high-level capabilities of a pool of future senior managers; the managers were profiled and then

interviewed by two consultants who explored each manager's action logic and how it constrained and enabled him or her to perform current and recent roles. Challenges were discussed as well as a view of the individual's potential and a possible developmental plan. After the exercise, several managers, whose Individualist and Strategist capabilities had not been fully understood by the company, were appreciated and engaged differently in their roles. What's more, the organization's own definition of leadership talent was reframed to include the capabilities of the Individualist and Strategist action logics. This in turn demanded that the company radically revisit its competency framework to incorporate such expectations as "sees issues from multiple perspectives" and "creates deep change without formal power."

Now that we've looked generally at some of the changes and interventions that can support leadership development, let's turn to some specifics about how the most common transformations are apt to take place.

From Expert to Achiever

This transformation is the most commonly observed and practiced among businesspeople and by those in management and executive education. For the past generation or more, the training departments of large companies have been supporting the development of managers from Experts into Achievers by running programs with titles like “Management by Objectives,” “Effective Delegation,” and “Managing People for Results.” These programs typically emphasize getting results through flexible strategies rather than through one right method used in one right way.

Observant leaders and executive coaches can also formulate well-structured exercises and questions related to everyday work to help Experts become aware of the different assumptions they and others may be making. These efforts can help Experts practice new conversational strategies such as, “You may be right, but I’d like to understand what leads you to believe that.” In addition, those wishing to push Experts to the next level should consider rewarding Achiever competencies like timely delivery of results, the ability to manage for performance, and the ability to implement strategic priorities.

Within business education, MBA programs are apt to encourage the development of the more pragmatic Achievers by frustrating the perfectionist Experts. The heavy workloads, use of multidisciplinary and ambiguous case studies, and teamwork requirements all promote the development of Achievers. By contrast, MSc programs, in particular disciplines such as finance or marketing research, tend to reinforce the Expert perspective.

Still, the transition from Expert to Achiever remains one of the most painful bottlenecks in most organizations. We’ve all heard the eternal lament of engineers, lawyers, and other professionals whose Expert success has saddled them with managerial duties, only to estrange them from the work they love. Their challenge becomes working as highly effective Achievers who can continue to use their in-depth expertise to succeed as leaders and managers.

From Achiever to Individualist

Although organizations and business schools have been relatively successful in developing leaders to the Achiever action logic, they have, with few exceptions, a dismal record in recognizing, supporting, and *actively* developing leaders to the Individualist and Strategist action logics, let alone to the Alchemist logic. This is not surprising. In many organizations, the Achiever, with his drive and focus on the endgame, is seen as the finish line for development: “This is a competitive industry—we need to keep a sharp focus on the bottom line.”

The development of leaders beyond the Achiever action logic requires a very different tack from that necessary to bring about the Expert-to-Achiever transformation. Interventions must encourage self-awareness on the part of the evolving leader as well as a greater awareness of other worldviews. In both business and personal relationships, speaking and listening must come to be experienced not as necessary, taken-for-granted ways of communicating predetermined ideas but as intrinsically forward-thinking, creative actions. Achievers use inquiry to determine whether they (and the teams and organization to which they belong) are accomplishing their goals and how they might accomplish them more effectively. The developing Individualist, however, begins to inquire about and reflect on the goals themselves—with the aim of improving future goals. Annual development plans that set new goals, are generated through probing and trusting conversation, are actively supported through executive coaching, and are carefully reviewed at the end of the cycle can be critical enablers at this point. Yet few boards and CEOs appreciate how valuable this time investment can be, and it is all too easily sacrificed in the face of short-term objectives, which can seem more pressing to leaders whose action logics are less developed.

Let’s go back to the case of Sharon, the Individualist we described earlier whose Achiever CEO wasn’t able to manage her. How might a coach or consultant have helped the CEO feel less threatened by Sharon and more capable of supporting her development while also being more open to his

own needs and potential? One way would have been to try role-playing, asking the CEO to play Sharon while the coach or consultant enacts the CEO role. The role-playing might have gone as follows:

“Sharon, I want to talk with you about your future here at our company. Your completion of the Czech project under budget and ahead of time is one more sign that you have the initiative, creativity, and determination to make the senior team here. At the same time, I’ve had to pick up a number of pieces after you that I shouldn’t have had to. I’d like to brainstorm together about how you can approach future projects in a way that eliminates this hassle and gets key players on your side. Then, we can chat several times over the next year as you begin to apply whatever new principles we come up with. Does this seem like a good use of our time, or do you have a different perspective on the issue?”

Note that the consultant in the CEO’s role offers clear praise, a clear description of a limitation, a proposed path forward, and an inquiry that empowers the CEO (playing Sharon) to reframe the dilemma if he wishes. Thus, instead of giving the CEO one-way advice about what he should do, the coach enacts a dialogic scenario with him, illustrating a new kind of practice and letting the CEO judge whether the enacted relationship is a positive one. The point is not so much to teach the CEO a new conversational repertoire but to make him more comfortable with how the Individualist sees and makes sense of the world around her and what feedback may motivate her to commit to further learning. Such specific experiments with new ways of listening and talking can gradually dissolve the fears associated with transformational learning.

To Strategist and Beyond

Leaders who are moving toward the Strategist and Alchemist action logics are no longer primarily seeking personal skills that will make them more effective within existing organizational systems. They will already have mastered many of those skills. Rather, they are exploring the disciplines and commitments entailed in creating projects, teams, networks, strategic alliances, and whole organizations on the basis of collaborative inquiry. It is this ongoing practice of reframing inquiry that makes them and their corporations so successful.

The path toward the Strategist and Alchemist action logics is qualitatively different from other leadership development processes. For a start, emergent Strategists and Alchemists are no longer seeking mentors to help them sharpen existing skills and to guide them toward influential networks (although they may seek spiritual and ethical guidance from mentors). Instead, they are seeking to engage in mutual mentoring with peers who are already part of their networks (such as board members, top managers, or leaders within a scientific discipline). The objective of this senior-peer mentoring is not, in conventional terms, to increase the chances of success but to create a sustainable community of people who can challenge the emergent leader's assumptions and practices and those of his company, industry, or other area of activity.

We witnessed just this kind of peer-to-peer development when one senior client became concerned that he, his company, and the industry as a whole were operating at the Achiever level. This concern, of course, was itself a sign of his readiness to transform beyond that logic. This executive—the CEO of a dental hygiene company—and his company were among the most successful of the parent company's subsidiaries. However, realizing that he and those around him had been keeping their heads down, he chose to initiate a research project—on introducing affordable dental hygiene in developing countries—that was decidedly out of the box for him and for the corporation.

The CEO's timing was right for such an initiative, and he used the

opportunity to engage in collaborative inquiry with colleagues across the country. Eventually, he proposed an educational and charitable venture, which the parent company funded. The executive was promoted to a new vice presidency for international ventures within the parent company—a role he exercised with an increased sense of collaboration and a greater feeling of social responsibility for his company in emerging markets.

Formal education and development processes can also guide individuals toward a Strategist action logic. Programs in which participants act as leaders and challenge their conventional assumptions about leading and organizing are very effective. Such programs will be either long term (one or two years) or repeated, intense experiences that nurture the moment-to-moment awareness of participants, always providing the shock of dissonance that stimulates them to reexamine their worldviews. Path-breaking programs of this type can be found at a few universities and consultancies around the globe. Bath University in the UK, for instance, sponsors a two-year master's degree in responsibility and business practice in which students work together during six one-week get-togethers. These programs involve small-learning teams, autobiographical writing, psychodrama, deep experiences in nature, and a yearlong business project that involves action and reflection. Interestingly, many people who attend these programs report that these experiences have had the transformative power of a life-altering event, such as a career or existential crisis or a new marriage.

Leadership Teams and Leadership Cultures Within Organizations

So far, our discussion has focused on the leadership styles of individuals. But we have found that our categories of leadership styles can be used to describe teams and organizations as well. Here we will talk briefly about the action logics of teams.

Over the long term, the most effective teams are those with a Strategist culture, in which the group sees business challenges as opportunities for growth and learning on the part of both individuals and the organization. A leadership team at one of the companies we worked with decided to invite managers from across departments to participate in time-to-market new product teams. Seen as a risky distraction, few managers volunteered, except for some Individualists and budding Strategists. However, senior management provided sufficient support and feedback to ensure the teams' early success. Soon, the first participants were promoted and leading their own cross-departmental teams. The Achievers in the organization, seeing that others were being promoted, started volunteering for these teams. Gradually, more people within the organization were experiencing shared leadership, mutual testing of one another's assumptions and practices, and individual challenges that contributed to their development as leaders.

Sadly, few companies use teams in this way. Most senior manager teams operate at the Achiever action logic—they prefer unambiguous targets and deadlines, and working with clear strategies, tactics, and plans, often against tight deadlines. They thrive in a climate of adversity (“When the going gets tough, the tough get going”) and derive great pleasure from pulling together and delivering. Typically, the team's leaders and several other members will be Achievers, with several Experts and perhaps one or two Individualists or Strategists (who typically feel ignored). Such Achiever teams are often impatient at slowing down to reflect, are apt to dismiss questions about goals and assumptions as “endless philosophizing,” and typically respond with hostile humor to creative exercises, calling them “off-the-wall” diversions.

These behaviors will ultimately limit an Achiever team's success.

The situation is worse at large, mature companies where senior management teams operate as Experts. Here, vice presidents see themselves as chiefs and their "teams" as an information-reporting formality. Team life is bereft of shared problem-solving, decision-making, or strategy-formulating efforts. Senior teams limited by the Diplomat action logic are even less functional. They are characterized by strong status differences, undiscussable norms, and ritual "court" ceremonies that are carefully stage-managed.

Individualist teams, which are more likely to be found in creative, consulting, and nonprofit organizations, are relatively rare and very different from Achiever, Expert, and Diplomat teams. In contrast to Achiever teams, they may be strongly reflective; in fact, excessive time may be spent reviewing goals, assumptions, and work practices. Because individual concerns and input are very important to these teams, rapid decision making may be difficult.

But like individual people, teams can change their style. For instance, we've seen Strategist CEOs help Individualist senior teams balance action and inquiry and so transform into Strategist teams. Another example is an Achiever senior team in a financial services company we worked with that was emerging from two years of harsh cost cutting during a market downturn. To adapt to a changing and growing financial services market, the company needed to become significantly more visionary and innovative and learn how to engage its workforce. To lead this transformation, the team had to start with itself. We worked with it to help team members understand the constraints of the Achiever orientation, which required a number of interventions over time. We began by working to improve the way the team discussed issues and by coaching individual members, including the CEO. As the team evolved, it became apparent that its composition needed to change: Two senior executives, who had initially seemed ideally suited to the group because of their achievements, had to be replaced when it became clear that they were unwilling to engage and experiment with the new approach.

During this reorientation, which lasted slightly more than two years, the team became an Individualist group with emergent Strategist capabilities. The CEO, who had profiled at Achiever/Individualist, now profiled as a Strategist, and most other team members showed one developmental move forward. The impact of this was also felt in the team's and organization's ethos: Once functionally divided, the team learned to accept and integrate the

diverse opinions of its members. Employee surveys reported increased engagement across the company. Outsiders began seeing the company as ahead of the curve, which meant the organization was better able to attract top talent. In the third year, bottom- and top-line results were well ahead of industry competitors.

The leader's voyage of development is not an easy one. Some people change little in their lifetimes; some change substantially. Despite the undeniably crucial role of genetics, human nature is not fixed. Those who are willing to work at developing themselves and becoming more self-aware can almost certainly evolve over time into truly transformational leaders. Few may become Alchemists, but many will have the desire and potential to become Individualists and Strategists. Corporations that help their executives and leadership teams examine their action logics can reap rich rewards.

Originally published in April 2005. Reprint R0504D

Discovering Your Authentic Leadership

by Bill George, Peter Sims, Andrew N. McLean, and Diana Mayer

DURING THE PAST 50 YEARS, leadership scholars have conducted more than 1,000 studies in an attempt to determine the definitive styles, characteristics, or personality traits of great leaders. None of these studies has produced a clear profile of the ideal leader. Thank goodness. If scholars had produced a cookie-cutter leadership style, individuals would be forever trying to imitate it. They would make themselves into personae, not people, and others would see through them immediately.

No one can be authentic by trying to imitate someone else. You can learn from others' experiences, but there is no way you can be successful when you are trying to be like them. People trust you when you are genuine and authentic, not a replica of someone else. Amgen CEO and president Kevin Sharer, who gained priceless experience working as Jack Welch's assistant in the 1980s, saw the downside of GE's cult of personality in those days. "Everyone wanted to be like Jack," he explains. "Leadership has many voices. You need to be who you are, not try to emulate somebody else."

Over the past five years, people have developed a deep distrust of leaders. It is increasingly evident that we need a new kind of business leader in the twenty-first century. In 2003, Bill George's book, *Authentic Leadership: Rediscovering the Secrets to Creating Lasting Value*, challenged a new generation to lead authentically. Authentic leaders demonstrate a passion for their purpose, practice their values consistently, and lead with their hearts as well as their heads. They establish long-term, meaningful relationships and have the self-discipline to get results. They know who they are.

Many readers of *Authentic Leadership*, including several CEOs, indicated that they had a tremendous desire to become authentic leaders and wanted to know how. As a result, our research team set out to answer the question, “How can people become and remain authentic leaders?” We interviewed 125 leaders to learn how they developed their leadership abilities. These interviews constitute the largest in-depth study of leadership development ever undertaken. Our interviewees discussed openly and honestly how they realized their potential and candidly shared their life stories, personal struggles, failures, and triumphs.

The people we talked with ranged in age from 23 to 93, with no fewer than 15 per decade. They were chosen based on their reputations for authenticity and effectiveness as leaders, as well as our personal knowledge of them. We also solicited recommendations from other leaders and academics. The resulting group includes women and men from a diverse array of racial, religious, and socioeconomic backgrounds and nationalities. Half of them are CEOs, and the other half comprises a range of profit and nonprofit leaders, midcareer leaders, and young leaders just starting on their journeys.

After interviewing these individuals, we believe we understand why more than 1,000 studies have not produced a profile of an ideal leader. Analyzing 3,000 pages of transcripts, our team was startled to see that these people did not identify any universal characteristics, traits, skills, or styles that led to their success. Rather, their leadership emerged from their life stories. Consciously and subconsciously, they were constantly testing themselves through real-world experiences and reframing their life stories to understand who they were at their core. In doing so, they discovered the purpose of their leadership and learned that being authentic made them more effective.

These findings are extremely encouraging: You do not have to be born with specific characteristics or traits of a leader. You do not have to wait for a tap on the shoulder. You do not have to be at the top of your organization. Instead, you can discover your potential right now. As one of our interviewees, Young & Rubicam chairman and CEO Ann Fudge, said, “All of us have the spark of leadership in us, whether it is in business, in government, or as a nonprofit volunteer. The challenge is to understand ourselves well enough to discover where we can use our leadership gifts to serve others.”

Discovering your authentic leadership requires a commitment to

developing yourself. Like musicians and athletes, you must devote yourself to a lifetime of realizing your potential. Most people Kroger CEO David Dillon has seen become good leaders were self-taught. Dillon said, “The advice I give to individuals in our company is not to expect the company to hand you a development plan. You need to take responsibility for developing yourself.”

In the following pages, we draw upon lessons from our interviews to describe how people become authentic leaders. First and most important, they frame their life stories in ways that allow them to see themselves not as passive observers of their lives but rather as individuals who can develop self-awareness from their experiences. Authentic leaders act on that awareness by practicing their values and principles, sometimes at substantial risk to themselves. They are careful to balance their motivations so that they are driven by these inner values as much as by a desire for external rewards or recognition. Authentic leaders also keep a strong support team around them, ensuring that they live integrated, grounded lives.

Learning from Your Life Story

The journey to authentic leadership begins with understanding the story of your life. Your life story provides the context for your experiences, and through it, you can find the inspiration to make an impact in the world. As the novelist John Barth once wrote, “The story of your life is not your life. It is your story.” In other words, it is your personal narrative that matters, not the mere facts of your life. Your life narrative is like a permanent recording playing in your head. Over and over, you replay the events and personal interactions that are important to your life, attempting to make sense of them to find your place in the world.

While the life stories of authentic leaders cover the full spectrum of experiences—including the positive impact of parents, athletic coaches, teachers, and mentors—many leaders reported that their motivation came from a difficult experience in their lives. They described the transformative effects of the loss of a job; personal illness; the untimely death of a close friend or relative; and feelings of being excluded, discriminated against, and rejected by peers. Rather than seeing themselves as victims, though, authentic leaders used these formative experiences to give meaning to their lives. They reframed these events to rise above their challenges and to discover their passion to lead.

Let’s focus now on one leader in particular, Novartis chairman and CEO Daniel Vasella, whose life story was one of the most difficult of all the people we interviewed. He emerged from extreme challenges in his youth to reach the pinnacle of the global pharmaceutical industry, a trajectory that illustrates the trials many leaders have to go through on their journeys to authentic leadership.

Vasella was born in 1953 to a modest family in Fribourg, Switzerland. His early years were filled with medical problems that stoked his passion to become a physician. His first recollections were of a hospital where he was admitted at age four when he suffered from food poisoning. Falling ill with asthma at age five, he was sent alone to the mountains of eastern Switzerland

for two summers. He found the four-month separations from his parents especially difficult because his caretaker had an alcohol problem and was unresponsive to his needs.

At age eight, Vasella had tuberculosis, followed by meningitis, and was sent to a sanatorium for a year. Lonely and homesick, he suffered a great deal that year, as his parents rarely visited him. He still remembers the pain and fear when the nurses held him down during the lumbar punctures so that he would not move. One day, a new physician arrived and took time to explain each step of the procedure. Vasella asked the doctor if he could hold a nurse's hand rather than being held down. "The amazing thing is that this time the procedure didn't hurt," Vasella recalls. "Afterward, the doctor asked me, 'How was that?' I reached up and gave him a big hug. These human gestures of forgiveness, caring, and compassion made a deep impression on me and on the kind of person I wanted to become."

Throughout his early years, Vasella's life continued to be unsettled. When he was ten, his 18-year-old sister passed away after suffering from cancer for two years. Three years later, his father died in surgery. To support the family, his mother went to work in a distant town and came home only once every three weeks. Left to himself, he and his friends held beer parties and got into frequent fights. This lasted for three years until he met his first girlfriend, whose affection changed his life.

At 20, Vasella entered medical school, later graduating with honors. During medical school, he sought out psychotherapy so he could come to terms with his early experiences and not feel like a victim. Through analysis, he reframed his life story and realized that he wanted to help a wider range of people than he could as an individual practitioner. Upon completion of his residency, he applied to become chief physician at the University of Zurich; however, the search committee considered him too young for the position.

Disappointed but not surprised, Vasella decided to use his abilities to increase his impact on medicine. At that time, he had a growing fascination with finance and business. He talked with the head of the pharmaceutical division of Sandoz, who offered him the opportunity to join the company's U.S. affiliate. In his five years in the United States, Vasella flourished in the stimulating environment, first as a sales representative and later as a product manager, and advanced rapidly through the Sandoz marketing organization.

When Sandoz merged with Ciba-Geigy in 1996, Vasella was named CEO of the combined companies, now called Novartis, despite his young age and

limited experience. Once in the CEO's role, Vasella blossomed as a leader. He envisioned the opportunity to build a great global health care company that could help people through lifesaving new drugs, such as Gleevec, which has proved to be highly effective for patients with chronic myeloid leukemia. Drawing on the physician role models of his youth, he built an entirely new Novartis culture centered on compassion, competence, and competition. These moves established Novartis as a giant in the industry and Vasella as a compassionate leader.

Vasella's experience is just one of dozens provided by authentic leaders who traced their inspiration directly from their life stories. Asked what empowered them to lead, these leaders consistently replied that they found their strength through transformative experiences. Those experiences enabled them to understand the deeper purpose of their leadership.

Knowing Your Authentic Self

When the 75 members of Stanford Graduate School of Business's Advisory Council were asked to recommend the most important capability for leaders to develop, their answer was nearly unanimous: self-awareness. Yet many leaders, especially those early in their careers, are trying so hard to establish themselves in the world that they leave little time for self-exploration. They strive to achieve success in tangible ways that are recognized in the external world—money, fame, power, status, or a rising stock price. Often their drive enables them to be professionally successful for a while, but they are unable to sustain that success. As they age, they may find something is missing in their lives and realize they are holding back from being the person they want to be. Knowing their authentic selves requires the courage and honesty to open up and examine their experiences. As they do so, leaders become more humane and willing to be vulnerable.

Of all the leaders we interviewed, David Pottruck, former CEO of Charles Schwab, had one of the most persistent journeys to self-awareness. An all-league football player in high school, Pottruck became MVP of his college team at the University of Pennsylvania. After completing his MBA at Wharton and a stint with Citigroup, he joined Charles Schwab as head of marketing, moving from New York to San Francisco. An extremely hard worker, Pottruck could not understand why his new colleagues resented the long hours he put in and his aggressiveness in pushing for results. "I thought my accomplishments would speak for themselves," he said. "It never occurred to me that my level of energy would intimidate and offend other people, because in my mind I was trying to help the company."

Pottruck was shocked when his boss told him, "Dave, your colleagues do not trust you." As he recalled, "That feedback was like a dagger to my heart. I was in denial, as I didn't see myself as others saw me. I became a lightning rod for friction, but I had no idea how self-serving I looked to other people. Still, somewhere in my inner core the feedback resonated as true." Pottruck realized that he could not succeed unless he identified and overcame his blind

spots.

Denial can be the greatest hurdle that leaders face in becoming self-aware. They all have egos that need to be stroked, insecurities that need to be smoothed, fears that need to be allayed. Authentic leaders realize that they have to be willing to listen to feedback—especially the kind they don't want to hear. It was only after his second divorce that Pottruck finally was able to acknowledge that he still had large blind spots: "After my second marriage fell apart, I thought I had a wife-selection problem." Then he worked with a counselor who delivered some hard truths: "The good news is you do not have a wife-selection problem; the bad news is you have a husband-behavior problem." Pottruck then made a determined effort to change. As he described it, "I was like a guy who has had three heart attacks and finally realizes he has to quit smoking and lose some weight."

These days Pottruck is happily remarried and listens carefully when his wife offers constructive feedback. He acknowledges that he falls back on his old habits at times, particularly in high stress situations, but now he has developed ways of coping with stress. "I have had enough success in life to have that foundation of self-respect, so I can take the criticism and not deny it. I have finally learned to tolerate my failures and disappointments and not beat myself up."

Practicing Your Values and Principles

The values that form the basis for authentic leadership are derived from your beliefs and convictions, but you will not know what your true values are until they are tested under pressure. It is relatively easy to list your values and to live by them when things are going well. When your success, your career, or even your life hangs in the balance, you learn what is most important, what you are prepared to sacrifice, and what trade-offs you are willing to make.

Leadership principles are values translated into action. Having a solid base of values and testing them under fire enables you to develop the principles you will use in leading. For example, a value such as “concern for others” might be translated into a leadership principle such as “create a work environment where people are respected for their contributions, provided job security, and allowed to fulfill their potential.”

Consider Jon Huntsman, the founder and chairman of Huntsman Corporation. His moral values were deeply challenged when he worked for the Nixon administration in 1972, shortly before Watergate. After a brief stint in the U.S. Department of Health, Education, and Welfare (HEW), he took a job under H.R. Haldeman, President Nixon’s powerful chief of staff. Huntsman said he found the experience of taking orders from Haldeman “very mixed. I wasn’t geared to take orders, irrespective of whether they were ethically or morally right.” He explained, “We had a few clashes, as plenty of things that Haldeman wanted to do were questionable. An amoral atmosphere permeated the White House.”

One day, Haldeman directed Huntsman to help him entrap a California congressman who had been opposing a White House initiative. The congressman was part owner of a plant that reportedly employed undocumented workers. To gather information to embarrass the congressman, Haldeman told Huntsman to get the plant manager of a company Huntsman owned to place some undocumented workers at the congressman’s plant in an undercover operation.

“There are times when we react too quickly and fail to realize

immediately what is right and wrong,” Huntsman recalled. “This was one of those times when I didn’t think it through. I knew instinctively it was wrong, but it took a few minutes for the notion to percolate. After 15 minutes, my inner moral compass made itself noticed and enabled me to recognize this wasn’t the right thing to do. Values that had accompanied me since childhood kicked in. Halfway through my conversation with our plant manager, I said to him, ‘Let’s not do this. I don’t want to play this game. Forget that I called.’”

Huntsman told Haldeman that he would not use his employees in this way. “Here I was saying no to the second most powerful person in the country. He didn’t appreciate responses like that, as he viewed them as signs of disloyalty. I might as well have been saying farewell. So be it. I left within the next six months.”

Balancing Your Extrinsic and Intrinsic Motivations

Because authentic leaders need to sustain high levels of motivation and keep their lives in balance, it is critically important for them to understand what drives them. There are two types of motivations—extrinsic and intrinsic. Although they are reluctant to admit it, many leaders are propelled to achieve by measuring their success against the outside world's parameters. They enjoy the recognition and status that come with promotions and financial rewards. Intrinsic motivations, on the other hand, are derived from their sense of the meaning of their life. They are closely linked to one's life story and the way one frames it. Examples include personal growth, helping other people develop, taking on social causes, and making a difference in the world. The key is to find a balance between your desires for external validation and the intrinsic motivations that provide fulfillment in your work.

Many interviewees advised aspiring leaders to be wary of getting caught up in social, peer, or parental expectations. Debra Dunn, who has worked in Silicon Valley for decades as a Hewlett-Packard executive, acknowledged the constant pressures from external sources: "The path of accumulating material possessions is clearly laid out. You know how to measure it. If you don't pursue that path, people wonder what is wrong with you. The only way to avoid getting caught up in materialism is to understand where you find happiness and fulfillment."

Moving away from the external validation of personal achievement is not always easy. Achievement-oriented leaders grow so accustomed to successive accomplishments throughout their early years that it takes courage to pursue their intrinsic motivations. But at some point, most leaders recognize that they need to address more difficult questions in order to pursue truly meaningful success. McKinsey's Alice Woodwark, who at 29 has already achieved notable success, reflected: "My version of achievement was pretty naive, born of things I learned early in life about praise and being valued. But if you're just chasing the rabbit around the course, you're not running toward anything meaningful."

Your Development as an Authentic Leader

As you read this article, think about the basis for your leadership development and the path you need to follow to become an authentic leader. Then ask yourself these questions:

1. **Which people and experiences in your early life had the greatest impact on you?**
2. **What tools do you use to become self-aware?** What is your authentic self? What are the moments when you say to yourself, this is the real me?
3. **What are your most deeply held values?** Where did they come from? Have your values changed significantly since your childhood? How do your values inform your actions?
4. **What motivates you extrinsically?** What are your intrinsic motivations? How do you balance extrinsic and intrinsic motivation in your life?
5. **What kind of support team do you have?** How can your support team make you a more authentic leader? How should you diversify your team to broaden your perspective?
6. **Is your life integrated?** Are you able to be the same person in all aspects of your life—personal, work, family, and community? If not, what is holding you back?
7. **What does being authentic mean in your life?** Are you more effective as a leader when you behave authentically? Have you ever paid a price for your authenticity as a leader? Was it worth it?
8. **What steps can you take today, tomorrow, and over the next year to develop your authentic leadership?**

Intrinsic motivations are congruent with your values and are more fulfilling than extrinsic motivations. John Thain, CEO of the New York Stock

Exchange, said, “I am motivated by doing a really good job at whatever I am doing, but I prefer to multiply my impact on society through a group of people.” Or as Ann Moore, chairman and CEO of Time, put it, “I came here 25 years ago solely because I loved magazines and the publishing world.” Moore had a dozen job offers after business school but took the lowest-paying one with Time because of her passion for publishing.

Building Your Support Team

Leaders cannot succeed on their own; even the most outwardly confident executives need support and advice. Without strong relationships to provide perspective, it is very easy to lose your way.

Authentic leaders build extraordinary support teams to help them stay on course. Those teams counsel them in times of uncertainty, help them in times of difficulty, and celebrate with them in times of success. After their hardest days, leaders find comfort in being with people on whom they can rely so they can be open and vulnerable. During the low points, they cherish the friends who appreciate them for who they are, not what they are. Authentic leaders find that their support teams provide affirmation, advice, perspective, and calls for course corrections when needed.

How do you go about building your support team? Most authentic leaders have a multifaceted support structure that includes their spouses or significant others, families, mentors, close friends, and colleagues. They build their networks over time, as the experiences, shared histories, and openness with people close to them create the trust and confidence they need in times of trial and uncertainty. Leaders must give as much to their supporters as they get from them so that mutually beneficial relationships can develop.

It starts with having at least one person in your life with whom you can be completely yourself, warts and all, and still be accepted unconditionally. Often that person is the only one who can tell you the honest truth. Most leaders have their closest relationships with their spouses, although some develop these bonds with another family member, a close friend, or a trusted mentor. When leaders can rely on unconditional support, they are more likely to accept themselves for who they really are.

Many relationships grow over time through an expression of shared values and a common purpose. Randy Komisar of venture capital firm Kleiner Perkins Caufield & Byers said his marriage to Hewlett-Packard's Debra Dunn is lasting because it is rooted in similar values. "Debra and I are very independent but extremely harmonious in terms of our personal

aspirations, values, and principles. We have a strong resonance around questions like, ‘What is your legacy in this world?’ It is important to be in sync about what we do with our lives.”

Many leaders have had a mentor who changed their lives. The best mentoring interactions spark mutual learning, exploration of similar values, and shared enjoyment. If people are only looking for a leg up from their mentors, instead of being interested in their mentors’ lives as well, the relationships will not last for long. It is the two-way nature of the connection that sustains it.

Personal and professional support groups can take many forms. Piper Jaffray’s Tad Piper is a member of an Alcoholics Anonymous group. He noted, “These are not CEOs. They are just a group of nice, hard-working people who are trying to stay sober, lead good lives, and work with each other about being open, honest, and vulnerable. We reinforce each other’s behavior by talking about our chemical dependency in a disciplined way as we go through the 12 steps. I feel blessed to be surrounded by people who are thinking about those kinds of issues and actually doing something, not just talking about them.”

Bill George’s experiences echo Piper’s: In 1974, he joined a men’s group that formed after a weekend retreat. More than 30 years later, the group is still meeting every Wednesday morning. After an opening period of catching up on each other’s lives and dealing with any particular difficulty someone may be facing, one of the group’s eight members leads a discussion on a topic he has selected. These discussions are open, probing, and often profound. The key to their success is that people say what they really believe without fear of judgment, criticism, or reprisal. All the members consider the group to be one of the most important aspects of their lives, enabling them to clarify their beliefs, values, and understanding of vital issues, as well as serving as a source of honest feedback when they need it most.

Integrating Your Life by Staying Grounded

Integrating their lives is one of the greatest challenges leaders face. To lead a balanced life, you need to bring together all of its constituent elements—work, family, community, and friends—so that you can be the same person in each environment. Think of your life as a house, with a bedroom for your personal life, a study for your professional life, a family room for your family, and a living room to share with your friends. Can you knock down the walls between these rooms and be the same person in each of them?

As John Donahoe, president of eBay Marketplaces and former worldwide managing director of Bain, stressed, being authentic means maintaining a sense of self no matter where you are. He warned, “The world can shape you if you let it. To have a sense of yourself as you live, you must make conscious choices. Sometimes the choices are really hard, and you make a lot of mistakes.”

Authentic leaders have a steady and confident presence. They do not show up as one person one day and another person the next. Integration takes discipline, particularly during stressful times when it is easy to become reactive and slip back into bad habits. Donahoe feels strongly that integrating his life has enabled him to become a more effective leader. “There is no nirvana,” he said. “The struggle is constant, as the trade-offs don’t get any easier as you get older.” But for authentic leaders, personal and professional lives are not a zero-sum game. As Donahoe said, “I have no doubt today that my children have made me a far more effective leader in the workplace. Having a strong personal life has made the difference.”

Leading is high-stress work. There is no way to avoid stress when you are responsible for people, organizations, outcomes, and managing the constant uncertainties of the environment. The higher you go, the greater your freedom to control your destiny but also the higher the degree of stress. The question is not whether you can avoid stress but how you can control it to maintain your own sense of equilibrium.

Authentic leaders are constantly aware of the importance of staying

grounded. Besides spending time with their families and close friends, authentic leaders get physical exercise, engage in spiritual practices, do community service, and return to the places where they grew up. All are essential to their effectiveness as leaders, enabling them to sustain their authenticity.

Empowering People to Lead

Now that we have discussed the process of discovering your authentic leadership, let's look at how authentic leaders empower people in their organizations to achieve superior long-term results, which is the bottom line for all leaders.

Authentic leaders recognize that leadership is not about their success or about getting loyal subordinates to follow them. They know the key to a successful organization is having empowered leaders at all levels, including those who have no direct reports. They not only inspire those around them, they empower those individuals to step up and lead.

A reputation for building relationships and empowering people was instrumental in chairman and CEO Anne Mulcahy's stunning turnaround of Xerox. When Mulcahy was asked to take the company's reins from her failed predecessor, Xerox had \$18 billion in debt, and all credit lines were exhausted. With the share price in free fall, morale was at an all-time low. To make matters worse, the SEC was investigating the company's revenue recognition practices.

Mulcahy's appointment came as a surprise to everyone—including Mulcahy herself. A Xerox veteran, she had worked in field sales and on the corporate staff for 25 years, but not in finance, R&D, or manufacturing. How could Mulcahy cope with this crisis when she had had no financial experience? She brought to the CEO role the relationships she had built over 25 years, an impeccable understanding of the organization, and, above all, her credibility as an authentic leader. She bled for Xerox, and everyone knew it. Because of that, they were willing to go the extra mile for her.

After her appointment, Mulcahy met personally with the company's top 100 executives to ask them if they would stay with the company despite the challenges ahead. "I knew there were people who weren't supportive of me," she said. "So I confronted a couple of them and said, 'This is about the company.'" The first two people Mulcahy talked with, both of whom ran big operating units, decided to leave, but the remaining 98 committed to stay.

Throughout the crisis, people in Xerox were empowered by Mulcahy to step up and lead in order to restore the company to its former greatness. In the end, her leadership enabled Xerox to avoid bankruptcy as she paid back \$10 billion in debt and restored revenue growth and profitability with a combination of cost savings and innovative new products. The stock price tripled as a result.

Like Mulcahy, all leaders have to deliver bottom-line results. By creating a virtuous circle in which the results reinforce the effectiveness of their leadership, authentic leaders are able to sustain those results through good times and bad. Their success enables them to attract talented people and align employees' activities with shared goals, as they empower others on their team to lead by taking on greater challenges. Indeed, superior results over a sustained period of time are the ultimate mark of an authentic leader. It may be possible to drive short-term outcomes without being authentic, but authentic leadership is the only way we know to create sustainable long-term results.

For authentic leaders, there are special rewards. No individual achievement can equal the pleasure of leading a group of people to achieve a worthy goal. When you cross the finish line together, all the pain and suffering you may have experienced quickly vanishes. It is replaced by a deep inner satisfaction that you have empowered others and thus made the world a better place. That's the challenge and the fulfillment of authentic leadership.

Originally published in February 2007. Reprint R0702H

In Praise of the Incomplete Leader

by Deborah Ancona, Thomas W. Malone, Wanda J. Orlikowski, and Peter M. Senge

WE'VE COME TO EXPECT A LOT OF OUR LEADERS. Top executives, the thinking goes, should have the intellectual capacity to make sense of unfathomably complex issues, the imaginative powers to paint a vision of the future that generates everyone's enthusiasm, the operational know-how to translate strategy into concrete plans, and the interpersonal skills to foster commitment to undertakings that could cost people's jobs should they fail. Unfortunately, no single person can possibly live up to those standards.

It's time to end the myth of the complete leader: the flawless person at the top who's got it all figured out. In fact, the sooner leaders stop trying to be all things to all people, the better off their organizations will be. In today's world, the executive's job is no longer to command and control but to cultivate and coordinate the actions of others at all levels of the organization. Only when leaders come to see themselves as incomplete—as having both strengths and weaknesses—will they be able to make up for their missing skills by relying on others.

Corporations have been becoming less hierarchical and more collaborative for decades, of course, as globalization and the growing importance of knowledge work have required that responsibility and initiative be distributed more widely. Moreover, it is now possible for large groups of people to coordinate their actions, not just by bringing lots of information to a few centralized places but also by bringing lots of information to lots of places through ever-growing networks within and beyond the firm. The sheer

complexity and ambiguity of problems is humbling. More and more decisions are made in the context of global markets and rapidly—sometimes radically—changing financial, social, political, technological, and environmental forces. Stakeholders such as activists, regulators, and employees all have claims on organizations.

No one person could possibly stay on top of everything. But the myth of the complete leader (and the attendant fear of appearing incompetent) makes many executives try to do just that, exhausting themselves and damaging their organizations in the process. The incomplete leader, by contrast, knows when to let go: when to let those who know the local market do the advertising plan or when to let the engineering team run with its idea of what the customer needs. The incomplete leader also knows that leadership exists throughout the organizational hierarchy—wherever expertise, vision, new ideas, and commitment are found.

We've worked with hundreds of people who have struggled under the weight of the myth of the complete leader. Over the past six years, our work at the MIT Leadership Center has included studying leadership in many organizations and teaching the topic to senior executives, middle managers, and MBA students. In our practice-based programs, we have analyzed numerous accounts of organizational change and watched leaders struggle to meld top-down strategic initiatives with vibrant ideas from the rest of the organization.

All this work has led us to develop a model of distributed leadership. This framework, which synthesizes our own research with ideas from other leadership scholars, views leadership as a set of four capabilities: *sensemaking* (understanding the context in which a company and its people operate), *relating* (building relationships within and across organizations), *visioning* (creating a compelling picture of the future), and *inventing* (developing new ways to achieve the vision).

Idea in Brief

Have you ever feigned confidence to superiors or reports? Hidden the fact you were confused by the latest business results or blindsided by a competitor's move? If so, you've bought into the **myth of the complete leader**: the flawless being at the top who's got it all figured out.

It's an alluring myth. But in today's world of increasingly complex problems, no human being can meet this standard. Leaders who try only exhaust themselves, endangering their organizations.

Ancona and her coauthors suggest a better way to lead: Accept that you're human, with strengths and weaknesses. Understand the four leadership capabilities all organizations need:

- Sensemaking—interpreting developments in the business environment
- Relating—building trusting relationships
- Visioning—communicating a compelling image of the future
- Inventing—coming up with new ways of doing things

Then find and work with others who can provide the capabilities you're missing.

Take this approach, and you promote leadership throughout your organization, unleashing the expertise, vision, and new ideas your company needs to excel.

While somewhat simplified, these capabilities span the intellectual and interpersonal, the rational and intuitive, and the conceptual and creative capacities required in today's business environment. Rarely, if ever, will someone be equally skilled in all four domains. Thus, incomplete leaders differ from incompetent leaders in that they understand what they're good at and what they're not and have good judgment about how they can work with

others to build on their strengths and offset their limitations.

Sometimes, leaders need to further develop the capabilities they are weakest in. The exhibits throughout this article provide some suggestions for when and how to do that. Other times, however, it's more important for leaders to find and work with others to compensate for their weaknesses. Teams and organizations—not just individuals—can use this framework to diagnose their strengths and weaknesses and find ways to balance their skill sets.

Idea in Practice

Incomplete leaders find people throughout their company who can complement their strengths and offset their weaknesses. To do this, understand the four leadership capabilities organizations need. Then diagnose your strength in each:

Capability	What it means	Example	Look for help in this capability if you ...
Sensemaking	Constantly understanding changes in the business environment and interpreting their ramifications for your industry and company	A CEO asks, "How will new technologies reshape our industry?" "How does globalization of labor markets affect our recruitment strategy?"	• Feel strongly that you're always right. • Frequently get blindsided by changes in your company or industry. • Feel resentful when things change.
Relating	Building trusting relationships, balancing advocacy (explaining your viewpoints) with inquiry (listening to understand others' viewpoints), and cultivating networks of supportive confidants	Former Southwest Airlines CEO Herb Kelleher excels at building trusting relationships. He wasn't afraid to tell employees he loved them, and reinforced those emotional bonds with equitable compensation and profit sharing.	• Blame others for failed projects. • Feel others are constantly letting you down or that they can't be trusted. • Frequently experience unpleasant, frustrating, or argumentative interactions with others.
Visioning	Creating credible and compelling images of a desired future that people in the organization want to create together	eBay founder Pierre Omidyar envisioned a new way of doing large-scale retailing: an online community where users took responsibility for what happened and had equal access to information.	• Often wonder, "Why are we doing this?" or "Does it really matter?" • Can't remember the last time you felt excited about your work. • Feel you're lacking sense of larger purpose.
Inventing	Creating new ways of approaching tasks or overcoming seemingly insurmountable problems to turn visions into reality	eBay CEO Meg Whitman helped bring Omidyar's vision of online retailing to life by inventing ways to deal with security, vendor reliability, and product diversification.	• Have difficulty relating the company's vision to what you're doing today. • Notice gaps between your firm's aspirations and the way work is organized. • Find that things tend to revert to business as usual.

Sensemaking

The term “sensemaking” was coined by organizational psychologist Karl Weick, and it means just what it sounds like: making sense of the world around us. Leaders are constantly trying to understand the contexts they are operating in. How will new technologies reshape the industry? How will changing cultural expectations shift the role of business in society? How does the globalization of labor markets affect recruitment and expansion plans?

Weick likened the process of sensemaking to cartography. What we map depends on where we look, what factors we choose to focus on, and what aspects of the terrain we decide to represent. Since these choices will shape the kind of map we produce, there is no perfect map of a terrain. Therefore, making sense is more than an act of analysis; it’s an act of creativity. (See the exhibit “Engage in Sensemaking.”)

Engage in sensemaking

- 1Get data from multiple sources: customers, suppliers, employees, competitors, other departments, and investors.
- 2Involve others in your sensemaking. Say what you think you are seeing, and check with people who have different perspectives from yours.
- 3Use early observations to shape small experiments in order to test your conclusions. Look for new ways to articulate alternatives and better ways to understand options.
- 4Do not simply apply existing frameworks but instead be open to new possibilities. Try not to describe the world in stereotypical ways, such as good guys and bad guys, victims and oppressors, or marketers and engineers.

The key for leaders is to determine what would be a useful map given their particular goals and then to draw one that adequately represents the situation the organization is facing at that moment. Executives who are strong in this capability know how to quickly capture the complexities of their environment and explain them to others in simple terms. This helps ensure that everyone is working from the same map, which makes it far easier to discuss and plan for the journey ahead. Leaders need to have the courage to present a map that highlights features they believe to be critical, even if their map doesn't conform to the dominant perspective.

When John Reed was CEO of Citibank, the company found itself in a real estate crisis. At the time, common wisdom said that Citibank would need to take a \$2 billion write-off, but Reed wasn't sure. He wanted a better understanding of the situation, so to map the problem, he met with federal regulators as well as his managers, the board, potential investors, economists, and real estate experts. He kept asking, "What am I missing here?" After those meetings, he had a much stronger grasp of the problem, and he

recalibrated the write-off to \$5 billion—which turned out to be a far more accurate estimate. Later, three quarters into the bank’s eight-quarter program to deal with the crisis, Reed realized that progress had stopped. He began talking to other CEOs known for their change management skills. This informal benchmarking process led him to devise an organizational redesign.

Throughout the crisis, real estate valuations, investors’ requirements, board demands, and management team expectations were all changing and constantly needed to be reassessed. Good leaders understand that sensemaking is a continuous process; they let the map emerge from a melding of observations, data, experiences, conversations, and analyses. In healthy organizations, this sort of sensemaking goes on all the time. People have ongoing dialogues about their interpretations of markets and organizational realities.

At IDEO, a product design firm, sensemaking is step one for all design teams. According to founder David Kelley, team members must act as anthropologists studying an alien culture to understand the potential product from all points of view. When brainstorming a new design, IDEO’s teams consider multiple perspectives—that is, they build multiple maps to inform their creative process. One IDEO team was charged with creating a new design for an emergency room. To better understand the experience of a key stakeholder—the patient—team members attached a camera to a patient’s head and captured his experience in the ER. The result: nearly ten full hours of film of the ceiling. The sensemaking provoked by this perspective led to a redesign of the ceiling that made it more aesthetically pleasing and able to display important information for patients.

Relating

Many executives who attempt to foster trust, optimism, and consensus often reap anger, cynicism, and conflict instead. That's because they have difficulty relating to others, especially those who don't make sense of the world the way they do. Traditional images of leadership didn't assign much value to relating. Flawless leaders shouldn't need to seek counsel from anyone outside their tight inner circle, the thinking went, and they were expected to issue edicts rather than connect on an emotional level. Times have changed, of course, and in this era of networks, being able to build trusting relationships is a requirement of effective leadership.

Three key ways to do this are *inquiring*, *advocating*, and *connecting*. The concepts of inquiring and advocating stem from the work of organizational development specialists Chris Argyris and Don Schon. Inquiring means listening with the intention of genuinely understanding the thoughts and feelings of the speaker. Here, the listener suspends judgment and tries to comprehend how and why the speaker has moved from the data of his or her experiences to particular interpretations and conclusions.

Advocating, as the term implies, means explaining one's own point of view. It is the flip side of inquiring, and it's how leaders make clear to others how they reached their interpretations and conclusions. Good leaders distinguish their observations from their opinions and judgments and explain their reasoning without aggression or defensiveness. People with strong relating skills are typically those who've found a healthy balance between inquiring and advocating: They actively try to understand others' views but are able to stand up for their own. (See the exhibit "Build Relationships.")

Build relationships

- 1Spend time trying to understand others' perspectives, listening with an open mind and without judgment.
- 2Encourage others to voice their opinions. What do they care about? How do they interpret what's going on? Why?
- 3Before expressing your ideas, try to anticipate how others will react to them and how you might best explain them.
- 4When expressing your ideas, don't just give a bottom line; explain your reasoning process.
- 5Assess the strengths of your current connections: How well do you relate to others when receiving advice? When giving advice? When thinking through difficult problems? When asking for help?

We've seen countless relationships undermined because people disproportionately emphasized advocating over inquiring. Even though managers pay lip service to the importance of mutual understanding and shared commitment to a course of action, often their real focus is on winning the argument rather than strengthening the connection. Worse, in many organizations, the imbalance goes so far that having one's point of view prevail is what is understood as leadership.

Effective relating does not mean avoiding interpersonal conflict altogether. Argyris and Schon found that "maintaining a smooth surface" of conviviality and apparent agreement is one of the most common defensive routines that limits team effectiveness. Balancing inquiring and advocating is ultimately about showing respect, challenging opinions, asking tough questions, and taking a stand.

Consider Twynstra Gudde (TG), one of the largest independent consulting companies in the Netherlands. A few years ago, it replaced the role of CEO with a team of four managing directors who share leadership responsibilities.

Given this unique structure, it's vital that these directors effectively relate to one another. They've adopted simple rules, such as a requirement that each leader give his opinion on every issue, majority-rules voting, and veto power for each director.

Clearly, for TG's senior team model to work, members must be skilled at engaging in dialogue together. They continually practice both inquiring and advocating, and because each director can veto a decision, each must thoroughly explain his reasoning to convince the others' that his perspective has merit. It's not easy to reach this level of mutual respect and trust, but over time, the team members' willingness to create honest connections with one another has paid off handsomely. Although they don't always reach consensus, they are able to settle on a course of action. Since this new form of leadership was introduced, TG has thrived: The company's profits have doubled, and employee satisfaction levels have improved. What's more, TG's leadership structure has served as a model for cooperation throughout the organization as well as in the firm's relations with its clients.

The third aspect of relating, connecting, involves cultivating a network of confidants who can help a leader accomplish a wide range of goals. Leaders who are strong in this capability have many people they can turn to who can help them think through difficult problems or support them in their initiatives. They understand that the time spent building and maintaining these connections is time spent investing in their leadership skills. Because no one person can possibly have all the answers, or indeed, know all the right questions to ask, it's crucial that leaders be able to tap into a network of people who can fill in the gaps.

Visioning

Sensemaking and relating can be called the enabling capabilities of leadership. They help set the conditions that motivate and sustain change. The next two leadership capabilities—what we call “visioning” and inventing—are creative and action oriented: They produce the focus and energy needed to make change happen.

Visioning involves creating compelling images of the future. While sensemaking charts a map of what is, visioning produces a map of what could be and, more important, what a leader wants the future to be. It consists of far more than pinning a vision statement to the wall. Indeed, a shared vision is not a static thing—it’s an ongoing process. Like sensemaking, visioning is dynamic and collaborative, a process of articulating what the members of an organization want to create together.

Fundamentally, visioning gives people a sense of meaning in their work. Leaders who are skilled in this capability are able to get people excited about their view of the future while inviting others to help crystallize that image. (See the exhibit “Create a Vision.”) If they realize other people aren’t joining in or buying into the vision, they don’t just turn up the volume; they engage in a dialogue about the reality they hope to produce. They use stories and metaphors to paint a vivid picture of what the vision will accomplish, even if they don’t have a comprehensive plan for getting there. They know that if the vision is credible and compelling enough, others will generate ideas to advance it.

Create a vision

- 1Practice creating a vision in many arenas, including your work life, your home life, and in community groups. Ask yourself, “What do I want to create?”
- 2Develop a vision about something that inspires you. Your enthusiasm will motivate you and others. Listen to what they find exciting and important.
- 3Expect that not all people will share your passion. Be prepared to explain why people should care about your vision and what can be achieved through it. If people don’t get it, don’t just turn up the volume. Try to construct a shared vision.
- 4Don’t worry if you don’t know how to accomplish the vision. If it is compelling and credible, other people will discover all sorts of ways to make it real—ways you never could have imagined on your own.
- 5Use images, metaphors, and stories to convey complex situations that will enable others to act.

In South Africa in the early 1990s, a joke was making the rounds: Given the country’s daunting challenges, people had two options, one practical and the other miraculous. The practical option was for everyone to pray for a band of angels to come down from heaven and fix things. The miraculous option was for people to talk with one another until they could find a way forward. In F.W. de Klerk’s famous speech in 1990—his first after assuming leadership—he called for a nonracist South Africa and suggested that negotiation was the only way to achieve a peaceful transition. That speech sparked a set of changes that led to Nelson Mandela’s release from Robben Island prison and the return to the country of previously banned political leaders.

Few of South Africa’s leaders agreed on much of anything regarding the

country's future. It seemed like a long shot, at best, that a scenario-planning process convened by a black professor from the University of the Western Cape and facilitated by a white Canadian from Royal Dutch Shell would be able to bring about any sort of change. But they, together with members of the African National Congress (ANC), the radical Pan Africanist Congress (PAC), and the white business community, were charged with forging a new path for South Africa.

When the team members first met, they focused on collective sensemaking. Their discussions then evolved into a yearlong visioning process. In his book, *Solving Tough Problems*, Adam Kahane, the facilitator, says the group started by telling stories of “left-wing revolution, right-wing revolts, and free market utopias.” Eventually, the leadership team drafted a set of scenarios that described the many paths toward disaster and the one toward sustainable development.

They used metaphors and clear imagery to convey the various paths in language that was easy to understand. One negative scenario, for instance, was dubbed “Ostrich”: A nonrepresentative white government sticks its head in the sand, trying to avoid a negotiated settlement with the black majority. Another negative scenario was labeled “Icarus”: A constitutionally unconstrained black government comes to power with noble intentions and embarks on a huge, unsustainable public-spending spree that crashes the economy. This scenario contradicted the popular belief that the country was rich and could simply redistribute wealth from whites to blacks. The Icarus scenario set the stage for a fundamental (and controversial) shift in economic thinking in the ANC and other left-wing parties—a shift that led the ANC government to “strict and consistent fiscal discipline,” according to Kahane.

The group's one positive scenario involved the government adopting a set of sustainable policies that would put the country on a path of inclusive growth to successfully rebuild the economy and establish democracy. This option was called “Flamingo,” invoking the image of a flock of beautiful birds all taking flight together.

This process of visioning unearthed an extraordinary collective sense of possibility in South Africa. Instead of talking about what other people should do to advance some agenda, the leaders spoke about what they could do to create a better future for everyone. They didn't have an exact implementation plan at the ready, but by creating a credible vision, they paved the way for others to join in and help make their vision a reality.

Leaders who excel in visioning walk the walk; they work to embody the core values and ideas contained in the vision. Darcy Winslow, Nike's global director for women's footwear, is a good example. A 14-year veteran at Nike, Winslow previously held the position of general manager of sustainable business opportunities at the shoe and apparel giant. Her work in that role reflected her own core values, including her passion for the environment. "We had come to see that our customers' health and our own ability to compete were inseparable from the health of the environment," she says. So she initiated the concept of ecologically intelligent product design. Winslow's team worked at determining the chemical composition and environmental effects of every material and process Nike used. They visited factories in China and collected samples of rubber, leather, nylon, polyester, and foams to determine their chemical makeup. This led Winslow and her team to develop a list of "positive" materials—those that weren't harmful to the environment—that they hoped to use in more Nike products. "Environmental sustainability" was no longer just an abstract term on a vision statement; the team now felt a mandate to realize the vision.

Inventing

Even the most compelling vision will lose its power if it floats, unconnected, above the everyday reality of organizational life. To transform a vision of the future into a present-day reality, leaders need to devise processes that will give it life. This inventing is what moves a business from the abstract world of ideas to the concrete world of implementation. In fact, inventing is similar to execution, but the label “inventing” emphasizes that this process often requires creativity to help people figure out new ways of working together.

To realize a new vision, people usually can't keep doing the same things they've been doing. They need to conceive, design, and put into practice new ways of interacting and organizing. Some of the most famous examples of large-scale organizational innovation come from the automotive industry: Henry Ford's conception of the assembly-line factory and Toyota's famed integrated production system.

More recently, Pierre Omidyar, the founder of eBay, invented through his company a new way of doing large-scale retailing. His vision was of an online community where users would take responsibility for what happened. In a 2001 BusinessWeek Online interview, Omidyar explained, “I had the idea that I wanted to create an efficient market and a level playing field where everyone had equal access to information. I wanted to give the power of the market back to individuals, not just large corporations. That was the driving motivation for creating eBay at the start.”

Consequently, eBay outsources most of the functions of traditional retailing—purchasing, order fulfillment, and customer service, for example—to independent sellers worldwide. The company estimates that more than 430,000 people make their primary living from selling wares on eBay. If those individuals were all employees of eBay, it would be the second largest private employer in the United States after Wal-Mart.

The people who work through eBay are essentially independent store owners, and, as such, they have a huge amount of autonomy in how they do their work. They decide what to sell, when to sell it, how to price, and how to

advertise. Coupled with this individual freedom is global scale. EBay's infrastructure enables them to sell their goods all over the world. What makes eBay's inventing so radical is that it represents a new relationship between an organization and its parts. Unlike typical outsourcing, eBay doesn't pay its retailers—they pay the company.

Inventing doesn't have to occur on such a grand scale. It happens every time a person creates a way of approaching a task or figures out how to overcome a previously insurmountable obstacle. In their book *Car Launch*, George Roth and Art Kleiner describe a highly successful product development team in the automobile industry that struggled with completing its designs on time. Much of the source of the problem, the team members concluded, came from the stovepipe organizational structure found in the product development division. Even though they were a "colocated" team dedicated to designing a common new car, members were divided by their different technical expertise, experience, jargon, and norms of working.

When the team invented a mechanical prototyping device that complemented its computer-aided design tools, the group members found that it facilitated a whole new way of collaborating. Multiple groups within the team could quickly create physical mock-ups of design ideas to be tested by the various engineers from different specialties in the team. The group called the device "the harmony buck," because it helped people break out of their comfortable engineering specialties and solve interdependent design problems together. Development of a "full body" physical mock-up of the new car allowed engineers to hang around the prototype, providing a central focal point for their interactions. It enabled them to more easily identify and raise cross-functional issues, and it facilitated mutual problem solving and coordination.

In sum, leaders must be able to succeed at inventing, and this requires both attention to detail and creativity. (See the exhibit "Cultivate Inventiveness.")

Cultivate inventiveness

- 1 Don't assume that the way things have always been done is the best way to do them.
 - 2 When a new task or change effort emerges, encourage creative ways of getting it done.
 - 3 Experiment with different ways of organizing work. Find alternative methods for grouping and linking people.
 - 4 When working to understand your current environment, ask yourself, "What other options are possible?"
-

Balancing the Four Capabilities

Sensemaking, relating, visioning, and inventing are interdependent. Without sensemaking, there's no common view of reality from which to start. Without relating, people work in isolation or, worse, strive toward different aims. Without visioning, there's no shared direction. And without inventing, a vision remains illusory. No one leader, however, will excel at all four capabilities in equal measure.

Typically, leaders are strong in one or two capabilities. Intel chairman Andy Grove is the quintessential sensemaker, for instance, with a gift for recognizing strategic inflection points that can be exploited for competitive advantage. Herb Kelleher, the former CEO of Southwest Airlines, excels at relating. He remarked in the journal *Leader to Leader* that "We are not afraid to talk to our people with emotion. We're not afraid to tell them, 'We love you.' Because we do." With this emotional connection comes equitable compensation and profit sharing.

Apple CEO Steve Jobs is a visionary whose ambitious dreams and persuasiveness have catalyzed remarkable successes for Apple, Next, and Pixar. Meg Whitman, the CEO of eBay, helped bring Pierre Omidyar's vision of online retailing to life by inventing ways to deal with security, vendor reliability, and product diversification.

Once leaders diagnose their own capabilities, identifying their unique set of strengths and weaknesses, they must search for others who can provide the things they're missing. (See the sidebar "Examining Your Leadership Capabilities.") Leaders who choose only people who mirror themselves are likely to find their organizations tilting in one direction, missing one or more essential capabilities needed to survive in a changing, complex world. That's why it's important to examine the whole organization to make sure it is appropriately balanced as well. It's the leader's responsibility to create an environment that lets people complement one another's strengths and offset one another's weaknesses. In this way, leadership is distributed across multiple people throughout the organization.

Examining Your Leadership Capabilities

Few people wake up in the morning and say, “I’m a poor sensemaker” or “I just can’t relate to others.” They tend to experience their own weaknesses more as chronic or inexplicable failures in the organization or in those around them. The following descriptions will help you recognize opportunities to develop your leadership capabilities and identify openings for working with others.

Signs of Weak Sensemaking

- 1You feel strongly that you are usually right and others are often wrong.
- 2You feel your views describe reality correctly, but others’ views do not.
- 3You find you are often blindsided by changes in your organization or industry.
- 4When things change, you typically feel resentful. (That’s not the way it should be!)

Signs of Weak Relating

- 1You blame others for failed projects.
- 2You feel others are constantly letting you down or failing to live up to your expectations.
- 3You find that many of your interactions at work are unpleasant, frustrating, or argumentative.
- 4You find many of the people you work with untrustworthy.

Signs of Weak Visioning

- 1You feel your work involves managing an endless series of crises.
- 2You feel like you're bouncing from pillar to post with no sense of larger purpose.
- 3You often wonder, "Why are we doing this?" or "Does it really matter?"
- 4You can't remember the last time you talked to your family or a friend with excitement about your work.

Signs of Weak Inventing

- 1Your organization's vision seems abstract to you.
- 2You have difficulty relating your company's vision to what you are doing today.
- 3You notice dysfunctional gaps between your organization's aspirations and the way work is organized.
- 4You find that things tend to revert to business as usual.

Years ago, one of us attended a three-day meeting on leadership with 15 top managers from different companies. At the close of it, participants were asked to reflect on their experience as leaders. One executive, responsible for more than 50,000 people in his division of a manufacturing corporation, drew two pictures on a flip chart. The image on the left was what he projected to

the outside world: It was a large, intimidating face holding up a huge fist. The image on the right represented how he saw himself: a small face with wide eyes, hair standing on end, and an expression of sheer terror.

We believe that most leaders experience that profound dichotomy every day, and it's a heavy burden. How many times have you feigned confidence to superiors or reports when you were really unsure? Have you ever felt comfortable conceding that you were confused by the latest business results or caught off guard by a competitor's move? Would you ever admit to feeling inadequate to cope with the complex issues your firm was facing? Anyone who can identify with these situations knows firsthand what it's like to be trapped in the myth of the complete leader—the person at the top without flaws. It's time to put that myth to rest, not only for the sake of frustrated leaders but also for the health of organizations. Even the most talented leaders require the input and leadership of others, constructively solicited and creatively applied. It's time to celebrate the incomplete—that is, the human—leader.

Originally published in February 2007. Reprint R0702E

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First eBook Edition: February 2011

ISBN: 978-1-4221-5798-5

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What Is Strategy?

by Michael E. Porter

I. Operational Effectiveness Is Not Strategy

For almost two decades, managers have been learning to play by a new set of rules. Companies must be flexible to respond rapidly to competitive and market changes. They must benchmark continuously to achieve best practice. They must outsource aggressively to gain efficiencies. And they must nurture a few core competencies in race to stay ahead of rivals.

Positioning—once the heart of strategy—is rejected as too static for today's dynamic markets and changing technologies. According to the new dogma, rivals can quickly copy any market position, and competitive advantage is, at best, temporary.

But those beliefs are dangerous half-truths, and they are leading more and more companies down the path of mutually destructive competition. True, some barriers to competition are falling as regulation eases and markets become global. True, companies have properly invested energy in becoming leaner and more nimble. In many industries, however, what some call *hypercompetition* is a self-inflicted wound, not the inevitable outcome of a changing paradigm of competition.

The root of the problem is the failure to distinguish between operational effectiveness and strategy. The quest for productivity, quality, and speed has spawned a remarkable number of management tools and techniques: total quality management, benchmarking, time-based competition, outsourcing, partnering, reengineering, change management. Although the resulting operational improvements have often been dramatic, many companies have been frustrated by their inability to translate those gains into sustainable profitability. And bit by bit, almost imperceptibly, management tools have taken the place of strategy. As managers push to improve on all fronts, they move farther away from viable competitive positions.

Operational effectiveness: necessary but not sufficient

Operational effectiveness and strategy are both essential to superior performance, which, after all, is the primary goal of any enterprise. But they work in very different ways.

A company can outperform rivals only if it can establish a difference that it can preserve. It must deliver greater value to customers or create comparable value at a lower cost, or do both. The arithmetic of superior profitability then follows: delivering greater value allows a company to charge higher average unit prices; greater efficiency results in lower average unit costs.

Ultimately, all differences between companies in cost or price derive from the hundreds of activities required to create, produce, sell, and deliver their products or services, such as calling on customers, assembling final products, and training employees. Cost is generated by performing activities, and cost advantage arises from performing particular activities more efficiently than competitors. Similarly, differentiation arises from both the choice of activities and how they are performed. Activities, then, are the basic units of competitive advantage. Overall advantage or disadvantage results from all a company's activities, not only a few.¹

Operational effectiveness (OE) means performing similar activities *better* than rivals perform them. Operational effectiveness includes but is not limited to efficiency. It refers to any number of practices that allow a company to better utilize its inputs by, for example, reducing defects in products or developing better products faster. In contrast, strategic positioning means performing *different* activities from rivals' or performing similar activities in *different* ways.

Differences in operational effectiveness among companies are pervasive. Some companies are able to get more out of their inputs than others because they eliminate wasted effort, employ more advanced technology, motivate employees better, or have greater insight into managing particular activities or sets of activities. Such differences in operational effectiveness are an important source of differences in profitability among competitors because they directly affect relative cost positions and levels of differentiation.

Idea in Brief

The myriad activities that go into creating, producing, selling, and delivering a product or service are the basic units of competitive advantage. **Operational effectiveness** means performing these activities better—that is, faster, or with fewer inputs and defects—than rivals. Companies can reap enormous advantages from operational effectiveness, as Japanese firms demonstrated in the 1970s and 1980s with such practices as total quality management and continuous improvement. But from a competitive standpoint, the problem with operational effectiveness is that best practices are easily emulated. As all competitors in an industry adopt them, the **productivity frontier**—the maximum value a company can deliver at a given cost, given the best available technology, skills, and management techniques—shifts outward, lowering costs and improving value at the same time. Such competition produces absolute improvement in operational effectiveness, but relative improvement for no one. And the more benchmarking that companies do, the more **competitive convergence** you have—that is, the more indistinguishable companies are from one another.

Strategic positioning attempts to achieve sustainable competitive advantage by preserving what is distinctive about a company. It means performing *different* activities from rivals, or performing *similar* activities in different ways.

Differences in operational effectiveness were at the heart of the Japanese challenge to Western companies in the 1980s. The Japanese were so far ahead of rivals in operational effectiveness that they could offer lower cost and superior quality at the same time. It is worth dwelling on this point, because so much recent thinking about competition depends on it. Imagine for a moment a *productivity frontier* that constitutes the sum of all existing

best practices at any given time. Think of it as the maximum value that a company delivering a particular product or service can create at a given cost, using the best available technologies, skills, management techniques, and purchased inputs. The productivity frontier can apply to individual activities, to groups of linked activities such as order processing and manufacturing, and to an entire company's activities. When a company improves its operational effectiveness, it moves toward the frontier. Doing so may require capital investment, different personnel, or simply new ways of managing.

Idea in Practice

Three key principles underlie strategic positioning.

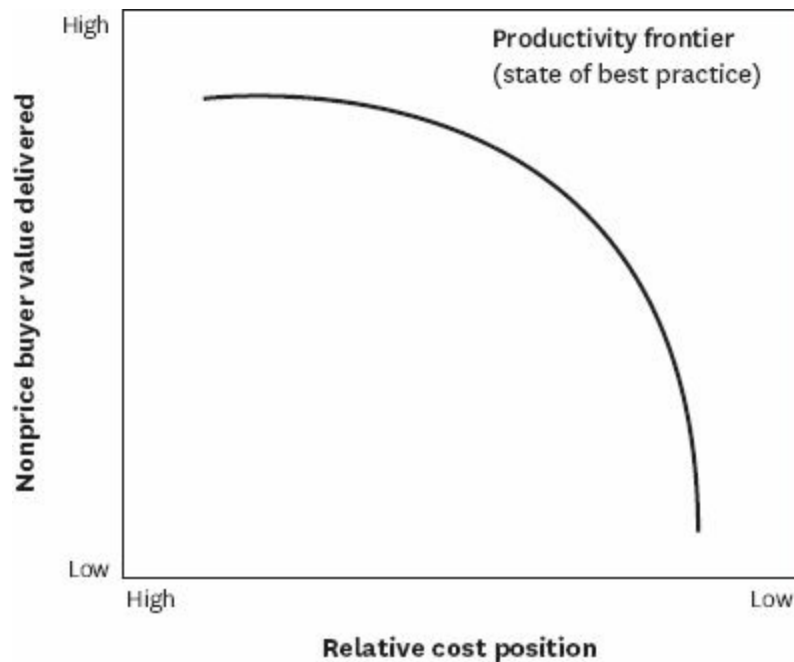
1. **Strategy is the creation of a unique and valuable position, involving a different set of activities.** Strategic position emerges from three distinct sources:
 - serving few needs of many customers (Jiffy Lube provides only auto lubricants)
 - serving broad needs of few customers (Bessemer Trust targets only very high-wealth clients)
 - serving broad needs of many customers in a narrow market (Carmike Cinemas operates only in cities with a population under 200,000)
2. **Strategy requires you to make trade-offs in competing—to choose what *not* to do.** Some competitive activities are incompatible; thus, gains in one area can be achieved only at the expense of another area. For example, Neutrogena soap is positioned more as a medicinal product than as a cleansing agent. The company says “no” to sales based on deodorizing, gives up large volume, and sacrifices manufacturing efficiencies. By contrast, Maytag’s decision to extend its product line and acquire other brands represented a failure to make difficult trade-offs: the boost in revenues came at the expense of return on sales.
3. **Strategy involves creating “fit” among a company’s activities.** Fit has to do with the ways a company’s activities

interact and reinforce one another. For example, Vanguard Group aligns all of its activities with a low-cost strategy; it distributes funds directly to consumers and minimizes portfolio turnover. Fit drives both competitive advantage and sustainability: when activities mutually reinforce each other, competitors can't easily imitate them. When Continental Lite tried to match a few of Southwest Airlines' activities, but not the whole interlocking system, the results were disastrous.

Employees need guidance about how to deepen a strategic position rather than broaden or compromise it. About how to extend the company's uniqueness while strengthening the fit among its activities. This work of deciding which target group of customers and needs to serve requires discipline, the ability to set limits, and forthright communication. Clearly, strategy and leadership are inextricably linked.

The productivity frontier is constantly shifting outward as new technologies and management approaches are developed and as new inputs become available. Laptop computers, mobile communications, the Internet, and software such as Lotus Notes, for example, have redefined the productivity frontier for sales-force operations and created rich possibilities for linking sales with such activities as order processing and after-sales support. Similarly, lean production, which involves a family of activities, has allowed substantial improvements in manufacturing productivity and asset utilization.

Operational effectiveness versus strategic positioning



For at least the past decade, managers have been preoccupied with improving operational effectiveness. Through programs such as TQM, time-based competition, and benchmarking, they have changed how they perform activities in order to eliminate inefficiencies, improve customer satisfaction, and achieve best practice. Hoping to keep up with shifts in the productivity frontier, managers have embraced continuous improvement, empowerment, change management, and the so-called learning organization. The popularity of outsourcing and the virtual corporation reflect the growing recognition that it is difficult to perform all activities as productively as specialists.

As companies move to the frontier, they can often improve on multiple dimensions of performance at the same time. For example, manufacturers that adopted the Japanese practice of rapid changeovers in the 1980s were able to lower cost and improve differentiation simultaneously. What were once believed to be real trade-offs—between defects and costs, for example—turned out to be illusions created by poor operational effectiveness. Managers have learned to reject such false trade-offs.

Constant improvement in operational effectiveness is necessary to achieve superior profitability. However, it is not usually sufficient. Few companies have competed successfully on the basis of operational effectiveness over an extended period, and staying ahead of rivals gets harder every day. The most obvious reason for that is the rapid diffusion of best practices. Competitors

can quickly imitate management techniques, new technologies, input improvements, and superior ways of meeting customers' needs. The most generic solutions—those that can be used in multiple settings—diffuse the fastest. Witness the proliferation of OE techniques accelerated by support from consultants.

OE competition shifts the productivity frontier outward, effectively raising the bar for everyone. But although such competition produces absolute improvement in operational effectiveness, it leads to relative improvement for no one. Consider the \$5 billion-plus U.S. commercial-printing industry. The major players—R.R. Donnelley & Sons Company, Quebecor, World Color Press, and Big Flower Press—are competing head to head, serving all types of customers, offering the same array of printing technologies (gravure and web offset), investing heavily in the same new equipment, running their presses faster, and reducing crew sizes. But the resulting major productivity gains are being captured by customers and equipment suppliers, not retained in superior profitability. Even industry-leader Donnelley's profit margin, consistently higher than 7% in the 1980s, fell to less than 4.6% in 1995. This pattern is playing itself out in industry after industry. Even the Japanese, pioneers of the new competition, suffer from persistently low profits. (See the sidebar "Japanese Companies Rarely Have Strategies.")

The second reason that improved operational effectiveness is insufficient—competitive convergence—is more subtle and insidious. The more benchmarking companies do, the more they look alike. The more that rivals outsource activities to efficient third parties, often the same ones, the more generic those activities become. As rivals imitate one another's improvements in quality, cycle times, or supplier partnerships, strategies converge and competition becomes a series of races down identical paths that no one can win. Competition based on operational effectiveness alone is mutually destructive, leading to wars of attrition that can be arrested only by limiting competition.

The recent wave of industry consolidation through mergers makes sense in the context of OE competition. Driven by performance pressures but lacking strategic vision, company after company has had no better idea than to buy up its rivals. The competitors left standing are often those that outlasted others, not companies with real advantage.

After a decade of impressive gains in operational effectiveness, many

companies are facing diminishing returns. Continuous improvement has been etched on managers' brains. But its tools unwittingly draw companies toward imitation and homogeneity. Gradually, managers have let operational effectiveness supplant strategy. The result is zero-sum competition, static or declining prices, and pressures on costs that compromise companies' ability to invest in the business for the long term.

Japanese Companies Rarely Have Strategies

THE JAPANESE TRIGGERED A GLOBAL revolution in operational effectiveness in the 1970s and 1980s, pioneering practices such as total quality management and continuous improvement. As a result, Japanese manufacturers enjoyed substantial cost and quality advantages for many years.

But Japanese companies rarely developed distinct strategic positions of the kind discussed in this article. Those that did—Sony, Canon, and Sega, for example—were the exception rather than the rule. Most Japanese companies imitate and emulate one another. All rivals offer most if not all product varieties, features, and services; they employ all channels and match one another's plant configurations.

The dangers of Japanese-style competition are now becoming easier to recognize. In the 1980s, with rivals operating far from the productivity frontier, it seemed possible to win on both cost and quality indefinitely. Japanese companies were all able to grow in an expanding domestic economy and by penetrating global markets. They appeared unstoppable. But as the gap in operational effectiveness narrows, Japanese companies are increasingly caught in a trap of their own making. If they are to escape the mutually destructive battles now ravaging their performance, Japanese companies will have to learn strategy.

To do so, they may have to overcome strong cultural barriers. Japan is notoriously consensus oriented, and companies have a strong tendency to mediate differences among individuals rather than accentuate them. Strategy, on the other hand, requires hard choices. The Japanese also have a deeply ingrained service tradition that predisposes them to go to great lengths to satisfy any need a customer expresses. Companies that compete in that way end up blurring their distinct positioning, becoming all things to all customers.

This discussion of Japan is drawn from the author's research with Hirotaka Takeuchi, with help from Mariko Sakakibara.

II. Strategy Rests on Unique Activities

Competitive strategy is about being different. It means deliberately choosing a different set of activities to deliver a unique mix of value.

Southwest Airlines Company, for example, offers short-haul, low-cost, point-to-point service between midsize cities and secondary airports in large cities. Southwest avoids large airports and does not fly great distances. Its customers include business travelers, families, and students. Southwest's frequent departures and low fares attract price-sensitive customers who otherwise would travel by bus or car, and convenience-oriented travelers who would choose a full-service airline on other routes.

Most managers describe strategic positioning in terms of their customers: "Southwest Airlines serves price- and convenience-sensitive travelers," for example. But the essence of strategy is in the activities—choosing to perform activities differently or to perform different activities than rivals. Otherwise, a strategy is nothing more than a marketing slogan that will not withstand competition.

A full-service airline is configured to get passengers from almost any point A to any point B. To reach a large number of destinations and serve passengers with connecting flights, full-service airlines employ a hub-and-spoke system centered on major airports. To attract passengers who desire more comfort, they offer first-class or business-class service. To accommodate passengers who must change planes, they coordinate schedules and check and transfer baggage. Because some passengers will be traveling for many hours, full-service airlines serve meals.

Southwest, in contrast, tailors all its activities to deliver low-cost, convenient service on its particular type of route. Through fast turnarounds at the gate of only 15 minutes, Southwest is able to keep planes flying longer hours than rivals and provide frequent departures with fewer aircraft. Southwest does not offer meals, assigned seats, interline baggage checking, or premium classes of service. Automated ticketing at the gate encourages customers to bypass travel agents, allowing Southwest to avoid their commissions. A standardized fleet of 737 aircraft boosts the efficiency of maintenance.

Southwest has staked out a unique and valuable strategic position based on a tailored set of activities. On the routes served by Southwest, a full-service airline could never be as convenient or as low cost.

Ikea, the global furniture retailer based in Sweden, also has a clear strategic positioning. Ikea targets young furniture buyers who want style at low cost. What turns this marketing concept into a strategic positioning is the tailored set of activities that make it work. Like Southwest, Ikea has chosen to perform activities differently from its rivals.

Finding New Positions: The Entrepreneurial Edge

STRATEGIC COMPETITION CAN BE THOUGHT of as the process of perceiving new positions that woo customers from established positions or draw new customers into the market. For example, superstores offering depth of merchandise in a single product category take market share from broad-line department stores offering a more limited selection in many categories. Mail-order catalogs pick off customers who crave convenience. In principle, incumbents and entrepreneurs face the same challenges in finding new strategic positions. In practice, new entrants often have the edge.

Strategic positionings are often not obvious, and finding them requires creativity and insight. New entrants often discover unique positions that have been available but simply overlooked by established competitors. Ikea, for example, recognized a customer group that had been ignored or served poorly. Circuit City Stores' entry into used cars, CarMax, is based on a new way of performing activities—extensive refurbishing of cars, product guarantees, no-haggle pricing, sophisticated use of in-house customer financing—that has long been open to incumbents.

New entrants can prosper by occupying a position that a competitor once held but has ceded through years of imitation and straddling. And entrants coming from other industries can create new positions because of distinctive activities drawn from their other businesses. CarMax borrows heavily from Circuit City's expertise in inventory management, credit, and other activities in consumer electronics retailing.

Most commonly, however, new positions open up because of change. New customer groups or purchase occasions arise; new needs emerge as societies evolve; new distribution channels appear; new technologies are developed; new machinery or information systems become available. When such changes happen, new entrants, unencumbered by a long history in the industry, can often more easily perceive the potential for a

new way of competing. Unlike incumbents, newcomers can be more flexible because they face no trade-offs with their existing activities.

Consider the typical furniture store. Showrooms display samples of the merchandise. One area might contain 25 sofas; another will display five dining tables. But those items represent only a fraction of the choices available to customers. Dozens of books displaying fabric swatches or wood samples or alternate styles offer customers thousands of product varieties to choose from. Salespeople often escort customers through the store, answering questions and helping them navigate this maze of choices. Once a customer makes a selection, the order is relayed to a third-party manufacturer. With luck, the furniture will be delivered to the customer's home within six to eight weeks. This is a value chain that maximizes customization and service but does so at high cost.

In contrast, Ikea serves customers who are happy to trade off service for cost. Instead of having a sales associate trail customers around the store, Ikea uses a self-service model based on clear, in-store displays. Rather than rely solely on third-party manufacturers, Ikea designs its own low-cost, modular, ready-to-assemble furniture to fit its positioning. In huge stores, Ikea displays every product it sells in room-like settings, so customers don't need a decorator to help them imagine how to put the pieces together. Adjacent to the furnished showrooms is a warehouse section with the products in boxes on pallets. Customers are expected to do their own pickup and delivery, and Ikea will even sell you a roof rack for your car that you can return for a refund on your next visit.

Although much of its low-cost position comes from having customers "do it themselves," Ikea offers a number of extra services that its competitors do not. In-store child care is one. Extended hours are another. Those services are uniquely aligned with the needs of its customers, who are young, not wealthy, likely to have children (but no nanny), and, because they work for a living, have a need to shop at odd hours.

The origins of strategic positions

Strategic positions emerge from three distinct sources, which are not mutually exclusive and often overlap. First, positioning can be based on producing a subset of an industry's products or services. I call this *variety-based positioning* because it is based on the choice of product or service varieties rather than customer segments. Variety-based positioning makes economic sense when a company can best produce particular products or services using distinctive sets of activities.

Jiffy Lube International, for instance, specializes in automotive lubricants and does not offer other car repair or maintenance services. Its value chain produces faster service at a lower cost than broader line repair shops, a combination so attractive that many customers subdivide their purchases, buying oil changes from the focused competitor, Jiffy Lube, and going to rivals for other services.

The Vanguard Group, a leader in the mutual fund industry, is another example of variety-based positioning. Vanguard provides an array of common stock, bond, and money market funds that offer predictable performance and rock-bottom expenses. The company's investment approach deliberately sacrifices the possibility of extraordinary performance in any one year for good relative performance in every year. Vanguard is known, for example, for its index funds. It avoids making bets on interest rates and steers clear of narrow stock groups. Fund managers keep trading levels low, which holds expenses down; in addition, the company discourages customers from rapid buying and selling because doing so drives up costs and can force a fund manager to trade in order to deploy new capital and raise cash for redemptions. Vanguard also takes a consistent low-cost approach to managing distribution, customer service, and marketing. Many investors include one or more Vanguard funds in their portfolio, while buying aggressively managed or specialized funds from competitors.

The people who use Vanguard or Jiffy Lube are responding to a superior value chain for a particular type of service. A variety-based positioning can serve a wide array of customers, but for most it will meet only a subset of their needs.

A second basis for positioning is that of serving most or all the needs of a particular group of customers. I call this *needs-based positioning*, which comes closer to traditional thinking about targeting a segment of customers. It arises when there are groups of customers with differing needs, and when a tailored set of activities can serve those needs best. Some groups of customers are more price sensitive than others, demand different product features, and need varying amounts of information, support, and services. Ikea's customers are a good example of such a group. Ikea seeks to meet all the home furnishing needs of its target customers, not just a subset of them.

The Connection with Generic Strategies

IN *COMPETITIVE STRATEGY* (The Free Press, 1985), I introduced the concept of generic strategies—cost leadership, differentiation, and focus—to represent the alternative strategic positions in an industry. The generic strategies remain useful to characterize strategic positions at the simplest and broadest level. Vanguard, for instance, is an example of a cost leadership strategy, whereas Ikea, with its narrow customer group, is an example of cost-based focus. Neutrogena is a focused differentiator. The bases for positioning—varieties, needs, and access—carry the understanding of those generic strategies to a greater level of specificity. Ikea and Southwest are both cost-based focusers, for example, but Ikea's focus is based on the needs of a customer group, and Southwest's is based on offering a particular service variety.

The generic strategies framework introduced the need to choose in order to avoid becoming caught between what I then described as the inherent contradictions of different strategies. Trade-offs between the activities of incompatible positions explain those contradictions. Witness Continental Lite, which tried and failed to compete in two ways at once.

A variant of needs-based positioning arises when the same customer has different needs on different occasions or for different types of transactions. The same person, for example, may have different needs when traveling on business than when traveling for pleasure with the family. Buyers of cans—beverage companies, for example—will likely have different needs from their primary supplier than from their secondary source.

It is intuitive for most managers to conceive of their business in terms of the customers' needs they are meeting. But a critical element of needs-based positioning is not at all intuitive and is often overlooked. Differences in needs will not translate into meaningful positions unless the best set of activities to satisfy them *also* differs. If that were not the case, every competitor could meet those same needs, and there would be nothing unique or valuable about

the positioning.

In private banking, for example, Bessemer Trust Company targets families with a minimum of \$5 million in investable assets who want capital preservation combined with wealth accumulation. By assigning one sophisticated account officer for every 14 families, Bessemer has configured its activities for personalized service. Meetings, for example, are more likely to be held at a client's ranch or yacht than in the office. Bessemer offers a wide array of customized services, including investment management and estate administration, oversight of oil and gas investments, and accounting for racehorses and aircraft. Loans, a staple of most private banks, are rarely needed by Bessemer's clients and make up a tiny fraction of its client balances and income. Despite the most generous compensation of account officers and the highest personnel cost as a percentage of operating expenses, Bessemer's differentiation with its target families produces a return on equity estimated to be the highest of any private banking competitor.

Citibank's private bank, on the other hand, serves clients with minimum assets of about \$250,000 who, in contrast to Bessemer's clients, want convenient access to loans—from jumbo mortgages to deal financing. Citibank's account managers are primarily lenders. When clients need other services, their account manager refers them to other Citibank specialists, each of whom handles prepackaged products. Citibank's system is less customized than Bessemer's and allows it to have a lower manager-to-client ratio of 1:125. Biannual office meetings are offered only for the largest clients. Both Bessemer and Citibank have tailored their activities to meet the needs of a different group of private banking customers. The same value chain cannot profitably meet the needs of both groups.

The third basis for positioning is that of segmenting customers who are accessible in different ways. Although their needs are similar to those of other customers, the best configuration of activities to reach them is different. I call this *access-based positioning*. Access can be a function of customer geography or customer scale—or of anything that requires a different set of activities to reach customers in the best way.

Segmenting by access is less common and less well understood than the other two bases. Carmike Cinemas, for example, operates movie theaters exclusively in cities and towns with populations under 200,000. How does Carmike make money in markets that are not only small but also won't support big-city ticket prices? It does so through a set of activities that result

in a lean cost structure. Carmike's small-town customers can be served through standardized, low-cost theater complexes requiring fewer screens and less sophisticated projection technology than big-city theaters. The company's proprietary information system and management process eliminate the need for local administrative staff beyond a single theater manager. Carmike also reaps advantages from centralized purchasing, lower rent and payroll costs (because of its locations), and rock-bottom corporate overhead of 2% (the industry average is 5%). Operating in small communities also allows Carmike to practice a highly personal form of marketing in which the theater manager knows patrons and promotes attendance through personal contacts. By being the dominant if not the only theater in its markets—the main competition is often the high school football team—Carmike is also able to get its pick of films and negotiate better terms with distributors.

Rural versus urban-based customers are one example of access driving differences in activities. Serving small rather than large customers or densely rather than sparsely situated customers are other examples in which the best way to configure marketing, order processing, logistics, and after-sale service activities to meet the similar needs of distinct groups will often differ.

Positioning is not only about carving out a niche. A position emerging from any of the sources can be broad or narrow. A focused competitor, such as Ikea, targets the special needs of a subset of customers and designs its activities accordingly. Focused competitors thrive on groups of customers who are overserved (and hence overpriced) by more broadly targeted competitors, or underserved (and hence underpriced). A broadly targeted competitor—for example, Vanguard or Delta Air Lines—serves a wide array of customers, performing a set of activities designed to meet their common needs. It ignores or meets only partially the more idiosyncratic needs of particular customer groups.

Whatever the basis—variety, needs, access, or some combination of the three—positioning requires a tailored set of activities because it is always a function of differences on the supply side; that is, of differences in activities. However, positioning is not always a function of differences on the demand, or customer, side. Variety and access positionings, in particular, do not rely on *any* customer differences. In practice, however, variety or access differences often accompany needs differences. The tastes—that is, the needs—of Carmike's small-town customers, for instance, run more toward

comedies, Westerns, action films, and family entertainment. Carmike does not run any films rated NC-17.

Having defined positioning, we can now begin to answer the question, “What is strategy?” Strategy is the creation of a unique and valuable position, involving a different set of activities. If there were only one ideal position, there would be no need for strategy. Companies would face a simple imperative—win the race to discover and preempt it. The essence of strategic positioning is to choose activities that are different from rivals’. If the same set of activities were best to produce all varieties, meet all needs, and access all customers, companies could easily shift among them and operational effectiveness would determine performance.

III. A Sustainable Strategic Position Requires Trade-offs

Choosing a unique position, however, is not enough to guarantee a sustainable advantage. A valuable position will attract imitation by incumbents, who are likely to copy it in one of two ways.

First, a competitor can reposition itself to match the superior performer. J.C. Penney, for instance, has been repositioning itself from a Sears clone to a more upscale, fashion-oriented, soft-goods retailer. A second and far more common type of imitation is straddling. The straddler seeks to match the benefits of a successful position while maintaining its existing position. It grafts new features, services, or technologies onto the activities it already performs.

For those who argue that competitors can copy any market position, the airline industry is a perfect test case. It would seem that nearly any competitor could imitate any other airline's activities. Any airline can buy the same planes, lease the gates, and match the menus and ticketing and baggage handling services offered by other airlines.

Continental Airlines saw how well Southwest was doing and decided to straddle. While maintaining its position as a full-service airline, Continental also set out to match Southwest on a number of point-to-point routes. The airline dubbed the new service Continental Lite. It eliminated meals and first-class service, increased departure frequency, lowered fares, and shortened turnaround time at the gate. Because Continental remained a full-service airline on other routes, it continued to use travel agents and its mixed fleet of planes and to provide baggage checking and seat assignments.

But a strategic position is not sustainable unless there are trade-offs with other positions. Trade-offs occur when activities are incompatible. Simply put, a trade-off means that more of one thing necessitates less of another. An airline can choose to serve meals—adding cost and slowing turnaround time at the gate—or it can choose not to, but it cannot do both without bearing major inefficiencies.

Trade-offs create the need for choice and protect against repositioners and straddlers. Consider Neutrogena soap. Neutrogena Corporation's variety-based positioning is built on a "kind to the skin," residue-free soap formulated for pH balance. With a large detail force calling on dermatologists, Neutrogena's marketing strategy looks more like a drug company's than a soap maker's. It advertises in medical journals, sends direct mail to doctors, attends medical conferences, and performs research at its own Skincare Institute. To reinforce its positioning, Neutrogena originally focused its distribution on drugstores and avoided price promotions. Neutrogena uses a slow, more expensive manufacturing process to mold its fragile soap.

In choosing this position, Neutrogena said no to the deodorants and skin softeners that many customers desire in their soap. It gave up the large-volume potential of selling through supermarkets and using price promotions. It sacrificed manufacturing efficiencies to achieve the soap's desired attributes. In its original positioning, Neutrogena made a whole raft of trade-offs like those, trade-offs that protected the company from imitators.

Trade-offs arise for three reasons. The first is inconsistencies in image or reputation. A company known for delivering one kind of value may lack credibility and confuse customers—or even undermine its reputation—if it delivers another kind of value or attempts to deliver two inconsistent things at the same time. For example, Ivory soap, with its position as a basic, inexpensive everyday soap, would have a hard time reshaping its image to match Neutrogena's premium "medical" reputation. Efforts to create a new image typically cost tens or even hundreds of millions of dollars in a major industry—a powerful barrier to imitation.

Second, and more important, trade-offs arise from activities themselves. Different positions (with their tailored activities) require different product configurations, different equipment, different employee behavior, different skills, and different management systems. Many trade-offs reflect inflexibilities in machinery, people, or systems. The more Ikea has configured its activities to lower costs by having its customers do their own assembly and delivery, the less able it is to satisfy customers who require higher levels of service.

However, trade-offs can be even more basic. In general, value is destroyed if an activity is overdesigned or underdesigned for its use. For example, even if a given salesperson were capable of providing a high level

of assistance to one customer and none to another, the salesperson's talent (and some of his or her cost) would be wasted on the second customer. Moreover, productivity can improve when variation of an activity is limited. By providing a high level of assistance all the time, the salesperson and the entire sales activity can often achieve efficiencies of learning and scale.

Finally, trade-offs arise from limits on internal coordination and control. By clearly choosing to compete in one way and not another, senior management makes organizational priorities clear. Companies that try to be all things to all customers, in contrast, risk confusion in the trenches as employees attempt to make day-to-day operating decisions without a clear framework.

Positioning trade-offs are pervasive in competition and essential to strategy. They create the need for choice and purposefully limit what a company offers. They deter straddling or repositioning, because competitors that engage in those approaches undermine their strategies and degrade the value of their existing activities.

Trade-offs ultimately grounded Continental Lite. The airline lost hundreds of millions of dollars, and the CEO lost his job. Its planes were delayed leaving congested hub cities or slowed at the gate by baggage transfers. Late flights and cancellations generated a thousand complaints a day. Continental Lite could not afford to compete on price and still pay standard travel-agent commissions, but neither could it do without agents for its full-service business. The airline compromised by cutting commissions for all Continental flights across the board. Similarly, it could not afford to offer the same frequent-flier benefits to travelers paying the much lower ticket prices for Lite service. It compromised again by lowering the rewards of Continental's entire frequent-flier program. The results: angry travel agents and full-service customers.

Continental tried to compete in two ways at once. In trying to be low cost on some routes and full service on others, Continental paid an enormous straddling penalty. If there were no trade-offs between the two positions, Continental could have succeeded. But the absence of trade-offs is a dangerous half-truth that managers must unlearn. Quality is not always free. Southwest's convenience, one kind of high quality, happens to be consistent with low costs because its frequent departures are facilitated by a number of low-cost practices—fast gate turnarounds and automated ticketing, for example. However, other dimensions of airline quality—an assigned seat, a

meal, or baggage transfer—require costs to provide.

In general, false trade-offs between cost and quality occur primarily when there is redundant or wasted effort, poor control or accuracy, or weak coordination. Simultaneous improvement of cost and differentiation is possible only when a company begins far behind the productivity frontier or when the frontier shifts outward. At the frontier, where companies have achieved current best practice, the trade-off between cost and differentiation is very real indeed.

After a decade of enjoying productivity advantages, Honda Motor Company and Toyota Motor Corporation recently bumped up against the frontier. In 1995, faced with increasing customer resistance to higher automobile prices, Honda found that the only way to produce a less-expensive car was to skimp on features. In the United States, it replaced the rear disk brakes on the Civic with lower-cost drum brakes and used cheaper fabric for the back seat, hoping customers would not notice. Toyota tried to sell a version of its best-selling Corolla in Japan with unpainted bumpers and cheaper seats. In Toyota's case, customers rebelled, and the company quickly dropped the new model.

For the past decade, as managers have improved operational effectiveness greatly, they have internalized the idea that eliminating trade-offs is a good thing. But if there are no trade-offs companies will never achieve a sustainable advantage. They will have to run faster and faster just to stay in place.

As we return to the question, What is strategy? we see that trade-offs add a new dimension to the answer. Strategy is making trade-offs in competing. The essence of strategy is choosing what *not* to do. Without trade-offs, there would be no need for choice and thus no need for strategy. Any good idea could and would be quickly imitated. Again, performance would once again depend wholly on operational effectiveness.

IV. Fit Drives Both Competitive Advantage and Sustainability

Positioning choices determine not only which activities a company will perform and how it will configure individual activities but also how activities relate to one another. While operational effectiveness is about achieving excellence in individual activities, or functions, strategy is about *combining* activities.

Southwest's rapid gate turnaround, which allows frequent departures and greater use of aircraft, is essential to its high-convenience, low-cost positioning. But how does Southwest achieve it? Part of the answer lies in the company's well-paid gate and ground crews, whose productivity in turnarounds is enhanced by flexible union rules. But the bigger part of the answer lies in how Southwest performs other activities. With no meals, no seat assignment, and no interline baggage transfers, Southwest avoids having to perform activities that slow down other airlines. It selects airports and routes to avoid congestion that introduces delays. Southwest's strict limits on the type and length of routes make standardized aircraft possible: every aircraft Southwest turns is a Boeing 737.

What is Southwest's core competence? Its key success factors? The correct answer is that everything matters. Southwest's strategy involves a whole system of activities, not a collection of parts. Its competitive advantage comes from the way its activities fit and reinforce one another.

Fit locks out imitators by creating a chain that is as strong as its *strongest* link. As in most companies with good strategies, Southwest's activities complement one another in ways that create real economic value. One activity's cost, for example, is lowered because of the way other activities are performed. Similarly, one activity's value to customers can be enhanced by a company's other activities. That is the way strategic fit creates competitive advantage and superior profitability.

Types of fit

The importance of fit among functional policies is one of the oldest ideas in strategy. Gradually, however, it has been supplanted on the management agenda. Rather than seeing the company as a whole, managers have turned to “core” competencies, “critical” resources, and “key” success factors. In fact, fit is a far more central component of competitive advantage than most realize.

Fit is important because discrete activities often affect one another. A sophisticated sales force, for example, confers a greater advantage when the company’s product embodies premium technology and its marketing approach emphasizes customer assistance and support. A production line with high levels of model variety is more valuable when combined with an inventory and order processing system that minimizes the need for stocking finished goods, a sales process equipped to explain and encourage customization, and an advertising theme that stresses the benefits of product variations that meet a customer’s special needs. Such complementarities are pervasive in strategy. Although some fit among activities is generic and applies to many companies, the most valuable fit is strategy-specific because it enhances a position’s uniqueness and amplifies trade-offs.²

There are three types of fit, although they are not mutually exclusive. First-order fit is *simple consistency* between each activity (function) and the overall strategy. Vanguard, for example, aligns all activities with its low-cost strategy. It minimizes portfolio turnover and does not need highly compensated money managers. The company distributes its funds directly, avoiding commissions to brokers. It also limits advertising, relying instead on public relations and word-of-mouth recommendations. Vanguard ties its employees’ bonuses to cost savings.

Consistency ensures that the competitive advantages of activities cumulate and do not erode or cancel themselves out. It makes the strategy easier to communicate to customers, employees, and shareholders, and improves implementation through single-mindedness in the corporation.

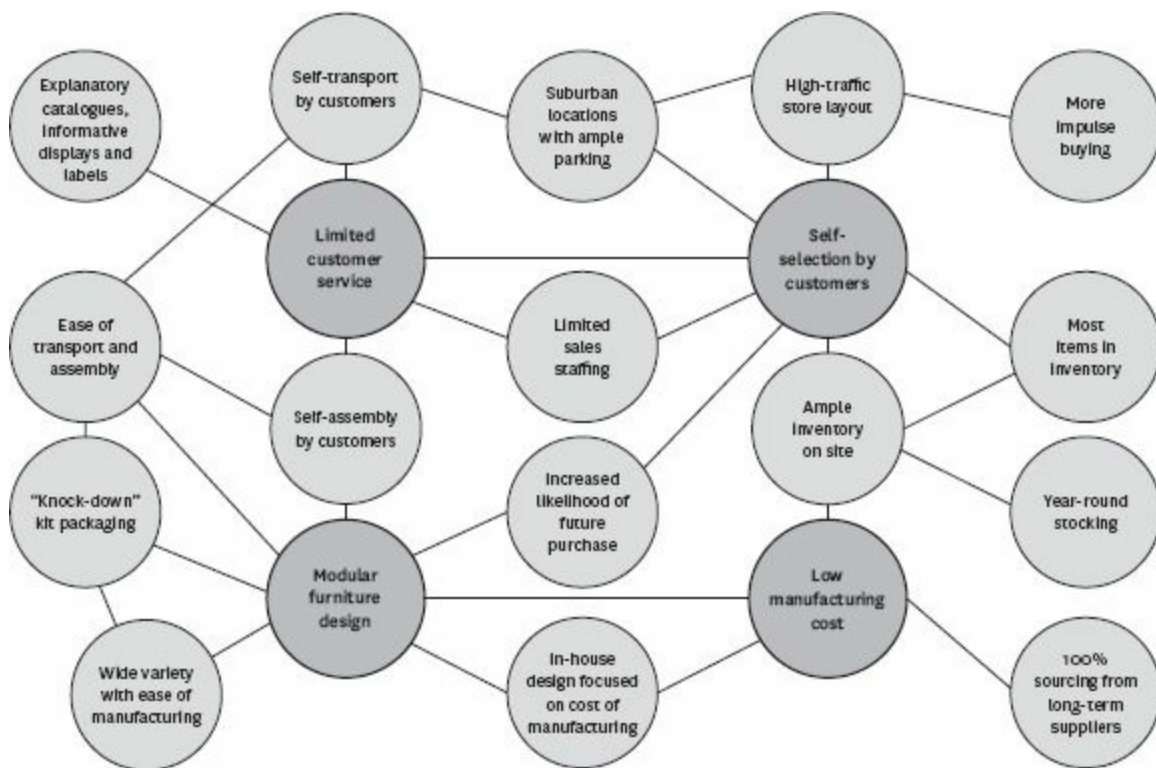
Second-order fit occurs when *activities are reinforcing*. Neutrogena, for example, markets to upscale hotels eager to offer their guests a soap

recommended by dermatologists. Hotels grant Neutrogena the privilege of using its customary packaging while requiring other soaps to feature the hotel's name. Once guests have tried Neutrogena in a luxury hotel, they are more likely to purchase it at the drugstore or ask their doctor about it. Thus Neutrogena's medical and hotel marketing activities reinforce one another, lowering total marketing costs.

In another example, Bic Corporation sells a narrow line of standard, low-priced pens to virtually all major customer markets (retail, commercial, promotional, and giveaway) through virtually all available channels. As with any variety-based positioning serving a broad group of customers, Bic emphasizes a common need (low price for an acceptable pen) and uses marketing approaches with a broad reach (a large sales force and heavy television advertising). Bic gains the benefits of consistency across nearly all activities, including product design that emphasizes ease of manufacturing, plants configured for low cost, aggressive purchasing to minimize material costs, and in-house parts production whenever the economics dictate.

Mapping activity systems

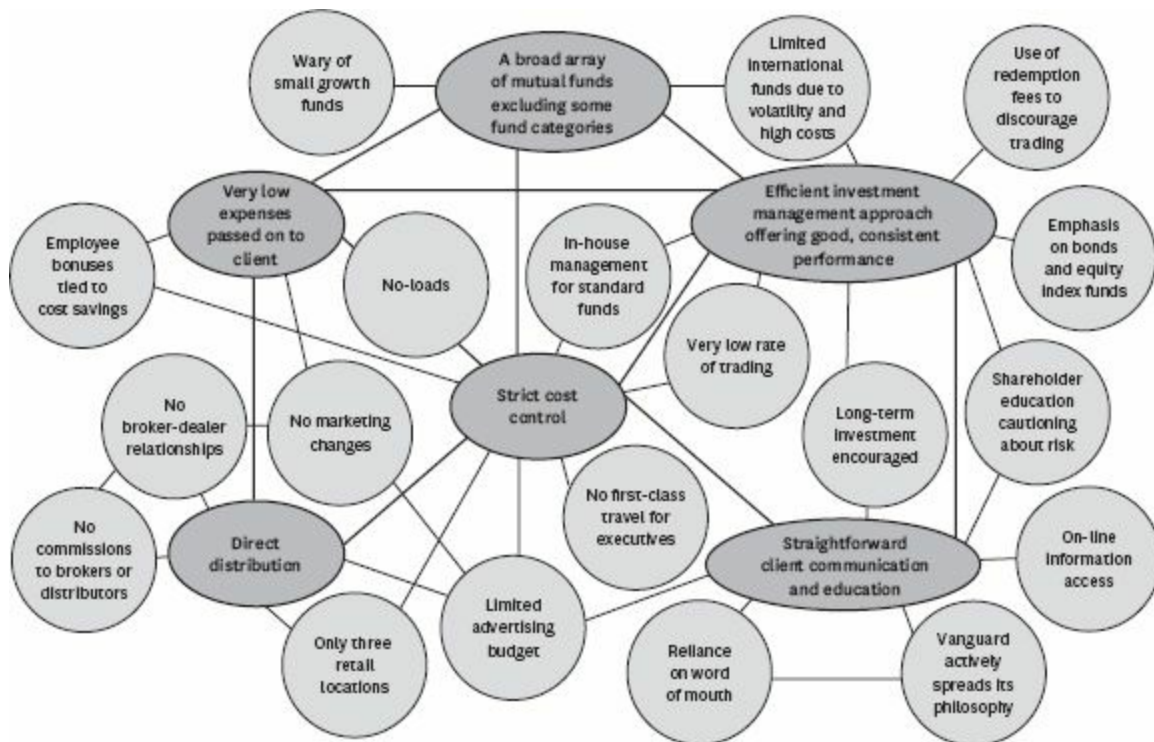
Activity-system maps, such as this one for Ikea, show how a company's strategic position is contained in a set of tailored activities designed to deliver it. In companies with a clear strategic position, a number of higher-order strategic themes (in dark grey) can be identified and implemented through clusters of tightly linked activities (in light grey).



Yet Bic goes beyond simple consistency because its activities are reinforcing. For example, the company uses point-of-sale displays and frequent packaging changes to stimulate impulse buying. To handle point-of-sale tasks, a company needs a large sales force. Bic's is the largest in its industry, and it handles point-of-sale activities better than its rivals do. Moreover, the combination of point-of-sale activity, heavy television advertising, and packaging changes yields far more impulse buying than any activity in isolation could.

Vanguard's activity system

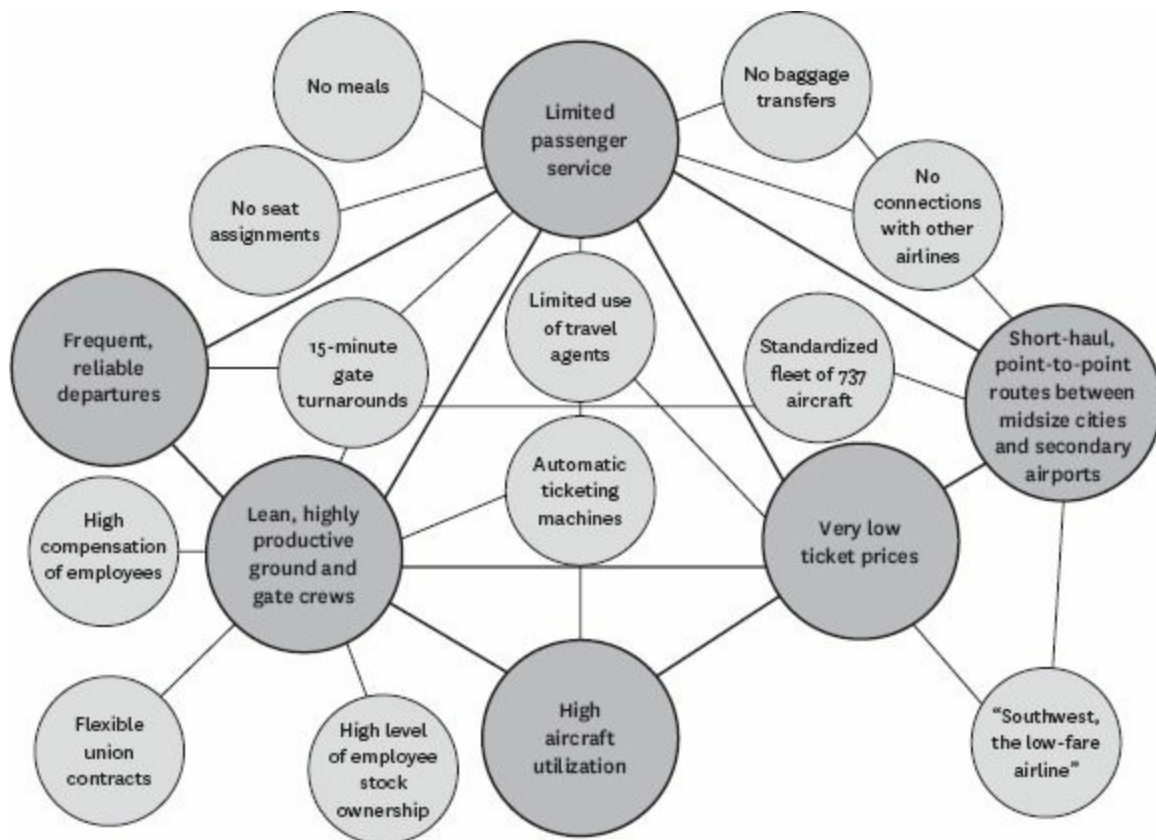
Activity-system maps can be useful for examining and strengthening strategic fit. A set of basic questions should guide the process. First, is each activity consistent with the overall positioning—the varieties produced, the needs served, and the type of customers accessed? Ask those responsible for each activity to identify how other activities within the company improve or detract from their performance. Second, are there ways to strengthen how activities and groups of activities reinforce one another? Finally, could changes in one activity eliminate the need to perform others?



Third-order fit goes beyond activity reinforcement to what I call *optimization of effort*. The Gap, a retailer of casual clothes, considers product availability in its stores a critical element of its strategy. The Gap could keep products either by holding store inventory or by restocking from warehouses. The Gap has optimized its effort across these activities by restocking its

selection of basic clothing almost daily out of three warehouses, thereby minimizing the need to carry large in-store inventories. The emphasis is on restocking because the Gap's merchandising strategy sticks to basic items in relatively few colors. While comparable retailers achieve turns of three to four times per year, the Gap turns its inventory seven and a half times per year. Rapid restocking, moreover, reduces the cost of implementing the Gap's short model cycle, which is six to eight weeks long.³

Southwest Airlines' activity system



Coordination and information exchange across activities to eliminate redundancy and minimize wasted effort are the most basic types of effort optimization. But there are higher levels as well. Product design choices, for example, can eliminate the need for after-sale service or make it possible for customers to perform service activities themselves. Similarly, coordination with suppliers or distribution channels can eliminate the need for some in-house activities, such as end-user training.

In all three types of fit, the whole matters more than any individual part. Competitive advantage grows out of the *entire system* of activities. The fit among activities substantially reduces cost or increases differentiation. Beyond that, the competitive value of individual activities—or the associated

skills, competencies, or resources—cannot be decoupled from the system or the strategy. Thus in competitive companies it can be misleading to explain success by specifying individual strengths, core competencies, or critical resources. The list of strengths cuts across many functions, and one strength blends into others. It is more useful to think in terms of themes that pervade many activities, such as low cost, a particular notion of customer service, or a particular conception of the value delivered. These themes are embodied in nests of tightly linked activities.

Fit and sustainability

Strategic fit among many activities is fundamental not only to competitive advantage but also to the sustainability of that advantage. It is harder for a rival to match an array of interlocked activities than it is merely to imitate a particular sales-force approach, match a process technology, or replicate a set of product features. Positions built on systems of activities are far more sustainable than those built on individual activities.

Consider this simple exercise. The probability that competitors can match any activity is often less than one. The probabilities then quickly compound to make matching the entire system highly unlikely ($.9 \times .9 = .81$; $.9 \times .9 \times .9 \times .9 = .66$, and so on). Existing companies that try to reposition or straddle will be forced to reconfigure many activities. And even new entrants, though they do not confront the trade-offs facing established rivals, still face formidable barriers to imitation.

The more a company's positioning rests on activity systems with second- and third-order fit, the more sustainable its advantage will be. Such systems, by their very nature, are usually difficult to untangle from outside the company and therefore hard to imitate. And even if rivals can identify the relevant interconnections, they will have difficulty replicating them. Achieving fit is difficult because it requires the integration of decisions and actions across many independent subunits.

A competitor seeking to match an activity system gains little by imitating only some activities and not matching the whole. Performance does not improve; it can decline. Recall Continental Lite's disastrous attempt to imitate Southwest.

Finally, fit among a company's activities creates pressures and incentives to improve operational effectiveness, which makes imitation even harder. Fit means that poor performance in one activity will degrade the performance in others, so that weaknesses are exposed and more prone to get attention. Conversely, improvements in one activity will pay dividends in others. Companies with strong fit among their activities are rarely inviting targets. Their superiority in strategy and in execution only compounds their advantages and raises the hurdle for imitators.

When activities complement one another, rivals will get little benefit from imitation unless they successfully match the whole system. Such situations tend to promote winner-take-all competition. The company that builds the best activity system—Toys R Us, for instance—wins, while rivals with similar strategies—Child World and Lionel Leisure—fall behind. Thus finding a new strategic position is often preferable to being the second or third imitator of an occupied position.

The most viable positions are those whose activity systems are incompatible because of tradeoffs. Strategic positioning sets the trade-off rules that define how individual activities will be configured and integrated. Seeing strategy in terms of activity systems only makes it clearer why organizational structure, systems, and processes need to be strategy-specific. Tailoring organization to strategy, in turn, makes complementarities more achievable and contributes to sustainability.

One implication is that strategic positions should have a horizon of a decade or more, not of a single planning cycle. Continuity fosters improvements in individual activities and the fit across activities, allowing an organization to build unique capabilities and skills tailored to its strategy. Continuity also reinforces a company's identity.

Conversely, frequent shifts in positioning are costly. Not only must a company reconfigure individual activities, but it must also realign entire systems. Some activities may never catch up to the vacillating strategy. The inevitable result of frequent shifts in strategy, or of failure to choose a distinct position in the first place, is “me-too” or hedged activity configurations, inconsistencies across functions, and organizational dissonance.

What is strategy? We can now complete the answer to this question. Strategy is creating fit among a company's activities. The success of a strategy depends on doing many things well—not just a few—and integrating among them. If there is no fit among activities, there is no distinctive strategy and little sustainability. Management reverts to the simpler task of overseeing independent functions, and operational effectiveness determines an organization's relative performance.

V. Rediscovering Strategy

The failure to choose

Why do so many companies fail to have a strategy? Why do managers avoid making strategic choices? Or, having made them in the past, why do managers so often let strategies decay and blur?

Commonly, the threats to strategy are seen to emanate from outside a company because of changes in technology or the behavior of competitors. Although external changes can be the problem, the greater threat to strategy often comes from within. A sound strategy is undermined by a misguided view of competition, by organizational failures, and, especially, by the desire to grow.

Managers have become confused about the necessity of making choices. When many companies operate far from the productivity frontier, trade-offs appear unnecessary. It can seem that a well-run company should be able to beat its ineffective rivals on all dimensions simultaneously. Taught by popular management thinkers that they do not have to make trade-offs, managers have acquired a macho sense that to do so is a sign of weakness.

Unnerved by forecasts of hypercompetition, managers increase its likelihood by imitating everything about their competitors. Exhorted to think in terms of revolution, managers chase every new technology for its own sake.

Alternative Views of Strategy

The Implicit Strategy Model of the Past Decade

- One ideal competitive position in the industry
- Benchmarking of all activities and achieving best practice
- Aggressive outsourcing and partnering to gain efficiencies
- Advantages rest on a few key success factors, critical resources, core competencies
- Flexibility and rapid responses to all competitive and market changes

Sustainable Competitive Advantage

- Unique competitive position for the company
- Activities tailored to strategy
- Clear trade-offs and choices vis-à-vis competitors
- Competitive advantage arises from fit across activities
- Sustainability comes from the activity system, not the parts
- Operational effectiveness a given

The pursuit of operational effectiveness is seductive because it is concrete and actionable. Over the past decade, managers have been under increasing pressure to deliver tangible, measurable performance improvements. Programs in operational effectiveness produce reassuring progress, although superior profitability may remain elusive. Business publications and consultants flood the market with information about what other companies are doing, reinforcing the best-practice mentality. Caught up in the race for operational effectiveness, many managers simply do not understand the need to have a strategy.

Companies avoid or blur strategic choices for other reasons as well. Conventional wisdom within an industry is often strong, homogenizing competition. Some managers mistake “customer focus” to mean they must serve all customer needs or respond to every request from distribution channels. Others cite the desire to preserve flexibility.

Reconnecting with Strategy

MOST COMPANIES OWE THEIR INITIAL success to a unique strategic position involving clear trade-offs. Activities once were aligned with that position. The passage of time and the pressures of growth, however, led to compromises that were, at first, almost imperceptible. Through a succession of incremental changes that each seemed sensible at the time, many established companies have compromised their way to homogeneity with their rivals.

The issue here is not with the companies whose historical position is no longer viable; their challenge is to start over, just as a new entrant would. At issue is a far more common phenomenon: the established company achieving mediocre returns and lacking a clear strategy. Through incremental additions of product varieties, incremental efforts to serve new customer groups, and emulation of rivals' activities, the existing company loses its clear competitive position. Typically, the company has matched many of its competitors' offerings and practices and attempts to sell to most customer groups.

A number of approaches can help a company reconnect with strategy. The first is a careful look at what it already does. Within most well-established companies is a core of uniqueness. It is identified by answering questions such as the following:

- Which of our product or service varieties are the most distinctive?
- Which of our product or service varieties are the most profitable?
- Which of our customers are the most satisfied?

- Which customers, channels, or purchase occasions are the most profitable?
- Which of the activities in our value chain are the most different and effective?

Around this core of uniqueness are encrustations added incrementally over time. Like barnacles, they must be removed to reveal the underlying strategic positioning. A small percentage of varieties or customers may well account for most of a company's sales and especially its profits. The challenge, then, is to refocus on the unique core and realign the company's activities with it. Customers and product varieties at the periphery can be sold or allowed through inattention or price increases to fade away.

A company's history can also be instructive. What was the vision of the founder? What were the products and customers that made the company? Looking backward, one can reexamine the original strategy to see if it is still valid. Can the historical positioning be implemented in a modern way, one consistent with today's technologies and practices? This sort of thinking may lead to a commitment to renew the strategy and may challenge the organization to recover its distinctiveness. Such a challenge can be galvanizing and can instill the confidence to make the needed trade-offs.

Organizational realities also work against strategy. Trade-offs are frightening, and making no choice is sometimes preferred to risking blame for a bad choice. Companies imitate one another in a type of herd behavior, each assuming rivals know something they do not. Newly empowered employees, who are urged to seek every possible source of improvement, often lack a vision of the whole and the perspective to recognize trade-offs. The failure to choose sometimes comes down to the reluctance to disappoint valued managers or employees.

The growth trap

Among all other influences, the desire to grow has perhaps the most perverse effect on strategy. Trade-offs and limits appear to constrain growth. Serving one group of customers and excluding others, for instance, places a real or imagined limit on revenue growth. Broadly targeted strategies emphasizing low price result in lost sales with customers sensitive to features or service. Differentiators lose sales to price-sensitive customers.

Managers are constantly tempted to take incremental steps that surpass those limits but blur a company's strategic position. Eventually, pressures to grow or apparent saturation of the target market lead managers to broaden the position by extending product lines, adding new features, imitating competitors' popular services, matching processes, and even making acquisitions. For years, Maytag Corporation's success was based on its focus on reliable, durable washers and dryers, later extended to include dishwashers. However, conventional wisdom emerging within the industry supported the notion of selling a full line of products. Concerned with slow industry growth and competition from broad-line appliance makers, Maytag was pressured by dealers and encouraged by customers to extend its line. Maytag expanded into refrigerators and cooking products under the Maytag brand and acquired other brands—Jenn-Air, Hardwick Stove, Hoover, Admiral, and Magic Chef—with disparate positions. Maytag has grown substantially from \$684 million in 1985 to a peak of \$3.4 billion in 1994, but return on sales has declined from 8% to 12% in the 1970s and 1980s to an average of less than 1% between 1989 and 1995. Cost cutting will improve this performance, but laundry and dishwasher products still anchor Maytag's profitability.

Neutrogena may have fallen into the same trap. In the early 1990s, its U.S. distribution broadened to include mass merchandisers such as Wal-Mart Stores. Under the Neutrogena name, the company expanded into a wide variety of products—eye-makeup remover and shampoo, for example—in which it was not unique and which diluted its image, and it began turning to price promotions.

Compromises and inconsistencies in the pursuit of growth will erode the

competitive advantage a company had with its original varieties or target customers. Attempts to compete in several ways at once create confusion and undermine organizational motivation and focus. Profits fall, but more revenue is seen as the answer. Managers are unable to make choices, so the company embarks on a new round of broadening and compromises. Often, rivals continue to match each other until desperation breaks the cycle, resulting in a merger or downsizing to the original positioning.

Profitable growth

Many companies, after a decade of restructuring and cost-cutting, are turning their attention to growth. Too often, efforts to grow blur uniqueness, create compromises, reduce fit, and ultimately undermine competitive advantage. In fact, the growth imperative is hazardous to strategy.

Emerging Industries and Technologies

DEVELOPING A STRATEGY IN A newly emerging industry or in a business undergoing revolutionary technological changes is a daunting proposition. In such cases, managers face a high level of uncertainty about the needs of customers, the products and services that will prove to be the most desired, and the best configuration of activities and technologies to deliver them. Because of all this uncertainty, imitation and hedging are rampant: unable to risk being wrong or left behind, companies match all features, offer all new services, and explore all technologies.

During such periods in an industry's development, its basic productivity frontier is being established or reestablished. Explosive growth can make such times profitable for many companies, but profits will be temporary because imitation and strategic convergence will ultimately destroy industry profitability. The companies that are enduringly successful will be those that begin as early as possible to define and embody in their activities a unique competitive position. A period of imitation may be inevitable in emerging industries, but that period reflects the level of uncertainty rather than a desired state of affairs.

In high-tech industries, this imitation phase often continues much longer than it should. Enraptured by technological change itself, companies pack more features—most of which are never used—into their products while slashing prices across the board. Rarely are trade-offs even considered. The drive for growth to satisfy market pressures leads companies into every product area. Although a few companies with fundamental advantages prosper, the majority are doomed to a rat race no one can win.

Ironically, the popular business press, focused on hot, emerging industries, is prone to presenting these special cases as proof that we have entered a new era of competition in which none of the old rules are

valid. In fact, the opposite is true.

What approaches to growth preserve and reinforce strategy? Broadly, the prescription is to concentrate on deepening a strategic position rather than broadening and compromising it. One approach is to look for extensions of the strategy that leverage the existing activity system by offering features or services that rivals would find impossible or costly to match on a stand-alone basis. In other words, managers can ask themselves which activities, features, or forms of competition are feasible or less costly to them because of complementary activities that their company performs.

Deepening a position involves making the company's activities more distinctive, strengthening fit, and communicating the strategy better to those customers who should value it. But many companies succumb to the temptation to chase "easy" growth by adding hot features, products, or services without screening them or adapting them to their strategy. Or they target new customers or markets in which the company has little special to offer. A company can often grow faster—and far more profitably—by better penetrating needs and varieties where it is distinctive than by slugging it out in potentially higher growth arenas in which the company lacks uniqueness. Carmike, now the largest theater chain in the United States, owes its rapid growth to its disciplined concentration on small markets. The company quickly sells any big-city theaters that come to it as part of an acquisition.

Globalization often allows growth that is consistent with strategy, opening up larger markets for a focused strategy. Unlike broadening domestically, expanding globally is likely to leverage and reinforce a company's unique position and identity.

Companies seeking growth through broadening within their industry can best contain the risks to strategy by creating stand-alone units, each with its own brand name and tailored activities. Maytag has clearly struggled with this issue. On the one hand, it has organized its premium and value brands into separate units with different strategic positions. On the other, it has created an umbrella appliance company for all its brands to gain critical mass. With shared design, manufacturing, distribution, and customer service, it will be hard to avoid homogenization. If a given business unit attempts to compete with different positions for different products or customers, avoiding compromise is nearly impossible.

The role of leadership

The challenge of developing or reestablishing a clear strategy is often primarily an organizational one and depends on leadership. With so many forces at work against making choices and tradeoffs in organizations, a clear intellectual framework to guide strategy is a necessary counterweight. Moreover, strong leaders willing to make choices are essential.

In many companies, leadership has degenerated into orchestrating operational improvements and making deals. But the leader's role is broader and far more important. General management is more than the stewardship of individual functions. Its core is strategy: defining and communicating the company's unique position, making trade-offs, and forging fit among activities. The leader must provide the discipline to decide which industry changes and customer needs the company will respond to, while avoiding organizational distractions and maintaining the company's distinctiveness. Managers at lower levels lack the perspective and the confidence to maintain a strategy. There will be constant pressures to compromise, relax trade-offs, and emulate rivals. One of the leader's jobs is to teach others in the organization about strategy—and to say no.

Strategy renders choices about what not to do as important as choices about what to do. Indeed, setting limits is another function of leadership. Deciding which target group of customers, varieties, and needs the company should serve is fundamental to developing a strategy. But so is deciding not to serve other customers or needs and not to offer certain features or services. Thus strategy requires constant discipline and clear communication. Indeed, one of the most important functions of an explicit, communicated strategy is to guide employees in making choices that arise because of trade-offs in their individual activities and in day-to-day decisions.

Improving operational effectiveness is a necessary part of management, but it is *not* strategy. In confusing the two, managers have unintentionally backed into a way of thinking about competition that is driving many industries toward competitive convergence, which is in no one's best interest and is not inevitable.

Managers must clearly distinguish operational effectiveness from strategy.

Both are essential, but the two agendas are different.

The operational agenda involves continual improvement everywhere there are no trade-offs. Failure to do this creates vulnerability even for companies with a good strategy. The operational agenda is the proper place for constant change, flexibility, and relentless efforts to achieve best practice. In contrast, the strategic agenda is the right place for defining a unique position, making clear trade-offs, and tightening fit. It involves the continual search for ways to reinforce and extend the company's position. The strategic agenda demands discipline and continuity; its enemies are distraction and compromise.

Strategic continuity does not imply a static view of competition. A company must continually improve its operational effectiveness and actively try to shift the productivity frontier; at the same time, there needs to be ongoing effort to extend its uniqueness while strengthening the fit among its activities. Strategic continuity, in fact, should make an organization's continual improvement more effective.

A company may have to change its strategy if there are major structural changes in its industry. In fact, new strategic positions often arise because of industry changes, and new entrants unencumbered by history often can exploit them more easily. However, a company's choice of a new position must be driven by the ability to find new trade-offs and leverage a new system of complementary activities into a sustainable advantage.

Originally published in November 1996. Reprint 96608

Notes

1. I first described the concept of activities and its use in understanding competitive advantage in *Competitive Advantage* (New York: The Free Press, 1985). The ideas in this article build on and extend that thinking.

2. Paul Milgrom and John Roberts have begun to explore the economics of systems of complementary functions, activities, and functions. Their focus is on the emergence of “modern manufacturing” as a new set of complementary activities, on the tendency of companies to react to external changes with coherent bundles of internal responses, and on the need for central coordination—a strategy—to align functional managers. In the latter case, they model what has long been a bedrock principle of strategy. See Paul Milgrom and John Roberts, “The Economics of Modern Manufacturing: Technology, Strategy, and Organization,” *American Economic Review* 80 (1990): 511–528; Paul Milgrom, Yingyi Qian, and John Roberts, “Complementarities, Momentum, and Evolution of Modern Manufacturing,” *American Economic Review* 81 (1991) 84–88; and Paul Milgrom and John Roberts, “Complementarities and Fit: Strategy, Structure, and Organizational Changes in Manufacturing,” *Journal of Accounting and Economics*, vol. 19 (March–May 1995): 179–208.

3. Material on retail strategies is drawn in part from Jan Rivkin, “The Rise of Retail Category Killers,” unpublished working paper, January 1995. Nicolaj Siggelkow prepared the case study on the Gap.

The Five Competitive Forces That Shape Strategy

by Michael E. Porter

IN ESSENCE, THE JOB of the strategist is to understand and cope with competition. Often, however, managers define competition too narrowly, as if it occurred only among today's direct competitors. Yet competition for profits goes beyond established industry rivals to include four other competitive forces as well: customers, suppliers, potential entrants, and substitute products. The extended rivalry that results from all five forces defines an industry's structure and shapes the nature of competitive interaction within an industry.

As different from one another as industries might appear on the surface, the underlying drivers of profitability are the same. The global auto industry, for instance, appears to have nothing in common with the worldwide market for art masterpieces or the heavily regulated health-care delivery industry in Europe. But to understand industry competition and profitability in each of those three cases, one must analyze the industry's underlying structure in terms of the five forces. (See "The five forces that shape industry competition.")

If the forces are intense, as they are in such industries as airlines, textiles, and hotels, almost no company earns attractive returns on investment. If the forces are benign, as they are in industries such as software, soft drinks, and

toiletries, many companies are profitable. Industry structure drives competition and profitability, not whether an industry produces a product or service, is emerging or mature, high tech or low tech, regulated or unregulated. While a myriad of factors can affect industry profitability in the short run—including the weather and the business cycle—industry structure, manifested in the competitive forces, sets industry profitability in the medium and long run. (See “Differences in Industry Profitability.”)

Understanding the competitive forces, and their underlying causes, reveals the roots of an industry’s current profitability while providing a framework for anticipating and influencing competition (and profitability) over time. A healthy industry structure should be as much a competitive concern to strategists as their company’s own position. Understanding industry structure is also essential to effective strategic positioning. As we will see, defending against the competitive forces and shaping them in a company’s favor are crucial to strategy.

Forces That Shape Competition

The configuration of the five forces differs by industry. In the market for commercial aircraft, fierce rivalry between dominant producers Airbus and Boeing and the bargaining power of the airlines that place huge orders for aircraft are strong, while the threat of entry, the threat of substitutes, and the power of suppliers are more benign. In the movie theater industry, the proliferation of substitute forms of entertainment and the power of the movie producers and distributors who supply movies, the critical input, are important.

The strongest competitive force or forces determine the profitability of an industry and become the most important to strategy formulation. The most salient force, however, is not always obvious.

For example, even though rivalry is often fierce in commodity industries, it may not be the factor limiting profitability. Low returns in the photographic film industry, for instance, are the result of a superior substitute product—as Kodak and Fuji, the world’s leading producers of photographic film, learned with the advent of digital photography. In such a situation, coping with the substitute product becomes the number one strategic priority.

Idea in Brief

You know that to sustain long-term profitability you must respond strategically to competition. And you naturally keep tabs on your **established** rivals. But as you scan the competitive arena, are you also looking *beyond* your direct competitors? As Porter explains in this update of his revolutionary 1979 HBR article, four additional competitive forces can hurt your prospective profits:

- Savvy **customers** can force down prices by playing you and your rivals against one another.
- Powerful **suppliers** may constrain your profits if they charge higher prices.
- Aspiring **entrants**, armed with new capacity and hungry for market share, can ratchet up the investment required for you to stay in the game.
- **Substitute offerings** can lure customers away.

Consider commercial aviation: It's one of the least profitable industries because all five forces are strong. **Established rivals** compete intensely on price. **Customers** are fickle, searching for the best deal regardless of carrier. **Suppliers**—plane and engine manufacturers, along with unionized labor forces—bargain away the lion's share of airlines' profits. **New players** enter the industry in a constant stream. And **substitutes** are readily available—such as train or car travel.

By analyzing all five competitive forces, you gain a complete picture of what's influencing profitability in your industry. You identify game-

changing trends early, so you can swiftly exploit them. And you spot ways to work around constraints on profitability—or even reshape the forces in your favor.

Industry structure grows out of a set of economic and technical characteristics that determine the strength of each competitive force. We will examine these drivers in the pages that follow, taking the perspective of an incumbent, or a company already present in the industry. The analysis can be readily extended to understand the challenges facing a potential entrant.

Threat of entry

New entrants to an industry bring new capacity and a desire to gain market share that puts pressure on prices, costs, and the rate of investment necessary to compete. Particularly when new entrants are diversifying from other markets, they can leverage existing capabilities and cash flows to shake up competition, as Pepsi did when it entered the bottled water industry, Microsoft did when it began to offer internet browsers, and Apple did when it entered the music distribution business.

Idea in Practice

By understanding how the five competitive forces influence profitability in your industry, you can develop a strategy for enhancing your company's long-term profits. Porter suggests the following:

Position Your Company Where the Forces Are Weakest

Example: In the heavy-truck industry, many buyers operate large fleets and are highly motivated to drive down truck prices. Trucks are built to regulated standards and offer similar features, so price competition is stiff; unions exercise considerable supplier power; and buyers can use substitutes such as cargo delivery by rail.

To create and sustain long-term profitability within this industry, heavy-truck maker Paccar chose to focus on one customer group where competitive forces are weakest: individual drivers who own their trucks and contract directly with suppliers. These operators have limited clout as buyers and are less price sensitive because of their emotional ties to and economic dependence on their own trucks.

For these customers, Paccar has developed such features as luxurious sleeper cabins, plush leather seats, and sleek exterior styling. Buyers can select from thousands of options to put their personal signature on these built-to-order trucks.

Customers pay Paccar a 10% premium, and the company has been profitable for 68 straight years and earned a long-run return on equity above 20%.

Exploit Changes in the Forces

Example: With the advent of the Internet and digital distribution of music, unauthorized downloading created an illegal but potent substitute for record companies' services. The record companies tried to develop

technical platforms for digital distribution themselves, but major labels didn't want to sell their music through a platform owned by a rival.

Into this vacuum stepped Apple, with its iTunes music store supporting its iPod music player. The birth of this powerful new gatekeeper has whittled down the number of major labels from six in 1997 to four today.

Reshape the Forces in Your Favor

Use tactics designed specifically to reduce the share of profits leaking to other players. For example:

- To neutralize **supplier power**, standardize specifications for parts so your company can switch more easily among vendors.
- To counter **customer power**, expand your services so it's harder for customers to leave you for a rival.
- To temper price wars initiated by **established rivals**, invest more heavily in products that differ significantly from competitors' offerings.
- To scare off **new entrants**, elevate the fixed costs of competing; for instance, by escalating your R&D expenditures.
- To limit the threat of **substitutes**, offer better value through wider product accessibility. Soft-drink producers did this by introducing vending machines and convenience store channels, which dramatically improved the availability of soft drinks relative to other beverages.

The threat of entry, therefore, puts a cap on the profit potential of an industry. When the threat is high, incumbents must hold down their prices or

boost investment to deter new competitors. In specialty coffee retailing, for example, relatively low entry barriers mean that Starbucks must invest aggressively in modernizing stores and menus.

The threat of entry in an industry depends on the height of entry barriers that are present and on the reaction entrants can expect from incumbents. If entry barriers are low and newcomers expect little retaliation from the entrenched competitors, the threat of entry is high and industry profitability is moderated. It is the *threat* of entry, not whether entry actually occurs, that holds down profitability.

Barriers to entry. Entry barriers are advantages that incumbents have relative to new entrants. There are seven major sources:

1. *Supply-side economies of scale.* These economies arise when firms that produce at larger volumes enjoy lower costs per unit because they can spread fixed costs over more units, employ more efficient technology, or command better terms from suppliers. Supply-side scale economies deter entry by forcing the aspiring entrant either to come into the industry on a large scale, which requires dislodging entrenched competitors, or to accept a cost disadvantage.

Scale economies can be found in virtually every activity in the value chain; which ones are most important varies by industry.¹ In microprocessors, incumbents such as Intel are protected by scale economies in research, chip fabrication, and consumer marketing. For lawn care companies like Scotts Miracle-Gro, the most important scale economies are found in the supply chain and media advertising. In small-package delivery, economies of scale arise in national logistical systems and information technology.

2. *Demand-side benefits of scale.* These benefits, also known as network effects, arise in industries where a buyer's willingness to pay for a company's product increases with the number of other buyers who also patronize the company. Buyers may trust larger companies more for a crucial product: Recall the old adage that no one ever got fired for buying from IBM (when it was the dominant computer maker). Buyers may also value being in a "network" with a larger number of fellow customers. For instance, online auction participants are attracted to eBay because it offers the most potential trading partners. Demand-side benefits of scale discourage entry by limiting the willingness of customers to buy from a newcomer and by reducing the

price the newcomer can command until it builds up a large base of customers.

3. *Customer switching costs.* Switching costs are fixed costs that buyers face when they change suppliers. Such costs may arise because a buyer who switches vendors must, for example, alter product specifications, retrain employees to use a new product, or modify processes or information systems. The larger the switching costs, the harder it will be for an entrant to gain customers. Enterprise resource planning (ERP) software is an example of a product with very high switching costs. Once a company has installed SAP's ERP system, for example, the costs of moving to a new vendor are astronomical because of embedded data, the fact that internal processes have been adapted to SAP, major retraining needs, and the mission-critical nature of the applications.

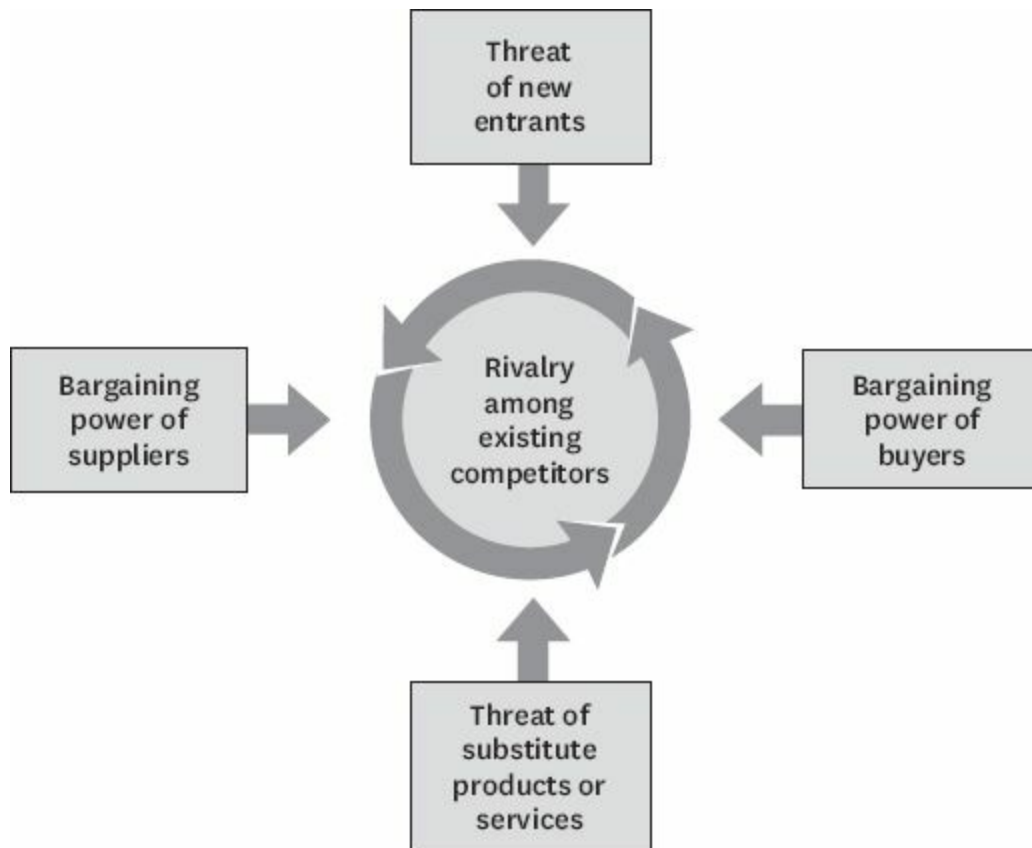
4. *Capital requirements.* The need to invest large financial resources in order to compete can deter new entrants. Capital may be necessary not only for fixed facilities but also to extend customer credit, build inventories, and fund start-up losses. The barrier is particularly great if the capital is required for unrecoverable and therefore harder-to-finance expenditures, such as up-front advertising or research and development. While major corporations have the financial resources to invade almost any industry, the huge capital requirements in certain fields limit the pool of likely entrants. Conversely, in such fields as tax preparation services or short-haul trucking, capital requirements are minimal and potential entrants plentiful.

It is important not to overstate the degree to which capital requirements alone deter entry. If industry returns are attractive and are expected to remain so, and if capital markets are efficient, investors will provide entrants with the funds they need. For aspiring air carriers, for instance, financing is available to purchase expensive aircraft because of their high resale value, one reason why there have been numerous new airlines in almost every region.

5. *Incumbency advantages independent of size.* No matter what their size, incumbents may have cost or quality advantages not available to potential rivals. These advantages can stem from such sources as proprietary technology, preferential access to the best raw material sources, preemption of the most favorable geographic locations, established brand identities, or cumulative experience that has allowed incumbents to learn how to produce more efficiently. Entrants try to bypass such advantages. Upstart discounters such as Target and Wal-Mart, for example, have located stores in freestanding sites rather than regional shopping centers where established

department stores were well entrenched.

The five forces that shape industry competition



6. *Unequal access to distribution channels.* The new entrant must, of course, secure distribution of its product or service. A new food item, for example, must displace others from the supermarket shelf via price breaks, promotions, intense selling efforts, or some other means. The more limited the wholesale or retail channels are and the more that existing competitors have tied them up, the tougher entry into an industry will be. Sometimes access to distribution is so high a barrier that new entrants must bypass distribution channels altogether or create their own. Thus, upstart low-cost airlines have avoided distribution through travel agents (who tend to favor established higher-fare carriers) and have encouraged passengers to book their own flights on the internet.

7. *Restrictive government policy.* Government policy can hinder or aid new entry directly, as well as amplify (or nullify) the other entry barriers. Government directly limits or even forecloses entry into industries through, for instance, licensing requirements and restrictions on foreign investment. Regulated industries like liquor retailing, taxi services, and airlines are visible examples. Government policy can heighten other entry barriers through such means as expansive patenting rules that protect proprietary technology from imitation or environmental or safety regulations that raise scale economies facing newcomers. Of course, government policies may also make entry easier—directly through subsidies, for instance, or indirectly by funding basic research and making it available to all firms, new and old, reducing scale economies.

Entry barriers should be assessed relative to the capabilities of potential entrants, which may be start-ups, foreign firms, or companies in related industries. And, as some of our examples illustrate, the strategist must be mindful of the creative ways newcomers might find to circumvent apparent barriers.

Expected retaliation. How potential entrants believe incumbents may react will also influence their decision to enter or stay out of an industry. If reaction is vigorous and protracted enough, the profit potential of participating in the industry can fall below the cost of capital. Incumbents often use public statements and responses to one entrant to send a message to other prospective entrants about their commitment to defending market share.

Newcomers are likely to fear expected retaliation if:

- Incumbents have previously responded vigorously to new entrants.
- Incumbents possess substantial resources to fight back, including excess cash and unused borrowing power, available productive capacity, or clout with distribution channels and customers.
- Incumbents seem likely to cut prices because they are committed to retaining market share at all costs or because the industry has high fixed costs, which create a strong motivation to drop prices to fill excess

capacity.

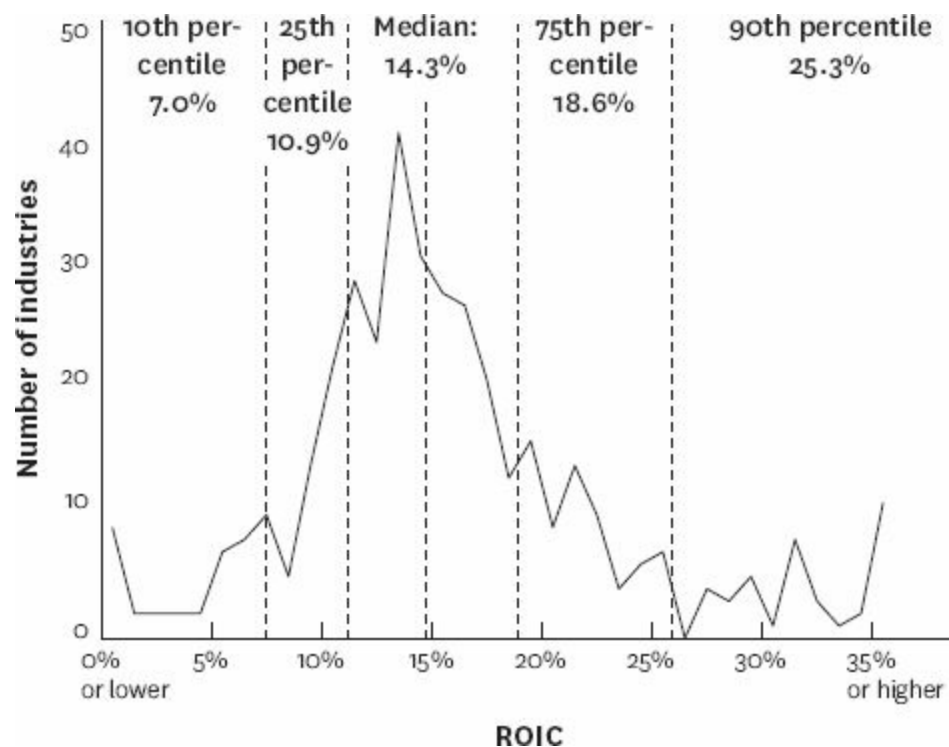
- Industry growth is slow so newcomers can gain volume only by taking it from incumbents.

Differences in Industry Profitability

THE AVERAGE RETURN on invested capital varies markedly from industry to industry. Between 1992 and 2006, for example, average return on invested capital in U.S. industries ranged as low as zero or even negative to more than 50%. At the high end are industries like soft drinks and prepackaged software, which have been almost six times more profitable than the airline industry over the period.

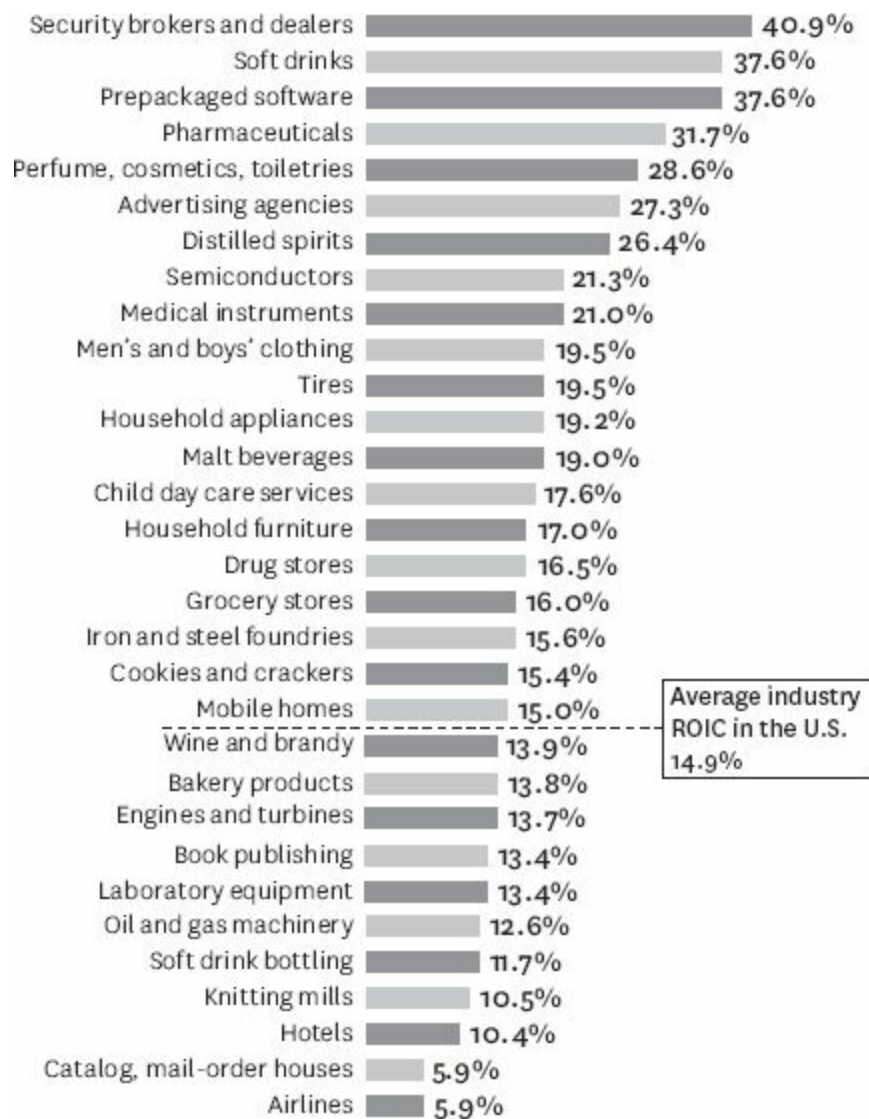
Average return on invested capital in U.S. industries, 1992–2006

Return on invested capital (ROIC) is the appropriate measure of profitability for strategy formulation, not to mention for equity investors. Return on sales or the growth rate of profits fail to account for the capital required to compete in the industry. Here, we utilize earnings before interest and taxes divided by average invested capital less excess cash as the measure of ROIC. This measure controls for idiosyncratic differences in capital structure and tax rates across companies and industries.



Profitability of selected U.S. industries

Average ROIC, 1992–2006



An analysis of barriers to entry and expected retaliation is obviously crucial for any company contemplating entry into a new industry. The challenge is to find ways to surmount the entry barriers without nullifying,

through heavy investment, the profitability of participating in the industry.

The power of suppliers

Powerful suppliers capture more of the value for themselves by charging higher prices, limiting quality or services, or shifting costs to industry participants. Powerful suppliers, including suppliers of labor, can squeeze profitability out of an industry that is unable to pass on cost increases in its own prices. Microsoft, for instance, has contributed to the erosion of profitability among personal computer makers by raising prices on operating systems. PC makers, competing fiercely for customers who can easily switch among them, have limited freedom to raise their prices accordingly.

Companies depend on a wide range of different supplier groups for inputs. A supplier group is powerful if:

- It is more concentrated than the industry it sells to. Microsoft's near monopoly in operating systems, coupled with the fragmentation of PC assemblers, exemplifies this situation.
- The supplier group does not depend heavily on the industry for its revenues. Suppliers serving many industries will not hesitate to extract maximum profits from each one. If a particular industry accounts for a large portion of a supplier group's volume or profit, however, suppliers will want to protect the industry through reasonable pricing and assist in activities such as R&D and lobbying.
- Industry participants face switching costs in changing suppliers. For example, shifting suppliers is difficult if companies have invested heavily in specialized ancillary equipment or in learning how to operate a supplier's equipment (as with Bloomberg terminals used by financial professionals). Or firms may have located their production lines adjacent to a supplier's manufacturing facilities (as in the case of some beverage companies and container manufacturers). When switching costs are high, industry participants find it hard to play suppliers off against one

another. (Note that suppliers may have switching costs as well. This limits their power.)

- Suppliers offer products that are differentiated. Pharmaceutical companies that offer patented drugs with distinctive medical benefits have more power over hospitals, health maintenance organizations, and other drug buyers, for example, than drug companies offering me-too or generic products.
- There is no substitute for what the supplier group provides. Pilots' unions, for example, exercise considerable supplier power over airlines partly because there is no good alternative to a well-trained pilot in the cockpit.
- The supplier group can credibly threaten to integrate forward into the industry. In that case, if industry participants make too much money relative to suppliers, they will induce suppliers to enter the market.

Industry Analysis in Practice

Good industry analysis looks rigorously at the structural underpinnings of profitability. A first step is to understand the appropriate time horizon. One of the essential tasks in industry analysis is to distinguish temporary or cyclical changes from structural changes. A good guideline for the appropriate time horizon is the full business cycle for the particular industry. For most industries, a three-to-five-year horizon is appropriate, although in some industries with long lead times, such as mining, the appropriate horizon might be a decade or more. It is average profitability over this period, not profitability in any particular year, that should be the focus of analysis.

The point of industry analysis is not to declare the industry attractive or unattractive but to understand the underpinnings of competition and the root causes of profitability. As much as possible, analysts should look at industry structure quantitatively, rather than be satisfied with lists of qualitative factors. Many elements of the five forces can be quantified: the percentage of the buyer's total cost accounted for by the industry's product (to understand buyer price sensitivity); the percentage of industry sales required to fill a plant or operate a logistical network of efficient scale (to help assess barriers to entry); the buyer's switching cost (determining the inducement an entrant or rival must offer customers).

The strength of the competitive forces affects prices, costs, and the investment required to compete; thus the forces are directly tied to the income statements and balance sheets of industry participants. Industry structure defines the gap between revenues and costs. For example, intense rivalry drives down prices or elevates the costs of marketing, R&D, or customer service, reducing margins. How much? Strong suppliers drive up input costs. How much? Buyer power lowers prices or elevates the costs of meeting buyers' demands, such as the requirement to hold more inventory or provide financing. How much?

Low barriers to entry or close substitutes limit the level of sustainable prices. How much? It is these economic relationships that sharpen the strategist's understanding of industry competition.

Finally, good industry analysis does not just list pluses and minuses but sees an industry in overall, systemic terms. Which forces are underpinning (or constraining) today's profitability? How might shifts in one competitive force trigger reactions in others? Answering such questions is often the source of true strategic insights.

The power of buyers

Powerful customers—the flip side of powerful suppliers—can capture more value by forcing down prices, demanding better quality or more service (thereby driving up costs), and generally playing industry participants off against one another, all at the expense of industry profitability. Buyers are powerful if they have negotiating leverage relative to industry participants, especially if they are price sensitive, using their clout primarily to pressure price reductions.

As with suppliers, there may be distinct groups of customers who differ in bargaining power. A customer group has negotiating leverage if:

- There are few buyers, or each one purchases in volumes that are large relative to the size of a single vendor. Large-volume buyers are particularly powerful in industries with high fixed costs, such as telecommunications equipment, offshore drilling, and bulk chemicals. High fixed costs and low marginal costs amplify the pressure on rivals to keep capacity filled through discounting.
- The industry's products are standardized or undifferentiated. If buyers believe they can always find an equivalent product, they tend to play one vendor against another.
- Buyers face few switching costs in changing vendors.
- Buyers can credibly threaten to integrate backward and produce the industry's product themselves if vendors are too profitable. Producers of soft drinks and beer have long controlled the power of packaging manufacturers by threatening to make, and at times actually making, packaging materials themselves.

A buyer group is price sensitive if:

- The product it purchases from the industry represents a significant fraction of its cost structure or procurement budget. Here buyers are likely to shop around and bargain hard, as consumers do for home mortgages. Where the product sold by an industry is a small fraction of buyers' costs or expenditures, buyers are usually less price sensitive.
- The buyer group earns low profits, is strapped for cash, or is otherwise under pressure to trim its purchasing costs. Highly profitable or cash-rich customers, in contrast, are generally less price sensitive (that is, of course, if the item does not represent a large fraction of their costs).
- The quality of buyers' products or services is little affected by the industry's product. Where quality is very much affected by the industry's product, buyers are generally less price sensitive. When purchasing or renting production quality cameras, for instance, makers of major motion pictures opt for highly reliable equipment with the latest features. They pay limited attention to price.
- The industry's product has little effect on the buyer's other costs. Here, buyers focus on price. Conversely, where an industry's product or service can pay for itself many times over by improving performance or reducing labor, material, or other costs, buyers are usually more interested in quality than in price. Examples include products and services like tax accounting or well logging (which measures below-ground conditions of oil wells) that can save or even make the buyer money. Similarly, buyers tend not to be price sensitive in services such as investment banking, where poor performance can be costly and embarrassing.

Most sources of buyer power apply equally to consumers and to business-to-business customers. Like industrial customers, consumers tend to be more price sensitive if they are purchasing products that are undifferentiated, expensive relative to their incomes, and of a sort where product performance

has limited consequences. The major difference with consumers is that their needs can be more intangible and harder to quantify.

Intermediate customers, or customers who purchase the product but are not the end user (such as assemblers or distribution channels), can be analyzed the same way as other buyers, with one important addition. Intermediate customers gain significant bargaining power when they can influence the purchasing decisions of customers downstream. Consumer electronics retailers, jewelry retailers, and agricultural-equipment distributors are examples of distribution channels that exert a strong influence on end customers.

Producers often attempt to diminish channel clout through exclusive arrangements with particular distributors or retailers or by marketing directly to end users. Component manufacturers seek to develop power over assemblers by creating preferences for their components with downstream customers. Such is the case with bicycle parts and with sweeteners. DuPont has created enormous clout by advertising its Stainmaster brand of carpet fibers not only to the carpet manufacturers that actually buy them but also to downstream consumers. Many consumers request Stainmaster carpet even though DuPont is not a carpet manufacturer.

The threat of substitutes

A substitute performs the same or a similar function as an industry's product by a different means. Videoconferencing is a substitute for travel. Plastic is a substitute for aluminum. E-mail is a substitute for express mail. Sometimes, the threat of substitution is downstream or indirect, when a substitute replaces a buyer industry's product. For example, lawn-care products and services are threatened when multifamily homes in urban areas substitute for single-family homes in the suburbs. Software sold to agents is threatened when airline and travel websites substitute for travel agents.

Substitutes are always present, but they are easy to overlook because they may appear to be very different from the industry's product: To someone searching for a Father's Day gift, neckties and power tools may be substitutes. It is a substitute to do without, to purchase a used product rather than a new one, or to do it yourself (bring the service or product in-house).

When the threat of substitutes is high, industry profitability suffers. Substitute products or services limit an industry's profit potential by placing a ceiling on prices. If an industry does not distance itself from substitutes through product performance, marketing, or other means, it will suffer in terms of profitability—and often growth potential.

Substitutes not only limit profits in normal times, they also reduce the bonanza an industry can reap in good times. In emerging economies, for example, the surge in demand for wired telephone lines has been capped as many consumers opt to make a mobile telephone their first and only phone line.

The threat of a substitute is high if:

- It offers an attractive price-performance trade-off to the industry's product. The better the relative value of the substitute, the tighter is the lid on an industry's profit potential. For example, conventional providers of long-distance telephone service have suffered from the advent of inexpensive internet-based phone services such as Vonage and Skype.

Similarly, video rental outlets are struggling with the emergence of cable and satellite video-on-demand services, online video rental services such as Netflix, and the rise of internet video sites like Google's YouTube.

- The buyer's cost of switching to the substitute is low. Switching from a proprietary, branded drug to a generic drug usually involves minimal costs, for example, which is why the shift to generics (and the fall in prices) is so substantial and rapid.
- Strategists should be particularly alert to changes in other industries that may make them attractive substitutes when they were not before. Improvements in plastic materials, for example, allowed them to substitute for steel in many automobile components. In this way, technological changes or competitive discontinuities in seemingly unrelated businesses can have major impacts on industry profitability. Of course the substitution threat can also shift in favor of an industry, which bodes well for its future profitability and growth potential.

Rivalry among existing competitors

Rivalry among existing competitors takes many familiar forms, including price discounting, new product introductions, advertising campaigns, and service improvements. High rivalry limits the profitability of an industry. The degree to which rivalry drives down an industry's profit potential depends, first, on the *intensity* with which companies compete and, second, on the *basis* on which they compete.

The intensity of rivalry is greatest if:

- Competitors are numerous or are roughly equal in size and power. In such situations, rivals find it hard to avoid poaching business. Without an industry leader, practices desirable for the industry as a whole go unenforced.
- Industry growth is slow. Slow growth precipitates fights for market share.
- Exit barriers are high. Exit barriers, the flip side of entry barriers, arise because of such things as highly specialized assets or management's devotion to a particular business. These barriers keep companies in the market even though they may be earning low or negative returns. Excess capacity remains in use, and the profitability of healthy competitors suffers as the sick ones hang on.
- Rivals are highly committed to the business and have aspirations for leadership, especially if they have goals that go beyond economic performance in the particular industry. High commitment to a business arises for a variety of reasons. For example, state-owned competitors may have goals that include employment or prestige. Units of larger companies may participate in an industry for image reasons or to offer a full line. Clashes of personality and ego have sometimes exaggerated

rivalry to the detriment of profitability in fields such as the media and high technology.

- Firms cannot read each other's signals well because of lack of familiarity with one another, diverse approaches to competing, or differing goals.

The strength of rivalry reflects not just the intensity of competition but also the basis of competition. The *dimensions* on which competition takes place, and whether rivals converge to compete on the *same dimensions*, have a major influence on profitability.

Rivalry is especially destructive to profitability if it gravitates solely to price because price competition transfers profits directly from an industry to its customers. Price cuts are usually easy for competitors to see and match, making successive rounds of retaliation likely. Sustained price competition also trains customers to pay less attention to product features and service.

Price competition is most liable to occur if:

- Products or services of rivals are nearly identical and there are few switching costs for buyers. This encourages competitors to cut prices to win new customers. Years of airline price wars reflect these circumstances in that industry.
- Fixed costs are high and marginal costs are low. This creates intense pressure for competitors to cut prices below their average costs, even close to their marginal costs, to steal incremental customers while still making some contribution to covering fixed costs. Many basic-materials businesses, such as paper and aluminum, suffer from this problem, especially if demand is not growing. So do delivery companies with fixed networks of routes that must be served regardless of volume.
- Capacity must be expanded in large increments to be efficient. The need for large capacity expansions, as in the polyvinyl chloride business, disrupts the industry's supply-demand balance and often leads to long and recurring periods of overcapacity and price cutting.

- The product is perishable. Perishability creates a strong temptation to cut prices and sell a product while it still has value. More products and services are perishable than is commonly thought. Just as tomatoes are perishable because they rot, models of computers are perishable because they soon become obsolete, and information may be perishable if it diffuses rapidly or becomes outdated, thereby losing its value. Services such as hotel accommodations are perishable in the sense that unused capacity can never be recovered.

Competition on dimensions other than price—on product features, support services, delivery time, or brand image, for instance—is less likely to erode profitability because it improves customer value and can support higher prices. Also, rivalry focused on such dimensions can improve value relative to substitutes or raise the barriers facing new entrants. While nonprice rivalry sometimes escalates to levels that undermine industry profitability, this is less likely to occur than it is with price rivalry.

As important as the dimensions of rivalry is whether rivals compete on the *same* dimensions. When all or many competitors aim to meet the same needs or compete on the same attributes, the result is zero-sum competition. Here, one firm's gain is often another's loss, driving down profitability. While price competition runs a stronger risk than nonprice competition of becoming zero sum, this may not happen if companies take care to segment their markets, targeting their low-price offerings to different customers.

Rivalry can be positive sum, or actually increase the average profitability of an industry, when each competitor aims to serve the needs of different customer segments, with different mixes of price, products, services, features, or brand identities. Such competition can not only support higher average profitability but also expand the industry, as the needs of more customer groups are better met. The opportunity for positive-sum competition will be greater in industries serving diverse customer groups. With a clear understanding of the structural underpinnings of rivalry, strategists can sometimes take steps to shift the nature of competition in a more positive direction.

Factors, Not Forces

Industry structure, as manifested in the strength of the five competitive forces, determines the industry's long-run profit potential because it determines how the economic value created by the industry is divided—how much is retained by companies in the industry versus bargained away by customers and suppliers, limited by substitutes, or constrained by potential new entrants. By considering all five forces, a strategist keeps overall structure in mind instead of gravitating to any one element. In addition, the strategist's attention remains focused on structural conditions rather than on fleeting factors.

It is especially important to avoid the common pitfall of mistaking certain visible attributes of an industry for its underlying structure. Consider the following:

Industry growth rate

A common mistake is to assume that fast-growing industries are always attractive. Growth does tend to mute rivalry, because an expanding pie offers opportunities for all competitors. But fast growth can put suppliers in a powerful position, and high growth with low entry barriers will draw in entrants. Even without new entrants, a high growth rate will not guarantee profitability if customers are powerful or substitutes are attractive. Indeed, some fast-growth businesses, such as personal computers, have been among the least profitable industries in recent years. A narrow focus on growth is one of the major causes of bad strategy decisions.

Technology and innovation

Advanced technology or innovations are not by themselves enough to make an industry structurally attractive (or unattractive). Mundane, low-technology industries with price-insensitive buyers, high switching costs, or high entry barriers arising from scale economies are often far more profitable than sexy industries, such as software and internet technologies, that attract competitors.²

Government

Government is not best understood as a sixth force because government involvement is neither inherently good nor bad for industry profitability. The best way to understand the influence of government on competition is to analyze how specific government policies affect the five competitive forces. For instance, patents raise barriers to entry, boosting industry profit potential. Conversely, government policies favoring unions may raise supplier power and diminish profit potential. Bankruptcy rules that allow failing companies to reorganize rather than exit can lead to excess capacity and intense rivalry. Government operates at multiple levels and through many different policies, each of which will affect structure in different ways.

Complementary products and services

Complements are products or services used together with an industry's product. Complements arise when the customer benefit of two products combined is greater than the sum of each product's value in isolation. Computer hardware and software, for instance, are valuable together and worthless when separated.

In recent years, strategy researchers have highlighted the role of complements, especially in high-technology industries where they are most obvious.³ By no means, however, do complements appear only there. The value of a car, for example, is greater when the driver also has access to gasoline stations, roadside assistance, and auto insurance.

Complements can be important when they affect the overall demand for an industry's product. However, like government policy, complements are not a sixth force determining industry profitability since the presence of strong complements is not necessarily bad (or good) for industry profitability. Complements affect profitability through the way they influence the five forces.

The strategist must trace the positive or negative influence of complements on all five forces to ascertain their impact on profitability. The presence of complements can raise or lower barriers to entry. In application software, for example, barriers to entry were lowered when producers of complementary operating system software, notably Microsoft, provided tool sets making it easier to write applications. Conversely, the need to attract producers of complements can raise barriers to entry, as it does in video game hardware.

The presence of complements can also affect the threat of substitutes. For instance, the need for appropriate fueling stations makes it difficult for cars using alternative fuels to substitute for conventional vehicles. But complements can also make substitution easier. For example, Apple's iTunes hastened the substitution from CDs to digital music.

Complements can factor into industry rivalry either positively (as when they raise switching costs) or negatively (as when they neutralize product differentiation). Similar analyses can be done for buyer and supplier power.

Sometimes companies compete by altering conditions in complementary industries in their favor, such as when videocassette-recorder producer JVC persuaded movie studios to favor its standard in issuing prerecorded tapes even though rival Sony's standard was probably superior from a technical standpoint.

Identifying complements is part of the analyst's work. As with government policies or important technologies, the strategic significance of complements will be best understood through the lens of the five forces.

Changes in Industry Structure

So far, we have discussed the competitive forces at a single point in time. Industry structure proves to be relatively stable, and industry profitability differences are remarkably persistent over time in practice. However, industry structure is constantly undergoing modest adjustment—and occasionally it can change abruptly.

Shifts in structure may emanate from outside an industry or from within. They can boost the industry's profit potential or reduce it. They may be caused by changes in technology, changes in customer needs, or other events. The five competitive forces provide a framework for identifying the most important industry developments and for anticipating their impact on industry attractiveness.

Shifting threat of new entry

Changes to any of the seven barriers described above can raise or lower the threat of new entry. The expiration of a patent, for instance, may unleash new entrants. On the day that Merck's patents for the cholesterol reducer Zocor expired, three pharmaceutical makers entered the market for the drug. Conversely, the proliferation of products in the ice cream industry has gradually filled up the limited freezer space in grocery stores, making it harder for new ice cream makers to gain access to distribution in North America and Europe.

Strategic decisions of leading competitors often have a major impact on the threat of entry. Starting in the 1970s, for example, retailers such as Wal-Mart, Kmart, and Toys "R" Us began to adopt new procurement, distribution, and inventory control technologies with large fixed costs, including automated distribution centers, bar coding, and point-of-sale terminals. These investments increased the economies of scale and made it more difficult for small retailers to enter the business (and for existing small players to survive).

Changing supplier or buyer power

As the factors underlying the power of suppliers and buyers change with time, their clout rises or declines. In the global appliance industry, for instance, competitors including Electrolux, General Electric, and Whirlpool have been squeezed by the consolidation of retail channels (the decline of appliance specialty stores, for instance, and the rise of big-box retailers like Best Buy and Home Depot in the United States). Another example is travel agents, who depend on airlines as a key supplier. When the internet allowed airlines to sell tickets directly to customers, this significantly increased their power to bargain down agents' commissions.

Shifting threat of substitution

The most common reason substitutes become more or less threatening over time is that advances in technology create new substitutes or shift price-performance comparisons in one direction or the other. The earliest microwave ovens, for example, were large and priced above \$2,000, making them poor substitutes for conventional ovens. With technological advances, they became serious substitutes. Flash computer memory has improved enough recently to become a meaningful substitute for low-capacity hard-disk drives. Trends in the availability or performance of complementary producers also shift the threat of substitutes.

New bases of rivalry

Rivalry often intensifies naturally over time. As an industry matures, growth slows. Competitors become more alike as industry conventions emerge, technology diffuses, and consumer tastes converge. Industry profitability falls, and weaker competitors are driven from the business. This story has played out in industry after industry; televisions, snowmobiles, and telecommunications equipment are just a few examples.

A trend toward intensifying price competition and other forms of rivalry, however, is by no means inevitable. For example, there has been enormous competitive activity in the U.S. casino industry in recent decades, but most of it has been positive-sum competition directed toward new niches and geographic segments (such as riverboats, trophy properties, Native American reservations, international expansion, and novel customer groups like families). Head-to-head rivalry that lowers prices or boosts the payouts to winners has been limited.

The nature of rivalry in an industry is altered by mergers and acquisitions that introduce new capabilities and ways of competing. Or, technological innovation can reshape rivalry. In the retail brokerage industry, the advent of the internet lowered marginal costs and reduced differentiation, triggering far more intense competition on commissions and fees than in the past.

In some industries, companies turn to mergers and consolidation not to improve cost and quality but to attempt to stop intense competition. Eliminating rivals is a risky strategy, however. The five competitive forces tell us that a profit windfall from removing today's competitors often attracts new competitors and backlash from customers and suppliers. In New York banking, for example, the 1980s and 1990s saw escalating consolidations of commercial and savings banks, including Manufacturers Hanover, Chemical, Chase, and Dime Savings. But today the retail-banking landscape of Manhattan is as diverse as ever, as new entrants such as Wachovia, Bank of America, and Washington Mutual have entered the market.

Implications for Strategy

Understanding the forces that shape industry competition is the starting point for developing strategy. Every company should already know what the average profitability of its industry is and how that has been changing over time. The five forces reveal *why* industry profitability is what it is. Only then can a company incorporate industry conditions into strategy.

The forces reveal the most significant aspects of the competitive environment. They also provide a baseline for sizing up a company's strengths and weaknesses: Where does the company stand versus buyers, suppliers, entrants, rivals, and substitutes? Most importantly, an understanding of industry structure guides managers toward fruitful possibilities for strategic action, which may include any or all of the following: positioning the company to better cope with the current competitive forces; anticipating and exploiting shifts in the forces; and shaping the balance of forces to create a new industry structure that is more favorable to the company. The best strategies exploit more than one of these possibilities.

Positioning the company

Strategy can be viewed as building defenses against the competitive forces or finding a position in the industry where the forces are weakest. Consider, for instance, the position of Paccar in the market for heavy trucks. The heavy-truck industry is structurally challenging. Many buyers operate large fleets or are large leasing companies, with both the leverage and the motivation to drive down the price of one of their largest purchases. Most trucks are built to regulated standards and offer similar features, so price competition is rampant. Capital intensity causes rivalry to be fierce, especially during the recurring cyclical downturns. Unions exercise considerable supplier power. Though there are few direct substitutes for an 18-wheeler, truck buyers face important substitutes for their services, such as cargo delivery by rail.

In this setting, Paccar, a Bellevue, Washington-based company with about 20% of the North American heavy-truck market, has chosen to focus on one group of customers: owner-operators—drivers who own their trucks and contract directly with shippers or serve as subcontractors to larger trucking companies. Such small operators have limited clout as truck buyers. They are also less price sensitive because of their strong emotional ties to and economic dependence on the product. They take great pride in their trucks, in which they spend most of their time.

Paccar has invested heavily to develop an array of features with owner-operators in mind: luxurious sleeper cabins, plush leather seats, noise-insulated cabins, sleek exterior styling, and so on. At the company's extensive network of dealers, prospective buyers use software to select among thousands of options to put their personal signature on their trucks. These customized trucks are built to order, not to stock, and delivered in six to eight weeks. Paccar's trucks also have aerodynamic designs that reduce fuel consumption, and they maintain their resale value better than other trucks. Paccar's roadside assistance program and IT-supported system for distributing spare parts reduce the time a truck is out of service. All these are crucial considerations for an owner-operator. Customers pay Paccar a 10% premium, and its Kenworth and Peterbilt brands are considered status symbols at truck stops.

Paccar illustrates the principles of positioning a company within a given industry structure. The firm has found a portion of its industry where the competitive forces are weaker—where it can avoid buyer power and price-based rivalry. And it has tailored every single part of the value chain to cope well with the forces in its segment. As a result, Paccar has been profitable for 68 years straight and has earned a long-run return on equity above 20%.

In addition to revealing positioning opportunities within an existing industry, the five forces framework allows companies to rigorously analyze entry and exit. Both depend on answering the difficult question: “What is the potential of this business?” Exit is indicated when industry structure is poor or declining and the company has no prospect of a superior positioning. In considering entry into a new industry, creative strategists can use the framework to spot an industry with a good future before this good future is reflected in the prices of acquisition candidates. Five forces analysis may also reveal industries that are not necessarily attractive for the average entrant but in which a company has good reason to believe it can surmount entry barriers at lower cost than most firms or has a unique ability to cope with the industry’s competitive forces.

Exploiting industry change

Industry changes bring the opportunity to spot and claim promising new strategic positions if the strategist has a sophisticated understanding of the competitive forces and their underpinnings. Consider, for instance, the evolution of the music industry during the past decade. With the advent of the internet and the digital distribution of music, some analysts predicted the birth of thousands of music labels (that is, record companies that develop artists and bring their music to market). This, the analysts argued, would break a pattern that had held since Edison invented the phonograph: Between three and six major record companies had always dominated the industry. The internet would, they predicted, remove distribution as a barrier to entry, unleashing a flood of new players into the music industry.

A careful analysis, however, would have revealed that physical distribution was not the crucial barrier to entry. Rather, entry was barred by other benefits that large music labels enjoyed. Large labels could pool the risks of developing new artists over many bets, cushioning the impact of inevitable failures. Even more important, they had advantages in breaking through the clutter and getting their new artists heard. To do so, they could promise radio stations and record stores access to well-known artists in exchange for promotion of new artists. New labels would find this nearly impossible to match. The major labels stayed the course, and new music labels have been rare.

This is not to say that the music industry is structurally unchanged by digital distribution. Unauthorized downloading created an illegal but potent substitute. The labels tried for years to develop technical platforms for digital distribution themselves, but major companies hesitated to sell their music through a platform owned by a rival. Into this vacuum stepped Apple with its iTunes music store, launched in 2003 to support its iPod music player. By permitting the creation of a powerful new gatekeeper, the major labels allowed industry structure to shift against them. The number of major record companies has actually declined—from six in 1997 to four today—as companies struggled to cope with the digital phenomenon.

When industry structure is in flux, new and promising competitive

positions may appear. Structural changes open up new needs and new ways to serve existing needs. Established leaders may overlook these or be constrained by past strategies from pursuing them. Smaller competitors in the industry can capitalize on such changes, or the void may well be filled by new entrants.

Shaping industry structure

When a company exploits structural change, it is recognizing, and reacting to, the inevitable. However, companies also have the ability to shape industry structure. A firm can lead its industry toward new ways of competing that alter the five forces for the better. In reshaping structure, a company wants its competitors to follow so that the entire industry will be transformed. While many industry participants may benefit in the process, the innovator can benefit most if it can shift competition in directions where it can excel.

An industry's structure can be reshaped in two ways: by redividing profitability in favor of incumbents or by expanding the overall profit pool. Redividing the industry pie aims to increase the share of profits to industry competitors instead of to suppliers, buyers, substitutes, and keeping out potential entrants. Expanding the profit pool involves increasing the overall pool of economic value generated by the industry in which rivals, buyers, and suppliers can all share.

Redividing profitability. To capture more profits for industry rivals, the starting point is to determine which force or forces are currently constraining industry profitability and address them. A company can potentially influence all of the competitive forces. The strategist's goal here is to reduce the share of profits that leak to suppliers, buyers, and substitutes or are sacrificed to deter entrants.

To neutralize supplier power, for example, a firm can standardize specifications for parts to make it easier to switch among suppliers. It can cultivate additional vendors, or alter technology to avoid a powerful supplier group altogether. To counter customer power, companies may expand services that raise buyers' switching costs or find alternative means of reaching customers to neutralize powerful channels. To temper profit-eroding price rivalry, companies can invest more heavily in unique products, as pharmaceutical firms have done, or expand support services to customers. To scare off entrants, incumbents can elevate the fixed cost of competing—for instance, by escalating their R&D or marketing expenditures. To limit the

threat of substitutes, companies can offer better value through new features or wider product accessibility. When soft-drink producers introduced vending machines and convenience store channels, for example, they dramatically improved the availability of soft drinks relative to other beverages.

Sysco, the largest food-service distributor in North America, offers a revealing example of how an industry leader can change the structure of an industry for the better. Food-service distributors purchase food and related items from farmers and food processors. They then warehouse and deliver these items to restaurants, hospitals, employer cafeterias, schools, and other food-service institutions. Given low barriers to entry, the food-service distribution industry has historically been highly fragmented, with numerous local competitors. While rivals try to cultivate customer relationships, buyers are price sensitive because food represents a large share of their costs. Buyers can also choose the substitute approaches of purchasing directly from manufacturers or using retail sources, avoiding distributors altogether. Suppliers wield bargaining power: They are often large companies with strong brand names that food preparers and consumers recognize. Average profitability in the industry has been modest.

Defining the Relevant Industry

DEFINING THE INDUSTRY IN WHICH competition actually takes place is important for good industry analysis, not to mention for developing strategy and setting business unit boundaries. Many strategy errors emanate from mistaking the relevant industry, defining it too broadly or too narrowly. Defining the industry too broadly obscures differences among products, customers, or geographic regions that are important to competition, strategic positioning, and profitability. Defining the industry too narrowly overlooks commonalities and linkages across related products or geographic markets that are crucial to competitive advantage. Also, strategists must be sensitive to the possibility that industry boundaries can shift.

The boundaries of an industry consist of two primary dimensions. First is the *scope of products or services*. For example, is motor oil used in cars part of the same industry as motor oil used in heavy trucks and stationary engines, or are these different industries? The second dimension is *geographic scope*. Most industries are present in many parts of the world. However, is competition contained within each state, or is it national? Does competition take place within regions such as Europe or North America, or is there a single global industry?

The five forces are the basic tool to resolve these questions. If industry structure for two products is the same or very similar (that is, if they have the same buyers, suppliers, barriers to entry, and so forth), then the products are best treated as being part of the same industry. If industry structure differs markedly, however, the two products may be best understood as separate industries.

In lubricants, the oil used in cars is similar or even identical to the oil used in trucks, but the similarity largely ends there. Automotive motor oil is sold to fragmented, generally unsophisticated customers through

numerous and often powerful channels, using extensive advertising. Products are packaged in small containers and logistical costs are high, necessitating local production. Truck and power generation lubricants are sold to entirely different buyers in entirely different ways using a separate supply chain. Industry structure (buyer power, barriers to entry, and so forth) is substantially different. Automotive oil is thus a distinct industry from oil for truck and stationary engine uses. Industry profitability will differ in these two cases, and a lubricant company will need a separate strategy for competing in each area.

Differences in the five competitive forces also reveal the geographic scope of competition. If an industry has a similar structure in every country (rivals, buyers, and so on), the presumption is that competition is global, and the five forces analyzed from a global perspective will set average profitability. A single global strategy is needed. If an industry has quite different structures in different geographic regions, however, each region may well be a distinct industry. Otherwise, competition would have leveled the differences. The five forces analyzed for each region will set profitability there.

The extent of differences in the five forces for related products or across geographic areas is a matter of degree, making industry definition often a matter of judgment. A rule of thumb is that where the differences in any one force are large, and where the differences involve more than one force, distinct industries may well be present.

Fortunately, however, even if industry boundaries are drawn incorrectly, careful five forces analysis should reveal important competitive threats. A closely related product omitted from the industry definition will show up as a substitute, for example, or competitors overlooked as rivals will be recognized as potential entrants. At the same time, the five forces analysis should reveal major differences within overly broad industries that will indicate the need to adjust industry boundaries or strategies.

Sysco recognized that, given its size and national reach, it might change this state of affairs. It led the move to introduce private-label distributor brands with specifications tailored to the food-service market, moderating

supplier power. Sysco emphasized value-added services to buyers such as credit, menu planning, and inventory management to shift the basis of competition away from just price. These moves, together with stepped-up investments in information technology and regional distribution centers, substantially raised the bar for new entrants while making the substitutes less attractive. Not surprisingly, the industry has been consolidating, and industry profitability appears to be rising.

Industry leaders have a special responsibility for improving industry structure. Doing so often requires resources that only large players possess. Moreover, an improved industry structure is a public good because it benefits every firm in the industry, not just the company that initiated the improvement. Often, it is more in the interests of an industry leader than any other participant to invest for the common good because leaders will usually benefit the most. Indeed, improving the industry may be a leader's most profitable strategic opportunity, in part because attempts to gain further market share can trigger strong reactions from rivals, customers, and even suppliers.

Typical Steps in Industry Analysis

Define the relevant industry:

- What products are in it? Which ones are part of another distinct industry?
- What is the geographic scope of competition?

Identify the participants and segment them into groups, if appropriate:

Who are

- the buyers and buyer groups?
- the suppliers and supplier groups?
- the competitors?
- the substitutes?
- the potential entrants?

Assess the underlying drivers of each competitive force to determine which forces are strong and which are weak and why.

Determine overall industry structure, and test the analysis for consistency:

- Why is the level of profitability what it is?
- Which are the *controlling* forces for profitability?
- Is the industry analysis consistent with actual long-run profitability?
- Are more-profitable players better positioned in relation to the five forces?

Analyze recent and likely future changes in each force, both positive and negative.

Identify aspects of industry structure that might be influenced by competitors, by new entrants, or by your company.

There is a dark side to shaping industry structure that is equally important to understand. Ill-advised changes in competitive positioning and operating practices can *undermine* industry structure. Faced with pressures to gain market share or enamored with innovation for its own sake, managers may trigger new kinds of competition that no incumbent can win. When taking actions to improve their own company's competitive advantage, then, strategists should ask whether they are setting in motion dynamics that will undermine industry structure in the long run. In the early days of the personal computer industry, for instance, IBM tried to make up for its late entry by offering an open architecture that would set industry standards and attract complementary makers of application software and peripherals. In the process, it ceded ownership of the critical components of the PC—the operating system and the microprocessor—to Microsoft and Intel. By standardizing PCs, it encouraged price-based rivalry and shifted power to suppliers. Consequently, IBM became the temporarily dominant firm in an industry with an enduringly unattractive structure.

Expanding the profit pool. When overall demand grows, the industry's quality level rises, intrinsic costs are reduced, or waste is eliminated, the pie

expands. The total pool of value available to competitors, suppliers, and buyers grows. The total profit pool expands, for example, when channels become more competitive or when an industry discovers latent buyers for its product that are not currently being served. When soft-drink producers rationalized their independent bottler networks to make them more efficient and effective, both the soft-drink companies and the bottlers benefited. Overall value can also expand when firms work collaboratively with suppliers to improve coordination and limit unnecessary costs incurred in the supply chain. This lowers the inherent cost structure of the industry, allowing higher profit, greater demand through lower prices, or both. Or, agreeing on quality standards can bring up industrywide quality and service levels, and hence prices, benefiting rivals, suppliers, and customers.

Expanding the overall profit pool creates win-win opportunities for multiple industry participants. It can also reduce the risk of destructive rivalry that arises when incumbents attempt to shift bargaining power or capture more market share. However, expanding the pie does not reduce the importance of industry structure. How the expanded pie is divided will ultimately be determined by the five forces. The most successful companies are those that expand the industry profit pool in ways that allow them to share disproportionately in the benefits.

Defining the industry

The five competitive forces also hold the key to defining the relevant industry (or industries) in which a company competes. Drawing industry boundaries correctly, around the arena in which competition actually takes place, will clarify the causes of profitability and the appropriate unit for setting strategy. A company needs a separate strategy for each distinct industry. Mistakes in industry definition made by competitors present opportunities for staking out superior strategic positions. (See the sidebar “Defining the Relevant Industry.”)

Competition and Value

The competitive forces reveal the drivers of industry competition. A company strategist who understands that competition extends well beyond existing rivals will detect wider competitive threats and be better equipped to address them. At the same time, thinking comprehensively about an industry's structure can uncover opportunities: differences in customers, suppliers, substitutes, potential entrants, and rivals that can become the basis for distinct strategies yielding superior performance. In a world of more open competition and relentless change, it is more important than ever to think structurally about competition.

Understanding industry structure is equally important for investors as for managers. The five competitive forces reveal whether an industry is truly attractive, and they help investors anticipate positive or negative shifts in industry structure before they are obvious. The five forces distinguish short-term blips from structural changes and allow investors to take advantage of undue pessimism or optimism. Those companies whose strategies have industry-transforming potential become far clearer. This deeper thinking about competition is a more powerful way to achieve genuine investment success than the financial projections and trend extrapolation that dominate today's investment analysis.

Common Pitfalls

In conducting the analysis avoid the following common mistakes:

- Defining the industry too broadly or too narrowly.
- Making lists instead of engaging in rigorous analysis.
- Paying equal attention to all of the forces rather than digging deeply into the most important ones.
- Confusing effect (price sensitivity) with cause (buyer economics).
- Using static analysis that ignores industry trends.
- Confusing cyclical or transient changes with true structural changes.
- Using the framework to declare an industry attractive or unattractive rather than using it to guide strategic choices.

If both executives and investors looked at competition this way, capital markets would be a far more effective force for company success and economic prosperity. Executives and investors would both be focused on the same fundamentals that drive sustained profitability. The conversation between investors and executives would focus on the structural, not the transient. Imagine the improvement in company performance—and in the economy as a whole—if all the energy expended in “pleasing the Street” were redirected toward the factors that create true economic value.

Originally published in January 2008. Reprint R0801E.

Notes

[1.](#) For a discussion of the value chain framework, see Michael E. Porter, *Competitive Advantage: Creating and Sustaining Superior Performance* (The Free Press, 1998).

[2.](#) For a discussion of how internet technology improves the attractiveness of some industries while eroding the profitability of others, see Michael E. Porter, “Strategy and the Internet” (HBR, March 2001).

[3.](#) See, for instance, Adam M. Brandenburger and Barry J. Nalebuff, *Co-opetition* (Currency Doubleday, 1996).

Building Your Company's Vision

by James C. Collins and Jerry I. Porras

*We shall not cease from exploration/And the end of all our
exploring/Will be to arrive where we started/And know the place for the
first time.*

—T.S. Eliot, *Four Quartets*

COMPANIES THAT ENJOY ENDURING success have core values and a core purpose that remain fixed while their business strategies and practices endlessly adapt to a changing world. The dynamic of preserving the core while stimulating progress is the reason that companies such as Hewlett-Packard, 3M, Johnson & Johnson, Procter & Gamble, Merck, Sony, Motorola, and Nordstrom became elite institutions able to renew themselves and achieve superior long-term performance. Hewlett-Packard employees have long known that radical change in operating practices, cultural norms, and business strategies does not mean losing the spirit of the HP Way—the company's core principles. Johnson & Johnson continually questions its structure and revamps its processes while preserving the ideals embodied in its credo. In 1996, 3M sold off several of its large mature businesses—a dramatic move that surprised the business press—to refocus on its enduring core purpose of solving unsolved problems innovatively. We studied companies such as these in our research for *Built to Last: Successful Habits of Visionary Companies* and found that they have outperformed the general

stock market by a factor of 12 since 1925.

Truly great companies understand the difference between what should never change and what should be open for change, between what is genuinely sacred and what is not. This rare ability to manage continuity and change—requiring a consciously practiced discipline—is closely linked to the ability to develop a vision. Vision provides guidance about what core to preserve and what future to stimulate progress toward. But *vision* has become one of the most overused and least understood words in the language, conjuring up different images for different people: of deeply held values, outstanding achievement, societal bonds, exhilarating goals, motivating forces, or *raison d'être*. We recommend a conceptual framework to define vision, add clarity and rigor to the vague and fuzzy concepts swirling around that trendy term, and give practical guidance for articulating a coherent vision within an organization. It is a prescriptive framework rooted in six years of research and refined and tested by our ongoing work with executives from a great variety of organizations around the world.

A well-conceived vision consists of two major components: *core ideology* and *envisioned future*. (See the exhibit “Articulating a vision.”) Core ideology, the yin in our scheme, defines what we stand for and why we exist. Yin is unchanging and complements yang, the envisioned future. The envisioned future is what we aspire to become, to achieve, to create—something that will require significant change and progress to attain.

Core Ideology

Core ideology defines the enduring character of an organization—a consistent identity that transcends product or market life cycles, technological breakthroughs, management fads, and individual leaders. In fact, the most lasting and significant contribution of those who build visionary companies is the core ideology. As Bill Hewlett said about his longtime friend and business partner David Packard upon Packard's death not long ago, "As far as the company is concerned, the greatest thing he left behind him was a code of ethics known as the HP Way." HP's core ideology, which has guided the company since its inception more than 50 years ago, includes a deep respect for the individual, a dedication to affordable quality and reliability, a commitment to community responsibility (Packard himself bequeathed his \$4.3 billion of Hewlett-Packard stock to a charitable foundation), and a view that the company exists to make technical contributions for the advancement and welfare of humanity. Company builders such as David Packard, Masaru Ibuka of Sony, George Merck of Merck, William McKnight of 3M, and Paul Galvin of Motorola understood that it is more important to know who you are than where you are going, for where you are going will change as the world around you changes. Leaders die, products become obsolete, markets change, new technologies emerge, and management fads come and go, but core ideology in a great company endures as a source of guidance and inspiration.

Idea in Brief

Hewlett-Packard. 3M. Sony. Companies with exceptionally durable visions that are “built to last.” What distinguishes their visions from most others, those empty muddles that get revised with every passing business fad, but never prompt anything more than a yawn? Enduring companies have clear plans for how they will advance into an uncertain future. But they are equally clear about how they will remain steadfast, about the values and purposes they will always stand for. This *Harvard Business Review* article describes the two components of any lasting vision: **core ideology** and an **envisioned future**.

Core ideology provides the glue that holds an organization together as it grows, decentralizes, diversifies, expands globally, and develops workplace diversity. Think of it as analogous to the principles of Judaism that held the Jewish people together for centuries without a homeland, even as they spread throughout the Diaspora. Or think of the truths held to be self-evident in the Declaration of Independence, or the enduring ideals and principles of the scientific community that bond scientists from every nationality together in the common purpose of advancing human knowledge. Any effective vision must embody the core ideology of the organization, which in turn consists of two distinct parts: core values, a system of guiding principles and tenets; and core purpose, the organization’s most fundamental reason for existence.

Idea in Practice

A company's practices and strategies should change continually; its core ideology should not. Core ideology defines a company's timeless character. It's the glue that holds the enterprise together even when everything else is up for grabs. Core ideology is something you *discover*—by looking inside. It's not something you can invent, much less fake.

A core ideology has two parts:

1. **Core values are the handful of guiding principles by which a company navigates.** They require no external justification. For example, Disney's core values of imagination and wholesomeness stem from the founder's belief that these should be nurtured for their own sake, not merely to capitalize on a business opportunity. Instead of changing its core values, a great company will change its markets—seek out different customers—in order to remain true to its core values.
2. **Core purpose is an organization's most fundamental reason for being.** It should not be confused with the company's current product lines or customer segments. Rather, it reflects people's idealistic motivations for doing the company's work. Disney's core purpose is to make people happy—not to build theme parks and make cartoons.

An envisioned future, the second component of an effective vision, has two elements:

1. **Big, Hairy, Audacious Goals (BHAGs) are ambitious plans**

that rev up the entire organization. They typically require 10 to 30 years' work to complete.

2. **2. Vivid descriptions paint a picture of what it will be like to achieve the BHAGs.** They make the goals vibrant, engaging—and tangible.

Example: In the 1950s, Sony's goal was to “become the company most known for changing the worldwide poor-quality image of Japanese products.” It made this BHAG vivid by adding, “Fifty years from now, our brand name will be as well known as any in the world ... and will signify innovation and quality... . ‘Made in Japan’ will mean something fine, not something shoddy.”

Don't confuse your company's core ideology with its envisioned future—in particular, don't confuse a BHAG with a core purpose. A BHAG is a clearly articulated goal that is reachable within 10 to 30 years. But your core purpose can never be completed.

Core values

Core values are the essential and enduring tenets of an organization. A small set of timeless guiding principles, core values require no external justification; they have *intrinsic* value and importance to those inside the organization. The Walt Disney Company's core values of imagination and wholesomeness stem not from market requirements but from the founder's inner belief that imagination and wholesomeness should be nurtured for their own sake. William Procter and James Gamble didn't instill in P&G's culture a focus on product excellence merely as a strategy for success but as an almost religious tenet. And that value has been passed down for more than 15 decades by P&G people. Service to the customer—even to the point of subservience—is a way of life at Nordstrom that traces its roots back to 1901, eight decades before customer service programs became stylish. For Bill Hewlett and David Packard, respect for the individual was first and foremost a deep personal value; they didn't get it from a book or hear it from a management guru. And Ralph S. Larsen, CEO of Johnson & Johnson, puts it this way: "The core values embodied in our credo might be a competitive advantage, but that is not *why* we have them. We have them because they define for us what we stand for, and we would hold them even if they became a competitive *disadvantage* in certain situations."

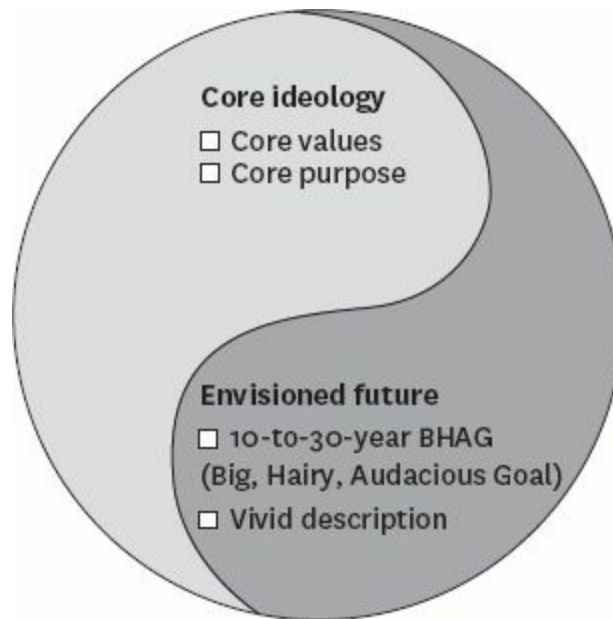
The point is that a great company decides for itself what values it holds to be core, largely independent of the current environment, competitive requirements, or management fads. Clearly, then, there is no universally right set of core values. A company need not have as its core value customer service (Sony doesn't) or respect for the individual (Disney doesn't) or quality (Wal-Mart Stores doesn't) or market focus (HP doesn't) or teamwork (Nordstrom doesn't). A company might have operating practices and business strategies around those qualities without having them at the essence of its being. Furthermore, great companies need not have likable or humanistic core values, although many do. The key is not *what* core values an organization has but that it has core values at all.

Companies tend to have only a few core values, usually between three and five. In fact, we found that none of the visionary companies we studied in our

book had more than five: most had only three or four. (See the sidebar “Core Values Are a Company’s Essential Tenets.”) And, indeed, we should expect that. Only a few values can be truly *core*—that is, so fundamental and deeply held that they will change seldom, if ever.

To identify the core values of your own organization, push with relentless honesty to define what values are truly central. If you articulate more than five or six, chances are that you are confusing core values (which do not change) with operating practices, business strategies, or cultural norms (which should be open to change). Remember, the values must stand the test of time. After you’ve drafted a preliminary list of the core values, ask about each one, If the circumstances changed and *penalized* us for holding this core value, would we still keep it? If you can’t honestly answer yes, then the value is not core and should be dropped from consideration.

Articulating a vision



A high-technology company wondered whether it should put quality on its list of core values. The CEO asked, “Suppose in ten years quality doesn’t make a hoot of difference in our markets. Suppose the only thing that matters is sheer speed and horsepower but not quality. Would we still want to put quality on our list of core values?” The members of the management team looked around at one another and finally said no. Quality stayed in the *strategy* of the company, and quality-improvement programs remained in place as a mechanism for stimulating progress; but quality did not make the list of core values.

The same group of executives then wrestled with leading-edge innovation as a core value. The CEO asked, “Would we keep innovation on the list as a core value, no matter how the world around us changed?” This time, the management team gave a resounding yes. The managers’ outlook might be summarized as, “We always want to do leading-edge innovation. That’s who we are. It’s really important to us and always will be. No matter what. And if our current markets don’t value it, we will find markets that do.” Leading-

edge innovation went on the list and will stay there. A company should not change its core values in response to market changes; rather, it should change markets, if necessary, to remain true to its core values.

Who should be involved in articulating the core values varies with the size, age, and geographic dispersion of the company, but in many situations we have recommended what we call a *Mars Group*. It works like this: Imagine that you've been asked to re-create the very best attributes of your organization on another planet but you have seats on the rocket ship for only five to seven people. Whom should you send? Most likely, you'll choose the people who have a gut-level understanding of your core values, the highest level of credibility with their peers, and the highest levels of competence. We'll often ask people brought together to work on core values to nominate a Mars Group of five to seven individuals (not necessarily all from the assembled group). Invariably, they end up selecting highly credible representatives who do a super job of articulating the core values precisely because they are exemplars of those values—a representative slice of the company's genetic code.

Even global organizations composed of people from widely diverse cultures can identify a set of shared core values. The secret is to work from the individual to the organization. People involved in articulating the core values need to answer several questions: What core values do you personally bring to your work? (These should be so fundamental that you would hold them regardless of whether or not they were rewarded.) What would you tell your children are the core values that you hold at work and that you hope *they* will hold when they become working adults? If you awoke tomorrow morning with enough money to retire for the rest of your life, would you continue to live those core values? Can you envision them being as valid for you 100 years from now as they are today? Would you want to hold those core values, even if at some point one or more of them became a competitive *disadvantage*? If you were to start a new organization tomorrow in a different line of work, what core values would you build into the new organization regardless of its industry? The last three questions are particularly important because they make the crucial distinction between enduring core values that should not change and practices and strategies that should be changing all the time.

Core Values Are a Company's Essential Tenets

Merck

- Corporate social responsibility
- Unequivocal excellence in all aspects of the company
- Science-based innovation
- Honesty and integrity
- Profit, but profit from work that benefits humanity

Nordstrom

- Service to the customer above all else
- Hard work and individual productivity
- Never being satisfied
- Excellence in reputation; being part of something special

Philip Morris

- The right to freedom of choice
- Winning—beating others in a good fight
- Encouraging individual initiative
- Opportunity based on merit; no one is entitled to anything
- Hard work and continuous self-improvement

Sony

- Elevation of the Japanese culture and national status
- Being a pioneer—not following others; doing the impossible
- Encouraging individual ability and creativity

Walt Disney

- No cynicism

- Nurturing and promulgation of “wholesome American values”
- Creativity, dreams, and imagination
- Fanatical attention to consistency and detail
- Preservation and control of the Disney magic

Core purpose

Core purpose, the second part of core ideology, is the organization's reason for being. An effective purpose reflects people's idealistic motivations for doing the company's work. It doesn't just describe the organization's output or target customers; it captures the soul of the organization. (See the sidebar "Core Purpose Is a Company's Reason for Being.") Purpose, as illustrated by a speech David Packard gave to HP employees in 1960, gets at the deeper reasons for an organization's existence beyond just making money. Packard said,

I want to discuss why a company exists in the first place. In other words, why are we here? I think many people assume, wrongly, that a company exists simply to make money. While this is an important result of a company's existence, we have to go deeper and find the real reasons for our being. As we investigate this, we inevitably come to the conclusion that a group of people get together and exist as an institution that we call a company so they are able to accomplish something collectively that they could not accomplish separately—they make a contribution to society, a phrase which sounds trite but is fundamental . . . You can look around [in the general business world and] see people who are interested in money and nothing else, but the underlying drives come largely from a desire to do something else: to make a product, to give a service—generally to do something which is of value.¹

Purpose (which should last at least 100 years) should not be confused with specific goals or business strategies (which should change many times in 100 years). Whereas you might achieve a goal or complete a strategy, you cannot fulfill a purpose; it is like a guiding star on the horizon—forever pursued but never reached. Yet although purpose itself does not change, it does inspire change. The very fact that purpose can never be fully realized means that an

organization can never stop stimulating change and progress.

In identifying purpose, some companies make the mistake of simply describing their current product lines or customer segments. We do not consider the following statement to reflect an effective purpose: “We exist to fulfill our government charter and participate in the secondary mortgage market by packaging mortgages into investment securities.” The statement is merely descriptive. A far more effective statement of purpose would be that expressed by the executives of the Federal National Mortgage Association, Fannie Mae: “To strengthen the social fabric by continually democratizing home ownership.” The secondary mortgage market as we know it might not even exist in 100 years, but strengthening the social fabric by continually democratizing home ownership can be an enduring purpose, no matter how much the world changes. Guided and inspired by this purpose, Fannie Mae launched in the early 1990s a series of bold initiatives, including a program to develop new systems for reducing mortgage underwriting costs by 40% in five years; programs to eliminate discrimination in the lending process (backed by \$5 billion in underwriting experiments); and an audacious goal to provide, by the year 2000, \$1 trillion targeted at 10 million families that had traditionally been shut out of home ownership—minorities, immigrants, and low-income groups.

Similarly, 3M defines its purpose not in terms of adhesives and abrasives but as the perpetual quest to solve unsolved problems innovatively—a purpose that is always leading 3M into new fields. McKinsey & Company’s purpose is not to do management consulting but to help corporations and governments be more successful: in 100 years, it might involve methods other than consulting. Hewlett-Packard doesn’t exist to make electronic test and measurement equipment but to make technical contributions that improve people’s lives—a purpose that has led the company far afield from its origins in electronic instruments. Imagine if Walt Disney had conceived of his company’s purpose as to make cartoons, rather than to make people happy; we probably wouldn’t have Mickey Mouse, Disneyland, EPCOT Center, or the Anaheim Mighty Ducks Hockey Team.

One powerful method for getting at purpose is the *five whys*. Start with the descriptive statement We make X products or We deliver X services, and then ask, Why is that important? five times. After a few whys, you’ll find that you’re getting down to the fundamental purpose of the organization.

We used this method to deepen and enrich a discussion about purpose

when we worked with a certain market-research company. The executive team first met for several hours and generated the following statement of purpose for their organization: To provide the best market-research data available. We then asked the following question: Why is it important to provide the best market-research data available? After some discussion, the executives answered in a way that reflected a deeper sense of their organization's purpose: To provide the best market-research data available so that our customers will understand their markets better than they could otherwise. A further discussion let team members realize that their sense of self-worth came not just from helping customers understand their markets better but also from making a *contribution* to their customers' success. This introspection eventually led the company to identify its purpose as: To contribute to our customers' success by helping them understand their markets. With this purpose in mind, the company now frames its product decisions not with the question Will it sell? but with the question Will it make a contribution to our customers' success?

Core Purpose Is a Company's Reason for Being

3M: To solve unsolved problems innovatively

Cargill: To improve the standard of living around the world

Fannie Mae: To strengthen the social fabric by continually democratizing home ownership

Hewlett-Packard: To make technical contributions for the advancement and welfare of humanity

Lost Arrow Corporation: To be a role model and a tool for social change

Pacific Theatres: To provide a place for people to flourish and to enhance the community

Mary Kay Cosmetics: To give unlimited opportunity to women

McKinsey & Company: To help leading corporations and governments be more successful

Merck: To preserve and improve human life

Nike: To experience the emotion of competition, winning, and crushing competitors

Sony: To experience the joy of advancing and applying technology for the benefit of the public

Telecare Corporation: To help people with mental impairments realize their full potential

Wal-Mart: To give ordinary folk the chance to buy the same things as

rich people

Walt Disney: To make people happy

The five whys can help companies in any industry frame their work in a more meaningful way. An asphalt and gravel company might begin by saying, We make gravel and asphalt products. After a few whys, it could conclude that making asphalt and gravel is important because the quality of the infrastructure plays a vital role in people's safety and experience; because driving on a pitted road is annoying and dangerous; because 747s cannot land safely on runways built with poor workmanship or inferior concrete; because buildings with substandard materials weaken with time and crumble in earthquakes. From such introspection may emerge this purpose: To make people's lives better by improving the quality of man-made structures. With a sense of purpose very much along those lines, Granite Rock Company of Watsonville, California, won the Malcolm Baldrige National Quality Award—not an easy feat for a small rock quarry and asphalt company. And Granite Rock has gone on to be one of the most progressive and exciting companies we've encountered in *any* industry.

Notice that none of the core purposes fall into the category “maximize shareholder wealth.” A primary role of core purpose is to guide and inspire. Maximizing shareholder wealth does not inspire people at all levels of an organization, and it provides precious little guidance. Maximizing shareholder wealth is the standard off-the-shelf purpose for those organizations that have not yet identified their true core purpose. It is a substitute—and a weak one at that.

When people in great organizations talk about their achievements, they say very little about earnings per share. Motorola people talk about impressive quality improvements and the effect of the products they create on the world. Hewlett-Packard people talk about their technical contributions to the marketplace. Nordstrom people talk about heroic customer service and remarkable individual performance by star salespeople. When a Boeing engineer talks about launching an exciting and revolutionary new aircraft, she does not say, “I put my heart and soul into this project because it would add 37 cents to our earnings per share.”

One way to get at the purpose that lies beyond merely maximizing

shareholder wealth is to play the “Random Corporate Serial Killer” game. It works like this: Suppose you could sell the company to someone who would pay a price that everyone inside and outside the company agrees is more than fair (even with a very generous set of assumptions about the expected future cash flows of the company). Suppose further that this buyer would guarantee stable employment for all employees at the same pay scale after the purchase but with no guarantee that those jobs would be in the same industry. Finally, suppose the buyer plans to kill the company after the purchase—its products or services would be discontinued, its operations would be shut down, its brand names would be shelved forever, and so on. The company would utterly and completely cease to exist. Would you accept the offer? Why or why not? What would be lost if the company ceased to exist? Why is it important that the company continue to exist? We’ve found this exercise to be very powerful for helping hard-nosed, financially focused executives reflect on their organization’s deeper reasons for being.

Another approach is to ask each member of the Mars Group, How could we frame the purpose of this organization so that if you woke up tomorrow morning with enough money in the bank to retire, you would nevertheless keep working here? What deeper sense of purpose would motivate you to continue to dedicate your precious creative energies to this company’s efforts?

As they move into the twenty-first century, companies will need to draw on the full creative energy and talent of their people. But why should people give full measure? As Peter Drucker has pointed out, the best and most dedicated people are ultimately volunteers, for they have the opportunity to do something else with their lives. Confronted with an increasingly mobile society, cynicism about corporate life, and an expanding entrepreneurial segment of the economy, companies more than ever need to have a clear understanding of their purpose in order to make work meaningful and thereby attract, motivate, and retain outstanding people.

Discovering Core Ideology

You do not create or set core ideology. You *discover* core ideology. You do not deduce it by looking at the external environment. You understand it by looking inside. Ideology has to be authentic. You cannot fake it. Discovering core ideology is not an intellectual exercise. Do not ask, What core values should we hold? Ask instead, What core values do we truly and passionately hold? You should not confuse values that you think the organization ought to have—but does not—with authentic core values. To do so would create cynicism throughout the organization. (“Who’re they trying to kid? We all know that isn’t a core value around here!”) Aspirations are more appropriate as part of your envisioned future or as part of your strategy, not as part of the core ideology. However, authentic core values that have weakened over time can be considered a legitimate part of the core ideology—as long as you acknowledge to the organization that you must work hard to revive them.

Also be clear that the role of core ideology is to guide and inspire, not to differentiate. Two companies can have the same core values or purpose. Many companies could have the purpose to make technical contributions, but few live it as passionately as Hewlett-Packard. Many companies could have the purpose to preserve and improve human life, but few hold it as deeply as Merck. Many companies could have the core value of heroic customer service, but few create as intense a culture around that value as Nordstrom. Many companies could have the core value of innovation, but few create the powerful alignment mechanisms that stimulate the innovation we see at 3M. The authenticity, the discipline, and the consistency with which the ideology is lived—not the content of the ideology—differentiate visionary companies from the rest of the pack.

Core ideology needs to be meaningful and inspirational only to people inside the organization; it need not be exciting to outsiders. Why not? Because it is the people inside the organization who need to commit to the organizational ideology over the long term. Core ideology can also play a role in determining who *is* inside and who is not. A clear and well-articulated

ideology attracts to the company people whose personal values are compatible with the company's core values; conversely, it repels those whose personal values are incompatible. You cannot impose new core values or purpose on people. Nor are core values and purpose things people can buy into. Executives often ask, How do we get people to share our core ideology? You don't. You can't. Instead, find people who are predisposed to share your core values and purpose; attract and retain those people; and let those who do not share your core values go elsewhere. Indeed, the very process of articulating core ideology may cause some people to leave when they realize that they are not personally compatible with the organization's core. Welcome that outcome. It is certainly desirable to retain within the core ideology a diversity of people and viewpoints. People who share the same core values and purpose do not necessarily all think or look the same.

Don't confuse core ideology itself with core-ideology statements. A company can have a very strong core ideology without a formal statement. For example, Nike has not (to our knowledge) formally articulated a statement of its core purpose. Yet, according to our observations, Nike has a powerful core purpose that permeates the entire organization: to experience the emotion of competition, winning, and crushing competitors. Nike has a campus that seems more like a shrine to the competitive spirit than a corporate office complex. Giant photos of Nike heroes cover the walls, bronze plaques of Nike athletes hang along the Nike Walk of Fame, statues of Nike athletes stand alongside the running track that rings the campus, and buildings honor champions such as Olympic marathoner Joan Benoit, basketball superstar Michael Jordan, and tennis pro John McEnroe. Nike people who do not feel stimulated by the competitive spirit and the urge to be ferocious simply do not last long in the culture. Even the company's name reflects a sense of competition: Nike is the Greek goddess of victory. Thus, although Nike has not formally articulated its purpose, it clearly has a strong one.

Identifying core values and purpose is therefore not an exercise in wordsmithery. Indeed, an organization will generate a variety of statements over time to describe the core ideology. In Hewlett-Packard's archives, we found more than half a dozen distinct versions of the HP Way, drafted by David Packard between 1956 and 1972. All versions stated the same principles, but the words used varied depending on the era and the circumstances. Similarly, Sony's core ideology has been stated many

different ways over the company's history. At its founding, Masaru Ibuka described two key elements of Sony's ideology: "We shall welcome technical difficulties and focus on highly sophisticated technical products that have great usefulness for society regardless of the quantity involved; we shall place our main emphasis on ability, performance, and personal character so that each individual can show the best in ability and skill."² Four decades later, this same concept appeared in a statement of core ideology called Sony Pioneer Spirit: "Sony is a pioneer and never intends to follow others. Through progress, Sony wants to serve the whole world. It shall be always a seeker of the unknown... . Sony has a principle of respecting and encouraging one's ability ... and always tries to bring out the best in a person. This is the vital force of Sony."³ Same core values, different words.

You should therefore focus on getting the content right—on capturing the essence of the core values and purpose. The point is not to create a perfect statement but to gain a deep understanding of your organization's core values and purpose, which can then be expressed in a multitude of ways. In fact, we often suggest that once the core has been identified, managers should generate their own statements of the core values and purpose to share with their groups.

Finally, don't confuse core ideology with the concept of core competence. Core competence is a strategic concept that defines your organization's capabilities—what you are particularly good at—whereas core ideology captures what you stand for and why you exist. Core competencies should be well aligned with a company's core ideology and are often rooted in it; but they are not the same thing. For example, Sony has a core competence of miniaturization—a strength that can be strategically applied to a wide array of products and markets. But it does not have a core *ideology* of miniaturization. Sony might not even have miniaturization as part of its strategy in 100 years, but to remain a great company, it will still have the same core values described in the Sony Pioneer Spirit and the same fundamental reason for being—namely, to advance technology for the benefit of the general public. In a visionary company like Sony, core competencies change over the decades, whereas core ideology does not.

Once you are clear about the core ideology, you should feel free to change absolutely *anything* that is not part of it. From then on, whenever someone says something should not change because "it's part of our culture" or "we've always done it that way" or any such excuse, mention this simple

rule: If it's not core, it's up for change. The strong version of the rule is, *If it's not core, change it!* Articulating core ideology is just a starting point, however. You also must determine what type of progress you want to stimulate.

Envisioned Future

The second primary component of the vision framework is *envisioned future*. It consists of two parts: a 10-to-30-year audacious goal plus vivid descriptions of what it will be like to achieve the goal. We recognize that the phrase *envisioned future* is somewhat paradoxical. On the one hand, it conveys concreteness—something visible, vivid, and real. On the other hand, it involves a time yet unrealized—with its dreams, hopes, and aspirations.

Vision-level BHAG

We found in our research that visionary companies often use bold missions—or what we prefer to call *BHAGs* (pronounced BEE-hags and shorthand for Big, Hairy, Audacious Goals)—as a powerful way to stimulate progress. All companies have goals. But there is a difference between merely having a goal and becoming committed to a huge, daunting challenge—such as climbing Mount Everest. A true BHAG is clear and compelling, serves as a unifying focal point of effort, and acts as a catalyst for team spirit. It has a clear finish line, so the organization can know when it has achieved the goal; people like to shoot for finish lines. A BHAG engages people—it reaches out and grabs them. It is tangible, energizing, highly focused. People get it right away; it takes little or no explanation. For example, NASA’s 1960s moon mission didn’t need a committee of wordsmiths to spend endless hours turning the goal into a verbose, impossible-to-remember mission statement. The goal itself was so easy to grasp—so compelling in its own right—that it could be said 100 different ways yet be easily understood by everyone. Most corporate statements we’ve seen do little to spur forward movement because they do not contain the powerful mechanism of a BHAG.

Although organizations may have many BHAGs at different levels operating at the same time, vision requires a special type of BHAG—a vision-level BHAG that applies to the entire organization and requires 10 to 30 years of effort to complete. Setting the BHAG that far into the future requires thinking beyond the current capabilities of the organization and the current environment. Indeed, inventing such a goal forces an executive team to be visionary, rather than just strategic or tactical. A BHAG should not be a sure bet—it will have perhaps only a 50% to 70% probability of success—but the organization must believe that it can reach the goal anyway. A BHAG should require extraordinary effort and perhaps a little luck. We have helped companies create a vision-level BHAG by advising them to think in terms of four broad categories: target BHAGs, common-enemy BHAGs, role-model BHAGs, and internal-transformation BHAGs. (See the sidebar “Big, Hairy, Audacious Goals Aid Long-Term Vision.”)

Vivid description

In addition to vision-level BHAGs, an envisioned future needs what we call vivid description—that is, a vibrant, engaging, and specific description of what it will be like to achieve the BHAG. Think of it as translating the vision from words into pictures, of creating an image that people can carry around in their heads. It is a question of painting a picture with your words. Picture painting is essential for making the 10-to-30-year BHAG tangible in people's minds.

For example, Henry Ford brought to life the goal of democratizing the automobile with this vivid description: “I will build a motor car for the great multitude... . It will be so low in price that no man making a good salary will be unable to own one and enjoy with his family the blessing of hours of pleasure in God's great open spaces... . When I'm through, everybody will be able to afford one, and everyone will have one. The horse will have disappeared from our highways, the automobile will be taken for granted ... [and we will] give a large number of men employment at good wages.”

The components-support division of a computer-products company had a general manager who was able to describe vividly the goal of becoming one of the most sought-after divisions in the company: “We will be respected and admired by our peers. . . . Our solutions will be actively sought by the end-product divisions, who will achieve significant product ‘hits’ in the marketplace largely because of our technical contribution... . We will have pride in ourselves... . The best up-and-coming people in the company will seek to work in our division... . People will give unsolicited feedback that they love what they are doing... . [Our own] people will walk on the balls of their feet... . [They] will willingly work hard because they want to... . Both employees and customers will feel that our division has contributed to their life in a positive way.”

Big, Hairy, Audacious Goals Aid Long-Term Vision

Target BHAGs can be quantitative or qualitative

- Become a \$125 billion company by the year 2000 (Wal-Mart, 1990)
- Democratize the automobile (Ford Motor Company, early 1900s)
- Become the company most known for changing the worldwide poor-quality image of Japanese products (Sony, early 1950s)
- Become the most powerful, the most serviceable, the most far-reaching world financial institution that has ever been (City Bank, predecessor to Citicorp, 1915)
- Become the dominant player in commercial aircraft and bring the world into the jet age (Boeing, 1950)

Common-enemy BHAGs involve David-versus-Goliath thinking

- Knock off RJR as the number one tobacco company in the world (Philip Morris, 1950s)

- Crush Adidas (Nike, 1960s)
- *Yamaha wo tsubusu!* We will destroy Yamaha! (Honda, 1970s)

Role-model BHAGs suit up-and-coming organizations

- Become the Nike of the cycling industry (Giro Sport Design, 1986)
- Become as respected in 20 years as Hewlett-Packard is today (Watkins-Johnson, 1996)
- Become the Harvard of the West (Stanford University, 1940s)

Internal-transformation BHAGs suit large, established organizations

- Become number one or number two in every market we serve and revolutionize this company to have the strengths of a big company combined with the leanness and agility of a small company (General Electric Company, 1980s)
- Transform this company from a defense contractor into the best diversified high-technology company in the world (Rockwell, 1995)
- Transform this division from a poorly respected internal

products supplier to one of the most respected, exciting, and sought-after divisions in the company (Components Support Division of a computer products company, 1989)

In the 1930s, Merck had the BHAG to transform itself from a chemical manufacturer into one of the preeminent drug-making companies in the world, with a research capability to rival any major university. In describing this envisioned future, George Merck said at the opening of Merck's research facility in 1933, "We believe that research work carried on with patience and persistence will bring to industry and commerce new life; and we have faith that in this new laboratory, with the tools we have supplied, science will be advanced, knowledge increased, and human life win ever a greater freedom from suffering and disease... . We pledge our every aid that this enterprise shall merit the faith we have in it. Let your light so shine—that those who seek the Truth, that those who toil that this world may be a better place to live in, that those who hold aloft that torch of science and knowledge through these social and economic dark ages, shall take new courage and feel their hands supported."

Passion, emotion, and conviction are essential parts of the vivid description. Some managers are uncomfortable expressing emotion about their dreams, but that's what motivates others. Churchill understood that when he described the BHAG facing Great Britain in 1940. He did not just say, "Beat Hitler." He said, "Hitler knows he will have to break us on this island or lose the war. If we can stand up to him, all Europe may be free, and the life of the world may move forward into broad, sunlit uplands. But if we fail, the whole world, including the United States, including all we have known and cared for, will sink into the abyss of a new Dark Age, made more sinister and perhaps more protracted by the lights of perverted science. Let us therefore brace ourselves to our duties and so bear ourselves that if the British Empire and its Commonwealth last for a thousand years, men will still say, 'This was their finest hour.'"

A few key points

Don't confuse core ideology and envisioned future. In particular, don't confuse core purpose and BHAGs. Managers often exchange one for the other, mixing the two together or failing to articulate both as distinct items. Core purpose—not some specific goal—is the reason why the organization exists. A BHAG is a clearly articulated goal. Core purpose can never be completed, whereas the BHAG is reachable in 10 to 30 years. Think of the core purpose as the star on the horizon to be chased forever; the BHAG is the mountain to be climbed. Once you have reached its summit, you move on to other mountains.

Identifying core ideology is a discovery process, but setting the envisioned future is a creative process. We find that executives often have a great deal of difficulty coming up with an exciting BHAG. They want to analyze their way into the future. We have found, therefore, that some executives make more progress by starting first with the vivid description and backing from there into the BHAG. This approach involves starting with questions such as, We're sitting here in 20 years; what would we love to see? What should this company look like? What should it feel like to employees? What should it have achieved? If someone writes an article for a major business magazine about this company in 20 years, what will it say? One biotechnology company we worked with had trouble envisioning its future. Said one member of the executive team, "Every time we come up with something for the entire company, it is just too generic to be exciting—something banal like 'advance biotechnology worldwide.'" Asked to paint a picture of the company in 20 years, the executives mentioned such things as "on the cover of *Business Week* as a model success story ... the *Fortune* most admired top-ten list ... the best science and business graduates want to work here ... people on airplanes rave about one of our products to seatmates ... 20 consecutive years of profitable growth ... an entrepreneurial culture that has spawned half a dozen new divisions from within ... management gurus use us as an example of excellent management and progressive thinking," and so on. From this, they were able to set the goal of becoming as well respected as Merck or as Johnson & Johnson in biotechnology.

It makes no sense to analyze whether an envisioned future is the right one. With a creation—and the task is creation of a future, not prediction—there can be no right answer. Did Beethoven create the right Ninth Symphony? Did Shakespeare create the right *Hamlet*? We can't answer these questions; they're nonsense. The envisioned future involves such essential questions as Does it get our juices flowing? Do we find it stimulating? Does it spur forward momentum? Does it get people going? The envisioned future should be so exciting in its own right that it would continue to keep the organization motivated even if the leaders who set the goal disappeared. City Bank, the predecessor of Citicorp, had the BHAG “to become the most powerful, the most serviceable, the most far-reaching world financial institution that has ever been”—a goal that generated excitement through multiple generations until it was achieved. Similarly, the NASA moon mission continued to galvanize people even though President John F. Kennedy (the leader associated with setting the goal) died years before its completion.

To create an effective envisioned future requires a certain level of unreasonable confidence and commitment. Keep in mind that a BHAG is not just a goal; it is a Big, Hairy, Audacious Goal. It's not reasonable for a small regional bank to set the goal of becoming “the most powerful, the most serviceable, the most far-reaching world financial institution that has ever been,” as City Bank did in 1915. It's not a tepid claim that “we will democratize the automobile,” as Henry Ford said. It was almost laughable for Philip Morris—as the sixth-place player with 9% market share in the 1950s—to take on the goal of defeating Goliath RJ Reynolds Tobacco Company and becoming number one. It was hardly modest for Sony, as a small, cash-strapped venture, to proclaim the goal of changing the poor-quality image of Japanese products around the world. (See the sidebar “Putting It All Together: Sony in the 1950s.”) Of course, it's not only the audacity of the goal but also the level of commitment to the goal that counts. Boeing didn't just envision a future dominated by its commercial jets; it bet the company on the 707 and, later, on the 747. Nike's people didn't just talk about the idea of crushing Adidas; they went on a crusade to fulfill the dream. Indeed, the envisioned future should produce a bit of the “gulp factor”: when it dawns on people what it will take to achieve the goal, there should be an almost audible gulp.

But what about failure to realize the envisioned future? In our research, we found that the visionary companies displayed a remarkable ability to

achieve even their most audacious goals. Ford did democratize the automobile; Citicorp did become the most far-reaching bank in the world; Philip Morris did rise from sixth to first and beat RJ Reynolds worldwide; Boeing did become the dominant commercial aircraft company; and it looks like Wal-Mart will achieve its \$125 billion goal, even without Sam Walton. In contrast, the comparison companies in our research frequently did not achieve their BHAGs, if they set them at all. The difference does not lie in setting easier goals: the visionary companies tended to have even more audacious ambitions. The difference does not lie in charismatic, visionary leadership: the visionary companies often achieved their BHAGs without such larger-than-life leaders at the helm. Nor does the difference lie in better strategy: the visionary companies often realized their goals more by an organic process of “let’s try a lot of stuff and keep what works” than by well-laid strategic plans. Rather, their success lies in building the strength of their organization as their primary way of creating the future.

Why did Merck become the preeminent drug-maker in the world? Because Merck’s architects built the best pharmaceutical research and development organization in the world. Why did Boeing become the dominant commercial aircraft company in the world? Because of its superb engineering and marketing organization, which had the ability to make projects like the 747 a reality. When asked to name the most important decisions that have contributed to the growth and success of Hewlett-Packard, David Packard answered entirely in terms of decisions to build the strength of the organization and its people.

Putting It All Together: Sony in the 1950s

Core Ideology

Core Values

- Elevation of the Japanese culture and national status
- Being a pioneer—not following others; doing the impossible
- Encouraging individual ability and creativity

Purpose

To experience the sheer joy of innovation and the application of technology for the benefit and pleasure of the general public

Envisioned Future

BHAG

Become the company most known for changing the worldwide poor-quality image of Japanese products

Vivid Description

We will create products that become pervasive around the world... . We will be the first Japanese company to go into the U.S. market and distribute directly... . We will succeed with innovations that U.S. companies have failed at—such as the transistor radio... . Fifty years from now, our brand name will be as well known as any in the world ... and will signify innovation and quality that rival the most innovative companies anywhere... . “Made in Japan” will mean something fine, not something shoddy.

Finally, in thinking about the envisioned future, beware of the We've Arrived Syndrome—a complacent lethargy that arises once an organization has achieved one BHAG and fails to replace it with another. NASA suffered from that syndrome after the successful moon landings. After you've landed on the moon, what do you do for an encore? Ford suffered from the syndrome when, after it succeeded in democratizing the automobile, it failed to set a new goal of equal significance and gave General Motors the opportunity to jump ahead in the 1930s. Apple Computer suffered from the syndrome after achieving the goal of creating a computer that nontechies could use. Start-up companies frequently suffer from the We've Arrived Syndrome after going public or after reaching a stage in which survival no longer seems in question. An envisioned future helps an organization only as long as it hasn't yet been achieved. In our work with companies, we frequently hear executives say, "It's just not as exciting around here as it used to be; we seem to have lost our momentum." Usually, that kind of remark signals that the organization has climbed one mountain and not yet picked a new one to climb.

Many executives thrash about with mission statements and vision statements. Unfortunately, most of those statements turn out to be a muddled stew of values, goals, purposes, philosophies, beliefs, aspirations, norms, strategies, practices, and descriptions. They are usually a boring, confusing, structurally unsound stream of words that evoke the response "True, but who cares?" Even more problematic, seldom do these statements have a direct link to the fundamental dynamic of visionary companies: preserve the core and stimulate progress. That dynamic, not vision or mission statements, is the primary engine of enduring companies. Vision simply provides the context for bringing this dynamic to life. Building a visionary company requires 1% vision and 99% alignment. When you have superb alignment, a visitor could drop in from outer space and infer your vision from the operations and activities of the company without ever reading it on paper or meeting a single senior executive.

Creating alignment may be your most important work. But the first step will always be to recast your vision or mission into an effective context for building a visionary company. If you do it right, you shouldn't have to do it again for at least a decade.

Originally published in September 1996. Reprint 96501.

Notes

1. David Packard, speech given to Hewlett-Packard's training group on March 8, 1960; courtesy of Hewlett-Packard Archives.
2. See Nick Lyons, *The Sony Vision* (New York: Crown Publishers, 1976). We also used a translation by our Japanese student Tsuneto Ikeda.
3. Akio Morita, *Made in Japan* (New York: E.P. Dutton, 1986), p. 147.

Reinventing Your Business Model

by Mark W. Johnson, Clayton M. Christensen, and Henning Kagermann

IN 2003, APPLE INTRODUCED the iPod with the iTunes store, revolutionizing portable entertainment, creating a new market, and transforming the company. In just three years, the iPod/iTunes combination became a nearly \$10 billion product, accounting for almost 50% of Apple's revenue. Apple's market capitalization catapulted from around \$1 billion in early 2003 to over \$150 billion by late 2007.

This success story is well known; what's less well known is that Apple was not the first to bring digital music players to market. A company called Diamond Multimedia introduced the Rio in 1998. Another firm, Best Data, introduced the Cabo 64 in 2000. Both products worked well and were portable and stylish. So why did the iPod, rather than the Rio or Cabo, succeed?

Apple did something far smarter than take a good technology and wrap it in a snazzy design. It took a good technology and wrapped it in a great business model. Apple's true innovation was to make downloading digital music easy and convenient. To do that, the company built a groundbreaking business model that combined hardware, software, and service. This approach worked like Gillette's famous blades-and-razor model in reverse: Apple essentially gave away the "blades" (low-margin iTunes music) to lock in purchase of the "razor" (the high-margin iPod). That model defined value in a new way and provided game-changing convenience to the consumer.

Business model innovations have reshaped entire industries and redistributed billions of dollars of value. Retail discounters such as Wal-Mart and Target, which entered the market with pioneering business models, now account for 75% of the total valuation of the retail sector. Low-cost U.S. airlines grew from a blip on the radar screen to 55% of the market value of all carriers. Fully 11 of the 27 companies born in the last quarter century that grew their way into the *Fortune* 500 in the past 10 years did so through business model innovation.

Stories of business model innovation from well-established companies like Apple, however, are rare. An analysis of major innovations within existing corporations in the past decade shows that precious few have been business-model related. And a recent American Management Association study determined that no more than 10% of innovation investment at global companies is focused on developing new business models.

Yet everyone's talking about it. A 2005 survey by the Economist Intelligence Unit reported that over 50% of executives believe business model innovation will become even more important for success than product or service innovation. A 2008 IBM survey of corporate CEOs echoed these results. Nearly all of the CEOs polled reported the need to adapt their business models; more than two-thirds said that extensive changes were required. And in these tough economic times, some CEOs are already looking to business model innovation to address permanent shifts in their market landscapes.

Senior managers at incumbent companies thus confront a frustrating question: Why is it so difficult to pull off the new growth that business model innovation can bring? Our research suggests two problems. The first is a lack of definition: Very little formal study has been done into the dynamics and processes of business model development. Second, few companies understand their existing business model well enough—the premise behind its development, its natural interdependencies, and its strengths and limitations. So they don't know when they can leverage their core business and when success requires a new business model.

Idea in Brief

When Apple introduced the iPod, it did something far smarter than wrap a good technology in a snazzy design. It wrapped a good technology in a **great business model**. Combining hardware, software, and service, the model provided game-changing convenience for consumers *and* record-breaking profits for Apple.

Great business models can reshape industries and drive spectacular growth. Yet many companies find business-model innovation difficult. Managers don't understand their existing model well enough to know when it needs changing—or how.

To determine whether your firm should alter its business model, Johnson, Christensen, and Kagermann advise these steps:

1. Articulate what makes your existing model successful. For example, what customer problem does it solve? How does it make money for your firm?
2. Watch for signals that your model needs changing, such as tough new competitors on the horizon.
3. Decide whether reinventing your model is worth the effort. The answer's yes only if the new model changes the industry or market.

After tackling these problems with dozens of companies, we have found that new business models often look unattractive to internal and external stakeholders—at the outset. To see past the borders of what is and into the land of the new, companies need a road map.

Idea in Practice

Understand Your Current Business Model

A successful model has these components:

- **Customer value proposition.** The model helps customers perform a specific “job” that alternative offerings don’t address.

Example: MinuteClinics enable people to visit a doctor’s office without appointments by making nurse practitioners available to treat minor health issues.

- **Profit formula.** The model generates value for your company through factors such as revenue model, cost structure, margins, and inventory turnover.

Example: The Tata Group’s inexpensive car, the Nano, is profitable because the company has reduced many cost structure elements, accepted lower-than-standard gross margins, and sold the Nano in large volumes to its target market: first-time car buyers in emerging markets.

- **Key resources and processes.** Your company has the people, technology, products, facilities, equipment, and brand required to deliver the value proposition to your targeted customers. And it has processes (training, manufacturing, service) to leverage those

resources.

Example: For Tata Motors to fulfill the requirements of the Nano's profit formula, it had to reconceive how a car is designed, manufactured, and distributed. It redefined its supplier strategy, choosing to outsource a remarkable 85% of the Nano's components and to use nearly 60% fewer vendors than normal to reduce transaction costs.

Identify When a New Model May Be Needed

These circumstances often require business model change:

An opportunity to ... Example

Address needs of large groups who find existing solutions too expensive or complicated.	The Nano's goal is to open car ownership to low-income consumers in emerging markets.

Capitalize on new technology, or leverage existing technologies in new markets.	A company develops a commercial application for a technology originally developed for military use.

Bring a job-to-be-done focus where it doesn't exist.	FedEx focused on performing customers' unmet "job": Receive packages faster and more reliably than any other service could.

A need to ...

Example

Fend off low-end disruptors.	Mini-mills threatened the integrated steel mills a generation ago by making steel at significantly lower prices.

Respond to shifts in competition.	Power-tool maker Hilti switched from selling to renting its tools in part because "good enough" low-end entrants had begun chipping away at the market for selling high-quality tools.

Ours consists of three simple steps. The first is to realize that success starts by not thinking about business models at all. It starts with thinking about the opportunity to satisfy a real customer who needs a job done. The second step is to construct a blueprint laying out how your company will fulfill that need at a profit. In our model, that plan has four elements. The third is to compare that model to your existing model to see how much you'd have to change it to capture the opportunity. Once you do, you will know if you can use your existing model and organization or need to separate out a new unit to execute a new model. Every successful company is already fulfilling a real customer need with an effective business model, whether that model is explicitly understood or not. Let's take a look at what that entails.

Business Model: A Definition

A business model, from our point of view, consists of four interlocking elements that, taken together, create and deliver value. The most important to get right, by far, is the first.

Customer value proposition (CVP)

A successful company is one that has found a way to create value for customers—that is, a way to help customers get an important job done. By “job” we mean a fundamental problem in a given situation that needs a solution. Once we understand the job and all its dimensions, including the full process for how to get it done, we can design the offering. The more important the job is to the customer, the lower the level of customer satisfaction with current options for getting the job done, and the better your solution is than existing alternatives at getting the job done (and, of course, the lower the price), the greater the CVP. Opportunities for creating a CVP are at their most potent, we have found, when alternative products and services have not been designed with the real job in mind and you can design an offering that gets that job—and only that job—done perfectly. We’ll come back to that point later.

Profit formula

The profit formula is the blueprint that defines how the company creates value for itself while providing value to the customer. It consists of the following:

- *Revenue model*: price x volume
- *Cost structure*: direct costs, indirect costs, economies of scale. Cost structure will be predominantly driven by the cost of the key resources required by the business model.
- *Margin model*: given the expected volume and cost structure, the contribution needed from each transaction to achieve desired profits.
- *Resource velocity*: how fast we need to turn over inventory, fixed assets, and other assets—and, overall, how well we need to utilize resources—to support our expected volume and achieve our anticipated profits.

People often think the terms “profit formulas” and “business models” are interchangeable. But how you make a profit is only one piece of the model. We’ve found it most useful to start by setting the price required to deliver the CVP and then work backwards from there to determine what the variable costs and gross margins must be. This then determines what the scale and resource velocity needs to be to achieve the desired profits.

Key resources

The key resources are assets such as the people, technology, products, facilities, equipment, channels, and brand required to deliver the value proposition to the targeted customer. The focus here is on the *key* elements that create value for the customer and the company, and the way those elements interact. (Every company also has generic resources that do not create competitive differentiation.)

Key processes

Successful companies have operational and managerial processes that allow them to deliver value in a way they can successfully repeat and increase in scale. These may include such recurrent tasks as training, development, manufacturing, budgeting, planning, sales, and service. Key processes also include a company's rules, metrics, and norms.

These four elements form the building blocks of any business. The customer value proposition and the profit formula define value for the customer and the company, respectively; key resources and key processes describe how that value will be delivered to both the customer and the company.

As simple as this framework may seem, its power lies in the complex interdependencies of its parts. Major changes to any of these four elements affect the others and the whole. Successful businesses devise a more or less stable system in which these elements bond to one another in consistent and complementary ways.

How Great Models Are Built

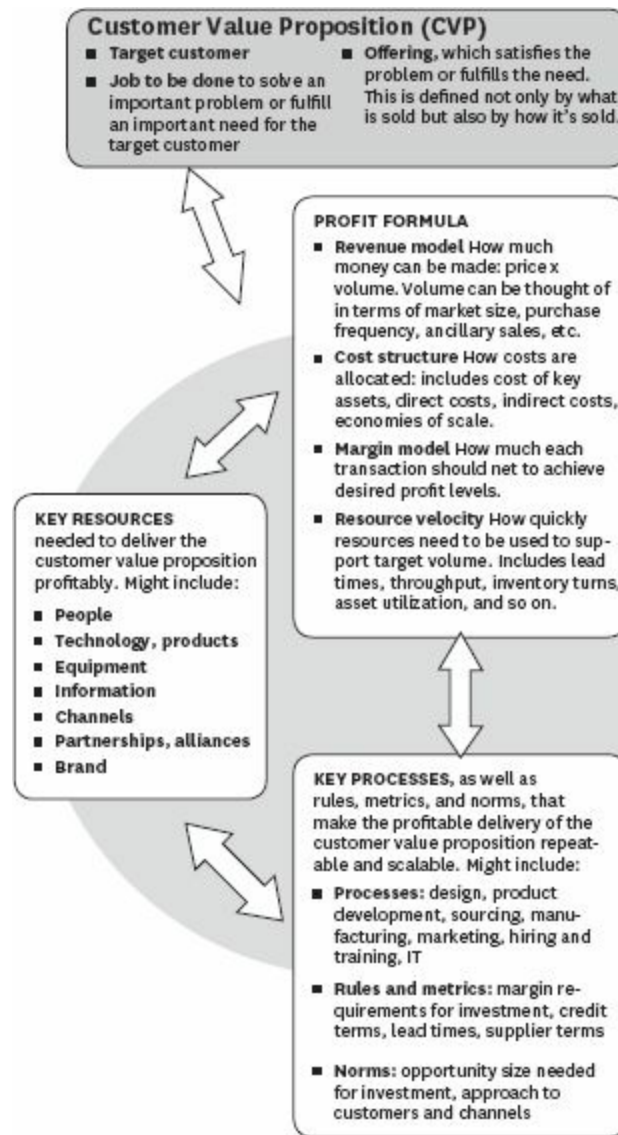
To illustrate the elements of our business model framework, we will look at what's behind two companies' game-changing business model innovations.

Creating a customer value proposition

It's not possible to invent or reinvent a business model without first identifying a clear customer value proposition. Often, it starts as a quite simple realization. Imagine, for a moment, that you are standing on a Mumbai road on a rainy day. You notice the large number of motor scooters snaking precariously in and out around the cars. As you look more closely, you see that most bear whole families—both parents and several children. Your first thought might be “That’s crazy!” or “That’s the way it is in developing countries—people get by as best they can.”

The Elements of a Successful Business Model

Every successful company already operates according to an effective business model. By systematically identifying all of its constituent parts, executives can understand how the model fulfills a potent value proposition in a profitable way using certain key resources and key processes. With that understanding, they can then judge how well the same model could be used to fulfill a radically different CVP—and what they'd need to do to construct a new one, if need be, to capitalize on that opportunity.



When Ratan Tata of Tata Group looked out over this scene, he saw a critical job to be done: providing a safer alternative for scooter families. He understood that the cheapest car available in India cost easily five times what a scooter did and that many of these families could not afford one. Offering an affordable, safer, all-weather alternative for scooter families was a powerful value proposition, one with the potential to reach tens of millions of people who were not yet part of the car-buying market. Ratan Tata also recognized that Tata Motors' business model could not be used to develop such a product at the needed price point.

At the other end of the market spectrum, Hilti, a Liechtenstein-based

manufacturer of high-end power tools for the construction industry, reconsidered the real job to be done for many of its current customers. A contractor makes money by finishing projects; if the required tools aren't available and functioning properly, the job doesn't get done. Contractors don't make money by *owning* tools; they make it by using them as efficiently as possible. Hilti could help contractors get the job done by selling tool *use* instead of the tools themselves—managing its customers' tool inventory by providing the best tool at the right time and quickly furnishing tool repairs, replacements, and upgrades, all for a monthly fee. To deliver on that value proposition, the company needed to create a fleet-management program for tools and in the process shift its focus from manufacturing and distribution to service. That meant Hilti had to construct a new profit formula and develop new resources and new processes.

The most important attribute of a customer value proposition is its precision: how perfectly it nails the customer job to be done—and nothing else. But such precision is often the most difficult thing to achieve. Companies trying to create the new often neglect to focus on *one* job; they dilute their efforts by attempting to do lots of things. In doing lots of things, they do nothing *really* well.

One way to generate a precise customer value proposition is to think about the four most common barriers keeping people from getting particular jobs done: insufficient wealth, access, skill, or time. Software maker Intuit devised QuickBooks to fulfill small-business owners' need to avoid running out of cash. By fulfilling that job with greatly simplified accounting software, Intuit broke the *skills barrier* that kept untrained small-business owners from using more-complicated accounting packages. MinuteClinic, the drugstore-based basic health care provider, broke the *time barrier* that kept people from visiting a doctor's office with minor health issues by making nurse practitioners available without appointments.

Designing a profit formula

Ratan Tata knew the only way to get families off their scooters and into cars would be to break the *wealth barrier* by drastically decreasing the price of the car. “What if I can change the game and make a car for one lakh?” Tata wondered, envisioning a price point of around US\$2,500, less than half the price of the cheapest car available. This, of course, had dramatic ramifications for the profit formula: It required both a significant drop in gross margins and a radical reduction in many elements of the cost structure. He knew, however, he could still make money if he could increase sales volume dramatically, and he knew that his target base of consumers was potentially huge.

For Hilti, moving to a contract management program required shifting assets from customers’ balance sheets to its own and generating revenue through a lease/subscription model. For a monthly fee, customers could have a full complement of tools at their fingertips, with repair and maintenance included. This would require a fundamental shift in all major components of the profit formula: the revenue stream (pricing, the staging of payments, and how to think about volume), the cost structure (including added sales development and contract management costs), and the supporting margins and transaction velocity.

Identifying key resources and processes

Having articulated the value proposition for both the customer and the business, companies must then consider the key resources and processes needed to deliver that value. For a professional services firm, for example, the key resources are generally its people, and the key processes are naturally people related (training and development, for instance). For a packaged goods company, strong brands and well-selected channel retailers might be the key resources, and associated brand-building and channel-management processes among the critical processes.

Hilti Sidesteps Commoditization

HILTI IS CAPITALIZING ON a game-changing opportunity to increase profitability by turning products into a service. Rather than sell tools (at lower and lower prices), it's selling a "just-the-tool-you-need-when-you-need-it, no-repair-or-storage-hassles" service. Such a radical change in customer value proposition required a shift in all parts of its business model.

Traditional power tool company

Sales of industrial and professional power tools and accessories

Low margins, high inventory turnover

Distribution channel, low-cost manufacturing plants in developing countries, R&D

Customer value proposition

Profit formula

Key resources and processes

Hilti's tool fleet management service

Leasing a comprehensive fleet of tools to increase contractors's on-site productivity

Higher margins; asset heavy; monthly payments for tool maintenance, repair, and replacement

Strong direct-sales approach, contract management, IT systems for inventory management and repair, warehousing

Oftentimes, it's not the individual resources and processes that make the difference but their relationship to one another. Companies will almost always need to integrate their key resources and processes in a unique way to get a job done perfectly for a set of customers. When they do, they almost always create enduring competitive advantage. Focusing first on the value proposition and the profit formula makes clear how those resources and processes need to interrelate. For example, most general hospitals offer a value proposition that might be described as, "We'll do anything for

anybody.” Being all things to all people requires these hospitals to have a vast collection of resources (specialists, equipment, and so on) that can’t be knit together in any proprietary way. The result is not just a lack of differentiation but dissatisfaction.

By contrast, a hospital that focuses on a specific value proposition can integrate its resources and processes in a unique way that delights customers. National Jewish Health in Denver, for example, is organized around a focused value proposition we’d characterize as, “If you have a disease of the pulmonary system, bring it here. We’ll define its root cause and prescribe an effective therapy.” Narrowing its focus has allowed National Jewish to develop processes that integrate the ways in which its specialists and specialized equipment work together.

For Tata Motors to fulfill the requirements of its customer value proposition and profit formula for the Nano, it had to reconceive how a car is designed, manufactured, and distributed. Tata built a small team of fairly young engineers who would not, like the company’s more-experienced designers, be influenced and constrained in their thinking by the automaker’s existing profit formulas. This team dramatically minimized the number of parts in the vehicle, resulting in a significant cost saving. Tata also reconceived its supplier strategy, choosing to outsource a remarkable 85% of the Nano’s components and use nearly 60% fewer vendors than normal to reduce transaction costs and achieve better economies of scale.

At the other end of the manufacturing line, Tata is envisioning an entirely new way of assembling and distributing its cars. The ultimate plan is to ship the modular components of the vehicles to a combined network of company-owned and independent entrepreneur-owned assembly plants, which will build them to order. The Nano will be designed, built, distributed, and serviced in a radically new way—one that could not be accomplished without a new business model. And while the jury is still out, Ratan Tata may solve a traffic safety problem in the process.

For Hilti, the greatest challenge lay in training its sales representatives to do a thoroughly new task. Fleet management is not a half-hour sale; it takes days, weeks, even months of meetings to persuade customers to buy a program instead of a product. Suddenly, field reps accustomed to dealing with crew leaders and on-site purchasing managers in mobile trailers found themselves staring down CEOs and CFOs across conference tables.

Additionally, leasing required new resources—new people, more robust

IT systems, and other new technologies—to design and develop the appropriate packages and then come to an agreement on monthly payments. Hilti needed a process for maintaining large arsenals of tools more inexpensively and effectively than its customers had. This required warehousing, an inventory management system, and a supply of replacement tools. On the customer management side, Hilti developed a website that enabled construction managers to view all the tools in their fleet and their usage rates. With that information readily available, the managers could easily handle the cost accounting associated with those assets.

Rules, norms, and metrics are often the last element to emerge in a developing business model. They may not be fully envisioned until the new product or service has been road tested. Nor should they be. Business models need to have the flexibility to change in their early years.

When a New Business Model Is Needed

Established companies should not undertake business-model innovation lightly. They can often create new products that disrupt competitors without fundamentally changing their own business model. Procter & Gamble, for example, developed a number of what it calls “disruptive market innovations” with such products as the Swiffer disposable mop and duster and Febreze, a new kind of air freshener. Both innovations built on P&G’s existing business model and its established dominance in household consumables.

There are clearly times, however, when creating new growth requires venturing not only into unknown market territory but also into unknown business model territory. When? The short answer is “When significant changes are needed to all four elements of your existing model.” But it’s not always that simple. Management judgment is clearly required. That said, we have observed five strategic circumstances that often require business model change:

1. The opportunity to address through disruptive innovation the needs of large groups of potential customers who are shut out of a market entirely because existing solutions are too expensive or complicated for them. This includes the opportunity to democratize products in emerging markets (or reach the bottom of the pyramid), as Tata’s Nano does.
2. The opportunity to capitalize on a brand-new technology by wrapping a new business model around it (Apple and MP3 players) or the opportunity to leverage a tested technology by bringing it to a whole new market (say, by offering military technologies in the commercial space or vice versa).
3. The opportunity to bring a job-to-be-done focus where one does not

yet exist. That's common in industries where companies focus on products or customer segments, which leads them to refine existing products more and more, increasing commoditization over time. A jobs focus allows companies to redefine industry profitability. For example, when FedEx entered the package delivery market, it did not try to compete through lower prices or better marketing. Instead, it concentrated on fulfilling an entirely unmet customer need to receive packages far, far faster, and more reliably, than any service then could. To do so, it had to integrate its key processes and resources in a vastly more efficient way. The business model that resulted from this job-to-be-done emphasis gave FedEx a significant competitive advantage that took UPS many years to copy.

4. The need to fend off low-end disrupters. If the Nano is successful, it will threaten other automobile makers, much as minimills threatened the integrated steel mills a generation ago by making steel at significantly lower cost.
5. The need to respond to a shifting basis of competition. Inevitably, what defines an acceptable solution in a market will change over time, leading core market segments to commoditize. Hilti needed to change its business model in part because of lower global manufacturing costs; "good enough" low-end entrants had begun chipping away at the market for high-quality power tools.

Of course, companies should not pursue business model reinvention unless they are confident that the opportunity is large enough to warrant the effort. And, there's really no point in instituting a new business model unless it's not only new to the company but in some way new or game-changing to the industry or market. To do otherwise would be a waste of time and money.

These questions will help you evaluate whether the challenge of business model innovation will yield acceptable results. Answering "yes" to all four greatly increases the odds of successful execution:

- Can you nail the job with a focused, compelling customer value

proposition?

- Can you devise a model in which all the elements—the customer value proposition, the profit formula, the key resources, and the key processes—work together to get the job done in the most efficient way possible?
- Can you create a new business development process unfettered by the often negative influences of your core business?
- Will the new business model disrupt competitors?

Creating a new model for a new business does not mean the current model is threatened or should be changed. A new model often reinforces and complements the core business, as Dow Corning discovered.

How Dow Corning Got Out of Its Own Way

When business model innovation is clearly called for, success lies not only in getting the model right but also in making sure the incumbent business doesn't in some way prevent the new model from creating value or thriving. That was a problem for Dow Corning when it built a new business unit—with a new profit formula—from scratch.

Dow Corning Embraces the Low End

Traditionally high-margin Dow Corning found new opportunities in low-margin offerings by setting up a separate business unit that operates in an entirely different way. By fundamentally differentiating its low-end and high-end offerings, the company avoided cannibalizing its traditional business even as it found new profits at the low end.

Established business		New business unit
Customized solutions, negotiated contracts	Customer value proposition	No frills, bulk prices, sold through the internet
High-margin, high-overhead retail prices pay for value-added services	Profit formula	Spot-market pricing, low overhead to accommodate lower margins, high throughput
R&D, sales, and services orientation	Key resources and processes	IT system, lowest-cost processes, maximum automation

For many years, Dow Corning had sold thousands of silicone-based products and provided sophisticated technical services to an array of industries. After years of profitable growth, however, a number of product areas were stagnating. A strategic review uncovered a critical insight: Its low-end product segment was commoditizing. Many customers experienced in silicone application no longer needed technical services; they needed basic products at low prices. This shift created an opportunity for growth, but to exploit that opportunity Dow Corning had to figure out a way to serve these customers with a lower-priced product. The problem was that both the business model and the culture were built on high-priced, innovative product and service packages. In 2002, in pursuit of what was essentially a commodity business for low-end customers, Dow Corning CEO Gary

Anderson asked executive Don Sheets to form a team to start a new business.

The team began by formulating a customer value proposition that it believed would fulfill the job to be done for these price-driven customers. It determined that the price point had to drop 15% (which for a commoditizing material was a huge reduction). As the team analyzed what that new customer value proposition would require, it realized reaching that point was going to take a lot more than merely eliminating services. Dramatic price reduction would call for a different profit formula with a fundamentally lower cost structure, which depended heavily on developing a new IT system. To sell more products faster, the company would need to use the internet to automate processes and reduce overhead as much as possible.

When the Old Model Will Work

YOU DON'T ALWAYS NEED a new business model to capitalize on a game-changing opportunity. Sometimes, as P&G did with its Swiffer, a company finds that its current model is revolutionary in a new market. When will the old model do? When you can fulfill the new customer value proposition:

- With your current profit formula
- Using most, if not all, of your current key resources and processes
- Using the same core metrics, rules, and norms you now use to run your business

Breaking the rules

As a mature and successful company, Dow Corning was full of highly trained employees used to delivering its high-touch, customized value proposition. To automate, the new business would have to be far more standardized, which meant instituting different and, overall, much stricter rules. For example, order sizes would be limited to a few, larger-volume options; order lead times would fall between two and four weeks (exceptions would cost extra); and credit terms would be fixed. There would be charges if a purchaser required customer service. The writing was on the wall: The new venture would be low-touch, self-service, and standardized. To succeed, Dow Corning would have to break the rules that had previously guided its success.

Sheets next had to determine whether this new venture, with its new rules, could succeed within the confines of Dow Corning's core enterprise. He set up an experimental war game to test how existing staff and systems would react to the requirements of the new customer value proposition. He got crushed as entrenched habits and existing processes thwarted any attempt to change the game. It became clear that the corporate antibodies would kill the initiative before it got off the ground. The way forward was clear: The new venture had to be free from existing rules and free to decide what rules would be appropriate in order for the new commodity line of business to thrive. To nurture the opportunity—and also protect the existing model—a new business unit with a new brand identity was needed. Xiameter was born.

Identifying new competencies

Following the articulation of the new customer value proposition and new profit formula, the Xiameter team focused on the new competencies it would need, its key resources and processes. Information technology, just a small part of Dow Corning's core competencies at that time, emerged as an essential part of the now web-enabled business. Xiameter also needed employees who could make smart decisions very quickly and who would thrive in a fast-changing environment, filled initially with lots of ambiguity. Clearly, new abilities would have to be brought into the business.

Although Xiameter would be established and run as a separate business unit, Don Sheets and the Xiameter team did not want to give up the incumbency advantage that deep knowledge of the industry and of their own products gave them. The challenge was to tap into the expertise without importing the old-rules mind-set. Sheets conducted a focused HR search within Dow Corning for risk takers. During the interview process, when he came across candidates with the right skills, he asked them to take the job on the spot, before they left the room. This approach allowed him to cherry-pick those who could make snap decisions and take big risks.

The secret sauce: patience

Successful new businesses typically revise their business models four times or so on the road to profitability. While a well-considered business-model-innovation process can often shorten this cycle, successful incumbents must tolerate initial failure and grasp the need for course correction. In effect, companies have to focus on learning and adjusting as much as on executing. We recommend companies with new business models be patient for growth (to allow the market opportunity to unfold) but impatient for profit (as an early validation that the model works). A profitable business is the best early indication of a viable model.

What Rules, Norms, and Metrics Are Standing in Your Way?

In any business, a fundamental understanding of the core model often fades into the mists of institutional memory, but it lives on in rules, norms, and metrics put in place to protect the status quo (for example, “Gross margins must be at 40%”). They are the first line of defense against any new model’s taking root in an existing enterprise.

Financial

- Gross margins
- Opportunity size
- Unit pricing
- Unit margin
- Time to breakeven
- Net present value calculations
- Fixed cost investment
- Credit items

Operational

- End-product quality
- Supplier quality
- Owned versus outsourced manufacturing
- Customer service
- Channels
- Lead times
- Throughput

Other

- Pricing
- Performance demands
- Product-development life cycles
- Basis for individuals' rewards and incentives
- Brand parameters

Accordingly, to allow for the trial and error that naturally accompanies the

creation of the new while also constructing a development cycle that would produce results and demonstrate feasibility with minimal resource outlay, Dow Corning kept the scale of Xiameter's operation small but developed an aggressive timetable for launch and set the goal of becoming profitable by the end of year one.

Xiameter paid back Dow Corning's investment in just three months and went on to become a major, transformative success. Beforehand, Dow Corning had had no online sales component; now 30% of sales originate online, nearly three times the industry average. Most of these customers are new to the company. Far from cannibalizing existing customers, Xiameter has actually supported the main business, allowing Dow Corning's salespeople to more easily enforce premium pricing for their core offerings while providing a viable alternative for the price-conscious.

Established companies' attempts at transformative growth typically spring from product or technology innovations. Their efforts are often characterized by prolonged development cycles and fitful attempts to find a market. As the Apple iPod story that opened this article suggests, truly transformative businesses are never exclusively about the discovery and commercialization of a great technology. Their success comes from enveloping the new technology in an appropriate, powerful business model.

Bob Higgins, the founder and general partner of Highland Capital Partners, has seen his share of venture success and failure in his 20 years in the industry. He sums up the importance and power of business model innovation this way: "I think historically where we [venture capitalists] fail is when we back technology. Where we succeed is when we back new business models."

Originally published in December 2008. Reprint R0812C.

Blue Ocean Strategy

by W. Chan Kim and Renée Mauborgne

A ONETIME ACCORDION PLAYER, stilt walker, and fire-eater, Guy Laliberté is now CEO of one of Canada's largest cultural exports, Cirque du Soleil. Founded in 1984 by a group of street performers, Cirque has staged dozens of productions seen by some 40 million people in 90 cities around the world. In 20 years, Cirque has achieved revenues that Ringling Bros. and Barnum & Bailey—the world's leading circus—took more than a century to attain.

Cirque's rapid growth occurred in an unlikely setting. The circus business was (and still is) in long-term decline. Alternative forms of entertainment—sporting events, TV, and video games—were casting a growing shadow. Children, the mainstay of the circus audience, preferred PlayStations to circus acts. There was also rising sentiment, fueled by animal rights groups, against the use of animals, traditionally an integral part of the circus. On the supply side, the star performers that Ringling and the other circuses relied on to draw in the crowds could often name their own terms. As a result, the industry was hit by steadily decreasing audiences and increasing costs. What's more, any new entrant to this business would be competing against a formidable incumbent that for most of the last century had set the industry standard.

How did Cirque profitably increase revenues by a factor of 22 over the last ten years in such an unattractive environment? The tagline for one of the first Cirque productions is revealing: "We reinvent the circus." Cirque did not make its money by competing within the confines of the existing industry or by stealing customers from Ringling and the others. Instead it created

uncontested market space that made the competition irrelevant. It pulled in a whole new group of customers who were traditionally noncustomers of the industry—adults and corporate clients who had turned to theater, opera, or ballet and were, therefore, prepared to pay several times more than the price of a conventional circus ticket for an unprecedented entertainment experience.

To understand the nature of Cirque's achievement, you have to realize that the business universe consists of two distinct kinds of space, which we think of as red and blue oceans. Red oceans represent all the industries in existence today—the known market space. In red oceans, industry boundaries are defined and accepted, and the competitive rules of the game are well understood. Here, companies try to outperform their rivals in order to grab a greater share of existing demand. As the space gets more and more crowded, prospects for profits and growth are reduced. Products turn into commodities, and increasing competition turns the water bloody.

Blue oceans denote all the industries *not* in existence today—the unknown market space, untainted by competition. In blue oceans, demand is created rather than fought over. There is ample opportunity for growth that is both profitable and rapid. There are two ways to create blue oceans. In a few cases, companies can give rise to completely new industries, as eBay did with the online auction industry. But in most cases, a blue ocean is created from within a red ocean when a company alters the boundaries of an existing industry. As will become evident later, this is what Cirque did. In breaking through the boundary traditionally separating circus and theater, it made a new and profitable blue ocean from within the red ocean of the circus industry.

Cirque is just one of more than 150 blue ocean creations that we have studied in over 30 industries, using data stretching back more than 100 years. We analyzed companies that created those blue oceans and their less successful competitors, which were caught in red oceans. In studying these data, we have observed a consistent pattern of strategic thinking behind the creation of new markets and industries, what we call blue ocean strategy. The logic behind blue ocean strategy parts with traditional models focused on competing in existing market space. Indeed, it can be argued that managers' failure to realize the differences between red and blue ocean strategy lies behind the difficulties many companies encounter as they try to break from the competition.

Idea in Brief

The best way to drive profitable growth? Stop competing in overcrowded industries. In those **red oceans**, companies try to outperform rivals to grab bigger slices of existing demand. As the space gets increasingly crowded, profit and growth prospects shrink. Products become commoditized. Ever-more-intense competition turns the water bloody.

How to avoid the fray? Kim and Mauborgne recommend creating **blue oceans**—uncontested market spaces where the competition is irrelevant. In blue oceans, you invent and capture new demand, and you offer customers a leap in value while also streamlining your costs. Results? Handsome profits, speedy growth—and brand equity that lasts for decades while rivals scramble to catch up.

Consider Cirque du Soleil—which invented a new industry that combined elements from traditional circus with elements drawn from sophisticated theater. In just 20 years, Cirque raked in revenues that Ringling Bros. and Barnum & Bailey—the world’s leading circus—needed more than a century to attain.

In this article, we present the concept of blue ocean strategy and describe its defining characteristics. We assess the profit and growth consequences of blue oceans and discuss why their creation is a rising imperative for companies in the future. We believe that an understanding of blue ocean strategy will help today’s companies as they struggle to thrive in an accelerating and expanding business universe.

Blue and Red Oceans

Although the term may be new, blue oceans have always been with us. Look back 100 years and ask yourself which industries known today were then unknown. The answer: Industries as basic as automobiles, music recording, aviation, petrochemicals, pharmaceuticals, and management consulting were unheard-of or had just begun to emerge. Now turn the clock back only 30 years and ask yourself the same question. Again, a plethora of multibillion-dollar industries jump out: mutual funds, cellular telephones, biotechnology, discount retailing, express package delivery, snowboards, coffee bars, and home videos, to name a few. Just three decades ago, none of these industries existed in a meaningful way.

Idea in Practice

How to begin creating blue oceans? Kim and Mauborgne offer these suggestions:

Understand the Logic Behind Blue Ocean Strategy

The logic behind blue ocean strategy is counterintuitive:

- **It's not about technology innovation.** Blue oceans seldom result from technological innovation. Often, the underlying technology already exists—and blue ocean creators link it to what buyers value. Compaq, for example, used existing technologies to create its ProSignia server, which gave buyers twice the file and print capability of the minicomputer at one-third the price.
- **You don't have to venture into distant waters to create blue oceans.** Most blue oceans are created from within, not beyond, the red oceans of existing industries. Incumbents often create blue oceans within their core businesses. Consider the megaplexes introduced by AMC—an established player in the movie-theater industry. Megaplexes provided movie-goers spectacular viewing experiences in stadium-size theater complexes at lower costs to theater owners.

Apply Blue Ocean Strategic Moves

To apply blue ocean strategic moves:

- **Never use the competition as a benchmark.** Instead, make the competition irrelevant by creating a leap in value for both yourself

and your customers. Ford did this with the Model T. Ford could have tried besting the fashionable, customized cars that wealthy people bought for weekend jaunts in the countryside. Instead, it offered a car for everyday use that was far more affordable, durable, and easy to use and fix than rivals' offerings. Model T sales boomed, and Ford's market share surged from 9% in 1908 to 61% in 1921.

- **Reduce your costs while also offering customers more value.** Cirque du Soleil omitted costly elements of traditional circus, such as animal acts and aisle concessions. Its reduced cost structure enabled it to provide sophisticated elements from theater that appealed to adult audiences—such as themes, original scores, and enchanting sets, all of which change year to year. The added value lured adults who had not gone to a circus for years and enticed them to come back more frequently—thereby increasing revenues. By offering the best of circus and theater, Cirque created a market space that, as yet, has no name—and no equals.

This time, put the clock forward 20 years. Ask yourself: How many industries that are unknown today will exist then? If history is any predictor of the future, the answer is many. Companies have a huge capacity to create new industries and re-create existing ones, a fact that is reflected in the deep changes that have been necessary in the way industries are classified. The half-century-old Standard Industrial Classification (SIC) system was replaced in 1997 by the North American Industry Classification System (NAICS). The new system expanded the ten SIC industry sectors into 20 to reflect the emerging realities of new industry territories—blue oceans. The services sector under the old system, for example, is now seven sectors ranging from information to health care and social assistance. Given that these classification systems are designed for standardization and continuity, such a replacement shows how significant a source of economic growth the creation of blue oceans has been.

Looking forward, it seems clear to us that blue oceans will remain the engine of growth. Prospects in most established market spaces—red oceans

—are shrinking steadily. Technological advances have substantially improved industrial productivity, permitting suppliers to produce an unprecedented array of products and services. And as trade barriers between nations and regions fall and information on products and prices becomes instantly and globally available, niche markets and monopoly havens are continuing to disappear. At the same time, there is little evidence of any increase in demand, at least in the developed markets, where recent United Nations statistics even point to declining populations. The result is that in more and more industries, supply is overtaking demand.

This situation has inevitably hastened the commoditization of products and services, stoked price wars, and shrunk profit margins. According to recent studies, major American brands in a variety of product and service categories have become more and more alike. And as brands become more similar, people increasingly base purchase choices on price. People no longer insist, as in the past, that their laundry detergent be Tide. Nor do they necessarily stick to Colgate when there is a special promotion for Crest, and vice versa. In overcrowded industries, differentiating brands becomes harder both in economic upturns and in downturns.

The Paradox of Strategy

Unfortunately, most companies seem becalmed in their red oceans. In a study of business launches in 108 companies, we found that 86% of those new ventures were line extensions—incremental improvements to existing industry offerings—and a mere 14% were aimed at creating new markets or industries. While line extensions did account for 62% of the total revenues, they delivered only 39% of the total profits. By contrast, the 14% invested in creating new markets and industries delivered 38% of total revenues and a startling 61% of total profits.

So why the dramatic imbalance in favor of red oceans? Part of the explanation is that corporate strategy is heavily influenced by its roots in military strategy. The very language of strategy is deeply imbued with military references—chief executive “officers” in “headquarters,” “troops” on the “front lines.” Described this way, strategy is all about red ocean competition. It is about confronting an opponent and driving him off a battlefield of limited territory. Blue ocean strategy, by contrast, is about doing business where there is no competitor. It is about creating new land, not dividing up existing land. Focusing on the red ocean therefore means accepting the key constraining factors of war—limited terrain and the need to beat an enemy to succeed. And it means denying the distinctive strength of the business world—the capacity to create new market space that is uncontested.

The tendency of corporate strategy to focus on winning against rivals was exacerbated by the meteoric rise of Japanese companies in the 1970s and 1980s. For the first time in corporate history, customers were deserting Western companies in droves. As competition mounted in the global marketplace, a slew of red ocean strategies emerged, all arguing that competition was at the core of corporate success and failure. Today, one hardly talks about strategy without using the language of competition. The term that best symbolizes this is “competitive advantage.” In the competitive-advantage worldview, companies are often driven to outperform rivals and

capture greater shares of existing market space.

Of course competition matters. But by focusing on competition, scholars, companies, and consultants have ignored two very important—and, we would argue, far more lucrative—aspects of strategy: One is to find and develop markets where there is little or no competition—blue oceans—and the other is to exploit and protect blue oceans. These challenges are very different from those to which strategists have devoted most of their attention.

Toward Blue Ocean Strategy

What kind of strategic logic is needed to guide the creation of blue oceans? To answer that question, we looked back over 100 years of data on blue ocean creation to see what patterns could be discerned. Some of our data are presented in “A snapshot of blue ocean creation.” It shows an overview of key blue ocean creations in three industries that closely touch people’s lives: autos—how people get to work; computers—what people use at work; and movie theaters—where people go after work for enjoyment. We found that:

A snapshot of blue ocean creation

This table identifies the strategic elements that were common to blue ocean creations in three different industries in different eras. It is not intended to be comprehensive in coverage or exhaustive in content. We chose to show American industries because they represented the largest and least-regulated market during our study period. The pattern of blue ocean creations exemplified by these three industries is consistent with what we observed in the other industries in our study.

Key blue ocean creations	Was the blue ocean created by a new entrant or an incumbent?	Was it driven by technology pioneering or value pioneering?	At the time of the blue ocean creation, was the industry attractive or unattractive?
Automobiles			
Ford Model T Unveiled in 1908, the Model T was the first mass-produced car, priced so that many Americans could afford it.	New entrant	Value pioneering* (mostly existing technologies)	Unattractive
GM's "car for every purse and purpose" GM created a blue ocean in 1924 by injecting fun and fashion into the car.	Incumbent	Value pioneering (some new technologies)	Attractive
Japanese fuel-efficient autos Japanese automakers created a blue ocean in the mid-1970s with small, reliable lines of cars.	Incumbent	Value pioneering (some new technologies)	Unattractive
Chrysler minivan With its 1984 minivan, Chrysler created a new class of automobile that was as easy to use as a car but had the passenger space of a van.	Incumbent	Value pioneering (mostly existing technologies)	Unattractive

Computers

CTR's tabulating machine In 1914, CTR created the business machine industry by simplifying, modularizing, and leasing tabulating machines. CTR later changed its name to IBM.	Incumbent	Value pioneering (some new technologies)	Unattractive
IBM 650 electronic computer and System/360 In 1952, IBM created the business computer industry by simplifying and reducing the power and price of existing technology. And it exploded the blue ocean created by the 650 when in 1964 it unveiled the System/360, the first modularized computer system.	Incumbent	Value pioneering (650: mostly existing technologies) Value and technology pioneering (System/360: new and existing technologies)	Nonexistent
Apple personal computer Although it was not the first home computer, the all-in-one, simple-to-use Apple II was a blue ocean creation when it appeared in 1978.	New entrant	Value pioneering (mostly existing technologies)	Unattractive
Compaq PC servers Compaq created a blue ocean in 1992 with its ProSignia server, which gave buyers twice the file and print capability of the minicomputer at one-third the price.	Incumbent	Value pioneering (mostly existing technologies)	Nonexistent

Dell built-to-order computers	New entrant	Value pioneering (mostly existing technologies)	Unattractive
In the mid-1990s, Dell created a blue ocean in a highly competitive industry by creating a new purchase and delivery experience for buyers.			
Movie theaters			
Nickelodeon	New entrant	Value pioneering (mostly existing technologies)	Nonexistent
The first Nickelodeon opened its doors in 1905, showing short films around-the-clock to working-class audiences for five cents.			
Palace theaters	Incumbent	Value pioneering (mostly existing technologies)	Attractive
Created by Roxy Rothapfel in 1914, these theaters provided an operalike environment for cinema viewing at an affordable price.			
AMC multiplex	Incumbent	Value pioneering (mostly existing technologies)	Unattractive
In the 1960s, the number of multiplexes in America's suburban shopping malls mushroomed. The multiplex gave viewers greater choice while reducing owners' costs.			
AMC megaplex	Incumbent	Value pioneering (mostly existing technologies)	Unattractive
Megaplexes, introduced in 1995, offered every current blockbuster and provided spectacular viewing experiences in theater complexes as big as stadiums, at a lower cost to theater owners.			

* Driven by value pioneering does not mean that technologies were not involved. Rather, it means that the defining technologies used had largely been in existence, whether in that industry or elsewhere.

Blue oceans are not about technology innovation

Leading-edge technology is sometimes involved in the creation of blue oceans, but it is not a defining feature of them. This is often true even in industries that are technology intensive. As the exhibit reveals, across all three representative industries, blue oceans were seldom the result of technological innovation per se; the underlying technology was often already in existence. Even Ford's revolutionary assembly line can be traced to the meatpacking industry in America. Like those within the auto industry, the blue oceans within the computer industry did not come about through technology innovations alone but by linking technology to what buyers valued. As with the IBM 650 and the Compaq PC server, this often involved simplifying the technology.

Incumbents often create blue oceans—and usually within their core businesses

GM, the Japanese automakers, and Chrysler were established players when they created blue oceans in the auto industry. So were CTR and its later incarnation, IBM, and Compaq in the computer industry. And in the cinema industry, the same can be said of palace theaters and AMC. Of the companies listed here, only Ford, Apple, Dell, and Nickelodeon were new entrants in their industries; the first three were start-ups, and the fourth was an established player entering an industry that was new to it. This suggests that incumbents are not at a disadvantage in creating new market spaces. Moreover, the blue oceans made by incumbents were usually within their core businesses. In fact, as the exhibit shows, most blue oceans are created from within, not beyond, red oceans of existing industries. This challenges the view that new markets are in distant waters. Blue oceans are right next to you in every industry.

Company and industry are the wrong units of analysis

The traditional units of strategic analysis—company and industry—have little explanatory power when it comes to analyzing how and why blue oceans are created. There is no consistently excellent company; the same company can be brilliant at one time and wrongheaded at another. Every company rises and falls over time. Likewise, there is no perpetually excellent industry; relative attractiveness is driven largely by the creation of blue oceans from within them.

The most appropriate unit of analysis for explaining the creation of blue oceans is the strategic move—the set of managerial actions and decisions involved in making a major market-creating business offering. Compaq, for example, is considered by many people to be “unsuccessful” because it was acquired by Hewlett-Packard in 2001 and ceased to be a company. But the firm’s ultimate fate does not invalidate the smart strategic move Compaq made that led to the creation of the multibillion-dollar market in PC servers, a move that was a key cause of the company’s powerful comeback in the 1990s.

Creating blue oceans builds brands

So powerful is blue ocean strategy that a blue ocean strategic move can create brand equity that lasts for decades. Almost all of the companies listed in the exhibit are remembered in no small part for the blue oceans they created long ago. Very few people alive today were around when the first Model T rolled off Henry Ford's assembly line in 1908, but the company's brand still benefits from that blue ocean move. IBM, too, is often regarded as an "American institution" largely for the blue oceans it created in computing; the 360 series was its equivalent of the Model T.

Our findings are encouraging for executives at the large, established corporations that are traditionally seen as the victims of new market space creation. For what they reveal is that large R&D budgets are not the key to creating new market space. The key is making the right strategic moves. What's more, companies that understand what drives a good strategic move will be well placed to create multiple blue oceans over time, thereby continuing to deliver high growth and profits over a sustained period. The creation of blue oceans, in other words, is a product of strategy and as such is very much a product of managerial action.

The Defining Characteristics

Our research shows several common characteristics across strategic moves that create blue oceans. We found that the creators of blue oceans, in sharp contrast to companies playing by traditional rules, never use the competition as a benchmark. Instead they make it irrelevant by creating a leap in value for both buyers and the company itself. (The exhibit “Red ocean versus blue ocean strategy” compares the chief characteristics of these two strategy models.)

Perhaps the most important feature of blue ocean strategy is that it rejects the fundamental tenet of conventional strategy: that a trade-off exists between value and cost. According to this thesis, companies can either create greater value for customers at a higher cost or create reasonable value at a lower cost. In other words, strategy is essentially a choice between differentiation and low cost. But when it comes to creating blue oceans, the evidence shows that successful companies pursue differentiation and low cost simultaneously.

To see how this is done, let us go back to Cirque du Soleil. At the time of Cirque’s debut, circuses focused on benchmarking one another and maximizing their shares of shrinking demand by tweaking traditional circus acts. This included trying to secure more and better-known clowns and lion tamers, efforts that raised circuses’ cost structure without substantially altering the circus experience. The result was rising costs without rising revenues and a downward spiral in overall circus demand. Enter Cirque. Instead of following the conventional logic of outpacing the competition by offering a better solution to the given problem—creating a circus with even greater fun and thrills—it redefined the problem itself by offering people the fun and thrill of the circus *and* the intellectual sophistication and artistic richness of the theater.

In designing performances that landed both these punches, Cirque had to reevaluate the components of the traditional circus offering. What the company found was that many of the elements considered essential to the fun and thrill of the circus were unnecessary and in many cases costly. For

instance, most circuses offer animal acts. These are a heavy economic burden, because circuses have to shell out not only for the animals but also for their training, medical care, housing, insurance, and transportation. Yet Cirque found that the appetite for animal shows was rapidly diminishing because of rising public concern about the treatment of circus animals and the ethics of exhibiting them.

Red ocean versus blue ocean strategy

The imperatives for red ocean and blue ocean strategies are starkly different.

Red ocean strategy	Blue ocean strategy
Compete in existing market space.	Create uncontested market space.
Beat the competition.	Make the competition irrelevant.
Exploit existing demand.	Create and capture new demand.
Make the value/cost trade-off.	Break the value/cost trade-off.
Align the whole system of a company's activities with its strategic choice of differentiation or low cost.	Align the whole system of a company's activities in pursuit of differentiation <i>and</i> low cost.

Similarly, although traditional circuses promoted their performers as stars, Cirque realized that the public no longer thought of circus artists as stars, at least not in the movie star sense. Cirque did away with traditional three-ring shows, too. Not only did these create confusion among spectators forced to switch their attention from one ring to another, they also increased the number of performers needed, with obvious cost implications. And while aisle concession sales appeared to be a good way to generate revenue, the high prices discouraged parents from making purchases and made them feel they were being taken for a ride.

Cirque found that the lasting allure of the traditional circus came down to just three factors: the clowns, the tent, and the classic acrobatic acts. So Cirque kept the clowns, while shifting their humor away from slapstick to a more enchanting, sophisticated style. It glamorized the tent, which many circuses had abandoned in favor of rented venues. Realizing that the tent, more than anything else, captured the magic of the circus, Cirque designed this classic symbol with a glorious external finish and a high level of

audience comfort. Gone were the sawdust and hard benches. Acrobats and other thrilling performers were retained, but Cirque reduced their roles and made their acts more elegant by adding artistic flair.

Even as Cirque stripped away some of the traditional circus offerings, it injected new elements drawn from the world of theater. For instance, unlike traditional circuses featuring a series of unrelated acts, each Cirque creation resembles a theater performance in that it has a theme and story line. Although the themes are intentionally vague, they bring harmony and an intellectual element to the acts. Cirque also borrows ideas from Broadway. For example, rather than putting on the traditional “once and for all” show, Cirque mounts multiple productions based on different themes and story lines. As with Broadway productions, too, each Cirque show has an original musical score, which drives the performance, lighting, and timing of the acts, rather than the other way around. The productions feature abstract and spiritual dance, an idea derived from theater and ballet. By introducing these factors, Cirque has created highly sophisticated entertainments. And by staging multiple productions, Cirque gives people reason to come to the circus more often, thereby increasing revenues.

Cirque offers the best of both circus and theater. And by eliminating many of the most expensive elements of the circus, it has been able to dramatically reduce its cost structure, achieving both differentiation and low cost. (For a depiction of the economics underpinning blue ocean strategy, see “The simultaneous pursuit of differentiation and low cost.”)

By driving down costs while simultaneously driving up value for buyers, a company can achieve a leap in value for both itself and its customers. Since buyer value comes from the utility and price a company offers, and a company generates value for itself through cost structure and price, blue ocean strategy is achieved only when the whole system of a company’s utility, price, and cost activities is properly aligned. It is this whole-system approach that makes the creation of blue oceans a sustainable strategy. Blue ocean strategy integrates the range of a firm’s functional and operational activities.

A rejection of the trade-off between low cost and differentiation implies a fundamental change in strategic mind-set—we cannot emphasize enough how fundamental a shift it is. The red ocean assumption that industry structural conditions are a given and firms are forced to compete within them is based on an intellectual worldview that academics call the *structuralist*

view, or *environmental determinism*. According to this view, companies and managers are largely at the mercy of economic forces greater than themselves. Blue ocean strategies, by contrast, are based on a worldview in which market boundaries and industries can be reconstructed by the actions and beliefs of industry players. We call this the *reconstructionist* view.

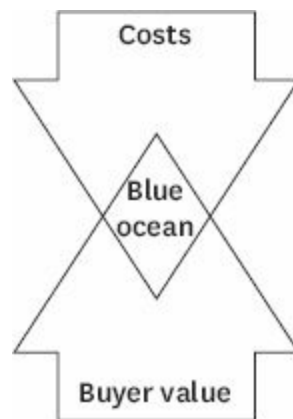
The founders of Cirque du Soleil clearly did not feel constrained to act within the confines of their industry. Indeed, is Cirque really a circus with all that it has eliminated, reduced, raised, and created? Or is it theater? If it is theater, then what genre—Broadway show, opera, ballet? The magic of Cirque was created through a reconstruction of elements drawn from all of these alternatives. In the end, Cirque is none of them and a little of all of them. From within the red oceans of theater and circus, Cirque has created a blue ocean of uncontested market space that has, as yet, no name.

Barriers to Imitation

Companies that create blue oceans usually reap the benefits without credible challenges for ten to 15 years, as was the case with Cirque du Soleil, Home Depot, Federal Express, Southwest Airlines, and CNN, to name just a few. The reason is that blue ocean strategy creates considerable economic and cognitive barriers to imitation.

The simultaneous pursuit of differentiation and low cost

A blue ocean is created in the region where a company's actions favorably affect both its cost structure and its value proposition to buyers. Cost savings are made from eliminating and reducing the factors an industry competes on. Buyer value is lifted by raising and creating elements the industry has never offered. Over time, costs are reduced further as scale economies kick in, due to the high sales volumes that superior value generates.



For a start, adopting a blue ocean creator's business model is easier to imagine than to do. Because blue ocean creators immediately attract customers in large volumes, they are able to generate scale economies very rapidly, putting would-be imitators at an immediate and continuing cost disadvantage. The huge economies of scale in purchasing that Wal-Mart enjoys, for example, have significantly discouraged other companies from imitating its business model. The immediate attraction of large numbers of customers can also create network externalities. The more customers eBay has online, the more attractive the auction site becomes for both sellers and buyers of wares, giving users few incentives to go elsewhere.

When imitation requires companies to make changes to their whole system of activities, organizational politics may impede a would-be competitor's ability to switch to the divergent business model of a blue ocean strategy. For instance, airlines trying to follow Southwest's example of

offering the speed of air travel with the flexibility and cost of driving would have faced major revisions in routing, training, marketing, and pricing, not to mention culture. Few established airlines had the flexibility to make such extensive organizational and operating changes overnight. Imitating a whole-system approach is not an easy feat.

The cognitive barriers can be just as effective. When a company offers a leap in value, it rapidly earns brand buzz and a loyal following in the marketplace. Experience shows that even the most expensive marketing campaigns struggle to unseat a blue ocean creator. Microsoft, for example, has been trying for more than ten years to occupy the center of the blue ocean that Intuit created with its financial software product Quicken. Despite all of its efforts and all of its investment, Microsoft has not been able to unseat Intuit as the industry leader.

In other situations, attempts to imitate a blue ocean creator conflict with the imitator's existing brand image. The Body Shop, for example, shuns top models and makes no promises of eternal youth and beauty. For the established cosmetic brands like Estée Lauder and L'Oréal, imitation was very difficult, because it would have signaled a complete invalidation of their current images, which are based on promises of eternal youth and beauty.

A Consistent Pattern

While our conceptual articulation of the pattern may be new, blue ocean strategy has always existed, whether or not companies have been conscious of the fact. Just consider the striking parallels between the Cirque du Soleil theater-circus experience and Ford's creation of the Model T.

At the end of the nineteenth century, the automobile industry was small and unattractive. More than 500 automakers in America competed in turning out handmade luxury cars that cost around \$1,500 and were enormously *unpopular* with all but the very rich. Anticar activists tore up roads, ringed parked cars with barbed wire, and organized boycotts of car-driving businessmen and politicians. Woodrow Wilson caught the spirit of the times when he said in 1906 that “nothing has spread socialistic feeling more than the automobile.” He called it “a picture of the arrogance of wealth.”

Instead of trying to beat the competition and steal a share of existing demand from other automakers, Ford reconstructed the industry boundaries of cars and horse-drawn carriages to create a blue ocean. At the time, horse-drawn carriages were the primary means of local transportation across America. The carriage had two distinct advantages over cars. Horses could easily negotiate the bumps and mud that stymied cars—especially in rain and snow—on the nation's ubiquitous dirt roads. And horses and carriages were much easier to maintain than the luxurious autos of the time, which frequently broke down, requiring expert repairmen who were expensive and in short supply. It was Henry Ford's understanding of these advantages that showed him how he could break away from the competition and unlock enormous untapped demand.

Ford called the Model T the car “for the great multitude, constructed of the best materials.” Like Cirque, the Ford Motor Company made the competition irrelevant. Instead of creating fashionable, customized cars for weekends in the countryside, a luxury few could justify, Ford built a car that, like the horse-drawn carriage, was for everyday use. The Model T came in just one color, black, and there were few optional extras. It was reliable and

durable, designed to travel effortlessly over dirt roads in rain, snow, or sunshine. It was easy to use and fix. People could learn to drive it in a day. And like Cirque, Ford went outside the industry for a price point, looking at horse-drawn carriages (\$400), not other autos. In 1908, the first Model T cost \$850; in 1909, the price dropped to \$609, and by 1924 it was down to \$290. In this way, Ford converted buyers of horse-drawn carriages into car buyers—just as Cirque turned theatergoers into circusgoers. Sales of the Model T boomed. Ford's market share surged from 9% in 1908 to 61% in 1921, and by 1923, a majority of American households had a car.

Even as Ford offered the mass of buyers a leap in value, the company also achieved the lowest cost structure in the industry, much as Cirque did later. By keeping the cars highly standardized with limited options and interchangeable parts, Ford was able to scrap the prevailing manufacturing system in which cars were constructed by skilled craftsmen who swarmed around one workstation and built a car piece by piece from start to finish. Ford's revolutionary assembly line replaced craftsmen with unskilled laborers, each of whom worked quickly and efficiently on one small task. This allowed Ford to make a car in just four days—21 days was the industry norm—creating huge cost savings.

Blue and red oceans have always coexisted and always will. Practical reality, therefore, demands that companies understand the strategic logic of both types of oceans. At present, competing in red oceans dominates the field of strategy in theory and in practice, even as businesses' need to create blue oceans intensifies. It is time to even the scales in the field of strategy with a better balance of efforts across both oceans. For although blue ocean strategists have always existed, for the most part their strategies have been largely unconscious. But once corporations realize that the strategies for creating and capturing blue oceans have a different underlying logic from red ocean strategies, they will be able to create many more blue oceans in the future.

Originally published in October 2004. Reprint R0401D.

The Secrets to Successful Strategy Execution

by Gary L. Neilson, Karla L. Martin, and Elizabeth Powers

A **BRILLIANT STRATEGY**, blockbuster product, or breakthrough technology can put you on the competitive map, but only solid execution can keep you there. You have to be able to deliver on your intent. Unfortunately, the majority of companies aren't very good at it, by their own admission. Over the past five years, we have invited many thousands of employees (about 25% of whom came from executive ranks) to complete an online assessment of their organizations' capabilities, a process that's generated a database of 125,000 profiles representing more than 1,000 companies, government agencies, and not-for-profits in over 50 countries. Employees at three out of every five companies rated their organization weak at execution—that is, when asked if they agreed with the statement “Important strategic and operational decisions are quickly translated into action,” the majority answered no.

Execution is the result of thousands of decisions made every day by employees acting according to the information they have and their own self-interest. In our work helping more than 250 companies learn to execute more effectively, we've identified four fundamental building blocks executives can use to influence those actions—clarifying decision rights, designing information flows, aligning motivators, and making changes to structure. (For simplicity's sake we refer to them as decision rights, information, motivators, and structure.)

In efforts to improve performance, most organizations go right to

structural measures because moving lines around the org chart seems the most obvious solution and the changes are visible and concrete. Such steps generally reap some short-term efficiencies quickly, but in so doing address only the symptoms of dysfunction, not its root causes. Several years later, companies usually end up in the same place they started. Structural change can and should be part of the path to improved execution, but it's best to think of it as the capstone, not the cornerstone, of any organizational transformation. In fact, our research shows that actions having to do with decision rights and information are far more important—about twice as effective—as improvements made to the other two building blocks. (See “What matters most to strategy execution.”)

Take, for example, the case of a global consumer packaged-goods company that lurched down the reorganization path in the early 1990s. (We have altered identifying details in this and other cases that follow.) Disappointed with company performance, senior management did what most companies were doing at that time: They restructured. They eliminated some layers of management and broadened spans of control. Management-staffing costs quickly fell by 18%. Eight years later, however, it was *déjà vu*. The layers had crept back in, and spans of control had once again narrowed. In addressing only structure, management had attacked the visible symptoms of poor performance but not the underlying cause—how people made decisions and how they were held accountable.

This time, management looked beyond lines and boxes to the mechanics of how work got done. Instead of searching for ways to strip out costs, they focused on improving execution—and in the process discovered the true reasons for the performance shortfall. Managers didn't have a clear sense of their respective roles and responsibilities. They did not intuitively understand which decisions were theirs to make. Moreover, the link between performance and rewards was weak. This was a company long on micromanaging and second-guessing, and short on accountability. Middle managers spent 40% of their time justifying and reporting upward or questioning the tactical decisions of their direct reports.

Idea in Brief

A brilliant strategy may put you on the competitive map. But only solid execution keeps you there. Unfortunately, most companies struggle with implementation. That's because they overrely on structural changes, such as reorganization, to execute their strategy.

Though structural change has its place in execution, it produces only short-term gains. For example, one company reduced its management layers as part of a strategy to address disappointing performance. Costs plummeted initially, but the layers soon crept back in.

Research by Neilson, Martin, and Powers shows that execution exemplars focus their efforts on two levers far more powerful than structural change:

- **Clarifying decision rights**—for instance, specifying who “owns” each decision and who must provide input
- **Ensuring information flows where it's needed**—such as promoting managers laterally so they build networks needed for the cross-unit collaboration critical to a new strategy

Tackle decision rights and information flows first, and only then **alter organizational structures** and **realign incentives** to *support* those moves.

Armed with this understanding, the company designed a new management model that established who was accountable for what and made the connection between performance and reward. For instance, the norm at this company, not unusual in the industry, had been to promote people quickly,

within 18 months to two years, before they had a chance to see their initiatives through. As a result, managers at every level kept doing their old jobs even after they had been promoted, peering over the shoulders of the direct reports who were now in charge of their projects and, all too frequently, taking over. Today, people stay in their positions longer so they can follow through on their own initiatives, and they're still around when the fruits of their labors start to kick in. What's more, results from those initiatives continue to count in their performance reviews for some time after they've been promoted, forcing managers to live with the expectations they'd set in their previous jobs. As a consequence, forecasting has become more accurate and reliable. These actions did yield a structure with fewer layers and greater spans of control, but that was a side effect, not the primary focus, of the changes.

Idea in Practice

The following levers matter *most* for successful strategy execution:

Decision Rights

- Ensure that everyone in your company knows which decisions and actions they're responsible for.

Example: In one global consumer-goods company, decisions made by divisional and geographic leaders were overridden by corporate functional leaders who controlled resource allocations. Decisions stalled. Overhead costs mounted as divisions added staff to create bulletproof cases for challenging corporate decisions. To support a new strategy hinging on sharper customer focus, the CEO designated accountability for profits unambiguously to the divisions.

- Encourage higher-level managers to delegate operational decisions.

Example: At one global charitable organization, country-level managers' inability to delegate led to decision paralysis. So the leadership team encouraged country managers to delegate standard operational tasks. This freed these managers to focus on developing the strategies needed to fulfill the organization's mission.

Information Flow

- Make sure important information about the competitive environment flows quickly to corporate headquarters. That way, the

top team can identify patterns and promulgate best practices throughout the company.

Example: At one insurance company, accurate information about projects' viability was censored as it moved up the hierarchy. To improve information flow to senior levels of management, the company took steps to create a more open, informal culture. Top executives began mingling with unit leaders during management meetings and held regular brown-bag lunches where people discussed the company's most pressing issues.

- Facilitate information flow across organizational boundaries.

Example: To better manage relationships with large, cross-product customers, a B2B company needed its units to talk with one another. It charged its newly created customer-focused marketing group with encouraging cross-company communication. The group issued regular reports showing performance against targets (by product and geography) and supplied root-cause analyses of performance gaps. Quarterly performance-management meetings further fostered the trust required for collaboration.

- Help field and line employees understand how their day-to-day choices affect your company's bottom line.

Example: At a financial services firm, salespeople routinely crafted customized one-off deals with clients that cost the company more than it made in revenues. Sales didn't understand the cost and complexity implications of these transactions. Management addressed the information misalignment by adopting a "smart customization" approach to sales. For customized deals, it established standardized back-office processes (such as risk assessment). It also developed analytical support tools to arm salespeople with accurate information on the cost implications of their proposed transactions. Profitability improved.

The Elements of Strong Execution

Our conclusions arise out of decades of practical application and intensive research. Nearly five years ago, we and our colleagues set out to gather empirical data to identify the actions that were most effective in enabling an organization to implement strategy. What particular ways of restructuring, motivating, improving information flows, and clarifying decision rights mattered the most? We started by drawing up a list of 17 traits, each corresponding to one or more of the four building blocks we knew could enable effective execution—traits like the free flow of information across organizational boundaries or the degree to which senior leaders refrain from getting involved in operating decisions. With these factors in mind, we developed an online profiler that allows individuals to assess the execution capabilities of their organizations. Over the next four years or so, we collected data from many thousands of profiles, which in turn allowed us to more precisely calibrate the impact of each trait on an organization's ability to execute. That allowed us to rank all 17 traits in order of their relative influence. (See "The 17 fundamental traits of organizational effectiveness.")

Ranking the traits makes clear how important decision rights and information are to effective strategy execution. The first eight traits map directly to decision rights and information. Only three of the 17 traits relate to structure, and none of those ranks higher than 13th. We'll walk through the top five traits here.

1. Everyone has a good idea of the decisions and actions for which he or she is responsible

In companies strong on execution, 71% of individuals agree with this statement; that figure drops to 32% in organizations weak on execution.

Blurring of decision rights tends to occur as a company matures. Young organizations are generally too busy getting things done to define roles and responsibilities clearly at the outset. And why should they? In a small company, it's not so difficult to know what other people are up to. So for a time, things work out well enough. As the company grows, however, executives come and go, bringing in with them and taking away different expectations, and over time the approval process gets ever more convoluted and murky. It becomes increasingly unclear where one person's accountability begins and another's ends.

One global consumer-durables company found this out the hard way. It was so rife with people making competing and conflicting decisions that it was hard to find anyone below the CEO who felt truly accountable for profitability. The company was organized into 16 product divisions aggregated into three geographic groups—North America, Europe, and International. Each of the divisions was charged with reaching explicit performance targets, but functional staff at corporate headquarters controlled spending targets—how R&D dollars were allocated, for instance. Decisions made by divisional and geographic leaders were routinely overridden by functional leaders. Overhead costs began to mount as the divisions added staff to help them create bulletproof cases to challenge corporate decisions.

Decisions stalled while divisions negotiated with functions, each layer weighing in with questions. Functional staffers in the divisions (financial analysts, for example) often deferred to their higher-ups in corporate rather than their division vice president, since functional leaders were responsible for rewards and promotions. Only the CEO and his executive team had the discretion to resolve disputes. All of these symptoms fed on one another and collectively hampered execution—until a new CEO came in.

The new chief executive chose to focus less on cost control and more on

profitable growth by redefining the divisions to focus on consumers. As part of the new organizational model, the CEO designated accountability for profits unambiguously to the divisions and also gave them the authority to draw on functional activities to support their goals (as well as more control of the budget). Corporate functional roles and decision rights were recast to better support the divisions' needs and also to build the cross-divisional links necessary for developing the global capabilities of the business as a whole. For the most part, the functional leaders understood the market realities—and that change entailed some adjustments to the operating model of the business. It helped that the CEO brought them into the organizational redesign process, so that the new model wasn't something imposed on them as much as it was something they engaged in and built together.

2. Important information about the competitive environment gets to headquarters quickly

On average, 77% of individuals in strong-execution organizations agree with this statement, whereas only 45% of those in weak- execution organizations do.

Headquarters can serve a powerful function in identifying patterns and promulgating best practices throughout business segments and geographic regions. But it can play this coordinating role only if it has accurate and up-to-date market intelligence. Otherwise, it will tend to impose its own agenda and policies rather than defer to operations that are much closer to the customer.

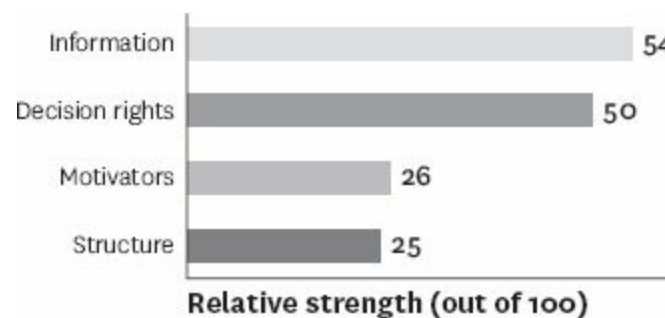
Consider the case of heavy-equipment manufacturer Caterpillar.¹ Today it is a highly successful \$45 billion global company, but a generation ago, Caterpillar's organization was so badly misaligned that its very existence was threatened. Decision rights were hoarded at the top by functional general offices located at headquarters in Peoria, Illinois, while much of the information needed to make those decisions resided in the field with sales managers. "It just took a long time to get decisions going up and down the functional silos, and they really weren't good business decisions; they were more functional decisions," noted one field executive. Current CEO Jim Owens, then a managing director in Indonesia, told us that such information that did make it to the top had been "whitewashed and varnished several times over along the way." Cut off from information about the external market, senior executives focused on the organization's internal workings, overanalyzing issues and second-guessing decisions made at lower levels, costing the company opportunities in fast-moving markets.

Pricing, for example, was based on cost and determined not by market realities but by the pricing general office in Peoria. Sales representatives across the world lost sale after sale to Komatsu, whose competitive pricing consistently beat Caterpillar's. In 1982, the company posted the first annual loss in its almost-60-year history. In 1983 and 1984, it lost \$1 million a day, seven days a week. By the end of 1984, Caterpillar had lost a billion dollars.

By 1988, then-CEO George Schaefer stood atop an entrenched bureaucracy that was, in his words, “telling me what I wanted to hear, not what I needed to know.” So, he convened a task force of “renegade” middle managers and tasked them with charting Caterpillar’s future.

What matters most to strategy execution

When a company fails to execute its strategy, the first thing managers often think to do is restructure. But our research shows that the fundamentals of good execution start with clarifying decision rights and making sure information flows where it needs to go. If you get those right, the correct structure and motivators often become obvious.



Ironically, the way to ensure that the right information flowed to headquarters was to make sure the right decisions were made much further down the organization. By delegating operational responsibility to the people closer to the action, top executives were free to focus on more global strategic issues. Accordingly, the company reorganized into business units, making each accountable for its own P&L statement. The functional general offices that had been all-powerful ceased to exist, literally overnight. Their talent and expertise, including engineering, pricing, and manufacturing, were parceled out to the new business units, which could now design their own products, develop their own manufacturing processes and schedules, and set their own prices. The move dramatically decentralized decision rights, giving the units control over market decisions. The business unit P&Ls were now measured consistently across the enterprise, as return on assets became the universal measure of success. With this accurate, up-to-date, and directly comparable information, senior decision makers at headquarters could make smart strategic choices and trade-offs rather than use outdated sales data to make ineffective, tactical marketing decisions.

The 17 fundamental traits of organizational effectiveness

From our survey research drawn from more than 26,000 people in 31 companies, we have distilled the traits that make organizations effective at implementing strategy. Here they are, in order of importance.

Rank	Organization Trait	Strength Index (Out of 100)
1	Everyone has a good idea of the decisions and actions for which he or she is responsible.	81
2	Important information about the competitive environment gets to headquarters quickly.	68
3	Once made, decisions are rarely second-guessed.	58
4	Information flows freely across organizational boundaries.	58
5	Field and line employees usually have the information they need to understand the bottom-line impact of their day-to-day choices.	55
6	Line managers have access to the metrics they need to measure the key drivers of their business.	48
7	Managers up the line get involved in operating decisions.	32
8	Conflicting messages are rarely sent to the market.	32
9	The individual performance-appraisal process differentiates among high, adequate, and low performers.	32
10	The ability to deliver on performance commitments strongly influences career advancement and compensation.	32
11	It is more accurate to describe the culture of this organization as "persuade and cajole" than "command and control."	29
12	The primary role of corporate staff here is to support the business units rather than to audit them.	29
13	Promotions can be lateral moves (from one position to another on the same level in the hierarchy).	29
14	Fast-track employees here can expect promotions more frequently than every three years.	23
15	On average, middle managers here have five or more direct reports.	19
16	If the firm has a bad year, but a particular division has a good year, the division head would still get a bonus.	13
17	Besides pay, many other things motivate individuals to do a good job.	10

Building Blocks
☒ Decision rights
 ☐ Information
 ☐ Motivators
 ☒ Structure

Within 18 months, the company was working in the new model. "This was a revolution that became a renaissance," Owens recalls, "a spectacular

transformation of a kind of sluggish company into one that actually has entrepreneurial zeal. And that transition was very quick because it was decisive and it was complete; it was thorough; it was universal, worldwide, all at one time.”

3. Once made, decisions are rarely second-guessed

Whether someone is second-guessing depends on your vantage point. A more senior and broader enterprise perspective can add value to a decision, but managers up the line may not be adding incremental value; instead, they may be stalling progress by redoing their subordinates' jobs while, in effect, shirking their own. In our research, 71% of respondents in weak-execution companies thought that decisions were being second-guessed, whereas only 45% of those from strong-execution organizations felt that way.

Recently, we worked with a global charitable organization dedicated to alleviating poverty. It had a problem others might envy: It was suffering from the strain brought on by a rapid growth in donations and a corresponding increase in the depth and breadth of its program offerings. As you might expect, this nonprofit was populated with people on a mission who took intense personal ownership of projects. It did not reward the delegation of even the most mundane administrative tasks. Country-level managers, for example, would personally oversee copier repairs. Managers' inability to delegate led to decision paralysis and a lack of accountability as the organization grew. Second-guessing was an art form. When there was doubt over who was empowered to make a decision, the default was often to have a series of meetings in which no decision was reached. When decisions were finally made, they had generally been vetted by so many parties that no one person could be held accountable. An effort to expedite decision-making through restructuring—by collocating key leaders with subject-matter experts in newly established central and regional centers of excellence—became instead another logjam. Key managers still weren't sure of their right to take advantage of these centers, so they didn't.

The nonprofit's management and directors went back to the drawing board. We worked with them to design a decision-making map, a tool to help identify where different types of decisions should be taken, and with it they clarified and enhanced decision rights at all levels of management. All managers were then actively encouraged to delegate standard operational tasks. Once people had a clear idea of what decisions they should and should not be making, holding them accountable for decisions felt fair. What's more,

now they could focus their energies on the organization's mission. Clarifying decision rights and responsibilities also improved the organization's ability to track individual achievement, which helped it chart new and appealing career-advancement paths.

4. Information flows freely across organizational boundaries

When information does not flow horizontally across different parts of the company, units behave like silos, forfeiting economies of scale and the transfer of best practices. Moreover, the organization as a whole loses the opportunity to develop a cadre of up-and-coming managers well versed in all aspects of the company's operations. Our research indicates that only 21% of respondents from weak-execution companies thought information flowed freely across organizational boundaries whereas 55% of those from strong-execution firms did. Since scores for even the strong companies are pretty low, though, this is an issue that most companies can work on.

A cautionary tale comes from a business-to-business company whose customer and product teams failed to collaborate in serving a key segment: large, cross-product customers. To manage relationships with important clients, the company had established a customer-focused marketing group, which developed customer outreach programs, innovative pricing models, and tailored promotions and discounts. But this group issued no clear and consistent reports of its initiatives and progress to the product units and had difficulty securing time with the regular cross-unit management to discuss key performance issues. Each product unit communicated and planned in its own way, and it took tremendous energy for the customer group to understand the units' various priorities and tailor communications to each one. So the units were not aware, and had little faith, that this new division was making constructive inroads into a key customer segment. Conversely (and predictably), the customer team felt the units paid only perfunctory attention to its plans and couldn't get their cooperation on issues critical to multiproduct customers, such as potential trade-offs and volume discounts.

Historically, this lack of collaboration hadn't been a problem because the company had been the dominant player in a high-margin market. But as the market became more competitive, customers began to view the firm as unreliable and, generally, as a difficult supplier, and they became increasingly reluctant to enter into favorable relationships.

Once the issues became clear, though, the solution wasn't terribly complicated, involving little more than getting the groups to talk to one another. The customer division became responsible for issuing regular reports to the product units showing performance against targets, by product and geographic region, and for supplying a supporting root-cause analysis. A standing performance-management meeting was placed on the schedule every quarter, creating a forum for exchanging information face-to-face and discussing outstanding issues. These moves bred the broader organizational trust required for collaboration.

5. Field and line employees usually have the information they need to understand the bottom-line impact of their day-to-day choices

Rational decisions are necessarily bounded by the information available to employees. If managers don't understand what it will cost to capture an incremental dollar in revenue, they will always pursue the incremental revenue. They can hardly be faulted, even if their decision is—in the light of full information—wrong. Our research shows that 61% of individuals in strong-execution organizations agree that field and line employees have the information they need to understand the bottom-line impact of their decisions. This figure plummets to 28% in weak-execution organizations.

We saw this unhealthy dynamic play out at a large, diversified financial-services client, which had been built through a series of successful mergers of small regional banks. In combining operations, managers had chosen to separate front-office bankers who sold loans from back-office support groups who did risk assessments, placing each in a different reporting relationship and, in many cases, in different locations. Unfortunately, they failed to institute the necessary information and motivation links to ensure smooth operations. As a result, each pursued different, and often competing, goals.

For example, salespeople would routinely enter into highly customized one-off deals with clients that cost the company more than they made in revenues. Sales did not have a clear understanding of the cost and complexity implications of these transactions. Without sufficient information, sales staff believed that the back-end people were sabotaging their deals, while the support groups considered the front-end people to be cowboys. At year's end, when the data were finally reconciled, management would bemoan the sharp increase in operational costs, which often erased the profit from these transactions.

Executives addressed this information misalignment by adopting a “smart customization” approach to sales. They standardized the end-to-end processes used in the majority of deals and allowed for customization only in select circumstances. For these customized deals, they established clear back-office

processes and analytical support tools to arm salespeople with accurate information on the cost implications of the proposed transactions. At the same time, they rolled out common reporting standards and tools for both the front- and back-office operations to ensure that each group had access to the same data and metrics when making decisions. Once each side understood the business realities confronted by the other, they cooperated more effectively, acting in the whole company's best interests—and there were no more year-end surprises.

About the Data

WE TESTED ORGANIZATIONAL effectiveness by having people fill out an online diagnostic, a tool comprising 19 questions (17 that describe organizational traits and two that describe outcomes).

To determine which of the 17 traits in our profiler are most strongly associated with excellence in execution, we looked at 31 companies in our database for which we had responses from at least 150 individual (anonymously completed) profiles, for a total of 26,743 responses. Applying regression analysis to each of the 31 data sets, we correlated the 17 traits with our measure of organizational effectiveness, which we defined as an affirmative response to the outcome statement, “Important strategic and operational decisions are quickly translated into action.” Then we ranked the traits in order, according to the number of data sets in which the trait exhibited a significant correlation with our measure of success within a 90% confidence interval. Finally, we indexed the result to a 100-point scale. The top trait—“Everyone has a good idea of the decisions and actions for which he or she is responsible”—exhibited a significant positive correlation with our success indicator in 25 of the 31 data sets, for an index score of 81.

Creating a Transformation Program

The four building blocks that managers can use to improve strategy execution—decision rights, information, structure, and motivators—are inextricably linked. Unclear decision rights not only paralyze decision making but also impede information flow, divorce performance from rewards, and prompt workarounds that subvert formal reporting lines. Blocking information results in poor decisions, limited career development, and a reinforcement of structural silos. So what to do about it?

Since each organization is different and faces a unique set of internal and external variables, there is no universal answer to that question. The first step is to identify the sources of the problem. In our work, we often begin by having a company's employees take our profiling survey and consolidating the results. The more people in the organization who take the survey, the better.

Once executives understand their company's areas of weakness, they can take any number of actions. "Mapping improvements to the building blocks: Some sample tactics" shows 15 possible steps that can have an impact on performance. (The options listed represent only a sampling of the dozens of choices managers might make.) All of these actions are geared toward strengthening one or more of the 17 traits. For example, if you were to take steps to "clarify and streamline decision making" you could potentially strengthen two traits: "Everyone has a good idea of the decisions and actions for which he or she is responsible," and "Once made, decisions are rarely second-guessed."

You certainly wouldn't want to put 15 initiatives in a single transformation program. Most organizations don't have the managerial capacity or organizational appetite to take on more than five or six at a time. And as we've stressed, you should first take steps to address decision rights and information, and then design the necessary changes to motivators and structure to support the new design.

To help companies understand their shortcomings and construct the

improvement program that will have the greatest impact, we have developed an organizational-change simulator. This interactive tool accompanies the profiler, allowing you to try out different elements of a change program virtually, to see which ones will best target your company's particular area of weakness. (For an overview of the simulation process, see the sidebar "Test Drive Your Organization's Transformation.")

To get a sense of the process from beginning to end—from taking the diagnostic profiler, to formulating your strategy, to launching your organizational transformation—consider the experience of a leading insurance company we'll call *Goodward Insurance*. *Goodward* was a successful company with strong capital reserves and steady revenue and customer growth. Still, its leadership wanted to further enhance execution to deliver on an ambitious five-year strategic agenda that included aggressive targets in customer growth, revenue increases, and cost reduction, which would require a new level of teamwork. While there were pockets of cross-unit collaboration within the company, it was far more common for each unit to focus on its own goals, making it difficult to spare resources to support another unit's goals. In many cases there was little incentive to do so anyway: Unit A's goals might require the involvement of Unit B to succeed, but Unit B's goals might not include supporting Unit A's effort.

Mapping improvements to the building blocks: some sample tactics

Companies can take a host of steps to improve their ability to execute strategy. The 15 here are only some of the possible examples. Every one strengthens one or more of the building blocks executives can use to improve their strategy-execution capability: clarifying decision rights, improving information, establishing the right motivators, and restructuring the organization.

- ☒ Focus corporate staff on supporting business-unit decision making.
- ☒ Clarify and streamline decision making at each operating level.
- ☒ Focus headquarters on important strategic questions.
- ☒ ☐ Create centers of excellence by consolidating similar functions into a single organizational unit.
- ☒ ☐ ☐ Assign process owners to coordinate activities that span organizational functions.
- ☒ ☐ Establish individual performance measures.
- ☐ Improve field-to-headquarters information flow.
- ☐ Define and distribute daily operating metrics to the field or line.
- ☐ ☐ Create cross-functional teams.
- ☐ Introduce differentiating performance awards.
- ☐ Expand nonmonetary rewards to recognize exceptional performers.
- ☐ ☒ Increase position tenure.
- ☐ ☒ Institute lateral moves and rotations.
- ☒ Broaden spans of control.

Building blocks ☒ Decision rights ☐ Information ☐ Motivators ☒ Structure

The company had initiated a number of enterprisewide projects over the years, which had been completed on time and on budget, but these often had to be reworked because stakeholder needs hadn't been sufficiently taken into account. After launching a shared-services center, for example, the company had to revisit its operating model and processes when units began hiring shadow staff to focus on priority work that the center wouldn't expedite. The center might decide what technology applications, for instance, to develop on its own rather than set priorities according to what was most important to the organization.

In a similar way, major product launches were hindered by insufficient coordination among departments. The marketing department would develop new coverage options without asking the claims-processing group whether it had the ability to process the claims. Since it didn't, processors had to create expensive manual work-arounds when the new kinds of claims started pouring in. Nor did marketing ask the actuarial department how these products would affect the risk profile and reimbursement expenses of the company, and for some of the new products, costs did indeed increase.

To identify the greatest barriers to building a stronger execution culture, Goodward Insurance gave the diagnostic survey to all of its 7,000-plus employees and compared the organization's scores on the 17 traits with those from strong-execution companies. Numerous previous surveys (employee-satisfaction, among others) had elicited qualitative comments identifying the barriers to execution excellence. But the diagnostic survey gave the company quantifiable data that it could analyze by group and by management level to determine which barriers were most hindering the people actually charged with execution. As it turned out, middle management was far more pessimistic than the top executives in their assessment of the organization's execution ability. Their input became especially critical to the change agenda ultimately adopted.

Through the survey, Goodward Insurance uncovered impediments to execution in three of the most influential organizational traits:

Information did not flow freely across organizational boundaries. Sharing information was never one of Goodward's hallmarks, but managers had always dismissed the mounting anecdotal evidence of poor cross-divisional information flow as "some other group's problem." The organizational diagnostic data, however, exposed such plausible deniability as an inadequate excuse. In fact, when the CEO reviewed the profiler results with his direct reports, he held up the chart on cross-group information flows and declared, "We've been discussing this problem for several years, and yet you always say that it's so-and-so's problem, not mine. Sixty-seven percent of [our] respondents said that they do not think information flows freely across divisions. This is not so-and-so's problem—it's our problem. You just don't get results that low [unless it comes] from everywhere. We are all on the hook for fixing this."

Contributing to this lack of horizontal information flow was a dearth of lateral promotions. Because Woodward had always promoted up rather than over and up, most middle and senior managers remained within a single group. They were not adequately apprised of the activities of the other groups, nor did they have a network of contacts across the organization.

Important information about the competitive environment did not get to headquarters quickly. The diagnostic data and subsequent surveys and interviews with middle management revealed that the wrong information was moving up the org chart. Mundane day-to-day decisions were escalated to the executive level—the top team had to approve midlevel hiring decisions, for instance, and bonuses of \$1,000—limiting Woodward’s agility in responding to competitors’ moves, customers’ needs, and changes in the broader marketplace. Meanwhile, more important information was so heavily filtered as it moved up the hierarchy that it was all but worthless for rendering key verdicts. Even if lower-level managers knew that a certain project could never work for highly valid reasons, they would not communicate that dim view to the top team. Nonstarters not only started, they kept going. For instance, the company had a project under way to create new incentives for its brokers. Even though this approach had been previously tried without success, no one spoke up in meetings or stopped the project because it was a priority for one of the top-team members.

Test-Drive Your Organization's Transformation

YOU KNOW YOUR ORGANIZATION could perform better. You are faced with dozens of levers you could conceivably pull if you had unlimited time and resources. But you don't. You operate in the real world.

How, then, do you make the most-educated and cost-efficient decisions about which change initiatives to implement? We've developed a way to test the efficacy of specific actions (such as clarifying decision rights, forming cross-functional teams, or expanding nonmonetary rewards) without risking significant amounts of time and money. You can go to www.simulator-orgeffectiveness.com to assemble and try out various five-step organizational-change programs and assess which would be the most effective and efficient in improving execution at your company.

You begin the simulation by selecting one of seven organizational profiles that most resembles the current state of your organization. If you're not sure, you can take a five-minute diagnostic survey. This online survey automatically generates an organizational profile and baseline execution-effectiveness score. (Although 100 is a perfect score, nobody is perfect; even the most effective companies often score in the 60s and 70s.)

Having established your baseline, you use the simulator to chart a possible course you'd like to take to improve your execution capabilities by selecting five out of a possible 28 actions. Ideally, these moves should directly address the weakest links in your organizational profile. To help you make the right choices, the simulator offers insights that shed further light on how a proposed action influences particular organizational elements.

Once you have made your selections, the simulator executes the steps you've elected and processes them through a web-based engine that

evaluates them using empirical relationships identified from 31 companies representing more than 26,000 data observations. It then generates a bar chart indicating how much your organization's execution score has improved and where it now stands in relation to the highest-performing companies from our research and the scores of other people like you who have used the simulator starting from the same original profile you did. If you wish, you may then advance to the next round and pick another five actions. What you will see is illustrated below.

The beauty of the simulator is its ability to consider—consequence-free—the impact on execution of endless combinations of possible actions. Each simulation includes only two rounds, but you can run the simulation as many times as you like. The simulator has also been used for team competition within organizations, and we've found that it engenders very engaging and productive dialogue among senior executives.

While the simulator cannot capture all of the unique situations an organization might face, it is a useful tool for assessing and building a targeted and effective organization-transformation program. It serves as a vehicle to stimulate thinking about the impact of various changes, saving untold amounts of time and resources in the process.



No one had a good idea of the decisions and actions for which he or

she was responsible. The general lack of information flow extended to decision rights, as few managers understood where their authority ended and another's began. Accountability even for day-to-day decisions was unclear, and managers did not know whom to ask for clarification. Naturally, confusion over decision rights led to second-guessing. Fifty-five percent of respondents felt that decisions were regularly second-guessed at Woodward.

To Woodward's credit, its top executives immediately responded to the results of the diagnostic by launching a change program targeted at all three problem areas. The program integrated early, often symbolic, changes with longer-term initiatives, in an effort to build momentum and galvanize participation and ownership. Recognizing that a passive-aggressive attitude toward people perceived to be in power solely as a result of their position in the hierarchy was hindering information flow, they took immediate steps to signal their intention to create a more informal and open culture. One symbolic change: the seating at management meetings was rearranged. The top executives used to sit in a separate section, the physical space between them and the rest of the room fraught with symbolism. Now they intermingled, making themselves more accessible and encouraging people to share information informally. Regular brown-bag lunches were established with members of the C-suite, where people had a chance to discuss the overall culture-change initiative, decision rights, new mechanisms for communicating across the units, and so forth. Seating at these events was highly choreographed to ensure that a mix of units was represented at each table. Icebreaker activities were designed to encourage individuals to learn about other units' work.

Meanwhile, senior managers commenced the real work of remedying issues relating to information flows and decision rights. They assessed their own informal networks to understand how people making key decisions got their information, and they identified critical gaps. The outcome was a new framework for making important decisions that clearly specifies who owns each decision, who must provide input, who is ultimately accountable for the results, and how results are defined. Other longer-term initiatives include:

- Pushing certain decisions down into the organization to better align decision rights with the best available information. Most hiring and

bonus decisions, for instance, have been delegated to immediate managers, so long as they are within preestablished boundaries relating to numbers hired and salary levels. Being clear about who needs what information is encouraging cross-group dialogue.

- Identifying and eliminating duplicative committees.
- Pushing metrics and scorecards down to the group level, so that rather than focus on solving the mystery of *who* caused a problem, management can get right to the root cause of *why* the problem occurred. A well-designed scorecard captures not only outcomes (like sales volume or revenue) but also leading indicators of those outcomes (such as the number of customer calls or completed customer plans). As a result, the focus of management conversations has shifted from trying to explain the past to charting the future—anticipating and preventing problems.
- Making the planning process more inclusive. Groups are explicitly mapping out the ways their initiatives depend on and affect one another; shared group goals are assigned accordingly.
- Enhancing the middle management career path to emphasize the importance of lateral moves to career advancement.

Goodward Insurance has just embarked on this journey. The insurer has distributed ownership of these initiatives among various groups and management levels so that these efforts don't become silos in themselves. Already, solid improvement in the company's execution is beginning to emerge. The early evidence of success has come from employee-satisfaction surveys: Middle management responses to the questions about levels of cross-unit collaboration and clarity of decision making have improved as much as 20 to 25 percentage points. And high performers are already reaching across boundaries to gain a broader understanding of the full business, even if it doesn't mean a better title right away.

Execution is a notorious and perennial challenge. Even at the companies that

are best at it—what we call “resilient organizations”—just two-thirds of employees agree that important strategic and operational decisions are quickly translated into action. As long as companies continue to attack their execution problems primarily or solely with structural or motivational initiatives, they will continue to fail. As we’ve seen, they may enjoy short-term results, but they will inevitably slip back into old habits because they won’t have addressed the root causes of failure. Such failures can almost always be fixed by ensuring that people truly understand what they are responsible for and who makes which decisions—and then giving them the information they need to fulfill their responsibilities. With these two building blocks in place, structural and motivational elements will follow.

Originally published in June 2008. Reprint R0806C.

Notes

[1.](#) The details for this example have been taken from Gary L. Neilson and Bruce A. Pasternack, *Results: Keep What's Good, Fix What's Wrong, and Unlock Great Performance* (Random House, 2005).

Using the Balanced Scorecard as a Strategic Management System

by Robert S. Kaplan and David P. Norton

AS COMPANIES AROUND the world transform themselves for competition that is based on information, their ability to exploit intangible assets has become far more decisive than their ability to invest in and manage physical assets. Several years ago, in recognition of this change, we introduced a concept we called the *balanced scorecard*. The balanced scorecard supplemented traditional financial measures with criteria that measured performance from three additional perspectives—those of customers, internal business processes, and learning and growth. (See “Translating vision and strategy: Four perspectives.”) It therefore enabled companies to track financial results while simultaneously monitoring progress in building the capabilities and acquiring the intangible assets they would need for future growth. The scorecard wasn’t a replacement for financial measures; it was their complement.

Recently, we have seen some companies move beyond our early vision for the scorecard to discover its value as the cornerstone of a new strategic management system. Used this way, the score- card addresses a serious deficiency in traditional management systems: their inability to link a company’s long-term strategy with its short-term actions.

Most companies’ operational and management control systems are built around financial measures and targets, which bear little relation to the company’s progress in achieving long-term strategic objectives. Thus the

emphasis most companies place on short-term financial measures leaves a gap between the development of a strategy and its implementation.

Managers using the balanced scorecard do not have to rely on short-term financial measures as the sole indicators of the company's performance. The scorecard lets them introduce four new management processes that, separately and in combination, contribute to linking long-term strategic objectives with short-term actions. (See "Managing strategy: Four processes.")

The first new process—*translating the vision*—helps managers build a consensus around the organization's vision and strategy. Despite the best intentions of those at the top, lofty statements about becoming "best in class," "the number one supplier," or an "empowered organization" don't translate easily into operational terms that provide useful guides to action at the local level. For people to act on the words in vision and strategy statements, those statements must be expressed as an integrated set of objectives and measures, agreed upon by all senior executives, that describe the long-term drivers of success.

The second process—*communicating and linking*—lets managers communicate their strategy up and down the organization and link it to departmental and individual objectives. Traditionally, departments are evaluated by their financial performance, and individual incentives are tied to short-term financial goals. The scorecard gives managers a way of ensuring that all levels of the organization understand the long-term strategy and that both departmental and individual objectives are aligned with it.

The third process—*business planning*—enables companies to integrate their business and financial plans. Almost all organizations today are implementing a variety of change programs, each with its own champions, gurus, and consultants, and each competing for senior executives' time, energy, and resources. Managers find it difficult to integrate those diverse initiatives to achieve their strategic goals—a situation that leads to frequent disappointments with the programs' results. But when managers use the ambitious goals set for balanced scorecard measures as the basis for allocating resources and setting priorities, they can undertake and coordinate only those initiatives that move them toward their long-term strategic objectives.

Idea in Brief

Why do budgets often bear little direct relation to a company's long-term strategic objectives? Because they don't take enough into consideration. A balanced scorecard augments traditional financial measures with benchmarks for performance in three key nonfinancial areas:

- a company's relationship with its customers
- its key internal processes
- its learning and growth.

When performance measures for these areas are added to the financial metrics, the result is not only a broader perspective on the company's health and activities, it's also a powerful organizing framework. A sophisticated instrument panel for coordinating and fine-tuning a company's operations and businesses so that all activities are aligned with its strategy.

The fourth process—*feedback and learning*—gives companies the capacity for what we call strategic learning. Existing feedback and review processes focus on whether the company, its departments, or its individual employees have met their budgeted financial goals. With the balanced scorecard at the center of its management systems, a company can monitor short-term results from the three additional perspectives—customers, internal business processes, and learning and growth—and evaluate strategy in the light of recent performance. The scorecard thus enables companies to modify strategies to reflect real-time learning.

Idea in Practice

The balanced scorecard relies on four processes to bind short-term activities to long-term objectives:

1. Translating the Vision

By relying on measurement, the scorecard forces managers to come to agreement on the metrics they will use to operationalize their lofty visions.

Example: A bank had articulated its strategy as providing “superior service to targeted customers.” But the process of choosing operational measures for the four areas of the scorecard made executives realize that they first needed to reconcile divergent views of who the targeted customers were and what constituted superior service.

2. Communicating and Linking

When a scorecard is disseminated up and down the organizational chart, strategy becomes a tool available to everyone. As the high-level scorecard cascades down to individual business units, overarching strategic objectives and measures are translated into objectives and measures appropriate to each particular group. Tying these targets to individual performance and compensation systems yields “personal scorecards.” Thus, individual employees understand how their own productivity supports the overall strategy.

3. Business Planning

Most companies have separate procedures (and sometimes units) for

strategic planning and budgeting. Little wonder, then, that typical long-term planning is, in the words of one executive, where “the rubber meets the sky.” The discipline of creating a balanced scorecard forces companies to integrate the two functions, thereby ensuring that financial budgets do indeed support strategic goals. After agreeing on performance measures for the four scorecard perspectives, companies identify the most influential “drivers” of the desired outcomes and then set milestones for gauging the progress they make with these drivers.

4. Feedback and Learning

By supplying a mechanism for strategic feedback and review, the balanced scorecard helps an organization foster a kind of learning often missing in companies: the ability to reflect on inferences and adjust theories about cause-and-effect relationships.

Feedback about products and services. New learning about key internal processes. Technological discoveries. All this information can be fed into the scorecard, enabling strategic refinements to be made continually. Thus, at any point in the implementation, managers can know whether the strategy is working—and if not, why.

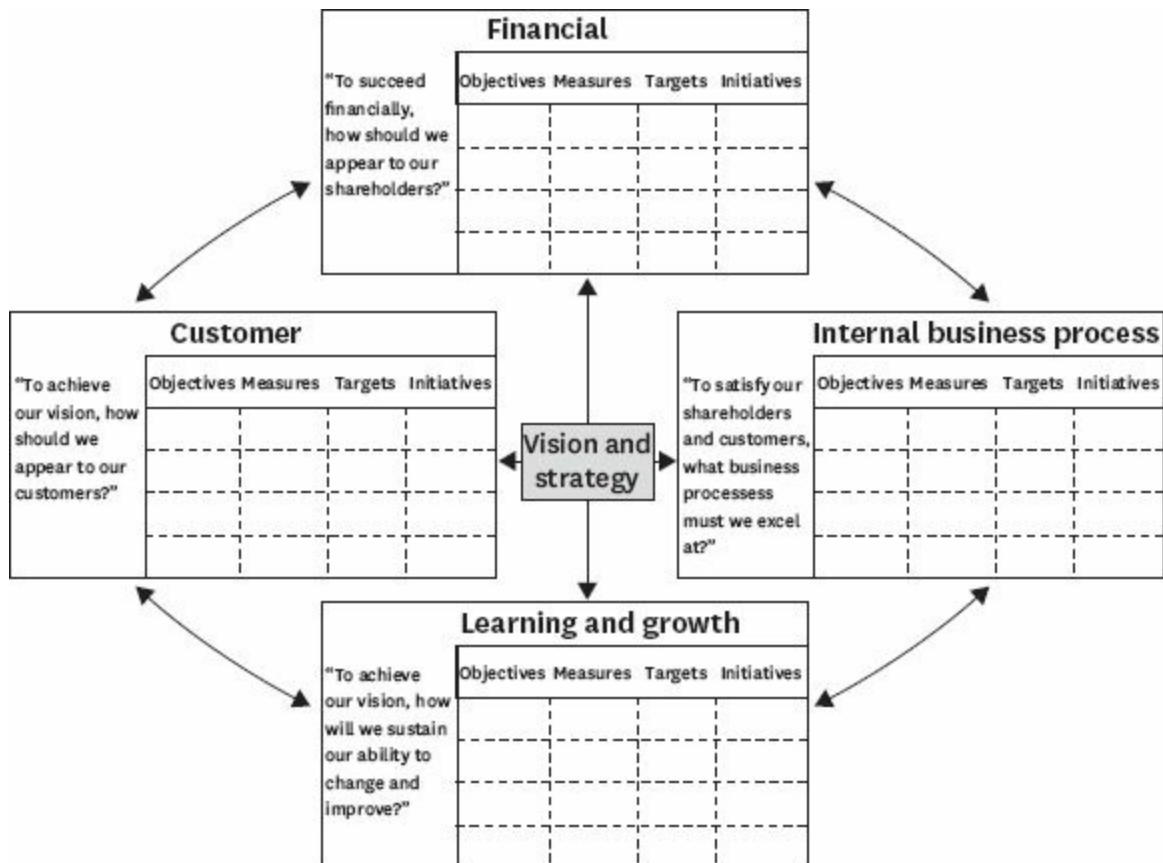
None of the more than 100 organizations that we have studied or with which we have worked implemented their first balanced scorecard with the intention of developing a new strategic management system. But in each one, the senior executives discovered that the scorecard supplied a framework and thus a focus for many critical management processes: departmental and individual goal setting, business planning, capital allocations, strategic initiatives, and feedback and learning. Previously, those processes were uncoordinated and often directed at short-term operational goals. By building the scorecard, the senior executives started a process of change that has gone well beyond the original idea of simply broadening the company’s performance measures.

For example, one insurance company—let’s call it National Insurance—developed its first balanced scorecard to create a new vision for itself as an underwriting specialist. But once National started to use it, the scorecard allowed the CEO and the senior management team not only to introduce a

new strategy for the organization but also to overhaul the company's management system. The CEO subsequently told employees in a letter addressed to the whole organization that National would thenceforth use the balanced scorecard and the philosophy that it represented to manage the business.

National built its new strategic management system step-by-step over 30 months, with each step representing an incremental improvement. (See "How one company built a strategic management system ...") The iterative sequence of actions enabled the company to reconsider each of the four new management processes two or three times before the system stabilized and became an established part of National's overall management system. Thus the CEO was able to transform the company so that everyone could focus on achieving long-term strategic objectives—something that no purely financial framework could do.

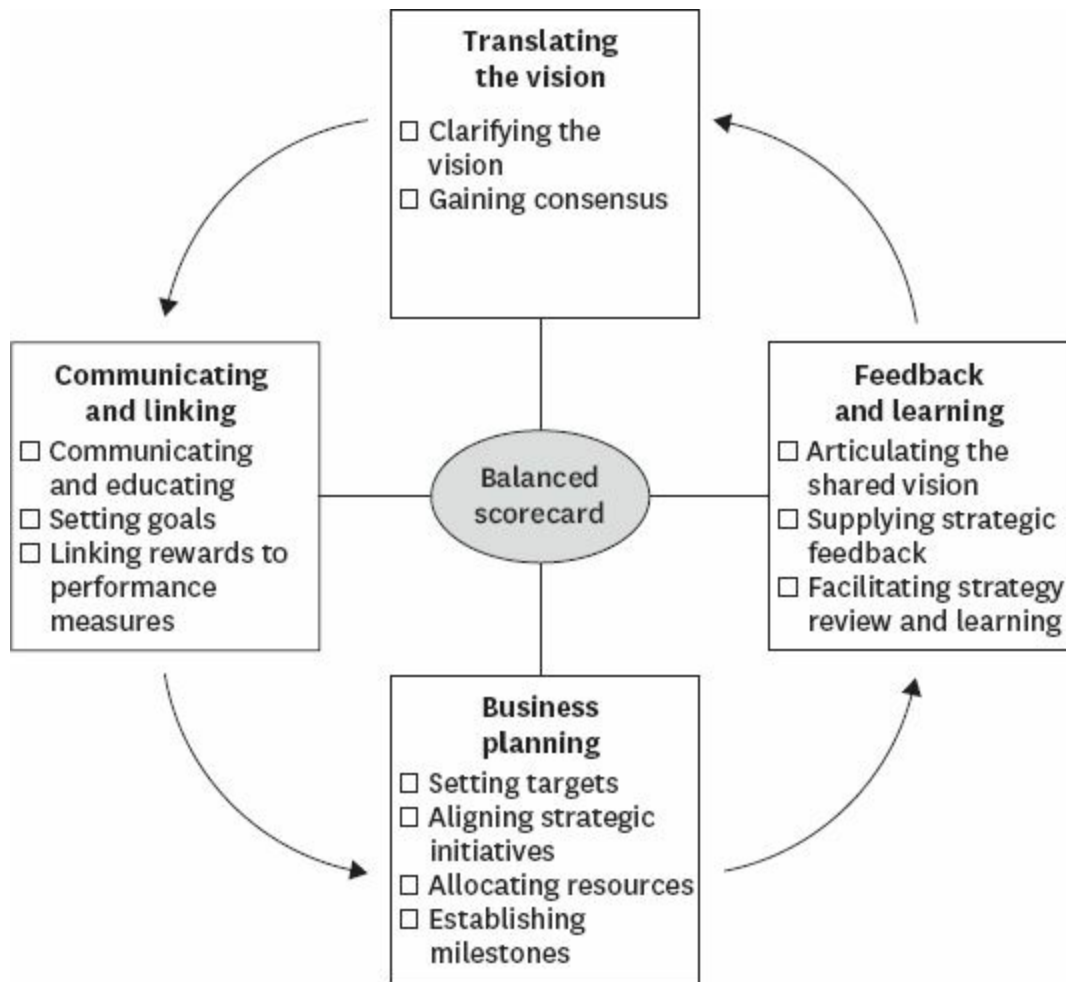
Translation vision and strategy: four perspectives



Translating the Vision

The CEO of an engineering construction company, after working with his senior management team for several months to develop a mission statement, got a phone call from a project manager in the field. “I want you to know,” the distraught manager said, “that I believe in the mission statement. I want to act in accordance with the mission statement. I’m here with my customer. What am I supposed to do?”

Managing strategy: four processes



The mission statement, like those of many other organizations, had declared an intention to “use high-quality employees to provide services that surpass customers’ needs.” But the project manager in the field with his employees and his customer did not know how to translate those words into the appropriate actions. The phone call convinced the CEO that a large gap existed between the mission statement and employees’ knowledge of how their day-to-day actions could contribute to realizing the company’s vision.

Metro Bank (not its real name), the result of a merger of two competitors,

encountered a similar gap while building its balanced scorecard. The senior executive group thought it had reached agreement on the new organization's overall strategy: "to provide superior service to targeted customers." Research had revealed five basic market segments among existing and potential customers, each with different needs. While formulating the measures for the customer-perspective portion of their balanced scorecard, however, it became apparent that although the 25 senior executives agreed on the words of the strategy, each one had a different definition of *superior service* and a different image of the *targeted customers*.

How one company built a strategic management system

...

2A Communicate to middle managers. The top three layers of management (100 people) are brought together to learn about and discuss the new strategy. The balanced scorecard is the communication vehicle. (months 4-5)

2B Develop business unit scorecards. Using the corporate scorecard as a template, each business unit translates its strategy into its own scorecard. (months 6-9)

5 Refine the vision. The review of business unit scorecards identifies several cross-business issues not initially included in the corporate strategy. The corporate scorecard is updated. (month 12)

Time frame (in months)

0	1	2	3	4	5	6	7	8	9	10	11	12

Actions:

1 Clarify the vision. Ten members of a newly formed executive team work together for three months. A balanced scorecard is developed to translate a generic vision into a strategy that is understood and can be communicated. The process helps build consensus and commitment to the strategy.

3A Eliminate nonstrategic investments. The corporate scorecard, by clarifying strategic priorities, identifies many active programs that are not contributing to the strategy. (month 6)

3B Launch corporate change programs. The corporate scorecard identifies the need for cross-business change programs. They are launched while the business units prepare their scorecards. (month 6)

4 Review business unit scorecards. The CEO and the executive team review the individual business units' scorecards. The review permits the CEO to participate knowledgeably in shaping business unit strategy. (months 9-11)

7 Update long-range plan and budget. Five-year goals are established for each measure. The investments required to meet those goals are identified and funded. The first year of the five-year plan becomes the annual budget. (months 15-17)

9 Conduct annual strategy review. At the start of the third year, the initial strategy has been achieved and the corporate strategy requires updating. The executive committee lists ten strategic issues. Each business unit is asked to develop a position on each issue as a prelude to updating its strategy and scorecard. (months 25-26)

13	14	15	16	17	18	19	20	21	22	23	24	25	26

6A Communicate the balanced scorecard to the entire company. At the end of one year, when the management teams are comfortable with the strategic approach, the scorecard is disseminated to the entire organization. (month 12-ongoing)

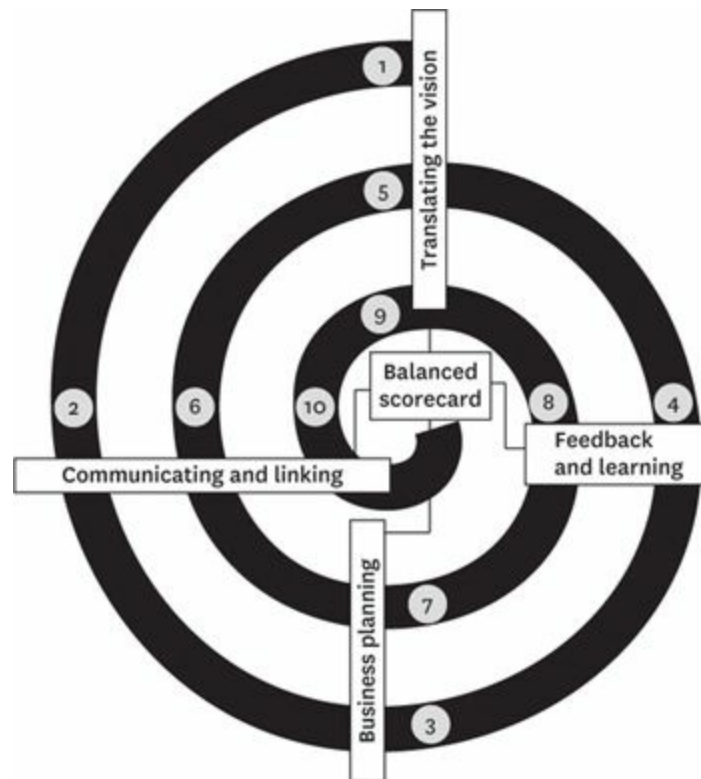
6B Establish individual performance objectives. The top three layers of management link their individual objectives and incentive compensation to their scorecards. (months 13-14)

8 Conduct monthly and quarterly reviews. After corporate approval of the business unit scorecards, a monthly review process, supplemented by quarterly reviews that focus more heavily on strategic issues, begins. (month 18-ongoing)

10 Link everyone's performance to the balanced scorecard. All employees are asked to link their individual objectives to the balanced scorecard. The entire organization's incentive compensation is linked to the scorecard. (months 25-26)

Note: Steps 7, 8, 9, and 10 are performed on a regular schedule. The balanced scorecard is now a routine part of the management process.

... around the balanced scorecard



The exercise of developing operational measures for the four perspectives on the bank's scorecard forced the 25 executives to clarify the meaning of the strategy statement. Ultimately, they agreed to stimulate revenue growth through new products and services and also agreed on the three most desirable customer segments. They developed scorecard measures for the specific products and services that should be delivered to customers in the targeted segments as well as for the relationship the bank should build with customers in each segment. The scorecard also highlighted gaps in employees' skills and in information systems that the bank would have to close in order to deliver the selected value propositions to the targeted customers. Thus, creating a balanced scorecard forced the bank's senior managers to arrive at a consensus and then to translate their vision into terms that had meaning to the people who would realize the vision.

Communicating and Linking

“The top ten people in the business now understand the strategy better than ever before. It’s too bad,” a senior executive of a major oil company complained, “that we can’t put this in a bottle so that everyone could share it.” With the balanced scorecard, he can.

One company we have worked with deliberately involved three layers of management in the creation of its balanced scorecard. The senior executive group formulated the financial and customer objectives. It then mobilized the talent and information in the next two levels of managers by having them formulate the internal-business-process and learning-and-growth objectives that would drive the achievement of the financial and customer goals. For example, knowing the importance of satisfying customers’ expectations of on-time delivery, the broader group identified several internal business processes—such as order processing, scheduling, and fulfillment—in which the company had to excel. To do so, the company would have to retrain frontline employees and improve the information systems available to them. The group developed performance measures for those critical processes and for staff and systems capabilities.

Broad participation in creating a scorecard takes longer, but it offers several advantages: Information from a larger number of managers is incorporated into the internal objectives; the managers gain a better understanding of the company’s long-term strategic goals; and such broad participation builds a stronger commitment to achieving those goals. But getting managers to buy into the scorecard is only a first step in linking individual actions to corporate goals.

The balanced scorecard signals to everyone what the organization is trying to achieve for shareholders and customers alike. But to align employees’ individual performances with the overall strategy, scorecard users generally engage in three activities: communicating and educating, setting goals, and linking rewards to performance measures.

Communicating and educating

Implementing a strategy begins with educating those who have to execute it. Whereas some organizations opt to hold their strategy close to the vest, most believe that they should disseminate it from top to bottom. A broad-based communication program shares with all employees the strategy and the critical objectives they have to meet if the strategy is to succeed. Onetime events such as the distribution of brochures or newsletters and the holding of “town meetings” might kick off the program. Some organizations post bulletin boards that illustrate and explain the balanced scorecard measures, then update them with monthly results. Others use groupware and electronic bulletin boards to distribute the scorecard to the desktops of all employees and to encourage dialogue about the measures. The same media allow employees to make suggestions for achieving or exceeding the targets.

The balanced scorecard, as the embodiment of business unit strategy, should also be communicated upward in the organization—to corporate headquarters and to the corporate board of directors. With the scorecard, business units can quantify and communicate their long-term strategies to senior executives using a comprehensive set of linked financial and nonfinancial measures. Such communication informs the executives and the board in specific terms that long-term strategies designed for competitive success are in place. The measures also provide the basis for feedback and accountability. Meeting short-term financial targets should not constitute satisfactory performance when other measures indicate that the long-term strategy is either not working or not being implemented well.

Should the balanced scorecard be communicated beyond the boardroom to external shareholders? We believe that as senior executives gain confidence in the ability of the scorecard measures to monitor strategic performance and predict future financial performance, they will find ways to inform outside investors about those measures without disclosing competitively sensitive information.

Skandia, an insurance and financial services company based in Sweden, issues a supplement to its annual report called “The Business Navigator”—“an instrument to help us navigate into the future and thereby

stimulate renewal and development.” The supplement describes Skandia’s strategy and the strategic measures the company uses to communicate and evaluate the strategy. It also provides a report on the company’s performance along those measures during the year. The measures are customized for each operating unit and include, for example, market share, customer satisfaction and retention, employee competence, employee empowerment, and technology deployment.

Communicating the balanced scorecard promotes commitment and accountability to the business’s long-term strategy. As one executive at Metro Bank declared, “The balanced scorecard is both motivating and obligating.”

Setting goals

Mere awareness of corporate goals, however, is not enough to change many people's behavior. Somehow, the organization's high-level strategic objectives and measures must be translated into objectives and measures for operating units and individuals.

The exploration group of a large oil company developed a technique to enable and encourage individuals to set goals for themselves that were consistent with the organization's. It created a small, fold-up, personal scorecard that people could carry in their shirt pockets or wallets. (See "The personal scorecard.") The scorecard contains three levels of information. The first describes corporate objectives, measures, and targets. The second leaves room for translating corporate targets into targets for each business unit. For the third level, the company asks both individuals and teams to articulate which of their own objectives would be consistent with the business unit and corporate objectives, as well as what initiatives they would take to achieve their objectives. It also asks them to define up to five performance measures for their objectives and to set targets for each measure. The personal scorecard helps to communicate corporate and business unit objectives to the people and teams performing the work, enabling them to translate the objectives into meaningful tasks and targets for themselves. It also lets them keep that information close at hand—in their pockets.

Linking rewards to performance measures

Should compensation systems be linked to balanced scorecard measures? Some companies, believing that tying financial compensation to performance is a powerful lever, have moved quickly to establish such a linkage. For example, an oil company that we'll call Pioneer Petroleum uses its scorecard as the sole basis for computing incentive compensation. The company ties 60% of its executives' bonuses to their achievement of ambitious targets for a weighted average of four financial indicators: return on capital, profitability, cash flow, and operating cost. It bases the remaining 40% on indicators of customer satisfaction, dealer satisfaction, employee satisfaction, and environmental responsibility (such as a percentage change in the level of emissions to water and air). Pioneer's CEO says that linking compensation to the scorecard has helped to align the company with its strategy. "I know of no competitor," he says, "who has this degree of alignment. It is producing results for us."

As attractive and as powerful as such linkage is, it nonetheless carries risks. For instance, does the company have the right measures on the scorecard? Does it have valid and reliable data for the selected measures? Could unintended or unexpected consequences arise from the way the targets for the measures are achieved? Those are questions that companies should ask.

The personal scorecard

Corporate objectives

- ☐ Double our corporate value in seven years.
- ☐ Increase our earnings by an average of 20% per year.
- ☐ Achieve an internal rate of return 2% above the cost of capital.
- ☐ Increase both production and reserves by 20% in the next decade.

Corporate targets					Scorecard measures	Business unit targets					Team/individual objectives and initiatives
1995	1996	1997	1998	1999		1995	1996	1997	1998	1999	
					Financial						1.
100	120	160	180	250	Earnings (in \$ millions)						
100	450	200	210	225	Net cash flow						
100	85	80	75	70	Overhead and operating expenses						2.
					Operating						
100	75	73	70	64	Production costs per barrel						
100	97	93	90	82	Development costs per barrel						
100	105	108	108	110	Total annual production						3.
					Team/individual measures	Targets					
1.											
2.											
3.											4.
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5.											
Name:											5.
Location:											

Furthermore, companies traditionally handle multiple objectives in a compensation formula by assigning weights to each objective and calculating incentive compensation by the extent to which each weighted objective was achieved. This practice permits substantial incentive compensation to be paid if the business unit overachieves on a few objectives even if it falls far short on others. A better approach would be to establish minimum threshold levels for a critical subset of the strategic measures. Individuals would earn no incentive compensation if performance in a given period fell short of any threshold. This requirement should motivate people to achieve a more balanced performance across short- and long-term objectives.

Some organizations, however, have reduced their emphasis on short-term,

formula-based incentive systems as a result of introducing the balanced scorecard. They have discovered that dialogue among executives and managers about the scorecard—both the formulation of the measures and objectives and the explanation of actual versus targeted results—provides a better opportunity to observe managers' performance and abilities. Increased knowledge of their managers' abilities makes it easier for executives to set incentive rewards subjectively and to defend those subjective evaluations—a process that is less susceptible to the game playing and distortions associated with explicit, formula-based rules.

One company we have studied takes an intermediate position. It bases bonuses for business unit managers on two equally weighted criteria: their achievement of a financial objective—economic value added—over a three-year period and a subjective assessment of their performance on measures drawn from the customer, internal- business-process, and learning-and-growth perspectives of the balanced scorecard.

That the balanced scorecard has a role to play in the determination of incentive compensation is not in doubt. Precisely what that role should be will become clearer as more companies experiment with linking rewards to scorecard measures.

Business Planning

“Where the rubber meets the sky”: That’s how one senior executive describes his company’s long-range-planning process. He might have said the same of many other companies because their financially based management systems fail to link change programs and resource allocation to long-term strategic priorities.

The problem is that most organizations have separate procedures and organizational units for strategic planning and for resource allocation and budgeting. To formulate their strategic plans, senior executives go off-site annually and engage for several days in active discussions facilitated by senior planning and development managers or external consultants. The outcome of this exercise is a strategic plan articulating where the company expects (or hopes or prays) to be in three, five, and ten years. Typically, such plans then sit on executives’ bookshelves for the next 12 months.

Meanwhile, a separate resource-allocation and budgeting process run by the finance staff sets financial targets for revenues, expenses, profits, and investments for the next fiscal year. The budget it produces consists almost entirely of financial numbers that generally bear little relation to the targets in the strategic plan.

Which document do corporate managers discuss in their monthly and quarterly meetings during the following year? Usually only the budget, because the periodic reviews focus on a comparison of actual and budgeted results for every line item. When is the strategic plan next discussed? Probably during the next annual off-site meeting, when the senior managers draw up a new set of three-, five-, and ten-year plans.

The very exercise of creating a balanced scorecard forces companies to integrate their strategic planning and budgeting processes and therefore helps to ensure that their budgets support their strategies. Scorecard users select measures of progress from all four scorecard perspectives and set targets for each of them. Then they determine which actions will drive them toward their targets, identify the measures they will apply to those drivers from the four

perspectives, and establish the short-term milestones that will mark their progress along the strategic paths they have selected. Building a scorecard thus enables a company to link its financial budgets with its strategic goals.

For example, one division of the Style Company (not its real name) committed to achieving a seemingly impossible goal articulated by the CEO: to double revenues in five years. The forecasts built into the organization's existing strategic plan fell \$1 billion short of this objective. The division's managers, after considering various scenarios, agreed to specific increases in five different performance drivers: the number of new stores opened, the number of new customers attracted into new and existing stores, the percentage of shoppers in each store converted into actual purchasers, the portion of existing customers retained, and average sales per customer.

By helping to define the key drivers of revenue growth and by committing to targets for each of them, the division's managers eventually grew comfortable with the CEO's ambitious goal.

The process of building a balanced scorecard—clarifying the strategic objectives and then identifying the few critical drivers—also creates a framework for managing an organization's various change programs. These initiatives—reengineering, employee empowerment, time-based management, and total quality management, among others—promise to deliver results but also compete with one another for scarce resources, including the scarcest resource of all: senior managers' time and attention.

Shortly after the merger that created it, Metro Bank, for example, launched more than 70 different initiatives. The initiatives were intended to produce a more competitive and successful institution, but they were inadequately integrated into the overall strategy. After building their balanced scorecard, Metro Bank's managers dropped many of those programs—such as a marketing effort directed at individuals with very high net worth—and consolidated others into initiatives that were better aligned with the company's strategic objectives. For example, the managers replaced a program aimed at enhancing existing low-level selling skills with a major initiative aimed at retraining salespersons to become trusted financial advisers, capable of selling a broad range of newly introduced products to the three selected customer segments. The bank made both changes because the scorecard enabled it to gain a better understanding of the programs required to achieve its strategic objectives.

Once the strategy is defined and the drivers are identified, the scorecard

influences managers to concentrate on improving or reengineering those processes most critical to the organization's strategic success. That is how the scorecard most clearly links and aligns action with strategy.

The final step in linking strategy to actions is to establish specific short-term targets, or milestones, for the balanced scorecard measures. Milestones are tangible expressions of managers' beliefs about when and to what degree their current programs will affect those measures.

In establishing milestones, managers are expanding the traditional budgeting process to incorporate strategic as well as financial goals. Detailed financial planning remains important, but financial goals taken by themselves ignore the three other balanced scorecard perspectives. In an integrated planning and budgeting process, executives continue to budget for short-term financial performance, but they also introduce short-term targets for measures in the customer, internal-business-process, and learning-and-growth perspectives. With those milestones established, managers can continually test both the theory underlying the strategy and the strategy's implementation.

At the end of the business-planning process, managers should have set targets for the long-term objectives they would like to achieve in all four scorecard perspectives; they should have identified the strategic initiatives required and allocated the necessary resources to those initiatives; and they should have established milestones for the measures that mark progress toward achieving their strategic goals.

Feedback and Learning

“With the balanced scorecard,” a CEO of an engineering company told us, “I can continually test my strategy. It’s like performing real-time research.” That is exactly the capability that the scorecard should give senior managers: the ability to know at any point in its implementation whether the strategy they have formulated is, in fact, working, and if not, why.

The first three management processes—translating the vision, communicating and linking, and business planning—are vital for implementing strategy, but they are not sufficient in an unpredictable world. Together they form an important single-loop-learning process—single-loop in the sense that the objective remains constant, and any departure from the planned trajectory is seen as a defect to be remedied. This single-loop process does not require or even facilitate reexamination of either the strategy or the techniques used to implement it in light of current conditions.

Most companies today operate in a turbulent environment with complex strategies that, though valid when they were launched, may lose their validity as business conditions change. In this kind of environment, where new threats and opportunities arise constantly, companies must become capable of what Chris Argyris calls *double-loop learning*—learning that produces a change in people’s assumptions and theories about cause-and-effect relationships. (See “Teaching Smart People How to Learn,” HBR May–June 1991.)

Budget reviews and other financially based management tools cannot engage senior executives in double-loop learning—first, because these tools address performance from only one perspective, and second, because they don’t involve strategic learning. Strategic learning consists of gathering feedback, testing the hypotheses on which strategy was based, and making the necessary adjustments.

The balanced scorecard supplies three elements that are essential to strategic learning. First, it articulates the company’s shared vision, defining in clear and operational terms the results that the company, as a team, is trying to achieve. The scorecard communicates a holistic model that links individual

efforts and accomplishments to business unit objectives.

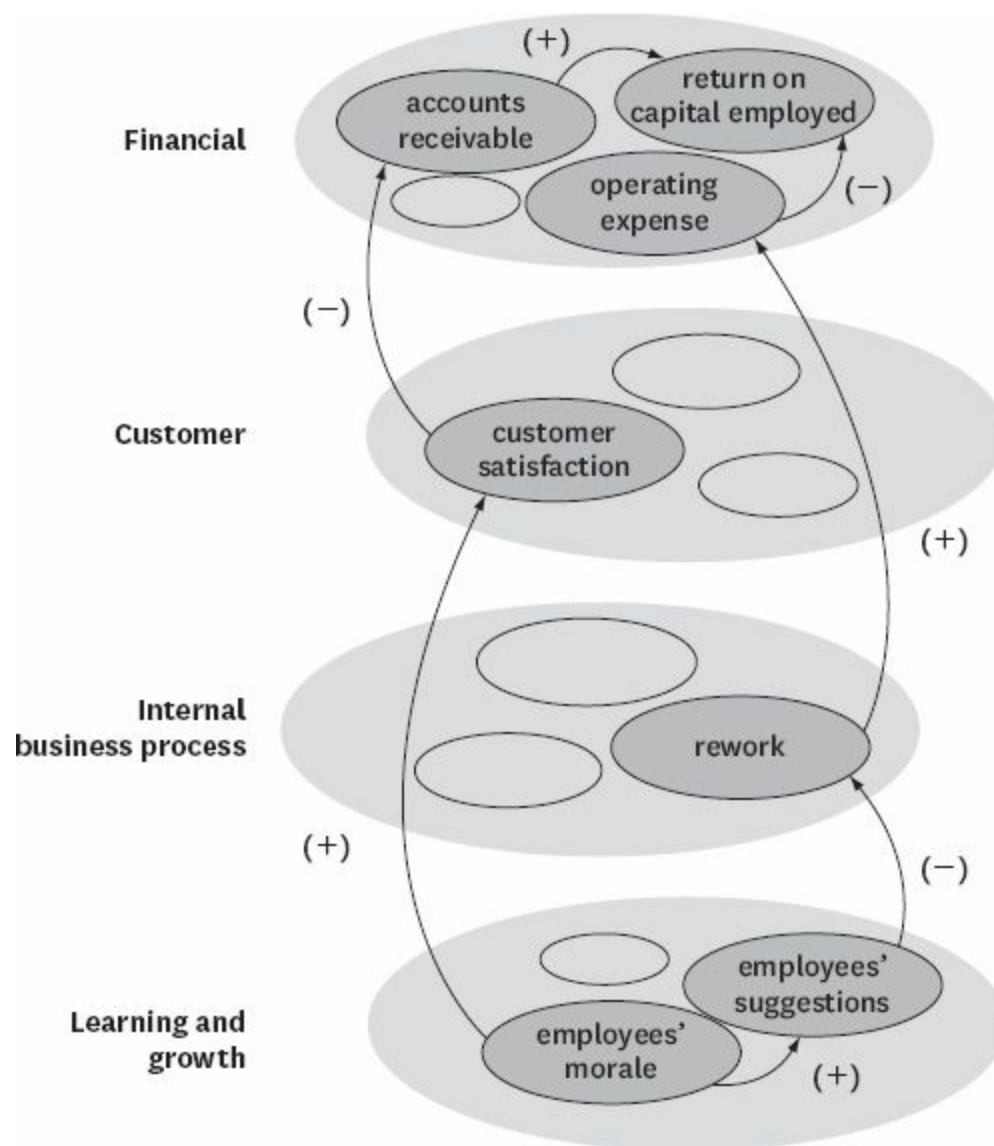
Second, the scorecard supplies the essential strategic feedback system. A business strategy can be viewed as a set of hypotheses about cause-and-effect relationships. A strategic feedback system should be able to test, validate, and modify the hypotheses embedded in a business unit's strategy. By establishing short-term goals, or milestones, within the business-planning process, executives are forecasting the relationship between changes in performance drivers and the associated changes in one or more specified goals. For example, executives at Metro Bank estimated the amount of time it would take for improvements in training and in the availability of information systems before employees could sell multiple financial products effectively to existing and new customers. They also estimated how great the effect of that selling capability would be.

Another organization attempted to validate its hypothesized cause-and-effect relationships in the balanced scorecard by measuring the strength of the linkages among measures in the different perspectives. (See the exhibit "How one company linked measures from the four perspectives.") The company found significant correlations between employees' morale, a measure in the learning-and-growth perspective, and customer satisfaction, an important customer perspective measure. Customer satisfaction, in turn, was correlated with faster payment of invoices—a relationship that led to a substantial reduction in accounts receivable and hence a higher return on capital employed. The company also found correlations between employees' morale and the number of suggestions made by employees (two learning-and-growth measures) as well as between an increased number of suggestions and lower rework (an internal-business-process measure). Evidence of such strong correlations help to confirm the organization's business strategy. If, however, the expected correlations are not found over time, it should be an indication to executives that the theory underlying the unit's strategy may not be working as they had anticipated.

Especially in large organizations, accumulating sufficient data to document significant correlations and causation among balanced scorecard measures can take a long time—months or years. Over the short term, managers' assessment of strategic impact may have to rest on subjective and qualitative judgments. Eventually, however, as more evidence accumulates, organizations may be able to provide more objectively grounded estimates of cause-and-effect relationships. But just getting managers to think

systematically about the assumptions underlying their strategy is an improvement over the current practice of making decisions based on short-term operational results.

How one company linked measures from the four perspectives



Third, the scorecard facilitates the strategy review that is essential to strategic learning. Traditionally, companies use the monthly or quarterly meetings between corporate and division executives to analyze the most

recent period's financial results. Discussions focus on past performance and on explanations of why financial objectives were not achieved. The balanced scorecard, with its specification of the causal relationships between performance drivers and objectives, allows corporate and business unit executives to use their periodic review sessions to evaluate the validity of the unit's strategy and the quality of its execution. If the unit's employees and managers have delivered on the performance drivers (retraining of employees, availability of information systems, and new financial products and services, for instance), then their failure to achieve the expected outcomes (higher sales to targeted customers, for example) signals that the theory underlying the strategy may not be valid. The disappointing sales figures are an early warning.

Managers should take such disconfirming evidence seriously and reconsider their shared conclusions about market conditions, customer value propositions, competitors' behavior, and internal capabilities. The result of such a review may be a decision to reaffirm their belief in the current strategy but to adjust the quantitative relationship among the strategic measures on the balanced scorecard. But they also might conclude that the unit needs a different strategy (an example of double-loop learning) in light of new knowledge about market conditions and internal capabilities. In any case, the scorecard will have stimulated key executives to learn about the viability of their strategy. This capacity for enabling organizational learning at the executive level—strategic learning—is what distinguishes the balanced scorecard, making it invaluable for those who wish to create a strategic management system.

Toward a New Strategic Management System

Many companies adopted early balanced scorecard concepts to improve their performance measurement systems. They achieved tangible but narrow results. Adopting those concepts provided clarification, consensus, and focus on the desired improvements in performance. More recently, we have seen companies expand their use of the balanced scorecard, employing it as the foundation of an integrated and iterative strategic management system. Companies are using the scorecard to

- clarify and update strategy;
- communicate strategy throughout the company;
- align unit and individual goals with the strategy;
- link strategic objectives to long-term targets and annual budgets;
- identify and align strategic initiatives; and
- conduct periodic performance reviews to learn about and improve strategy.

The balanced scorecard enables a company to align its management processes and focuses the entire organization on implementing long-term strategy. At National Insurance, the scorecard provided the CEO and his managers with a central framework around which they could redesign each piece of the company's management system. And because of the cause-and-effect linkages inherent in the scorecard framework, changes in one component of the system reinforced earlier changes made elsewhere. Therefore, every change made over the 30-month period added to the

momentum that kept the organization moving forward in the agreed-upon direction.

Without a balanced scorecard, most organizations are unable to achieve a similar consistency of vision and action as they attempt to change direction and introduce new strategies and processes. The balanced scorecard provides a framework for managing the implementation of strategy while also allowing the strategy itself to evolve in response to changes in the company's competitive, market, and technological environments.

Originally published in January 1996. Reprint R0707M.

Transforming Corner-Office Strategy into Frontline Action

by Orit Gadiesh and James L. Gilbert

WE ALL KNOW THE BENEFITS of pushing decision making from the CEO's office out to the far reaches of an organization. Fleeting business opportunities can be seized quickly. Products and services better reflect subtle shifts in customers' preferences. Empowered workers are motivated to innovate and take risks.

But while the value of such an approach is clear, particularly in a volatile business environment, there is also a built-in risk: an organization in which everyone is a decision maker has the potential to spin out of control. Within a single company, it's tricky to achieve both decentralized decision making and coherent strategic action. Still, some companies—think General Electric, America Online, Vanguard, Dell, Wal-Mart, Southwest Airlines, and eBay—have done just that.

These companies employ what we call a *strategic principle*, a memorable and actionable phrase that distills a company's corporate strategy into its unique essence and communicates it throughout the organization. (For a list of companies' strategic principles, see "It's all in a phrase.")

This tool—which we have observed in use at about a dozen companies, even though they don't label it as such—would always serve a company well. But it has become particularly useful in today's rapidly and constantly changing business environment. Indeed, in our conversations and work with more than 50 CEOs over the past two years, we have come to appreciate the

strategic principle's power—its ability to help companies maintain strategic focus while fostering the flexibility among employees that permits innovation and a rapid response to opportunities. Strategic principles are likely to become even more crucial to corporate success in the years ahead.

Distillation and Communication

To better understand what a strategic principle is and how it can be used, it may be helpful to look at a military analogy: the rules of engagement for battle. For example, Admiral Lord Nelson's crews in Britain's eighteenth-century wars against the French were guided by a simple strategic principle: whatever you do, get alongside an enemy ship.

The Royal Navy's seamanship, training, and experience gave it the advantage every time it engaged one-on-one against any of Europe's lesser fleets. So Nelson rejected as impractical the common practice of an admiral attempting to control a fleet through the use of flag signals. Instead, he gave his captains strategic parameters—they knew they had to battle rival ships one-on-one—leaving them to determine exactly how to engage in such combat. By using a strategic principle instead of explicit signals to direct his forces, Nelson consistently defeated the French, including a great victory in the dark of night, when signals would have been useless. Nelson's rule of engagement was simple enough for every one of his officers and sailors to know by heart. And it was enduring, a valid directive that was good until the relative naval capabilities of Britain and its rivals changed.

The distillation of a company's strategy into a pithy, memorable, and prescriptive phrase is important because a brilliant business strategy, like an insightful approach to warfare, is of little use unless people understand it well enough to apply it—both to anticipated decisions and unforeseen opportunities. In our work, we often see evidence of what we call the 80-100 rule: you're better off with a strategy that is 80% right and 100% implemented than one that is 100% right but doesn't drive consistent action throughout the company. A strategic principle can help a company balance that ratio.

Idea in Brief

Southwest Airlines keeps soaring. Its stock price rose a compounded 21,000% between 1972 and 1992 and leapt 300% between 1995 and 2000.

Why does Southwest succeed while so many other airlines fail? Because it sticks to its powerful **strategic principle**: “Meet customers’ short-haul travel needs at fares competitive with the cost of automobile travel.” This pithy, memorable, action-oriented phrase distills Southwest’s unique strategy and communicates it throughout the company.

An effective **strategic principle** lets a company simultaneously:

- maintain strategic focus,
- empower workers to innovate and take risks,
- seize fleeting opportunities,
- create products and services that meet subtle shifts in customers’ needs.

In today’s rapidly changing world, companies must integrate decentralized decision making *with* coherent, strategic action. A well-crafted, skillfully implemented **strategic principle** lets them strike that delicate balance.

The beauty of having a corporate strategic principle—a company should have only one—is that everyone in an organization, the executives in the front office as well as people in the operating units, can knowingly work

toward the same strategic objective without being rigid about how they do so. Decisions don't always have to make the slow trip to and from the executive suite. When a strategic principle is well crafted and effectively communicated, managers at all levels can be trusted to make decisions that advance rather than undermine company strategy.

Idea in Practice

Hallmarks of Powerful Strategic Principles

A successful strategic principle:

- Forces trade-offs between competing resources.

Example: Southwest Airlines' 1983 expansion to the high-traffic Denver area *seemed* sensible. But unusually long delays there due to bad weather and taxi time would have forced Southwest to increase ticket prices—preventing it from adhering to its strategic principle of offering air fares competitive with the cost of auto travel. The company pulled out of Denver.

- Tests the strategic soundness of particular decisions by linking leaders' strategic insights with line operators' pragmatic sense.

Example: AOL's strategic principle, "Consumer connectivity first—anytime, anywhere," tested the wisdom of a powerful business decision: expanding AOL's global network through alliances with local partners, rather than using its own technology everywhere. Partners' understanding of local culture greatly increased customers' connectivity.

- Sets clear boundaries within which employees operate and

experiment.

Example: At mutual-fund giant The Vanguard Group, frontline employees conceived a potent idea: Let customers access their accounts on-line, but limit on-line trading. This move kept Vanguard's costs low, enabling the company to stick to its strategic principle: creating "unmatchable value for investors/owners."

Creating and Communicating Your Strategic Principle

Capturing and communicating the essence of your company's strategy in a simple, memorable, actionable phrase isn't easy. These steps can help:

1. **Draft a working strategic principle.** Summarize your *corporate strategy*—your plan to allocate scarce resources in order to create value that distinguishes you from competitors—in a brief phrase. That phrase becomes your working *strategic principle*.
2. **Test its endurance.** A good strategic principle endures. Ask: Does our working strategic principle capture the timeless essence of our company's unique competitive value?
3. **Test its communicative power.** Ask: Is the phrase clear, concise, memorable? Would you feel proud to paint it on the side of your firm's trucks, as Wal-Mart does?
4. **Test its ability to promote and guide action.** Ask: Does the principle exhibit the three essential attributes: forcing trade-offs, testing the wisdom of business moves, setting boundaries for employees' experimentation?
5. **Communicate it.** Communicate your strategic principle

consistently, simply, and repeatedly. You'll know you've succeeded when employees—as well as business writers, MBA students, and competitors— all “chant the rant.”

Given what we've said so far, a strategic principle might seem to be a mission statement by another name. But while both help employees understand a company's direction, the two are different tools that communicate different things. A mission statement informs a company's *culture*. A strategic principle drives a company's *strategy*. A mission statement is *aspirational*: it gives people something to strive for. A strategic principle is *action oriented*: it enables people to do something now. A mission statement is meant to *inspire* frontline workers. A strategic principle enables them to *act* quickly by giving them explicit guidance to make strategically consistent choices.

Consider the difference between GE's mission statement and its strategic principle. The company's mission statement exhorts GE's leaders—“always with unyielding integrity”—to be “passionately focused on driving customer success” and to “create an environment of ‘stretch,’ excitement, informality, and trust,” among other things. The language is aspirational and emotional. By contrast, GE's well-known strategic principle—“Be number one or number two in every industry in which we compete, or get out”—is action oriented. The first part of the phrase is an explicit strategic challenge, and the second part leaves no question in line managers' minds about what they should do.

Three Defining Attributes

A strategic principle, as the distillation of a company's strategy, should guide a company's allocation of scarce resources—capital, time, management's attention, labor, and brand—in order to build a sustainable competitive advantage. It should tell a company what to do and, just as important, what not to do. More specifically, an effective strategic principle does the following:

- It forces trade-offs between competing resource demands;
- It tests the strategic soundness of a particular action;
- It sets clear boundaries within which employees must operate while granting them freedom to experiment within those constraints.

These three qualities can be seen in America Online's strategic principle. CEO Steve Case says personal interaction on-line is the soul of the Internet, and he has positioned AOL to create that interaction. Thus, AOL's strategic principle in the years leading up to its recent merger with Time Warner has been "Consumer connectivity first—anytime, anywhere."

This strategic principle has helped AOL make tough choices when allocating its resources. For example, in 1997, the company needed cash to grow, so it sold off its network infrastructure and outsourced that capability—a risky move at a time when it appeared that network ownership might be the key to success on the Internet. In keeping with its strategic principle, AOL instead spent its time and cash on improving connectivity at its Web site, focusing particularly on access, navigation, and interaction. As a result, it avoided investing capital in what turned out to be a relatively low-return business.

Its strategic principle has also helped AOL test whether a given business move makes strategic sense. For instance, the Internet company has chosen to expand its global network through alliances with local partners, even though that approach can take longer than simply transplanting AOL's own technology and know-how. AOL acknowledges that a local partner better understands the native culture and community, which is essential for connecting with customers.

Finally, AOL's strategic principle has spurred focused experimentation in the field by clearly defining employees' latitude for making moves. For example, AOL's former vice president of marketing, Jan Brandt, mailed more than 250 million AOL diskettes to consumers nationwide. The innovative campaign turned the company into one of the best-known names in cyberspace—all because Brandt, now AOL's vice chair and chief marketing officer, guided by the principle of connecting consumers, put her resources into empowering AOL's target community rather than sinking time and money into slick advertising.

As AOL's experience illustrates, a strong strategic principle can inform high-level corporate decisions—those involving divestitures, for example—as well as decisions made by department heads or others further down in an organization. It also frees up CEOs from constant involvement in the implementation of their strategic mandates. “The genius of a great leader is to leave behind him a situation that common sense, without the grace of genius, can deal with successfully,” said journalist and political thinker Walter Lippman. Scratch the surface of a number of high-performing companies, and you'll find that strategic principles are connecting the strategic insights—if not always the genius—of leaders with the pragmatic sense of line operators.

Now More Than Ever

In the past, a strategic principle was nice to have but was hardly required, unless a company found itself in a trying business situation. Today, many companies simultaneously face four situations that make a strategic principle crucial for success: decentralization, rapid growth, technological change, and institutional turmoil.

For the reasons mentioned above, *decentralization* is becoming common at companies of all stripes; thus, there is a corresponding need for a mechanism to ensure coherent strategic action. Especially in the case of diversified conglomerates, where strategy is formed in each of the business units, a strategic principle can help executives maintain consistency while giving unit managers the freedom to tailor their strategies to meet their own needs. It can also clarify the value of the center at such far-flung companies. For example, GE's long-standing strategic principle of always being number one or number two in an industry offers a powerful rationale for how a conglomerate can create value but still give individual units considerable strategic freedom.

A strategic principle is also crucial when a company is experiencing *rapid growth*. During such times, it's increasingly the case that less-experienced managers are forced to make decisions about nettlesome issues for which there may be no precedent. A clear and precise strategic principle can help counteract this shortage of experience. This is particularly true when a start-up company is growing rapidly in an established industry. For instance, as Southwest Airlines began to grow quickly, it might have been tempted to mimic its rivals' ultimately unsuccessful strategies if it hadn't had its own strategic principle to follow: "Meet customers' short-haul travel needs at fares competitive with the cost of automobile travel." Likewise, eBay, whose principle is "Focus on trading communities," might have been tempted, like many Internet marketplaces, to diversify into all sorts of services. But eBay has chosen to outsource certain services—for instance, management of the photos that sellers post on the site to illustrate the items they put up for bid—

while it continues to invest in services like Billpoint, which lets sellers accept credit-card payments from bidders. EBay's strategic principle has ensured that the entire company stays focused on the core trading business.

The staggering pace of *technological change* over the past decade has been costly for companies that don't have a strategic principle. Never before in business has there been more uncertainty combined with so great an emphasis on speed. Managers in high-tech industries in particular must react immediately to sudden and unexpected developments. Often, the sum of the reactions across the organization ends up defining the company's strategic course. A strategic principle—for example, Dell's mandate to sell direct to end users—helps ensure that the decisions made by frontline managers in such circumstances add up to a consistent, coherent strategy.

It's all in a phrase

A handful of companies have distilled their strategy into a phrase and have used it to drive consistent strategic action throughout their organizations.

Company	Strategic Principle
America Online	<i>Consumer connectivity first—anytime, anywhere</i>
Dell	<i>Be direct</i>
eBay	<i>Focus on trading communities</i>
General Electric	<i>Be number one or number two in every industry in which we compete, or get out</i>
Southwest Airlines	<i>Meet customers' short-haul travel needs at fares competitive with the cost of automobile travel</i>
Vanguard	<i>Unmatchable value for the investor-owner</i>
Wal-Mart	<i>Low prices, every day</i>

Finally, a strategic principle can help provide continuity during periods of *organizational turmoil*. An increasingly common example of turmoil in this era of short-term CEOs is leadership succession. A new CEO can bring with him or her a new strategy—but not necessarily a new strategic principle. For instance, when Jack Brennan took over as chairman and CEO at Vanguard five years ago, the strategic transition was seamless, despite some tension around the leadership transition. He maintained the mutual fund company's strategic principle—"Unmatchable value for the investor-owner"—thereby allowing managers to pursue their strategic objectives without many of the distractions so often associated with leadership changes. (For our own experience with organizational turmoil and strategic principles, see the sidebar "Bain & Company: Case Study of a Strategic Principle.")

Bain & Company: Case Study of a Strategic Principle

I LEARNED THE MOST ABOUT strategic principles in the trenches at Bain & Company when, a decade ago, we almost went bankrupt.

Bill Bain founded Bain & Company nearly 30 years ago on the basis of a simple but powerful notion: “The product of a consultant should be results for clients—not reports.” Over time, this mandate to deliver results through strategy became Bain’s strategic principle. It remains so today.

This directive fosters specific action, as an effective strategic principle should. It means that, from the very beginning of an assignment, you are constantly thinking about how a recommendation will get implemented. It also requires you to tell clients the truth, even if it’s difficult, because you can’t achieve results by whitewashing problems. And this strategic principle has teeth: Bain has always measured partners’ performance according to the results they achieve for their clients, not just on billings to the firm.

That was the company I joined. And for many years it grew rapidly, all the time guided by its strategic principle. Then, just over a decade ago, the founding partners decided to get their money out and sold 30% of the firm to an employee stock-option plan. This saddled us with hundreds of millions of dollars of debt and tens of millions of dollars of interest payments. The move, whose details initially were not disclosed to the rest of us, was based on the assumption that the company would continue its historic growth rate of 50% a year, which couldn’t be sustained at the size we had become. When growth slowed, the details came to light.

The nonfounding partners faced a critical choice. Everybody had attractive offers. Competitors and the press predicted we wouldn't survive. Recruits and clients were watchful. To make a long story short, we sat down around a conference table and resolved to turn the company around. The key to doing that, we decided, was to stick with our strategic principle.

What followed was a couple of years during which adhering to that goal was achingly difficult. But doing so forced important trade-offs. In one case, right in the middle of the crisis, we pulled out of a major assignment that was inconsistent with our principle. We believed the projects that the client was determined to undertake could not produce significant results for the company. Today, we all believe that had we veered from our principle in that instance, we would not be around.

More recently, our strategic principle has freed us to explore other ventures. Seven years ago, for instance, we became interested in private equity consulting, quite a different business from serving corporate clients. We initially struggled with the notion but quickly realized that it fit our strategic principle of delivering results through strategy, only to a new client segment. We knew that we could trust our colleagues forming the practice area to act consistently with the company's broader goals because the strategic principle was fundamental to their perspective. The strength of our shared principle permitted us to experiment and ultimately develop a successful new practice area.

Our principle continues to let partners develop new practices, markets, and interests quickly and without splintering the firm. It has given us the capacity to evolve and endure.

—*Orit Gadiesh*

Strategic Principles in Action

Strategic principles and their benefits can best be understood by seeing the results they create.

Forcing trade-offs at Southwest Airlines

Southwest Airlines is one of the air-travel industry's great success stories. It is the only airline that hasn't lost money in the past 25 years. Its stock price rose a compounded 21,000% between 1972 and 1992, and it is up 300% over the past five years, which have been difficult ones in the airline industry. For most companies, such rapid growth would cause problems: legions of frontline employees taking up the mantle of decision making from core executives and, inevitably, stumbling. But in Southwest's case, employees have consistently made trade-offs in keeping with the company's strategic principle.

The process for making important and complicated decisions about things like network design, service offerings, route selection and pricing, cabin design, and ticketing procedures is straightforward. That's because the trade-offs required by the strategic principle are clear. For instance, in 1983, Southwest initiated service to Denver, a potentially high-traffic destination and a seemingly sensible expansion of the company's presence in the Southwestern United States. However, the airline experienced longer and more consistent delays at Denver's Stapleton airport than it did anywhere else. These delays were caused not by slow turnaround at the gate but by increased taxi time on the runway and planes circling in the air because of bad weather. Southwest had to decide whether the potential growth from serving the Denver market was worth the higher costs associated with the delays, which would ultimately be reflected in higher ticket prices. The company turned to its strategic principle: would the airline be able to maintain fares competitive with the cost of automobile travel? Clearly, in Denver at least, it couldn't. Southwest pulled out of Stapleton three years after inaugurating the service there and has not returned.

Testing action at AOL

A large part of AOL's ability to move so far and so fast across untrod ground lies in its practice of testing potential moves against its strategic principle. Employees who see attractive opportunities can ask themselves whether seizing one or several will lead to deeper consumer connectivity or broader distribution. Take, for example, line manager Katherine Borescnik, now president of programming at AOL. Several years ago she noticed increased activity—call it consumer connectivity—around the bulletin-board folders created on the site by two irreverent stock analysts and AOL subscribers. She offered the analysts the chance to create their own financial site, which became Motley Fool, a point of connection and information for do-it-yourself investors.

And AOL's strategic principle reaches even deeper into the organization. The hundreds of acquisitions and deals that AOL has made in the past few years have involved numerous employees. While top officers make final decisions, employees on the ground first screen opportunities against the company's strategic principle. Furthermore, the integration efforts following acquisitions, while choreographed at the top, are executed by a coterie of managers who ensure that the plans comply with the company's strategic principle. "We have succeeded, both in our deal making and in our integration, because our acquisitions have all been driven by our focus on how our customers communicate and connect," says Ken Novack, AOL Time Warner's vice chairman.

AOL's massive merger with Time Warner clearly furthers AOL's strategic principle of enabling consumer connections "anytime, anywhere" by adding TV and cable access to the Internet company's current dial-up access on the personal computer. But integrating this merger, which will involve hundreds of employees making and executing thousands of decisions, may be the ultimate test of AOL's strategic principle.

Experimenting within boundaries at Vanguard

The Vanguard Group, with \$565 billion in assets under management, has quietly become a giant in the mutual fund industry. The company's strategy is a response to the inability of most mutual funds to beat the market, often because of the cost of their marketing activities, overhead, and frequent transactions. To counter this, Vanguard discourages investors from making frequent trades and keeps its own overhead and advertising costs far below the industry average. It passes the savings directly to investors, who, because Vanguard is a mutual rather than a public company, are the fund's owners.

While this was Vanguard's founding strategy, for years the company didn't communicate it widely to employees. As a result, they often suggested initiatives that were out of sync with the company's core strategy. "Midlevel managers would walk in holding the newspaper saying, 'Look at what Fidelity just did. How about if we do that?'" Jack Brennan says. It wasn't apparent to them that Vanguard's strategy was very different from that of its rival, which has higher costs and isn't mutually owned. Over the years, Vanguard has invested considerable energy in crafting a strategic principle and using it to disseminate the company's strategy. Now, because employees understand the strategy, top management trusts them to initiate moves on their own.

Consider Vanguard's response to a major trend in retail fund distribution: the emergence of the on-line channel. Industry surveys indicated that most investors wanted Internet access to their accounts and that on-line traders were more active than off-line traders. So Vanguard chose to integrate the Internet into its service in a way that furthered its strategy of keeping costs low: basically, it lets customers access their accounts on-line, but it limits Web-based trading. It should be noted that the original ideas for Vanguard's on-line initiatives, including early ventures with AOL, were conceived by frontline employees, not senior executives.

Brennan says the company's strategic principle affects the entire management process, including hiring, training, performance measurement, and incentives. He points to a hidden benefit of having a strong strategic principle: "You're more efficient and can run with a leaner management team

because everyone is on the same page.”

Creating a Strategic Principle

Many of the best and most conspicuous examples of strategic principles come from companies that were founded on them, companies such as eBay, Dell, Vanguard, Southwest Airlines, and Wal-Mart (“Low prices, every day”). The founders of those companies espoused a clear guiding principle that summarized the essence of what would become a full-blown business strategy. They attracted investors who believed it, hired employees who bought into it, and targeted customers who wanted it.

Leaders of long-standing multinationals, like GE, crafted their strategic principles at a critical juncture: when increasing corporate complexity threatened to confuse priorities on the front line and obscure the essence that truly differentiated their strategy from that of their rivals.

Companies in this second category, which represents most of the companies that are likely to contemplate creating a strategic principle, face a demanding exercise. It probably comes as no surprise that identifying the essence of your strategy so it can be translated into a simple, memorable phrase is no easy task. It’s a bit like corporate genomics: the principle must isolate and capture the corporate equivalent of the genetic code that differentiates your company from its competitors. This is somewhat like identifying the 2% of DNA that separates man from monkey—or, even more difficult and more apt, the .1% of DNA that differentiates each human being.

There are different ways to identify the elements that must be captured in a strategic principle, but keep in mind that a corporate strategy represents a plan to effectively allocate scarce resources to achieve sustainable competitive advantage. Managers need to ask themselves: how does my company allocate those resources to create value in a unique way, one that differentiates my company from competitors? Try to summarize the answer in a brief phrase that captures the essence of your company’s point of differentiation.

Once that idea has been expressed in a phrase, test the strategic principle for its enduring nature. Does it capture what you intend to do for only the

next three to five years, or does it capture a more timeless essence: the genetic code of your company's competitive differentiation? Then test the strategic principle for its communicative power. Is it clear, concise, and memorable? Would you feel proud to paint it on the side of a truck, as Wal-Mart does?

Finally, test the principle for its ability to promote and guide action. In particular, assess whether it exhibits the three attributes of an effective strategic principle. Will it force trade-offs? Will it serve as a test for the wisdom of a particular business move, especially one that might promote short-term profits at the expense of long-term strategy? Does it set boundaries within which people will nonetheless be free to experiment?

Given the importance of getting your strategic principle right, it is wise to gather feedback on these questions from executives and other employees during an incubation period. Once you are satisfied that the statement is accurate and compelling, disseminate it throughout the organization.

Of course, just as a brilliant strategy is worthless unless it is implemented, a powerful strategic principle is of no use unless it is communicated effectively. When CEO Jack Welch talks about aligning employees around GE's strategy and values, he emphasizes the need for consistency, simplicity, and repetition. The approach is neither flashy nor complicated, but it takes enormous discipline and could scarcely be more important. Welch has so broadly evangelized GE's "Be number one or number two" strategic principle that employees are not the only ones to chant the rant. So can most business writers, MBA students, and managers at other companies.

When Rethinking Is Required

No strategy is eternal, nor is any strategic principle. But even if the elements of your strategy change, the very essence of it is likely to remain the same. Thus, your strategy may shift substantially as your customers' demographics and needs change. It may have to be modified in light of your company's changing costs and assets compared with those of competitors. Strategic half-lives are shortening, and, in general, strategy should be reviewed every quarter and updated every year. But while it's worth revisiting your strategic principle every time you reexamine your strategy, it is likely to change only when there is a significant shift in the basic economics and opportunities of your market caused by, say, legislation or a completely new technology or business model.

Even then, your strategic principle may need only refining or expanding. GE's strategic principle has been enhanced, but not replaced, since Welch articulated it in 1981. Similarly, AOL's strategic principle will need to be broadened, but not necessarily jettisoned, following its merger with Time Warner. Ultimately, the merged company's strategic principle will also need to embody the importance of high-quality and relevant content, Time Warner's hallmark.

Vanguard takes explicit steps to ensure that the direction provided by its strategic principle remains current. For example, as part of an internal "devil's advocacy" process, managers are divided into groups to critique and defend past decisions and current policies. Recently, the group reconsidered two major strategic policies: the prohibitions against opening branch offices and against acquiring money management firms. After considerable discussion, the policies remained in place. According to CEO Brennan, "Sometimes the greatest value [of revisiting our strategic principle] is reconfirming what we're already doing." At the same time, Vanguard has the process to identify when change is needed.

Fundamental Principles

Respondents to Bain's annual survey of executives on the usefulness of management tools repeatedly cite the key role a mission statement can play in a company's success. We agree that a mission statement is crucial for promulgating a company's values and building a robust corporate culture. But it still leaves a large gap in a company's management communications portfolio. At least as important as a mission statement is something that promulgates a company's strategy—that is, a strategic principle.

The ability of frontline employees to execute a company's strategy without close central oversight is vital as the pace of technological change accelerates and as companies grow rapidly and become increasingly decentralized. To drive such behavior, a company needs to give employees a mandate broad enough to encourage enterprising behavior but specific enough to align employees' initiatives with company strategy.

While not a perfect analogy, the U.S. Constitution is in some ways like a strategic principle. It articulates and embodies the essence of the country's "strategy"—to guarantee liberty and justice for all of its citizens—while providing direction to those drafting the laws and regulations that implement the strategy. While no corporate strategy has liberty and justice at its heart, the elements of an effective strategy are just as central to the success of a company as those concepts are to the prosperity of the United States. And in neither case will success be realized unless the core strategy is communicated broadly and effectively.

Bain consultant Coleman Mark assisted with this article.

Originally published in May 2001. Reprint R0105D.

Turning Great Strategy into Great Performance

by Michael C. Mankins and Richard Steele

THREE YEARS AGO, THE LEADERSHIP team at a major manufacturer spent months developing a new strategy for its European business. Over the prior half-decade, six new competitors had entered the market, each deploying the latest in low-cost manufacturing technology and slashing prices to gain market share. The performance of the European unit—once the crown jewel of the company’s portfolio—had deteriorated to the point that top management was seriously considering divesting it.

To turn around the operation, the unit’s leadership team had recommended a bold new “solutions strategy”—one that would leverage the business’s installed base to fuel growth in after-market services and equipment financing. The financial forecasts were exciting—the strategy promised to restore the business’s industry-leading returns and growth. Impressed, top management quickly approved the plan, agreeing to provide the unit with all the resources it needed to make the turnaround a reality.

Today, however, the unit’s performance is nowhere near what its management team had projected. Returns, while better than before, remain well below the company’s cost of capital. The revenues and profits that managers had expected from services and financing have not materialized, and the business’s cost position still lags behind that of its major competitors.

At the conclusion of a recent half-day review of the business’s strategy and performance, the unit’s general manager remained steadfast and vowed

to press on. “It’s all about execution,” she declared. “The strategy we’re pursuing is the right one. We’re just not delivering the numbers. All we need to do is work harder, work smarter.”

The parent company’s CEO was not so sure. He wondered: Could the unit’s lackluster performance have more to do with a mistaken strategy than poor execution? More important, what should he do to get better performance out of the unit? Should he do as the general manager insisted and stay the course—focusing the organization more intensely on execution—or should he encourage the leadership team to investigate new strategy options? If execution was the issue, what should he do to help the business improve its game? Or should he just cut his losses and sell the business? He left the operating review frustrated and confused—not at all confident that the business would ever deliver the performance its managers had forecast in its strategic plan.

Talk to almost any CEO, and you’re likely to hear similar frustrations. For despite the enormous time and energy that goes into strategy development at most companies, many have little to show for the effort. Our research suggests that companies on average deliver only 63% of the financial performance their strategies promise. Even worse, the causes of this strategy-to-performance gap are all but invisible to top management. Leaders then pull the wrong levers in their attempts to turn around performance—pressing for better execution when they actually need a better strategy, or opting to change direction when they really should focus the organization on execution. The result: wasted energy, lost time, and continued underperformance.

But, as our research also shows, a select group of high-performing companies have managed to close the strategy-to-performance gap through better planning *and* execution. These companies—Barclays, Cisco Systems, Dow Chemical, 3M, and Roche, to name a few—develop realistic plans that are solidly grounded in the underlying economics of their markets and then use the plans to drive execution. Their disciplined planning and execution processes make it far less likely that they will face a shortfall in actual performance. And, if they do fall short, their processes enable them to discern the cause quickly and take corrective action. While these companies’ practices are broad in scope—ranging from unique forms of planning to integrated processes for deploying and tracking resources—our experience suggests that they can be applied by any business to help craft great plans and

turn them into great performance.

Idea in Brief

Most companies' strategies deliver only 63% of their promised financial value. Why? Leaders press for better execution when they really need a sounder strategy. Or they craft a new strategy when execution is the true weak spot.

How to avoid these errors? View strategic planning and execution as inextricably linked—then raise the bar for both simultaneously. Start by applying seven deceptively straightforward rules, including: keeping your strategy simple and concrete, making resource-allocation decisions early in the planning process, and continuously monitoring performance as you roll out your strategic plan.

By following these rules, you reduce the likelihood of performance shortfalls. And even if your strategy still stumbles, you quickly determine whether the fault lies with the strategy itself, your plan for pursuing it, or the execution process. The payoff? You make the *right* midcourse corrections—promptly. And as high-performing companies like Cisco Systems, Dow Chemical, and 3M have discovered, you boost your company's financial performance 60% to 100%.

The Strategy-to-Performance Gap

In the fall of 2004, our firm, Marakon Associates, in collaboration with the Economist Intelligence Unit, surveyed senior executives from 197 companies worldwide with sales exceeding \$500 million. We wanted to see how successful companies are at translating their strategies into performance. Specifically, how effective are they at meeting the financial projections set forth in their strategic plans? And when they fall short, what are the most common causes, and what actions are most effective in closing the strategy-to-performance gap? Our findings were revealing—and troubling.

While the executives we surveyed compete in very different product markets and geographies, they share many concerns about planning and execution. Virtually all of them struggle to produce the financial performance forecasts in their long-range plans. Furthermore, the processes they use to develop plans and monitor performance make it difficult to discern whether the strategy-to-performance gap stems from poor planning, poor execution, both, or neither. Specifically, we discovered:

Idea in Practice

Seven rules for successful strategy execution:

- **Keep it simple.** Avoid drawn-out descriptions of lofty goals. Instead, clearly describe what your company will and won't do.

Example: Executives at European investment-banking giant Barclays Capital stated they wouldn't compete with large U.S. investment banks or in unprofitable equity-market segments. Instead, they'd position Barclays for investors' burgeoning need for fixed income.

- **Challenge assumptions.** Ensure that the assumptions underlying your long-term strategic plans reflect real market economics and your organization's actual performance relative to rivals'.

Example: Struggling conglomerate Tyco commissioned cross-functional teams in each business unit to continuously analyze their markets' profitability and their offerings, costs, and price positioning relative to competitors'. Teams met with corporate executives biweekly to discuss their findings. The revamped process generated more realistic plans and contributed to Tyco's dramatic turnaround.

- **Speak the same language.** Unit leaders and corporate strategy, marketing, and finance teams must agree on a common framework for assessing performance. For example, some high-performing companies use benchmarking to estimate the size of the profit pool available in each market their company serves, the pool's potential growth, and the company's likely portion of that pool, given its market share and profitability. By using the shared approach,

executives easily agree on financial projections.

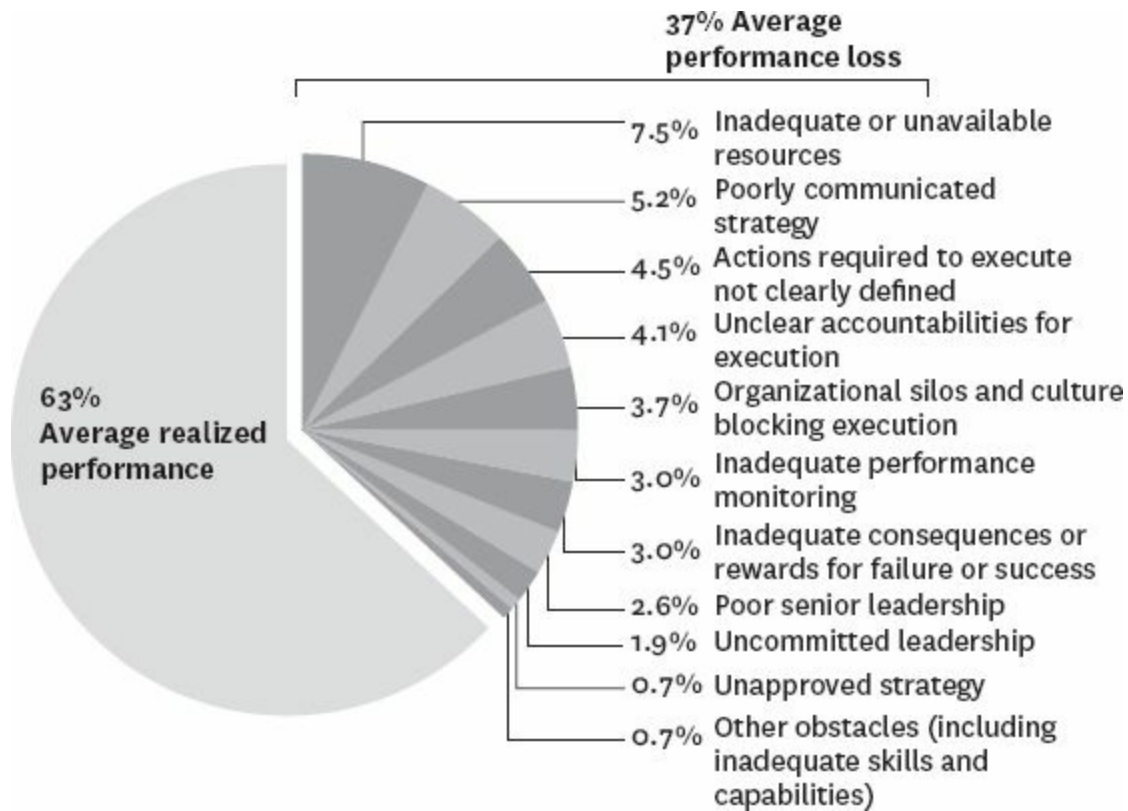
- **Discuss resource deployments early.** Challenge business units about when they'll need new resources to execute their strategy. By asking questions such as, "How fast can you deploy the new sales force?" and "How quickly will competitors respond?" you create more feasible forecasts and plans.
- **Identify priorities.** Delivering planned performance requires a few key actions taken at the right time, in the right way. Make strategic priorities explicit, so everyone knows what to focus on.
- **Continuously monitor performance.** Track real-time results against your plan, resetting planning assumptions and reallocating resources as needed. You'll remedy flaws in your plan *and* its execution—and avoid confusing the two.
- **Develop execution ability.** No strategy can be better than the people who must implement it. Make selection and development of managers a priority.

Example: Barclays' top executive team takes responsibility for all hiring. Members vet each others' potential hires and reward talented newcomers for superior execution. And stars aren't penalized if their business enters new markets with lower initial returns.

Companies rarely track performance against long-term plans

In our experience, less than 15% of companies make it a regular practice to go back and compare the business's results with the performance forecast for each unit in its prior years' strategic plans. As a result, top managers can't easily know whether the projections that underlie their capital-investment and portfolio-strategy decisions are in any way predictive of actual performance. More important, they risk embedding the same disconnect between results and forecasts in their future investment decisions. Indeed, the fact that so few companies routinely monitor actual versus planned performance may help explain why so many companies seem to pour good money after bad—continuing to fund losing strategies rather than searching for new and better options.

Where the performance goes



This chart shows the average performance loss implied by the importance ratings that managers in our survey gave to specific breakdowns in the planning and execution process.

Multiyear results rarely meet projections

When companies do track performance relative to projections over a number of years, what commonly emerges is a picture one of our clients recently described as a series of “diagonal venetian blinds,” where each year’s performance projections, when viewed side by side, resemble venetian blinds hung diagonally. (See “The venetian blinds of business.”) If things are going reasonably well, the starting point for each year’s new “blind” may be a bit higher than the prior year’s starting point, but rarely does performance match the prior year’s projection. The obvious implication: year after year of underperformance relative to plan.

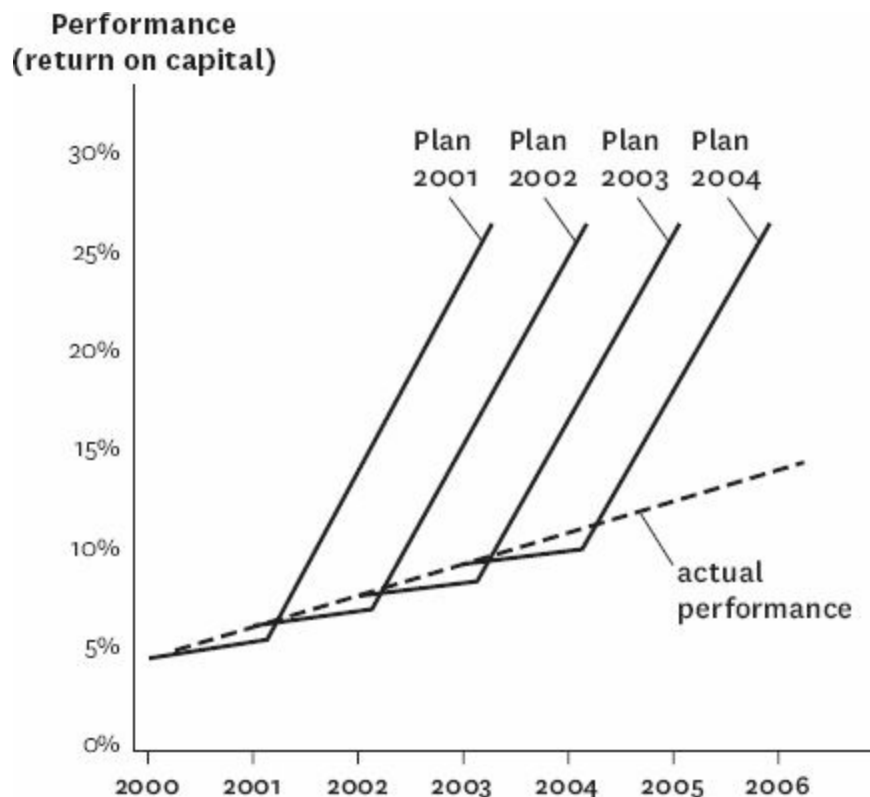
The venetian blinds phenomenon creates a number of related problems. First, because the plan’s financial forecasts are unreliable, senior management cannot confidently tie capital approval to strategic planning. Consequently, strategy development and resource allocation become decoupled, and the annual operating plan (or budget) ends up driving the company’s long-term investments and strategy. Second, portfolio management gets derailed. Without credible financial forecasts, top management cannot know whether a particular business is worth more to the company and its shareholders than to potential buyers. As a result, businesses that destroy shareholder value stay in the portfolio too long (in the hope that their performance will eventually turn around), and value-creating businesses are starved for capital and other resources. Third, poor financial forecasts complicate communications with the investment community. Indeed, to avoid coming up short at the end of the quarter, the CFO and head of investor relations frequently impose a “contingency” or “safety margin” on top of the forecast produced by consolidating the business-unit plans. Because this top-down contingency is wrong just as often as it is right, poor financial forecasts run the risk of damaging a company’s reputation with analysts and investors.

A lot of value is lost in translation

Given the poor quality of financial forecasts in most strategic plans, it is probably not surprising that most companies fail to realize their strategies' potential value. As we've mentioned, our survey indicates that, on average, most strategies deliver only 63% of their potential financial performance. And more than one-third of the executives surveyed placed the figure at less than 50%. Put differently, if management were to realize the full potential of its current strategy, the increase in value could be as much as 60% to 100%!

The venetian blinds of business

This figure illustrates a dynamic common to many companies. In January 2001, management approves a strategic plan (Plan 2001) that projects modest performance for the first year and a high rate of performance thereafter, as shown in the first solid line. For beating the first year's projection, the unit management is both commended and handsomely rewarded. A new plan is then prepared, projecting uninspiring results for the first year and once again promising a fast rate of performance improvement thereafter, as shown by the second solid line (Plan 2002). This, too, succeeds only partially, so another plan is drawn up, and so on. The actual rate of performance improvement can be seen by joining the start points of each plan (the dotted line).



As illustrated in “Where the performance goes,” the strategy-to-

performance gap can be attributed to a combination of factors, such as poorly formulated plans, misapplied resources, breakdowns in communication, and limited accountability for results. To elaborate, management starts with a strategy it believes will generate a certain level of financial performance and value over time (100%, as noted in the exhibit). But, according to the executives we surveyed, the failure to have the right resources in the right place at the right time strips away some 7.5% of the strategy's potential value. Some 5.2% is lost to poor communications, 4.5% to poor action planning, 4.1% to blurred accountabilities, and so on. Of course, these estimates reflect the average experience of the executives we surveyed and may not be representative of every company or every strategy. Nonetheless, they do highlight the issues managers need to focus on as they review their companies' processes for planning and executing strategies.

What emerges from our survey results is a sequence of events that goes something like this: Strategies are approved but poorly communicated. This, in turn, makes the translation of strategy into specific actions and resource plans all but impossible. Lower levels in the organization don't know what they need to do, when they need to do it, or what resources will be required to deliver the performance senior management expects. Consequently, the expected results never materialize. And because no one is held responsible for the shortfall, the cycle of underperformance gets repeated, often for many years.

Performance bottlenecks are frequently invisible to top management

The processes most companies use to develop plans, allocate resources, and track performance make it difficult for top management to discern whether the strategy-to-performance gap stems from poor planning, poor execution, both, or neither. Because so many plans incorporate overly ambitious projections, companies frequently write off performance shortfalls as “just another hockey-stick forecast.” And when plans are realistic and performance falls short, executives have few early-warning signals. They often have no way of knowing whether critical actions were carried out as expected, resources were deployed on schedule, competitors responded as anticipated, and so on. Unfortunately, without clear information on how and why performance is falling short, it is virtually impossible for top management to take appropriate corrective action.

The strategy-to-performance gap fosters a culture of underperformance

In many companies, planning and execution breakdowns are reinforced—even magnified—by an insidious shift in culture. In our experience, this change occurs subtly but quickly, and once it has taken root it is very hard to reverse. First, unrealistic plans create the expectation throughout the organization that plans simply will not be fulfilled. Then, as the expectation becomes experience, it becomes the norm that performance commitments won't be kept. So commitments cease to be binding promises with real consequences. Rather than stretching to ensure that commitments are kept, managers, expecting failure, seek to protect themselves from the eventual fallout. They spend time covering their tracks rather than identifying actions to enhance performance. The organization becomes less self-critical and less intellectually honest about its shortcomings. Consequently, it loses its capacity to perform.

Closing the Strategy-to-Performance Gap

As significant as the strategy-to-performance gap is at most companies, management can close it. A number of high-performing companies have found ways to realize more of their strategies' potential. Rather than focus on improving their planning and execution processes separately to close the gap, these companies work both sides of the equation, raising standards for both planning and execution simultaneously and creating clear links between them.

Our research and experience in working with many of these companies suggests they follow seven rules that apply to planning and execution. Living by these rules enables them to objectively assess any performance shortfall and determine whether it stems from the strategy, the plan, the execution, or employees' capabilities. And the same rules that allow them to spot problems early also help them prevent performance shortfalls in the first place. These rules may seem simple—even obvious—but when strictly and collectively observed, they can transform both the quality of a company's strategy and its ability to deliver results.

Rule 1: Keep it simple, make it concrete

At most companies, strategy is a highly abstract concept—often confused with vision or aspiration—and is not something that can be easily communicated or translated into action. But without a clear sense of where the company is headed and why, lower levels in the organization cannot put in place executable plans. In short, the link between strategy and performance can't be drawn because the strategy itself is not sufficiently concrete.

To start off the planning and execution process on the right track, high-performing companies avoid long, drawn-out descriptions of lofty goals and instead stick to clear language describing their course of action. Bob Diamond, CEO of Barclays Capital, one of the fastest-growing and best-performing investment banking operations in Europe, puts it this way: “We’ve been very clear about what we will and will not do. We knew we weren’t going to go head-to-head with U.S. bulge bracket firms. We communicated that we wouldn’t compete in this way and that we wouldn’t play in unprofitable segments within the equity markets but instead would invest to position ourselves for the euro, the burgeoning need for fixed income, and the end of Glass-Steigel. By ensuring everyone knew the strategy and how it was different, we’ve been able to spend more time on tasks that are key to executing this strategy.”

By being clear about what the strategy is and isn’t, companies like Barclays keep everyone headed in the same direction. More important, they safeguard the performance their counterparts lose to ineffective communications; their resource and action planning becomes more effective; and accountabilities are easier to specify.

Rule 2: Debate assumptions, not forecasts

At many companies, a business unit's strategic plan is little more than a negotiated settlement—the result of careful bargaining with the corporate center over performance targets and financial forecasts. Planning, therefore, is largely a political process—with unit management arguing for lower near-term profit projections (to secure higher annual bonuses) and top management pressing for more long-term stretch (to satisfy the board of directors and other external constituents). Not surprisingly, the forecasts that emerge from these negotiations almost always understate what each business unit can deliver in the near term and overstate what can realistically be expected in the long-term—the hockey-stick charts with which CEOs are all too familiar.

Even at companies where the planning process is isolated from the political concerns of performance evaluation and compensation, the approach used to generate financial projections often has built-in biases. Indeed, financial forecasting frequently takes place in complete isolation from the marketing or strategy functions. A business unit's finance function prepares a highly detailed line-item forecast whose short-term assumptions may be realistic, if conservative, but whose long-term assumptions are largely uninformed. For example, revenue forecasts are typically based on crude estimates about average pricing, market growth, and market share. Projections of long-term costs and working capital requirements are based on an assumption about annual productivity gains—expediently tied, perhaps, to some companywide efficiency program. These forecasts are difficult for top management to pick apart. Each line item may be completely defensible, but the overall plan and projections embed a clear upward bias—rendering them useless for driving strategy execution.

High-performing companies view planning altogether differently. They want their forecasts to drive the work they actually do. To make this possible, they have to ensure that the assumptions underlying their long-term plans reflect both the real economics of their markets and the performance experience of the company relative to competitors. Tyco CEO Ed Breen, brought in to turn the company around in July 2002, credits a revamped plan-

building process for contributing to Tyco's dramatic recovery. When Breen joined the company, Tyco was a labyrinth of 42 business units and several hundred profit centers, built up over many years through countless acquisitions. Few of Tyco's businesses had complete plans, and virtually none had reliable financial forecasts.

To get a grip on the conglomerate's complex operations, Breen assigned cross-functional teams at each unit, drawn from strategy, marketing, and finance, to develop detailed information on the profitability of Tyco's primary markets as well as the product or service offerings, costs, and price positioning relative to the competition. The teams met with corporate executives biweekly during Breen's first six months to review and discuss the findings. These discussions focused on the assumptions that would drive each unit's long-term financial performance, not on the financial forecasts themselves. In fact, once assumptions about market trends were agreed on, it was relatively easy for Tyco's central finance function to prepare externally oriented and internally consistent forecasts for each unit.

Separating the process of building assumptions from that of preparing financial projections helps to ground the business unit–corporate center dialogue in economic reality. Units can't hide behind specious details, and corporate center executives can't push for unrealistic goals. What's more, the fact-based discussion resulting from this kind of approach builds trust between the top team and each unit and removes barriers to fast and effective execution. "When you understand the fundamentals and performance drivers in a detailed way," says Bob Diamond, "you can then step back, and you don't have to manage the details. The team knows which issues it can get on with, which it needs to flag to me, and which issues we really need to work out together."

Rule 3: Use a rigorous framework, speak a common language

To be productive, the dialogue between the corporate center and the business units about market trends and assumptions must be conducted within a rigorous framework. Many of the companies we advise use the concept of profit pools, which draws on the competition theories of Michael Porter and others. In this framework, a business's long-term financial performance is tied to the total profit pool available in each of the markets it serves and its share of each profit pool—which, in turn, is tied to the business's market share and relative profitability versus competitors in each market.

In this approach, the first step is for the corporate center and the unit team to agree on the size and growth of each profit pool. Fiercely competitive markets, such as pulp and paper or commercial airlines, have small (or negative) total profit pools. Less competitive markets, like soft drinks or pharmaceuticals, have large total profit pools. We find it helpful to estimate the size of each profit pool directly—through detailed benchmarking—and then forecast changes in the pool's size and growth. Each business unit then assesses what share of the total profit pool it can realistically capture over time, given its business model and positioning. Competitively advantaged businesses can capture a large share of the profit pool—by gaining or sustaining a high market share, generating above-average profitability, or both. Competitively disadvantaged businesses, by contrast, typically capture a negligible share of the profit pool. Once the unit and the corporate center agree on the likely share of the pool the business will capture over time, the corporate center can easily create the financial projections that will serve as the unit's road map.

In our view, the specific framework a company uses to ground its strategic plans isn't all that important. What is critical is that the framework establish a common language for the dialogue between the corporate center and the units—one that the strategy, marketing, and finance teams all understand and use. Without a rigorous framework to link a business's performance in the product markets with its financial performance over time, it is very difficult for top

management to ascertain whether the financial projections that accompany a business unit's strategic plan are reasonable and realistically achievable. As a result, management can't know with confidence whether a performance shortfall stems from poor execution or an unrealistic and ungrounded plan.

Rule 4: Discuss resource deployments early

Companies can create more realistic forecasts and more executable plans if they discuss up front the level and timing of critical resource deployments. At Cisco Systems, for example, a cross-functional team reviews the level and timing of resource deployments early in the planning stage. These teams regularly meet with John Chambers (CEO), Dennis Powell (CFO), Randy Pond (VP of operations), and the other members of Cisco's executive team to discuss their findings and make recommendations. Once agreement is reached on resource allocation and timing at the unit level, those elements are factored into the company's two-year plan. Cisco then monitors each unit's actual resource deployments on a monthly basis (as well as its performance) to make sure things are going according to plan and that the plan is generating the expected results.

Challenging business units about when new resources need to be in place focuses the planning dialogue on what actually needs to happen across the company in order to execute each unit's strategy. Critical questions invariably surface, such as: How long will it take us to change customers' purchase patterns? How fast can we deploy our new sales force? How quickly will competitors respond? These are tough questions. But answering them makes the forecasts and the plans they accompany more feasible.

What's more, an early assessment of resource needs also informs discussions about market trends and drivers, improving the quality of the strategic plan and making it far more executable. In the course of talking about the resources needed to expand in the rapidly growing cable market, for example, Cisco came to realize that additional growth would require more trained engineers to improve existing products and develop new features. So, rather than relying on the functions to provide these resources from the bottom up, corporate management earmarked a specific number of trained engineers to support growth in cable. Cisco's financial-planning organization carefully monitors the engineering head count, the pace of feature development, and revenues generated by the business to make sure the strategy stays on track.

Rule 5: Clearly identify priorities

To deliver any strategy successfully, managers must make thousands of tactical decisions and put them into action. But not all tactics are equally important. In most instances, a few key steps must be taken—at the right time and in the right way—to meet planned performance. Leading companies make these priorities explicit so that each executive has a clear sense of where to direct his or her efforts.

At Textron, a \$10 billion multi-industrial conglomerate, each business unit identifies “improvement priorities” that it must act upon to realize the performance outlined in its strategic plan. Each improvement priority is translated into action items with clearly defined accountabilities, timetables, and key performance indicators (KPIs) that allow executives to tell how a unit is delivering on a priority. Improvement priorities and action items cascade to every level at the company—from the management committee (consisting of Textron’s top five executives) down to the lowest levels in each of the company’s ten business units. Lewis Campbell, Textron’s CEO, summarizes the company’s approach this way: “Everyone needs to know: ‘If I have only one hour to work, here’s what I’m going to focus on.’ Our goal deployment process makes each individual’s accountabilities and priorities clear.”

The Swiss pharmaceutical giant Roche goes as far as to turn its business plans into detailed performance contracts that clearly specify the steps needed and the risks that must be managed to achieve the plans. These contracts all include a “delivery agenda” that lists the five to ten critical priorities with the greatest impact on performance. By maintaining a delivery agenda at each level of the company, Chairman and CEO Franz Humer and his leadership team make sure “everyone at Roche understands exactly what we have agreed to do at a strategic level and that our strategy gets translated into clear execution priorities. Our delivery agenda helps us stay the course with the strategy decisions we have made so that execution is actually allowed to happen. We cannot control implementation from HQ, but we can agree on the priorities, communicate relentlessly, and hold managers accountable for executing against their commitments.”

Rule 6: Continuously monitor performance

Seasoned executives know almost instinctively whether a business has asked for too much, too little, or just enough resources to deliver the goods. They develop this capability over time—essentially through trial and error. High-performing companies use real-time performance tracking to help accelerate this trial-and-error process. They continuously monitor their resource deployment patterns and their results against plan, using continuous feedback to reset planning assumptions and reallocate resources. This real-time information allows management to spot and remedy flaws in the plan and shortfalls in execution—and to avoid confusing one with the other.

At Textron, for example, each KPI is carefully monitored, and regular operating reviews percolate performance shortfalls—or “red light” events—up through the management ranks. This provides CEO Lewis Campbell, CFO Ted French, and the other members of Textron’s management committee with the information they need to spot and fix breakdowns in execution.

A similar approach has played an important role in the dramatic revival of Dow Chemical’s fortunes. In December 2001, with performance in a free fall, Dow’s board of directors asked Bill Stavropoulos (Dow’s CEO from 1993 to 1999) to return to the helm. Stavropoulos and Andrew Liveris (the current CEO, then COO) immediately focused Dow’s entire top leadership team on execution through a project they called the Performance Improvement Drive. They began by defining clear performance metrics for each of Dow’s 79 business units. Performance on these key metrics was tracked against plans on a weekly basis, and the entire leadership team discussed any serious discrepancies first thing every Monday morning. As Liveris told us, the weekly monitoring sessions “forced everyone to live the details of execution” and let “the entire organization know how we were performing.”

Continuous monitoring of performance is particularly important in highly volatile industries, where events outside anyone’s control can render a plan irrelevant. Under CEO Alan Mulally, Boeing Commercial Airplanes’ leadership team holds weekly business performance reviews to track the division’s results against its multiyear plan. By tracking the deployment of resources as a leading indicator of whether a plan is being executed

effectively, BCA's leadership team can make course corrections each week rather than waiting for quarterly results to roll in.

Furthermore, by proactively monitoring the primary drivers of performance (such as passenger traffic patterns, airline yields and load factors, and new aircraft orders), BCA is better able to develop and deploy effective countermeasures when events throw its plans off course. During the SARS epidemic in late 2002, for example, BCA's leadership team took action to mitigate the adverse consequences of the illness on the business's operating plan within a week of the initial outbreak. The abrupt decline in air traffic to Hong Kong, Singapore, and other Asian business centers signaled that the number of future aircraft deliveries to the region would fall—perhaps precipitously. Accordingly, BCA scaled back its medium-term production plans (delaying the scheduled ramp-up of some programs and accelerating the shutdown of others) and adjusted its multiyear operating plan to reflect the anticipated financial impact.

Rule 7: Reward and develop execution capabilities

No list of rules on this topic would be complete without a reminder that companies have to motivate and develop their staffs; at the end of the day, no process can be better than the people who have to make it work. Unsurprisingly, therefore, nearly all of the companies we studied insisted that the selection and development of management was an essential ingredient in their success. And while improving the capabilities of a company's workforce is no easy task—often taking many years—these capabilities, once built, can drive superior planning and execution for decades.

For Barclays' Bob Diamond, nothing is more important than "ensuring that [the company] hires only A players." In his view, "the hidden costs of bad hiring decisions are enormous, so despite the fact that we are doubling in size, we insist that as a top team we take responsibility for all hiring. The jury of your peers is the toughest judgment, so we vet each others' potential hires and challenge each other to keep raising the bar." It's equally important to make sure that talented hires are rewarded for superior execution. To reinforce its core values of "client," "meritocracy," "team," and "integrity," Barclays Capital has innovative pay schemes that "ring fence" rewards. Stars don't lose out just because the business is entering new markets with lower returns during the growth phase. Says Diamond: "It's so bad for the culture if you don't deliver what you promised to people who have delivered... . You've got to make sure you are consistent and fair, unless you want to lose your most productive people."

Companies that are strong on execution also emphasize development. Soon after he became CEO of 3M, Jim McNerney and his top team spent 18 months hashing out a new leadership model for the company. Challenging debates among members of the top team led to agreement on six "leadership attributes"—namely, the ability to "chart the course," "energize and inspire others," "demonstrate ethics, integrity, and compliance," "deliver results," "raise the bar," and "innovate resourcefully." 3M's leadership agreed that these six attributes were essential for the company to become skilled at execution and known for accountability. Today, the leaders credit this model with helping 3M to sustain and even improve its consistently strong

performance.

The prize for closing the strategy-to-performance gap is huge—an increase in performance of anywhere from 60% to 100% for most companies. But this almost certainly understates the true benefits. Companies that create tight links between their strategies, their plans, and, ultimately, their performance often experience a cultural multiplier effect. Over time, as they turn their strategies into great performance, leaders in these organizations become much more confident in their own capabilities and much more willing to make the stretch commitments that inspire and transform large companies. In turn, individual managers who keep their commitments are rewarded—with faster progression and fatter paychecks—reinforcing the behaviors needed to drive any company forward.

Eventually, a culture of overperformance emerges. Investors start giving management the benefit of the doubt when it comes to bold moves and performance delivery. The result is a performance premium on the company's stock—one that further rewards stretch commitments and performance delivery. Before long, the company's reputation among potential recruits rises, and a virtuous circle is created in which talent begets performance, performance begets rewards, and rewards beget even more talent. In short, closing the strategy-to-performance gap is not only a source of immediate performance improvement but also an important driver of cultural change with a large and lasting impact on the organization's capabilities, strategies, and competitiveness.

Originally published in July 2005. Reprint R0507E.

Who Has the D?

How Clear Decision Roles Enhance Organizational Performance. by *Paul Rogers and Marcia Blenko*

DECISIONS ARE THE COIN of the realm in business. Every success, every mishap, every opportunity seized or missed is the result of a decision that someone made or failed to make. At many companies, decisions routinely get stuck inside the organization like loose change. But it's more than loose change that's at stake, of course; it's the performance of the entire organization. Never mind what industry you're in, how big and well known your company may be, or how clever your strategy is. If you can't make the right decisions quickly and effectively, and execute those decisions consistently, your business will lose ground.

Indeed, making good decisions and making them happen quickly are the hallmarks of high-performing organizations. When we surveyed executives at 350 global companies about their organizational effectiveness, only 15% said that they have an organization that helps the business outperform competitors. What sets those top performers apart is the quality, speed, and execution of their decision making. The most effective organizations score well on the major strategic decisions—which markets to enter or exit, which businesses to buy or sell, where to allocate capital and talent. But they truly shine when it comes to the critical operating decisions requiring consistency and speed—how to drive product innovation, the best way to position brands, how to manage channel partners.

Even in companies respected for their decisiveness, however, there can be ambiguity over who is accountable for which decisions. As a result, the entire decision-making process can stall, usually at one of four bottlenecks: global versus local, center versus business unit, function versus function, and inside versus outside partners.

The first of these bottlenecks, *global versus local* decision making, can occur in nearly every major business process and function. Decisions about

brand building and product development frequently get snared here, when companies wrestle over how much authority local businesses should have to tailor products for their markets. Marketing is another classic global versus local issue—should local markets have the power to determine pricing and advertising?

The second bottleneck, *center versus business unit* decision making, tends to afflict parent companies and their subsidiaries. Business units are on the front line, close to the customer; the center sees the big picture, sets broad goals, and keeps the organization focused on winning. Where should the decision-making power lie? Should a major capital investment, for example, depend on the approval of the business unit that will own it, or should headquarters make the final call?

Function versus function decision making is perhaps the most common bottleneck. Every manufacturer, for instance, faces a balancing act between product development and marketing during the design of a new product. Who should decide what? Cross-functional decisions too often result in ineffective compromise solutions, which frequently need to be revisited because the right people were not involved at the outset.

The fourth decision-making bottleneck, *inside versus outside partners*, has become familiar with the rise of outsourcing, joint ventures, strategic alliances, and franchising. In such arrangements, companies need to be absolutely clear about which decisions can be owned by the external partner (usually those about the execution of strategy) and which must continue to be made internally (decisions about the strategy itself). In the case of outsourcing, for instance, brand-name apparel and foot-wear marketers once assumed that overseas suppliers could be responsible for decisions about plant employees' wages and working conditions. Big mistake.

Idea in Brief

Decisions are the coin of the realm in business. Every success, every mishap, every opportunity seized or missed stems from a decision someone made—or failed to make. Yet in many firms, decisions routinely stall inside the organization—hurting the entire company's performance.

The culprit? Ambiguity over who's accountable for which decisions. In one auto manufacturer that was missing milestones for rolling out new models, marketers *and* product developers each thought they were responsible for deciding new models' standard features and colors. Result? Conflict over who had final say, endless revisiting of decisions—and missed deadlines that led to lost sales.

How to clarify decision accountability? Assign clear roles for the decisions that most affect your firm's performance—such as which markets to enter, where to allocate capital, and how to drive product innovation. Think “RAPID”: Who should **r**ecommend a course of action on a key decision? Who must **a**gree to a recommendation before it can move forward? Who will **p**erform the actions needed to implement the decision? Whose **i**nput is needed to determine the proposal's feasibility? Who **d**ecides—brings the decision to closure and commits the organization to implement it?

When you clarify decision roles, you make the *right* choices—swiftly and effectively.

Clearing the Bottlenecks

The most important step in unclogging decision-making bottlenecks is assigning clear roles and responsibilities. Good decision makers recognize which decisions really matter to performance. They think through who should recommend a particular path, who needs to agree, who should have input, who has ultimate responsibility for making the decision, and who is accountable for follow-through. They make the process routine. The result: better coordination and quicker response times.

Companies have devised a number of methods to clarify decision roles and assign responsibilities. We have used an approach called RAPID, which has evolved over the years, to help hundreds of companies develop clear decision-making guidelines. It is, for sure, not a panacea (an indecisive decision maker, for example, can ruin any good system), but it's an important start. The letters in RAPID stand for the primary roles in any decision-making process, although these roles are not performed exactly in this order: recommend, agree, perform, input, and decide—the “D.” (See the sidebar “A Decision-Making Primer.”)

Idea in Practice

The RAPID Decision Model

For every strategic decision, assign the following roles and responsibilities:

People Who Are Responsible For ...

...

Recommend • Making a proposal on a key decision, gathering input, and providing data and analysis to make a sensible choice in a timely fashion

- Consulting with input providers—hearing and incorporating their views, and winning their buy-in

Agree • Negotiating a modified proposal with the recommender if they have concerns about the original proposal
• Escalating unresolved issues to the decider if the “A” and “R” can’t resolve differences
• If necessary, exercising veto power over the recommendation

Perform • Executing a decision once it’s made
• Seeing that the decision is implemented promptly and effectively

Input • Providing relevant facts to the recommender that shed light on the proposal’s feasibility and practical implications

- Decide**
- Serving as the single point of accountability
 - Bringing the decision to closure by resolving any impasse in the decision-making process
 - Committing the organization to implementing the decision

Decision-Role Pitfalls

In assigning decision roles:

- Ensure that only one person “has the D.” If two or more people think they’re in charge of a particular decision, a tug-of-war results.
- Watch for a proliferation of “A’s.” Too many people with veto power can paralyze recommenders. If many people must agree, you probably haven’t pushed decisions down far enough in your organization.
- Avoid assigning too many “I’s.” When many people give input, at least some of them aren’t making meaningful contributions.

The RAPID Model in Action

Example: At British department-store chain John Lewis, company buyers wanted to increase sales and reduce complexity by offering fewer salt and pepper mill models. The company launched the streamlined product set without involving the sales staff. And sales fell. Upon visiting the stores, buyers saw that salespeople (not understanding the strategy behind the recommendation) had halved shelf space to match the reduction in product range, rather than maintaining the same space but stocking more of the products.

To fix the problem, the company “gave buyers the D” on how much

space product categories would have. Sales staff “had the A”: If space allocations didn’t make sense to them, they could force additional negotiations. They also “had the P,” implementing product layouts in stores.

Once decision roles were clarified, sales of salt and pepper mills exceeded original levels.

The people who *recommend* a course of action are responsible for making a proposal or offering alternatives. They need data and analysis to support their recommendations, as well as common sense about what’s reasonable, practical, and effective.

The people who *agree* to a recommendation are those who need to sign off on it before it can move forward. If they veto a proposal, they must either work with the recommender to come up with an alternative or elevate the issue to the person with the D. For decision making to function smoothly, only a few people should have such veto power. They may be executives responsible for legal or regulatory compliance or the heads of units whose operations will be significantly affected by the decision.

People with *input* responsibilities are consulted about the recommendation. Their role is to provide the relevant facts that are the basis of any good decision: How practical is the proposal? Can manufacturing accommodate the design change? Where there’s dissent or contrasting views, it’s important to get these people to the table at the right time. The recommender has no obligation to act on the input he or she receives but is expected to take it into account—particularly since the people who provide input are generally among those who must implement a decision. Consensus is a worthy goal, but as a decision-making standard, it can be an obstacle to action or a recipe for lowest-common-denominator compromise. A more practical objective is to get everyone involved to buy in to the decision.

Eventually, one person will *decide*. The decision maker is the single point of accountability who must bring the decision to closure and commit the organization to act on it. To be strong and effective, the person with the D needs good business judgment, a grasp of the relevant trade-offs, a bias for action, and a keen awareness of the organization that will execute the decision.

The final role in the process involves the people who will *perform* the decision. They see to it that the decision is implemented promptly and effectively. It's a crucial role. Very often, a good decision executed quickly beats a brilliant decision implemented slowly or poorly.

RAPID can be used to help redesign the way an organization works or to target a single bottleneck. Some companies use the approach for the top ten to 20 decisions, or just for the CEO and his or her direct reports. Other companies use it throughout the organization—to improve customer service by clarifying decision roles on the front line, for instance. When people see an effective process for making decisions, they spread the word. For example, after senior managers at a major U.S. retailer used RAPID to sort out a particularly thorny set of corporate decisions, they promptly built the process into their own functional organizations.

To see the process in action, let's look at the way four companies have worked through their decision-making bottlenecks.

Global Versus Local

Every major company today operates in global markets, buying raw materials in one place, shipping them somewhere else, and selling finished products all over the world. Most are trying simultaneously to build local presence and expertise, and to achieve economies of scale. Decision making in this environment is far from straightforward. Frequently, decisions cut across the boundaries between global and local managers, and sometimes across a regional layer in between: What investments will streamline our supply chain? How far should we go in standardizing products or tailoring them for local markets?

The trick in decision making is to avoid becoming either mindlessly global or hopelessly local. If decision-making authority tilts too far toward global executives, local customers' preferences can easily be overlooked, undermining the efficiency and agility of local operations. But with too much local authority, a company is likely to miss out on crucial economies of scale or opportunities with global clients.

To strike the right balance, a company must recognize its most important sources of value and make sure that decision roles line up with them. This was the challenge facing Martin Broughton, the former CEO and chairman of British American Tobacco, the second-largest tobacco company in the world. In 1993, when Broughton was appointed chief executive, BAT was losing ground to its nearest competitor. Broughton knew that the company needed to take better advantage of its global scale, but decision roles and responsibilities were at odds with this goal. Four geographic operating units ran themselves autonomously, rarely collaborating and sometimes even competing. Achieving consistency across global brands proved difficult, and cost synergies across the operating units were elusive. Industry insiders joked that "there are seven major tobacco companies in the world—and four of them are British American Tobacco." Broughton vowed to change the punch line.

A Decision-Making Primer

GOOD DECISION MAKING DEPENDS on assigning clear and specific roles. This sounds simple enough, but many companies struggle to make decisions because lots of people feel accountable—or no one does. RAPID and other tools used to analyze decision making give senior management teams a method for assigning roles and involving the relevant people. The key is to be clear who has input, who gets to decide, and who gets it done.

The five letters in RAPID correspond to the five critical decision-making roles: recommend, agree, perform, input, and decide. As you'll see, the roles are not carried out lockstep in this order—we took some liberties for the sake of creating a useful acronym.

Recommend

People in this role are responsible for making a proposal, gathering input, and providing the right data and analysis to make a sensible decision in a timely fashion. In the course of developing a proposal, recommenders consult with the people who provide input, not just hearing and incorporating their views but also building buy in along the way. Recommenders must have analytical skills, common sense, and organizational smarts.

Agree

Individuals in this role have veto power—yes or no—over the recommendation. Exercising the veto triggers a debate between themselves and the recommenders, which should lead to a modified proposal. If that takes too long, or if the two parties simply can't agree, they can escalate the issue to the person who has the D.

Input

These people are consulted on the decision. Because the people who provide input are typically involved in implementation, recommenders have a strong interest in taking their advice seriously. No input is binding, but this shouldn't undermine its importance. If the right people are not involved and motivated, the decision is far more likely to falter during execution.

Decide

The person with the D is the formal decision maker. He or she is ultimately accountable for the decision, for better or worse, and has the authority to resolve any impasse in the decision-making process and to commit the organization to action.

Perform

Once a decision is made, a person or group of people will be responsible for executing it. In some instances, the people responsible for implementing a decision are the same people who recommended it.

Writing down the roles and assigning accountability are essential steps, but good decision making also requires the right process. Too many rules can cause the process to collapse under its own weight. The most effective process is grounded in specifics but simple enough to adapt if necessary.

When the process gets slowed down, the problem can often be traced back to one of three trouble spots. First is a lack of clarity about who has the D. If more than one person think they have it for a particular decision, that decision will get caught up in a tug-of-war. The flip side can be equally damaging: No one is accountable for crucial decisions, and the business suffers. Second, a proliferation of people who have veto power can make life tough for recommenders. If a company has too many people in the "agree" role, it usually means that decisions are not pushed down far enough in the organization. Third, if there are a lot of people giving input, it's a signal that at least some of them aren't making a meaningful contribution.

The chief executive envisioned an organization that could take advantage of the opportunities a global business offers—global brands that could compete with established winners such as Altria Group’s Marlboro; global purchasing of important raw materials, including tobacco; and more consistency in innovation and customer management. But Broughton didn’t want the company to lose its nimbleness and competitive hunger in local markets by shifting too much decision-making power to global executives.

The first step was to clarify roles for the most important decisions. Procurement became a proving ground. Previously, each operating unit had identified its own suppliers and negotiated contracts for all materials. Under Broughton, a global procurement team was set up in headquarters and given authority to choose suppliers and negotiate pricing and quality for global materials, including bulk tobacco and certain types of packaging. Regional procurement teams were now given input into global materials strategies but ultimately had to implement the team’s decision. As soon as the global team signed contracts with suppliers, responsibility shifted to the regional teams, who worked out the details of delivery and service with the suppliers in their regions. For materials that did not offer global economies of scale (mentholated filters for the North American market, for example), the regional teams retained their decision-making authority.

As the effort to revamp decision making in procurement gained momentum, the company set out to clarify roles in all its major decisions. The process wasn’t easy. A company the size of British American Tobacco has a huge number of moving parts, and developing a practical system for making decisions requires sweating lots of details. What’s more, decision-making authority is power, and people are often reluctant to give it up.

It’s crucial for the people who will live with the new system to help design it. At BAT, Broughton created working groups led by people earmarked, implicitly or explicitly, for leadership roles in the future. For example, Paul Adams, who ultimately succeeded Broughton as chief executive, was asked to lead the group charged with redesigning decision making for brand and customer management. At the time, Adams was a regional head within one of the operating units. With other senior executives, including some of his own direct reports, Broughton specified that their role was to provide input, not to veto recommendations. Broughton didn’t make the common mistake of seeking consensus, which is often an obstacle to action. Instead, he made it clear that the objective was not deciding whether

to change the decision-making process but achieving buy in about how to do so as effectively as possible.

The new decision roles provided the foundation the company needed to operate successfully on a global basis while retaining flexibility at the local level. The focus and efficiency of its decision making were reflected in the company's results: After the decision-making overhaul, British American Tobacco experienced nearly ten years of growth well above the levels of its competitors in sales, profits, and market value. The company has gone on to have one of the best-performing stocks on the UK market and has reemerged as a major global player in the tobacco industry.

Center Versus Business Unit

The first rule for making good decisions is to involve the right people at the right level of the organization. For BAT, capturing economies of scale required its global team to appropriate some decision-making powers from regional divisions. For many companies, a similar balancing act takes place between executives at the center and managers in the business units. If too many decisions flow to the center, decision making can grind to a halt. The problem is different but no less critical if the decisions that are elevated to senior executives are the wrong ones.

Companies often grow into this type of problem. In small and midsize organizations, a single management team—sometimes a single leader—effectively handles every major decision. As a company grows and its operations become more complex, however, senior executives can no longer master the details required to make decisions in every business.

A change in management style, often triggered by the arrival of a new CEO, can create similar tensions. At a large British retailer, for example, the senior team was accustomed to the founder making all critical decisions. When his successor began seeking consensus on important issues, the team was suddenly unsure of its role, and many decisions stalled. It's a common scenario, yet most management teams and boards of directors don't specify how decision-making authority should change as the company does.

A growth opportunity highlighted that issue for Wyeth (then known as American Home Products) in late 2000. Through organic growth, acquisitions, and partnerships, Wyeth's pharmaceutical division had developed three sizable businesses: biotech, vaccines, and traditional pharmaceutical products. Even though each business had its own market dynamics, operating requirements, and research focus, most important decisions were pushed up to one group of senior executives. "We were using generalists across all issues," said Joseph M. Mahady, president of North American and global businesses for Wyeth Pharmaceuticals. "It was a signal that we weren't getting our best decision making."

The problem crystallized for Wyeth when managers in the biotech business saw a vital—but perishable—opportunity to establish a leading position with Enbrel, a promising rheumatoid arthritis drug. Competitors were working on the same class of drug, so Wyeth needed to move quickly. This meant expanding production capacity by building a new plant, which would be located at the Grange Castle Business Park in Dublin, Ireland.

The decision, by any standard, was a complex one. Once approved by regulators, the facility would be the biggest biotech plant in the world—and the largest capital investment Wyeth had ever undertaken. Yet peak demand for the drug was not easy to determine. What's more, Wyeth planned to market Enbrel in partnership with Immunex (now a part of Amgen). In its deliberations about the plant, therefore, Wyeth needed to factor in the requirements of building up its technical expertise, technology transfer issues, and an uncertain competitive environment.

Input on the decision filtered up slowly through a gauze of overlapping committees, leaving senior executives hungry for a more detailed grasp of the issues. Given the narrow window of opportunity, Wyeth acted quickly, moving from a first look at the Grange Castle project to implementation in six months. But in the midst of this process, Wyeth Pharmaceuticals' executives saw the larger issue: The company needed a system that would push more decisions down to the business units, where operational knowledge was greatest, and elevate the decisions that required the senior team's input, such as marketing strategy and manufacturing capacity.

In short order, Wyeth gave authority for many decisions to business unit managers, leaving senior executives with veto power over some of the more sensitive issues related to Grange Castle. But after that investment decision was made, the D for many subsequent decisions about the Enbrel business lay with Cavan Redmond, the executive vice president and general manager of Wyeth's biotech division, and his new management team. Redmond gathered input from managers in biotech manufacturing, marketing, forecasting, finance, and R&D, and quickly set up the complex schedules needed to collaborate with Immunex. Responsibility for execution rested firmly with the business unit, as always. But now Redmond, supported by his team, also had authority to make important decisions.

Grange Castle is paying off so far. Enbrel is among the leading brands for rheumatoid arthritis, with sales of \$1.7 billion through the first half of 2005. And Wyeth's metabolism for making decisions has increased. Recently,

when the U.S. Food and Drug Administration granted priority review status to another new drug, Tygacil, because of the antibiotic's efficacy against drug-resistant infections, Wyeth displayed its new reflexes. To keep Tygacil on a fast track, the company had to orchestrate a host of critical steps—refining the process technology, lining up supplies, ensuring quality control, allocating manufacturing capacity. The vital decisions were made one or two levels down in the biotech organization, where the expertise resided. “Instead of debating whether you can move your product into my shop, we had the decision systems in place to run it up and down the business units and move ahead rapidly with Tygacil,” said Mahady. The drug was approved by the FDA in June 2005 and moved into volume production a mere three days later.

Function Versus Function

Decisions that cut across functions are some of the most important a company faces. Indeed, cross-functional collaboration has become an axiom of business, essential for arriving at the best answers for the company and its customers. But fluid decision making across functional teams remains a constant challenge, even for companies known for doing it well, like Toyota and Dell. For instance, a team that thinks it's more efficient to make a decision without consulting other functions may wind up missing out on relevant input or being overruled by another team that believes—rightly or wrongly—it should have been included in the process. Many of the most important cross-functional decisions are, by their very nature, the most difficult to orchestrate, and that can string out the process and lead to sparring between fiefdoms and costly indecision.

A Recipe for a Decision-Making Bottleneck

AT ONE AUTOMAKER WE STUDIED, marketers and product developers were confused about who was responsible for making decisions about new models.

When we asked, “Who has the right to decide which features will be standard?”

64% of product developers said, “We do.”

83% of marketers said, “We do.”

When we asked, “Who has the right to decide which colors will be offered?”

77% of product developers said, “We do.”

61% of marketers said, “We do.”

Not surprisingly, the new models were delayed.

The theme here is a lack of clarity about who has the D. For example, at a global auto manufacturer that was missing its milestones for rolling out new models—and was paying the price in falling sales—it turned out that marketers and product developers were confused about which function was responsible for making decisions about standard features and color ranges for new models. When we asked the marketing team who had the D about which features should be standard, 83% said the marketers did. When we posed the same question to product developers, 64% said the responsibility rested with them. (See “A Recipe for a Decision-Making Bottleneck.”)

The practical difficulty of connecting functions through smooth decision making crops up frequently at retailers. John Lewis, the leading department store chain in the United Kingdom, might reasonably expect to overcome this

sort of challenge more readily than other retailers. Spedan Lewis, who built the business in the early twentieth century, was a pioneer in employee ownership. A strong connection between managers and employees permeated every aspect of the store's operations and remained vital to the company as it grew into the largest employee-owned business in the United Kingdom, with 59,600 employees and more than £5 billion in revenues in 2004.

Even at John Lewis, however, with its heritage of cooperation and teamwork, cross-functional decision making can be hard to sustain. Take salt and pepper mills, for instance. John Lewis, which prides itself on having great selection, stocked nearly 50 SKUs of salt and pepper mills, while most competitors stocked around 20. The company's buyers saw an opportunity to increase sales and reduce complexity by offering a smaller number of popular and well-chosen products in each price point and style.

When John Lewis launched the new range, sales fell. This made no sense to the buyers until they visited the stores and saw how the merchandise was displayed. The buyers had made their decision without fully involving the sales staff, who therefore did not understand the strategy behind the new selection. As a result, the sellers had cut shelf space in half to match the reduction in range, rather than devoting the same amount of shelf space to stocking more of each product.

To fix the communication problem, John Lewis needed to clarify decision roles. The buyers were given the D on how much space to allocate to each product category. If the space allocation didn't make sense to the sales staff, however, they had the authority to raise their concerns and force a new round of negotiations. They also had responsibility for implementing product layouts in the stores. When the communication was sorted out and shelf space was restored, sales of the salt and pepper mills climbed well above original levels.

Crafting a decision-making process that connected the buying and selling functions for salt and pepper mills was relatively easy; rolling it out across the entire business was more challenging. Salt and pepper mills are just one of several hundred product categories for John Lewis. This element of scale is one reason why cross-functional bottlenecks are not easy to unclog. Different functions have different incentives and goals, which are often in conflict. When it comes down to a struggle between two functions, there may be good reasons to locate the D in either place—buying or selling, marketing or product development.

Here, as elsewhere, someone needs to think objectively about where value is created and assign decision roles accordingly. Eliminating cross-functional bottlenecks actually has less to do with shifting decision-making responsibilities between departments and more to do with ensuring that the people with relevant information are allowed to share it. The decision maker is important, of course, but more important is designing a system that aligns decision making and makes it routine.

Inside Versus Outside Partners

Decision making within an organization is hard enough. Trying to make decisions between separate organizations on different continents adds layers of complexity that can scuttle the best strategy. Companies that outsource capabilities in pursuit of cost and quality advantages face this very challenge. Which decisions should be made internally? Which can be delegated to outsourcing partners?

These questions are also relevant for strategic partners—a global bank working with an IT contractor on a systems development project, for example, or a media company that acquires content from a studio—and for companies conducting part of their business through franchisees. There is no right answer to who should have the power to decide what. But the wrong approach is to assume that contractual arrangements can provide the answer.

An outdoor-equipment company based in the United States discovered this recently when it decided to scale up production of gas patio heaters for the lower end of the market. The company had some success manufacturing high-end products in China. But with the advent of superdiscounters like Wal-Mart, Target, and Home Depot, the company realized it needed to move more of its production overseas to feed these retailers with lower-cost offerings. The timetable left little margin for error: The company started tooling up factories in April and June of 2004, hoping to be ready for the Christmas season.

The Decision-Driven Organization

THE DEFINING CHARACTERISTIC of high-performing organizations is their ability to make good decisions and to make them happen quickly. The companies that succeed tend to follow a few clear principles.

Some decisions matter more than others

The decisions that are crucial to building value in the business are the ones that matter most. Some of them will be the big strategic decisions, but just as important are the critical operating decisions that drive the business day to day and are vital to effective execution.

Action is the goal

Good decision making doesn't end with a decision; it ends with implementation. The objective shouldn't be consensus, which often becomes an obstacle to action, but buy in.

Ambiguity is the enemy

Clear accountability is essential: Who contributes input, who makes the decision, and who carries it out? Without clarity, gridlock and delay are the most likely outcomes. Clarity doesn't necessarily mean concentrating authority in a few people; it means defining who has responsibility to make decisions, who has input, and who is charged with putting them into action.

Speed and adaptability are crucial

A company that makes good decisions quickly has a higher metabolism, which allows it to act on opportunities and overcome obstacles. The best decision makers create an environment where people can come together quickly and efficiently to make the most important decisions.

Decision roles trump the organizational chart

No decision-making structure will be perfect for every decision. The key is to involve the right people at the right level in the right part of the organization at the right time.

A well-aligned organization reinforces roles

Clear decision roles are critical, but they are not enough. If an organization does not reinforce the right approach to decision making through its measures and incentives, information flows, and culture, the behavior won't become routine.

Practicing beats preaching

Involve the people who will live with the new decision roles in designing them. The very process of thinking about new decision behaviors motivates people to adopt them.

A Decision Diagnostic

CONSIDER THE LAST THREE MEANINGFUL decisions you've been involved in and ask yourself the following questions.

1. Were the decisions right?
2. Were they made with appropriate speed?
3. Were they executed well?
4. Were the right people involved, in the right way?
5. Was it clear for each decision
 - who would recommend a solution?
 - who would provide input?
 - who had the final say?
 - who would be responsible for following through?
6. Were the decision roles, process, and time frame respected?
7. Were the decisions based on appropriate facts?
8. To the extent that there were divergent facts or opinions, was it clear who had the D?
9. Were the decision makers at the appropriate level in the company?

10. Did the organization's measures and incentives encourage the people involved to make the right decisions?

Right away, there were problems. Although the Chinese manufacturing partners understood costs, they had little idea what American consumers wanted. When expensive designs arrived from the head office in the United States, Chinese plant managers made compromises to meet contracted cost targets. They used a lower grade material, which discolored. They placed the power switch in a spot that was inconvenient for the user but easier to build. Instead of making certain parts from a single casting, they welded materials together, which looked terrible.

To fix these problems, the U.S. executives had to draw clear lines around which decisions should be made on which side of the ocean. The company broke down the design and manufacturing process into five steps and analyzed how decisions were made at each step. The company was also much more explicit about what the manufacturing specs would include and what the manufacturer was expected to do with them. The objective was not simply to clarify decision roles but to make sure those roles corresponded directly to the sources of value in the business. If a decision would affect the look and feel of the finished product, headquarters would have to sign off on it. But if a decision would not affect the customer's experience, it could be made in China. If, for example, Chinese engineers found a less expensive material that didn't compromise the product's look, feel, and functionality, they could make that change on their own.

To help with the transition to this system, the company put a team of engineers on-site in China to ensure a smooth handoff of the specs and to make decisions on issues that would become complex and time-consuming if elevated to the home office. Marketing executives in the home office insisted that it should take a customer ten minutes and no more than six steps to assemble the product at home. The company's engineers in China, along with the Chinese manufacturing team, had input into this assembly requirement and were responsible for execution. But the D resided with headquarters, and the requirement became a major design factor. Decisions about logistics, however, became the province of the engineering team in China: It would

figure out how to package the heaters so that one-third more boxes would fit into a container, which reduced shipping costs substantially.

If managers suddenly realize that they're spending less time sitting through meetings wondering why they are there, that's an early signal that companies have become better at making decisions. When meetings start with a common understanding about who is responsible for providing valuable input and who has the D, an organization's decision-making metabolism will get a boost.

No single lever turns a decision-challenged organization into a decision-driven one, of course, and no blueprint can provide for all the contingencies and business shifts a company is bound to encounter. The most successful companies use simple tools that help them recognize potential bottlenecks and think through decision roles and responsibilities with each change in the business environment. That's difficult to do—and even more difficult for competitors to copy. But by taking some very practical steps, any company can become more effective, beginning with its next decision.

Originally published in January 2006. Reprint R0601D.

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FEATURING
"Leading Change"
By John P. Kotter

On Change Management

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First eBook Edition: March 2011

ISBN: 978-1-4221-5800-5

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Leading Change

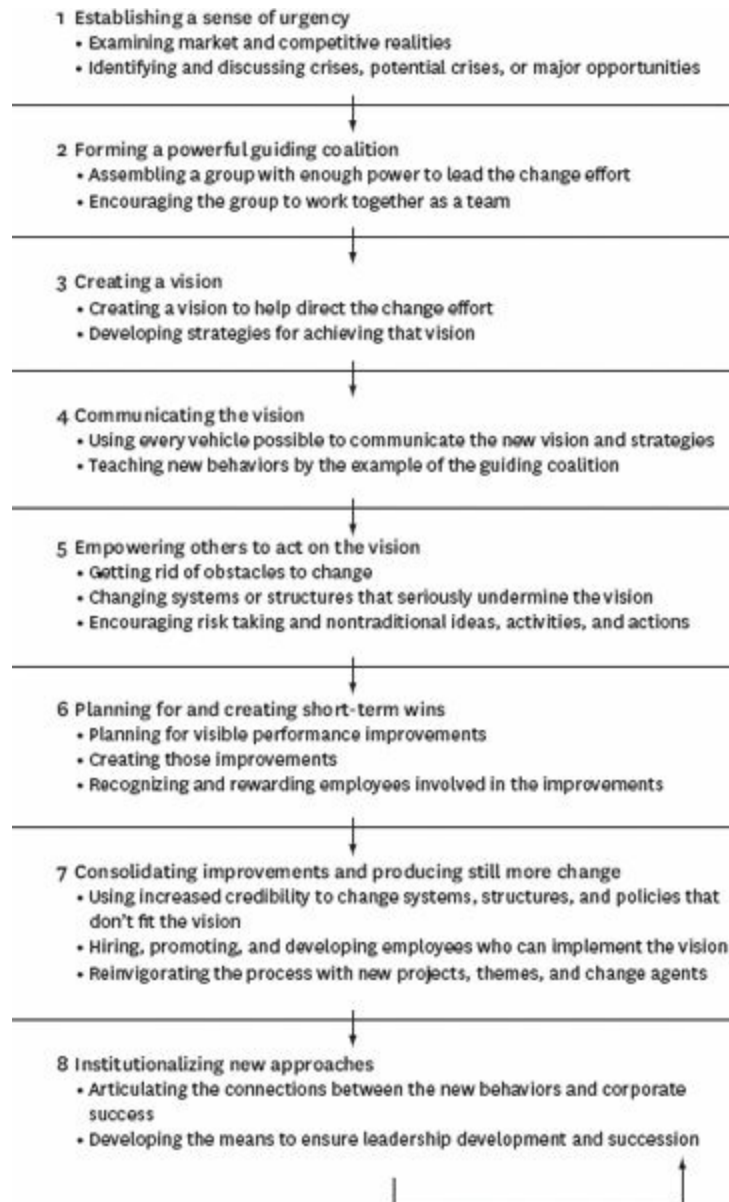
Why Transformation Efforts Fail. *by John P. Kotter*

OVER THE PAST DECADE, I have watched more than 100 companies try to remake themselves into significantly better competitors. They have included large organizations (Ford) and small ones (Landmark Communications), companies based in the United States (General Motors) and elsewhere (British Airways), corporations that were on their knees (Eastern Airlines), and companies that were earning good money (Bristol-Myers Squibb). These efforts have gone under many banners: total quality management, reengineering, rightsizing, restructuring, cultural change, and turnaround. But, in almost every case, the basic goal has been the same: to make fundamental changes in how business is conducted in order to help cope with a new, more challenging market environment.

A few of these corporate change efforts have been very successful. A few have been utter failures. Most fall somewhere in between, with a distinct tilt toward the lower end of the scale. The lessons that can be drawn are interesting and will probably be relevant to even more organizations in the increasingly competitive business environment of the coming decade.

The most general lesson to be learned from the more successful cases is that the change process goes through a series of phases that, in total, usually require a considerable length of time. Skipping steps creates only the illusion of speed and never produces a satisfying result. A second very general lesson is that critical mistakes in any of the phases can have a devastating impact, slowing momentum and negating hard-won gains. Perhaps because we have relatively little experience in renewing organizations, even very capable people often make at least one big error.

Eight steps to transforming your organization



Idea in Brief

Most major change initiatives—whether intended to boost quality, improve culture, or reverse a corporate death spiral—generate only lukewarm results. Many fail miserably.

Why? Kotter maintains that too many managers don't realize transformation is a *process*, not an event. It advances through stages that build on each other. And it takes years. Pressured to accelerate the process, managers skip stages. But shortcuts never work.

Equally troubling, even highly capable managers make critical mistakes—such as declaring victory too soon. Result? Loss of momentum, reversal of hard-won gains, and devastation of the entire transformation effort.

By understanding the stages of change—and the pitfalls unique to each stage—you boost your chances of a successful transformation. The payoff? Your organization flexes with tectonic shifts in competitors, markets, and technologies—leaving rivals far behind.

Error 1: Not Establishing a Great Enough Sense of Urgency

Most successful change efforts begin when some individuals or some groups start to look hard at a company's competitive situation, market position, technological trends, and financial performance. They focus on the potential revenue drop when an important patent expires, the five-year trend in declining margins in a core business, or an emerging market that everyone seems to be ignoring. They then find ways to communicate this information broadly and dramatically, especially with respect to crises, potential crises, or great opportunities that are very timely. This first step is essential because just getting a transformation program started requires the aggressive cooperation of many individuals. Without motivation, people won't help, and the effort goes nowhere.

Compared with other steps in the change process, phase one can sound easy. It is not. Well over 50% of the companies I have watched fail in this first phase. What are the reasons for that failure? Sometimes executives underestimate how hard it can be to drive people out of their comfort zones. Sometimes they grossly overestimate how successful they have already been in increasing urgency. Sometimes they lack patience: "Enough with the preliminaries; let's get on with it." In many cases, executives become paralyzed by the downside possibilities. They worry that employees with seniority will become defensive, that morale will drop, that events will spin out of control, that short-term business results will be jeopardized, that the stock will sink, and that they will be blamed for creating a crisis.

Idea in Practice

To give your transformation effort the best chance of succeeding, take

the right actions at each stage—and avoid common pitfalls

Stage	Actions needed	Pitfalls
Establish a sense of urgency	• Examine market and competitive realities for potential crises and untapped opportunities. • Convince at least 75% of your managers that the status quo is more dangerous than the unknown.	• Underestimating the difficulty of driving people from their comfort zones • Becoming paralyzed by risks
Form a powerful guiding coalition	• Assemble a group with shared commitment and enough power to lead the change effort. • Encourage them to work as a team outside the normal hierarchy.	• No prior experience in teamwork at the top • Relegating team leadership to an HR, quality, or strategic-planning executive rather than a senior line manager
Create a vision	• Create a vision to direct the change effort. • Develop strategies for realizing that vision.	• Presenting a vision that's too complicated or vague to be communicated in five minutes
Communicate the vision	• Use every vehicle possible to communicate the new vision and strategies for achieving it. • Teach new behaviors by the example of the guiding coalition.	• Undercommunicating the vision • Behaving in ways antithetical to the vision

Empower others to act on the vision	• Remove or alter systems or structures undermining the vision. • Encourage risk taking and nontraditional ideas, activities, and actions.	• Failing to remove powerful individuals who resist the change effort
Plan for and create short-term wins	• Define and engineer visible performance improvements. • Recognize and reward employees contributing to those improvements.	• Leaving short-term successes up to chance • Failing to score successes early enough (12–24 months into the change effort)
Consolidate improvements and produce more change	• Use increased credibility from early wins to change systems, structures, and policies undermining the vision. • Hire, promote, and develop employees who can implement the vision. • Reinvigorate the change process with new projects and change agents.	• Declaring victory too soon—with the first performance improvement • Allowing resisters to convince “troops” that the war has been won
Institutionalize new approaches	• Articulate connections between new behaviors and corporate success. • Create leadership development and succession plans consistent with the new approach.	• Not creating new social norms and shared values consistent with changes • Promoting people into leadership positions who don’t personify the new approach

A paralyzed senior management often comes from having too many managers and not enough leaders. Management’s mandate is to minimize risk and to keep the current system operating. Change, by definition, requires creating a new system, which in turn always demands leadership. Phase one in a renewal process typically goes nowhere until enough real leaders are promoted or hired into senior-level jobs.

Transformations often begin, and begin well, when an organization has a new head who is a good leader and who sees the need for a major change. If the renewal target is the entire company, the CEO is key. If change is needed in a division, the division general manager is key. When these individuals are not new leaders, great leaders, or change champions, phase one can be a huge

challenge.

Bad business results are both a blessing and a curse in the first phase. On the positive side, losing money does catch people's attention. But it also gives less maneuvering room. With good business results, the opposite is true: Convincing people of the need for change is much harder, but you have more resources to help make changes.

But whether the starting point is good performance or bad, in the more successful cases I have witnessed, an individual or a group always facilitates a frank discussion of potentially unpleasant facts about new competition, shrinking margins, decreasing market share, flat earnings, a lack of revenue growth, or other relevant indices of a declining competitive position. Because there seems to be an almost universal human tendency to shoot the bearer of bad news, especially if the head of the organization is not a change champion, executives in these companies often rely on outsiders to bring unwanted information. Wall Street analysts, customers, and consultants can all be helpful in this regard. The purpose of all this activity, in the words of one former CEO of a large European company, is "to make the status quo seem more dangerous than launching into the unknown."

In a few of the most successful cases, a group has manufactured a crisis. One CEO deliberately engineered the largest accounting loss in the company's history, creating huge pressures from Wall Street in the process. One division president commissioned first-ever customer satisfaction surveys, knowing full well that the results would be terrible. He then made these findings public. On the surface, such moves can look unduly risky. But there is also risk in playing it too safe: When the urgency rate is not pumped up enough, the transformation process cannot succeed, and the long-term future of the organization is put in jeopardy.

When is the urgency rate high enough? From what I have seen, the answer is when about 75% of a company's management is honestly convinced that business as usual is totally unacceptable. Anything less can produce very serious problems later on in the process.

Error 2: Not Creating a Powerful Enough Guiding Coalition

Major renewal programs often start with just one or two people. In cases of successful transformation efforts, the leadership coalition grows and grows over time. But whenever some minimum mass is not achieved early in the effort, nothing much worthwhile happens.

It is often said that major change is impossible unless the head of the organization is an active supporter. What I am talking about goes far beyond that. In successful transformations, the chairman or president or division general manager, plus another five or 15 or 50 people, come together and develop a shared commitment to excellent performance through renewal. In my experience, this group never includes all of the company's most senior executives because some people just won't buy in, at least not at first. But in the most successful cases, the coalition is always pretty powerful—in terms of titles, information and expertise, reputations, and relationships.

In both small and large organizations, a successful guiding team may consist of only three to five people during the first year of a renewal effort. But in big companies, the coalition needs to grow to the 20 to 50 range before much progress can be made in phase three and beyond. Senior managers always form the core of the group. But sometimes you find board members, a representative from a key customer, or even a powerful union leader.

Because the guiding coalition includes members who are not part of senior management, it tends to operate outside of the normal hierarchy by definition. This can be awkward, but it is clearly necessary. If the existing hierarchy were working well, there would be no need for a major transformation. But since the current system is not working, reform generally demands activity outside of formal boundaries, expectations, and protocol.

A high sense of urgency within the managerial ranks helps enormously in putting a guiding coalition together. But more is usually required. Someone needs to get these people together, help them develop a shared assessment of their company's problems and opportunities, and create a minimum level of

trust and communication. Off-site retreats, for two or three days, are one popular vehicle for accomplishing this task. I have seen many groups of five to 35 executives attend a series of these retreats over a period of months.

Companies that fail in phase two usually underestimate the difficulties of producing change and thus the importance of a powerful guiding coalition. Sometimes they have no history of teamwork at the top and therefore undervalue the importance of this type of coalition. Sometimes they expect the team to be led by a staff executive from human resources, quality, or strategic planning instead of a key line manager. No matter how capable or dedicated the staff head, groups without strong line leadership never achieve the power that is required.

Efforts that don't have a powerful enough guiding coalition can make apparent progress for a while. But, sooner or later, the opposition gathers itself together and stops the change.

Error 3: Lacking a Vision

In every successful transformation effort that I have seen, the guiding coalition develops a picture of the future that is relatively easy to communicate and appeals to customers, stockholders, and employees. A vision always goes beyond the numbers that are typically found in five-year plans. A vision says something that helps clarify the direction in which an organization needs to move. Sometimes the first draft comes mostly from a single individual. It is usually a bit blurry, at least initially. But after the coalition works at it for three or five or even 12 months, something much better emerges through their tough analytical thinking and a little dreaming. Eventually, a strategy for achieving that vision is also developed.

In one midsize European company, the first pass at a vision contained two-thirds of the basic ideas that were in the final product. The concept of global reach was in the initial version from the beginning. So was the idea of becoming preeminent in certain businesses. But one central idea in the final version—getting out of low value-added activities—came only after a series of discussions over a period of several months.

Without a sensible vision, a transformation effort can easily dissolve into a list of confusing and incompatible projects that can take the organization in the wrong direction or nowhere at all. Without a sound vision, the reengineering project in the accounting department, the new 360-degree performance appraisal from the human resources department, the plant's quality program, the cultural change project in the sales force will not add up in a meaningful way.

In failed transformations, you often find plenty of plans, directives, and programs but no vision. In one case, a company gave out four-inch-thick notebooks describing its change effort. In mind-numbing detail, the books spelled out procedures, goals, methods, and deadlines. But nowhere was there a clear and compelling statement of where all this was leading. Not surprisingly, most of the employees with whom I talked were either confused or alienated. The big, thick books did not rally them together or inspire

change. In fact, they probably had just the opposite effect.

In a few of the less successful cases that I have seen, management had a sense of direction, but it was too complicated or blurry to be useful. Recently, I asked an executive in a midsize company to describe his vision and received in return a barely comprehensible 30-minute lecture. Buried in his answer were the basic elements of a sound vision. But they were buried—deeply.

A useful rule of thumb: If you can't communicate the vision to someone in five minutes or less and get a reaction that signifies both understanding and interest, you are not yet done with this phase of the transformation process.

Error 4: Undercommunicating the Vision by a Factor of Ten

I've seen three patterns with respect to communication, all very common. In the first, a group actually does develop a pretty good transformation vision and then proceeds to communicate it by holding a single meeting or sending out a single communication. Having used about 0.0001% of the yearly intracompany communication, the group is startled when few people seem to understand the new approach. In the second pattern, the head of the organization spends a considerable amount of time making speeches to employee groups, but most people still don't get it (not surprising, since vision captures only 0.0005% of the total yearly communication). In the third pattern, much more effort goes into newsletters and speeches, but some very visible senior executives still behave in ways that are antithetical to the vision. The net result is that cynicism among the troops goes up, while belief in the communication goes down.

Transformation is impossible unless hundreds or thousands of people are willing to help, often to the point of making short-term sacrifices. Employees will not make sacrifices, even if they are unhappy with the status quo, unless they believe that useful change is possible. Without credible communication, and a lot of it, the hearts and minds of the troops are never captured.

This fourth phase is particularly challenging if the short-term sacrifices include job losses. Gaining understanding and support is tough when downsizing is a part of the vision. For this reason, successful visions usually include new growth possibilities and the commitment to treat fairly anyone who is laid off.

Executives who communicate well incorporate messages into their hour-by-hour activities. In a routine discussion about a business problem, they talk about how proposed solutions fit (or don't fit) into the bigger picture. In a regular performance appraisal, they talk about how the employee's behavior helps or undermines the vision. In a review of a division's quarterly performance, they talk not only about the numbers but also about how the

division's executives are contributing to the transformation. In a routine Q&A with employees at a company facility, they tie their answers back to renewal goals.

In more successful transformation efforts, executives use all existing communication channels to broadcast the vision. They turn boring, unread company newsletters into lively articles about the vision. They take ritualistic, tedious quarterly management meetings and turn them into exciting discussions of the transformation. They throw out much of the company's generic management education and replace it with courses that focus on business problems and the new vision. The guiding principle is simple: Use every possible channel, especially those that are being wasted on nonessential information.

Perhaps even more important, most of the executives I have known in successful cases of major change learn to "walk the talk." They consciously attempt to become a living symbol of the new corporate culture. This is often not easy. A 60-year-old plant manager who has spent precious little time over 40 years thinking about customers will not suddenly behave in a customer-oriented way. But I have witnessed just such a person change, and change a great deal. In that case, a high level of urgency helped. The fact that the man was a part of the guiding coalition and the vision-creation team also helped. So did all the communication, which kept reminding him of the desired behavior, and all the feedback from his peers and subordinates, which helped him see when he was not engaging in that behavior.

Communication comes in both words and deeds, and the latter are often the most powerful form. Nothing undermines change more than behavior by important individuals that is inconsistent with their words.

Error 5: Not Removing Obstacles to the New Vision

Successful transformations begin to involve large numbers of people as the process progresses. Employees are emboldened to try new approaches, to develop new ideas, and to provide leadership. The only constraint is that the actions fit within the broad parameters of the overall vision. The more people involved, the better the outcome.

To some degree, a guiding coalition empowers others to take action simply by successfully communicating the new direction. But communication is never sufficient by itself. Renewal also requires the removal of obstacles. Too often, an employee understands the new vision and wants to help make it happen, but an elephant appears to be blocking the path. In some cases, the elephant is in the person's head, and the challenge is to convince the individual that no external obstacle exists. But in most cases, the blockers are very real.

Sometimes the obstacle is the organizational structure: Narrow job categories can seriously undermine efforts to increase productivity or make it very difficult even to think about customers. Sometimes compensation or performance-appraisal systems make people choose between the new vision and their own self-interest. Perhaps worst of all are bosses who refuse to change and who make demands that are inconsistent with the overall effort.

One company began its transformation process with much publicity and actually made good progress through the fourth phase. Then the change effort ground to a halt because the officer in charge of the company's largest division was allowed to undermine most of the new initiatives. He paid lip service to the process but did not change his behavior or encourage his managers to change. He did not reward the unconventional ideas called for in the vision. He allowed human resource systems to remain intact even when they were clearly inconsistent with the new ideals. I think the officer's motives were complex. To some degree, he did not believe the company needed major change. To some degree, he felt personally threatened by all the change. To some degree, he was afraid that he could not produce both change

and the expected operating profit. But despite the fact that they backed the renewal effort, the other officers did virtually nothing to stop the one blocker. Again, the reasons were complex. The company had no history of confronting problems like this. Some people were afraid of the officer. The CEO was concerned that he might lose a talented executive. The net result was disastrous. Lower-level managers concluded that senior management had lied to them about their commitment to renewal, cynicism grew, and the whole effort collapsed.

In the first half of a transformation, no organization has the momentum, power, or time to get rid of all obstacles. But the big ones must be confronted and removed. If the blocker is a person, it is important that he or she be treated fairly and in a way that is consistent with the new vision. Action is essential, both to empower others and to maintain the credibility of the change effort as a whole.

Error 6: Not Systematically Planning for, and Creating, Short-Term Wins

Real transformation takes time, and a renewal effort risks losing momentum if there are no short-term goals to meet and celebrate. Most people won't go on the long march unless they see compelling evidence in 12 to 24 months that the journey is producing expected results. Without short-term wins, too many people give up or actively join the ranks of those people who have been resisting change.

One to two years into a successful transformation effort, you find quality beginning to go up on certain indices or the decline in net income stopping. You find some successful new product introductions or an upward shift in market share. You find an impressive productivity improvement or a statistically higher customer satisfaction rating. But whatever the case, the win is unambiguous. The result is not just a judgment call that can be discounted by those opposing change.

Creating short-term wins is different from hoping for short-term wins. The latter is passive, the former active. In a successful transformation, managers actively look for ways to obtain clear performance improvements, establish goals in the yearly planning system, achieve the objectives, and reward the people involved with recognition, promotions, and even money. For example, the guiding coalition at a U.S. manufacturing company produced a highly visible and successful new product introduction about 20 months after the start of its renewal effort. The new product was selected about six months into the effort because it met multiple criteria: It could be designed and launched in a relatively short period, it could be handled by a small team of people who were devoted to the new vision, it had upside potential, and the new product-development team could operate outside the established departmental structure without practical problems. Little was left to chance, and the win boosted the credibility of the renewal process.

Managers often complain about being forced to produce short-term wins, but I've found that pressure can be a useful element in a change effort. When

it becomes clear to people that major change will take a long time, urgency levels can drop. Commitments to produce short-term wins help keep the urgency level up and force detailed analytical thinking that can clarify or revise visions.

Error 7: Declaring Victory Too Soon

After a few years of hard work, managers may be tempted to declare victory with the first clear performance improvement. While celebrating a win is fine, declaring the war won can be catastrophic. Until changes sink deeply into a company's culture, a process that can take five to ten years, new approaches are fragile and subject to regression.

In the recent past, I have watched a dozen change efforts operate under the reengineering theme. In all but two cases, victory was declared and the expensive consultants were paid and thanked when the first major project was completed after two to three years. Within two more years, the useful changes that had been introduced slowly disappeared. In two of the ten cases, it's hard to find any trace of the reengineering work today.

Over the past 20 years, I've seen the same sort of thing happen to huge quality projects, organizational development efforts, and more. Typically, the problems start early in the process: The urgency level is not intense enough, the guiding coalition is not powerful enough, and the vision is not clear enough. But it is the premature victory celebration that kills momentum. And then the powerful forces associated with tradition take over.

Ironically, it is often a combination of change initiators and change resisters that creates the premature victory celebration. In their enthusiasm over a clear sign of progress, the initiators go overboard. They are then joined by resisters, who are quick to spot any opportunity to stop change. After the celebration is over, the resisters point to the victory as a sign that the war has been won and the troops should be sent home. Weary troops allow themselves to be convinced that they won. Once home, the foot soldiers are reluctant to climb back on the ships. Soon thereafter, change comes to a halt, and tradition creeps back in.

Instead of declaring victory, leaders of successful efforts use the credibility afforded by short-term wins to tackle even bigger problems. They go after systems and structures that are not consistent with the transformation vision and have not been confronted before. They pay great attention to who

is promoted, who is hired, and how people are developed. They include new reengineering projects that are even bigger in scope than the initial ones. They understand that renewal efforts take not months but years. In fact, in one of the most successful transformations that I have ever seen, we quantified the amount of change that occurred each year over a seven-year period. On a scale of one (low) to ten (high), year one received a two, year two a four, year three a three, year four a seven, year five an eight, year six a four, and year seven a two. The peak came in year five, fully 36 months after the first set of visible wins.

Error 8: Not Anchoring Changes in the Corporation's Culture

In the final analysis, change sticks when it becomes “the way we do things around here,” when it seeps into the bloodstream of the corporate body. Until new behaviors are rooted in social norms and shared values, they are subject to degradation as soon as the pressure for change is removed.

Two factors are particularly important in institutionalizing change in corporate culture. The first is a conscious attempt to show people how the new approaches, behaviors, and attitudes have helped improve performance. When people are left on their own to make the connections, they sometimes create very inaccurate links. For example, because results improved while charismatic Harry was boss, the troops link his mostly idiosyncratic style with those results instead of seeing how their own improved customer service and productivity were instrumental. Helping people see the right connections requires communication. Indeed, one company was relentless, and it paid off enormously. Time was spent at every major management meeting to discuss why performance was increasing. The company newspaper ran article after article showing how changes had boosted earnings.

The second factor is taking sufficient time to make sure that the next generation of top management really does personify the new approach. If the requirements for promotion don't change, renewal rarely lasts. One bad succession decision at the top of an organization can undermine a decade of hard work. Poor succession decisions are possible when boards of directors are not an integral part of the renewal effort. In at least three instances I have seen, the champion for change was the retiring executive, and although his successor was not a resistor, he was not a change champion. Because the boards did not understand the transformations in any detail, they could not see that their choices were not good fits. The retiring executive in one case tried unsuccessfully to talk his board into a less seasoned candidate who better personified the transformation. In the other two cases, the CEOs did not resist the boards' choices, because they felt the transformation could not

be undone by their successors. They were wrong. Within two years, signs of renewal began to disappear at both companies.

There are still more mistakes that people make, but these eight are the big ones. I realize that in a short article everything is made to sound a bit too simplistic. In reality, even successful change efforts are messy and full of surprises. But just as a relatively simple vision is needed to guide people through a major change, so a vision of the change process can reduce the error rate. And fewer errors can spell the difference between success and failure.

Originally published March 1995. Reprint R0701J

Change Through Persuasion

by David A. Garvin and Michael A. Roberto

FACED WITH THE NEED for massive change, most managers respond predictably. They revamp the organization's strategy, then round up the usual set of suspects—people, pay, and processes—shifting around staff, realigning incentives, and rooting out inefficiencies. They then wait patiently for performance to improve, only to be bitterly disappointed. For some reason, the right things still don't happen.

Why is change so hard? First of all, most people are reluctant to alter their habits. What worked in the past is good enough; in the absence of a dire threat, employees will keep doing what they've always done. And when an organization has had a succession of leaders, resistance to change is even stronger. A legacy of disappointment and distrust creates an environment in which employees automatically condemn the next turnaround champion to failure, assuming that he or she is "just like all the others." Calls for sacrifice and self-discipline are met with cynicism, skepticism, and knee-jerk resistance.

Our research into organizational transformation has involved settings as diverse as multinational corporations, government agencies, nonprofits, and high-performing teams like mountaineering expeditions and firefighting crews. We've found that for change to stick, leaders must design and run an effective persuasion campaign—one that begins weeks or months before the actual turnaround plan is set in concrete. Managers must perform significant work up front to ensure that employees will actually listen to tough messages, question old assumptions, and consider new ways of working. This means taking a series of deliberate but subtle steps to recast employees' prevailing views and create a new context for action. Such a shaping process must be

actively managed during the first few months of a turnaround, when uncertainty is high and setbacks are inevitable. Otherwise, there is little hope for sustained improvement.

Like a political campaign, a persuasion campaign is largely one of differentiation from the past. To the typical change-averse employee, all restructuring plans look alike. The trick for turnaround leaders is to show employees precisely how their plans differ from their predecessors'. They must convince people that the organization is truly on its deathbed—or, at the very least, that radical changes are required if it is to survive and thrive. (This is a particularly difficult challenge when years of persistent problems have been accompanied by few changes in the status quo.) Turnaround leaders must also gain trust by demonstrating through word and deed that they are the right leaders for the job and must convince employees that theirs is the correct plan for moving forward.

Accomplishing all this calls for a four-part communications strategy. Prior to announcing a policy or issuing a set of instructions, leaders need to set the stage for acceptance. At the time of delivery, they must create the frame through which information and messages are interpreted. As time passes, they must manage the mood so that employees' emotional states support implementation and follow-through. And at critical intervals, they must provide reinforcement to ensure that the desired changes take hold without backsliding.

In this article, we describe this process in more detail, drawing on the example of the turnaround of Beth Israel Deaconess Medical Center (BIDMC) in Boston. Paul Levy, who became CEO in early 2002, managed to bring the failing hospital back from the brink of ruin. We had ringside seats during the first six months of the turnaround. Levy agreed to hold videotaped interviews with us every two to four weeks during that period as we prepared a case study describing his efforts. He also gave us access to his daily calendar, as well as to assorted e-mail correspondence and internal memorandums and reports. From this wealth of data, we were able to track the change process as it unfolded, without the usual biases and distortions that come from 20/20 hindsight. The story of how Levy tilled the soil for change provides lessons for any CEO in a turnaround situation.

Idea in Brief

When a company is teetering on the brink of ruin, most turnaround leaders revamp strategy, shift around staff, and root out inefficiencies. Then they wait patiently for the payoff—only to suffer bitter disappointment as the expected improvements fail to materialize.

How to make change stick? Conduct a four-stage persuasion campaign: 1) Prepare your organization's cultural "soil" months before setting your turnaround plan in concrete— by convincing employees that your company can survive only through radical change. 2) Present your plan—explaining in detail its purpose and expected impact. 3) After executing the plan, manage employees' emotions by acknowledging the pain of change—while keeping people focused on the hard work ahead. 4) As the turnaround starts generating results, reinforce desired behavioral changes to prevent backsliding.

Using this four-part process, the CEO of Beth Israel Deaconess Medical Center (BIDMC) brought the failing hospital back from near-certain death. Hemorrhaging \$58 million in losses in 2001, BIDMC reported a \$37.4 million net gain from operations in 2004. Revenues rose, while costs shrank. Morale soared—as reflected by a drop in nursing turnover from between 15% and 16% in 2002 to just 3% by 2004.

Setting the Stage

Paul Levy was an unlikely candidate to run BIDMC. He was not a doctor and had never managed a hospital, though he had previously served as the executive dean for administration at Harvard Medical School. His claim to fame was his role as the architect of the Boston Harbor Cleanup, a multibillion-dollar pollution-control project that he had led several years earlier. (Based on this experience, Levy identified a common yet insidiously destructive organizational dynamic that causes dedicated teams to operate in counterproductive ways, which he described in “The Nut Island Effect: When Good Teams Go Wrong,” March 2001.) Six years after completing the Boston Harbor project, Levy approached the BIDMC board and applied for the job of cleaning up the troubled hospital.

Idea in Practice

Use these steps to persuade your workforce to embrace and execute needed change:

Set the Stage for Acceptance

Develop a bold message that provides compelling reasons to do things differently.

Example: On his first day as Beth Israel Deaconess Medical Center’s CEO, Paul Levy publicized the possibility that BIDMC would be sold to a for-profit institution. He delivered an all-hands-on-deck e-mail to the staff citing the hospital’s achievements while confirming that the threat of sale was real. The e-mail also signaled

actions he would take, including layoffs, and described his open management style (hallway chats, lunches with staff). In addition, Levy circulated a third-party, warts-and-all report on BIDMC's plight on the hospital's intranet—so staff could no longer claim ignorance.

Frame the Turnaround Plan

Present your turnaround plan in a way that helps people interpret your ideas correctly.

Example: Levy augmented his several-hundred-page plan with an e-mail that evoked BIDMC's mission and uncompromising values and reaffirmed the importance of remaining an academic medical center. He provided further details about the plan, emphasizing needed tough measures based on the third-party report. He also explained past plans' deficiencies, contrasting earlier efforts' top-down methods with his plan's collaborative approach. Employees thus felt the plan belonged to them.

Manage the Mood

Strike the right notes of optimism and realism to make employees feel cared for while also keeping them focused on your plan's execution.

Example: Levy acknowledged the pain of layoffs, then urged employees to look forward to “[setting] an example for what a unique academic medical center like ours means for this region.” He also issued progress updates while reminding people that BIDMC still needed to control costs. As financial performance picked up, he lavishly praised the staff.

Prevent Backsliding

Provide opportunities for employees to practice desired behaviors repeatedly. If necessary, publicly criticize disruptive, divisive behaviors.

Example: Levy had established meeting rules requiring staff to state their objections to decisions and to “disagree without being disagreeable.” When one medical chief e-mailed Levy complaining about a decision made during a meeting—and copied the other chiefs and board chairman—Levy took action. He responded with an e-mail to the same audience, publicly reprimanding the chief for his tone, lack of civility, and failure to follow the rule about speaking up during meetings.

Despite his lack of hospital management experience, Levy was appealing to the board. The Boston Harbor Cleanup was a difficult, highly visible change effort that required deft political and managerial skills. Levy had stood firm in the face of tough negotiations and often-heated public resistance and had instilled accountability in city and state agencies. He was also a known quantity to the board, having served on a BIDMC steering committee formed by the board chairman in 2001.

Levy saw the prospective job as one of public service. BIDMC was the product of a difficult 1996 merger between two hospitals—Beth Israel and Deaconess—each of which had distinguished reputations, several best-in-the-world departments and specializations, and deeply devoted staffs. The problems began after the merger. A misguided focus on clinical practice rather than backroom integration, a failure to cut costs, and the repeated inability to execute plans and adapt to changing conditions in the health care marketplace all contributed to BIDMC’s dismal performance.

By the time the board settled on Levy, affairs at BIDMC had reached the nadir. The hospital was losing \$50 million a year. Relations between the administration and medical staff were strained, as were those between management and the board of directors. Employees felt demoralized, having witnessed the rapid decline in their institution’s once-legendary status and the disappointing failure of its past leaders. A critical study was conducted by the Hunter Group, a leading health-care consulting firm. The report, detailing the dire conditions at the hospital and the changes needed to turn things around, had been completed but not yet released. Meanwhile, the state attorney general, who was responsible for overseeing charitable trusts, had put

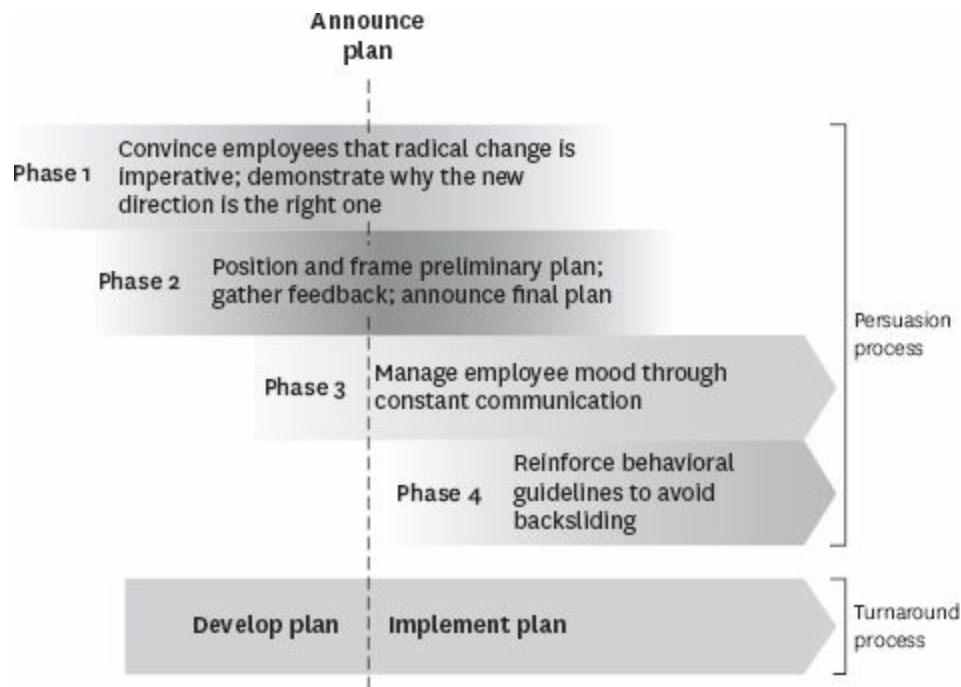
pressure on the board to sell the failing BIDMC to a for-profit institution.

Like many CEOs recruited to fix a difficult situation, Levy's first task was to gain a mandate for the changes ahead. He also recognized that crucial negotiations were best conducted before he took the job, when his leverage was greatest, rather than after taking the reins. In particular, he moved to secure the cooperation of the hospital board by flatly stating his conditions for employment. He told the directors, for example, that should they hire him, they could no longer interfere in day-to-day management decisions. In his second and third meetings with the board's search committee, Levy laid out his timetable and intentions. He insisted that the board decide on his appointment quickly so that he could be on the job before the release of the Hunter report. He told the committee that he intended to push for a smaller, more effective group of directors. Though the conditions were somewhat unusual, the board was convinced that Levy had the experience to lead a successful turnaround, and they accepted his terms. Levy went to work on January 7, 2002.

The next task was to set the stage with the hospital staff. Levy was convinced that the employees, hungry for a turnaround, would do their best to cooperate with him if he could emulate and embody the core values of the hospital culture, rather than impose his personal values. He chose to act as the managerial equivalent of a good doctor—that is, as one who, in dealing with a very ill patient, delivers both the bad news and the chances of success honestly and imparts a realistic sense of hope, without sugar coating.

The four phases of a persuasion campaign

A typical turnaround process consists of two stark phases: plan development, followed by an implementation that may or may not be welcomed by the organization. For the turnaround plan to be widely accepted and adopted, however, the CEO must develop a separate persuasion campaign, the goal of which is to create a continuously receptive environment for change. The campaign begins well before the CEO's first day on the job—or, if the CEO is long established, well before formal development work begins—and continues long after the final plan is announced.



Like any leader facing a turnaround, Levy also knew he had to develop a bold message that provided compelling reasons to do things differently and then cast that message in capital letters to signal the arrival of a new order. To give his message teeth, he linked it to an implicit threat. Taking his cue from his private discussions with the state attorney general, whom he had persuaded to keep the hospital open for the time being, Levy chose to publicize the very real possibility the hospital would be sold. While he realized he risked frightening the staff and the patients with this bad news, he believed that a strong wake-up call was necessary to get employees to face up to the situation.

During his first morning on the job, Levy delivered an all-hands-on-deck e-mail to the staff. The memo contained four broad messages. It opened with the good news, pointing out that the organization had much to be proud of (“This is a wonderful institution, representing the very best in academic medicine: exemplary patient care, extraordinary research, and fine teaching”). Second, Levy noted that the threat of sale was real (“This is our last chance”). Third, he signaled the kinds of actions employees could expect him to take (“There will be a reduction in staff”). And finally, he described the open management style he would adopt. He would manage by walking around—lunching with staff in the cafeteria, having impromptu conversations in the

hallways, talking with employees at every opportunity to discover their concerns. He would communicate directly with employees through e-mail rather than through intermediaries. He also noted that the Hunter report would be posted on the hospital intranet, where all employees would have the opportunity to review its recommendations and submit comments for the final turnaround plan. The direct, open tone of the e-mail memo signaled exactly how Levy's management style would differ from that of his predecessors.

In the afternoon, he disclosed BIDMC's situation in interviews with the *Boston Globe* and the *Boston Herald*, the city's two major newspapers. He told reporters the same thing he had told the hospital's employees: that, in the absence of a turnaround, the hospital would be sold to a for-profit chain and would therefore lose its status as a Harvard teaching hospital. Staving off a sale would require tough measures, including the laying off of anywhere from 500 to 700 employees. Levy insisted that there would be no nursing layoffs, in keeping with the hospital's core values of high-quality patient care. The newspaper reports, together with the memo circulated that morning, served to immediately reset employee expectations while dramatically increasing staff cooperation and willingness to accept whatever new initiatives might prove necessary to the hospital's survival.

Two days later, the critical Hunter report came out and was circulated via the hospital's intranet. Because the report had been produced by an objective third party, employees were open to its unvarnished, warts-and-all view of the hospital's current predicament. The facts were stark, and the staff could no longer claim ignorance. Levy received, and personally responded to, more than 300 e-mail suggestions for improvement in response to the report, many of which he later included in the turnaround plan.

Creating the Frame

Once the stage has been set for acceptance, effective leaders need to help employees interpret proposals for change. Complex plans can be interpreted in any number of ways; not all of them ensure acceptance and favorable outcomes. Skilled leaders therefore use “frames” to provide context and shape perspective for new proposals and plans. By framing the issues, leaders help people digest ideas in particular ways. A frame can take many forms: It can be a companywide presentation that prepares employees before an unexpected change, for example, or a radio interview that provides context following an unsettling layoff.

Levy used one particularly effective framing device to help employees interpret a preliminary draft of the turnaround plan. This device took the form of a detailed e-mail memo accompanying the dense, several-hundred-page plan. The memo explained, in considerable detail, the plan’s purpose and expected impact.

The first section of the memo sought to mollify critics and reduce the fears of doctors and nurses. Its tone was positive and uplifting; it discussed BIDMC’s mission, strategy, and uncompromising values, emphasizing the hospital’s “warm, caring environment.” This section of the letter also reaffirmed the importance of remaining an academic medical center, as well as reminding employees of their shared mission and ideals. The second part of the letter told employees what to expect, providing further details about the turnaround plan. It emphasized that tough measures and goals would be required but noted that the specific recommendations were based, for the most part, on the advice in the Hunter report, which employees had already reviewed. The message to employees was, “You’ve already seen and endorsed the Hunter report. There are no future surprises.”

The third part of the letter anticipated and responded to prospective concerns; this had the effect of circumventing objections. This section explicitly diagnosed past plans and explained their deficiencies, which were largely due to their having been imposed top-down, with little employee

ownership, buy-in, or discussion. Levy then offered a direct interpretation of what had gone wrong. Past plans, he said, had underestimated the size of the financial problem, set unrealistic expectations for new revenue growth, and failed to test implementation proposals. This section of the letter also drove home the need for change at a deeper, more visceral level than employees had experienced in the past. It emphasized that this plan was a far more collective effort than past proposals had been, because it incorporated many employee suggestions.

By framing the turnaround proposal this way, Levy accomplished two things. First, he was able to convince employees that the plan belonged to them. Second, the letter served as the basis for an ongoing communication platform. Levy reiterated its points at every opportunity—not only with employees but also in public meetings and in discussions with the press.

Managing the Mood

Turnarounds are depressing events, especially when they involve restructuring and downsizing. Relationships are disrupted, friends move on, and jobs disappear. In such settings, managing the mood of the organization becomes an essential leadership skill. Leaders must pay close attention to employees' emotions—the ebb and flow of their feelings and moods—and work hard to preserve a receptive climate for change. Often, this requires a delicate balancing act between presenting good and bad news in just the right proportion. Employees need to feel that their sacrifices have not been in vain and that their accomplishments have been recognized and rewarded. At the same time, they must be reminded that complacency is not an option. The communication challenge is daunting. One must strike the right notes of optimism and realism and carefully calibrate the timing, tone, and positioning of every message.

Paul Levy's challenge was threefold: to give remaining employees time to grieve and recover from layoffs and other difficult measures; to make them feel that he cared for and supported them; and to ensure that the turnaround plan proceeded apace. The process depended on mutual trust and employees' desire to succeed. "I had to calibrate the push and pull of congratulations and pressure, but I also depended on the staff's underlying value system and sense of mission," he said. "They were highly motivated, caring individuals who had stuck with the place through five years of hell. They wanted to do good."

The first step was to acknowledge employees' feelings of depression while helping them look to the future. Immediately after the first round of layoffs, people were feeling listless and dejected; Levy knew that releasing the final version of the turnaround plan too soon after the layoffs could be seen as cold. In an e-mail he sent to all employees a few days later, Levy explicitly empathized with employees' feelings ("This week is a sad one...it is hard for those of us remaining...offices are emptier than usual"). He then urged employees to look forward and concluded on a strongly optimistic note

(“...our target is not just survival: It is to thrive and set an example for what a unique academic medical center like ours means for this region”). His upbeat words were reinforced by a piece of good luck that weekend when the underdog New England Patriots won their first Super Bowl championship in dramatic fashion in the last 90 seconds of the game. When Levy returned to work the following Monday, employees were saying, “If the Patriots can do it, we can, too.”

The next task was to keep employees focused on the continuing hard work ahead. On April 12, two months into the restructuring process, Levy sent out a “Frequently Asked Questions” e-mail giving a generally favorable view of progress to date. At the same time, he spoke plainly about the need to control costs and reminded employees that merit pay increases would remain on hold. This was hardly the rosy picture that most employees were hoping for, of course. But Levy believed sufficient time had passed that employees could accommodate a more realistic and tough tone on his part.

A month later, everything changed. Operational improvements that were put in place during the first phase of the turnaround had begun to take hold. Financial performance was well ahead of budget, with the best results since the merger. In another e-mail, Levy praised employees lavishly. He also convened a series of open question-and-answer forums, where employees heard more details about the hospital’s tangible progress and received kudos for their accomplishments.

Dysfunctional Routines

Six Ways to Stop Change in Its Tracks

Just as people are creatures of habit, organizations thrive on routines. Management teams, for example, routinely cut budgets after performance deviates from plan. Routines—predictable, virtually automatic behaviors—are unstated, self-reinforcing, and remarkably resilient. Because they lead to more efficient cognitive processing, they are, for the most part, functional and highly desirable.

A culture of “no”

In organizations dominated by cynics and critics, there is always a good reason not to do something. Piling on criticism is an easy way to avoid taking risks and claim false superiority. Lou Gerstner gets credit for naming this routine, which he found on his arrival at IBM, but it is common in many organizations. Another CEO described her team's response to new initiatives by likening it to a skeet shoot: “Someone would yell, ‘Pull!’ there would be a deafening blast, and the idea would be in pieces on the ground.” This routine has two sources: a culture that overvalues criticism and analysis, and complex decision-making processes requiring multiple approvals, in which anybody can say “no” but nobody can say “yes.” It is especially likely in organizations that are divided into large subunits or segments, led by local leaders with great power who are often unwilling to comply with directives from above.

The dog and pony show must go on

Some organizations put so much weight on process that they confuse ends and means, form and content. How you present a proposal becomes more important than what you propose. Managers construct presentations carefully and devote large amounts of time to obtaining sign-offs. The result is death by PowerPoint. Despite the appearance of progress, there's little real headway.

The grass is always greener

To avoid facing challenges in their core business, some managers look to new products, new services, and new lines of business. At times, such diversification is healthy. But all too often these efforts are merely an avoidance tactic that keeps tough problems at arm's length.

Dysfunctional routines, by contrast, are barriers to action and change. Some are outdated behaviors that were appropriate once but are now unhelpful. Others manifest themselves in knee-jerk reactions, passivity, unproductive foot-dragging, and, sometimes, active resistance.

Dysfunctional routines are persistent, but they are not unchangeable. Novelty—the perception that current circumstances are truly different from those that previously prevailed—is one of the most potent forces for dislodging routines. To overcome them, leaders must clearly signal that the context has changed. They must work directly with employees to recognize and publicly examine dysfunctional routines and substitute desired behaviors.

After the meeting ends, debate begins

This routine is often hard to spot because so much of it takes place under cover. Cordial, apparently cooperative meetings are followed by resistance. Sometimes, resisters are covert; often, they end-run established forums entirely and take their concerns directly to the top. The result? Politics triumphs over substance, staff meetings become empty rituals, and meddling becomes the norm.

Ready, aim, aim. . .

Here, the problem is the organization's inability to settle on a definitive course of action. Staff members generate a continual stream of proposals and reports; managers repeatedly tinker with each one, fine tuning their choices without ever making a final decision. Often called "analysis paralysis," this pattern is common in perfectionist cultures where mistakes are career threatening and people who rock the boat drown.

This too shall pass

In organizations where prior leaders repeatedly proclaimed a state of crisis but then made few substantive changes, employees tend to be jaded. In such situations, they develop a heads-down, bunker mentality and a reluctance to respond to management directives. Most believe that the wisest course of action is to ignore new initiatives, work around them, or wait things out.

Reinforcing Good Habits

Without a doubt, the toughest challenge faced by leaders during a turnaround is to avoid backsliding into dysfunctional routines—habitual patterns of negative behavior by individuals and groups that are triggered automatically and unconsciously by familiar circumstances or stimuli. (For more on how such disruptive patterns work, see the sidebar “Dysfunctional Routines: Six Ways to Stop Change in Its Tracks.”) Employees need help maintaining new behaviors, especially when their old ways of working are deeply ingrained and destructive. Effective change leaders provide opportunities for employees to practice desired behaviors repeatedly, while personally modeling new ways of working and providing coaching and support.

In our studies of successful turnarounds, we’ve found that effective leaders explicitly reinforce organizational values on a constant basis, using actions to back up their words. Their goal is to change behavior, not just ways of thinking. For example, a leader can talk about values such as openness, tolerance, civility, teamwork, delegation, and direct communication in meetings and e-mails. But the message takes hold only if he or she also signals a dislike of disruptive, divisive behaviors by pointedly—and, if necessary, publicly—criticizing them.

At Beth Israel Deaconess Medical Center, the chiefs of medicine, surgery, orthopedics, and other key functions presented Levy with special behavioral challenges, particularly because he was not a doctor. Each medical chief was in essence a “mini-dean,” the head of a largely self-contained department with its own faculty, staff, and resources. As academic researchers, they were rewarded primarily for individual achievement. They had limited experience solving business or management problems.

In dealing with the chiefs, Levy chose an approach that blended with a strong dose of discipline with real-time, public reinforcement. He developed guidelines for behavior and insisted that everyone in the hospital measure up to them. In one of his earliest meetings with the chiefs, Levy presented a simple set of “meeting rules,” including such chestnuts as “state your

objections” and “disagree without being disagreeable,” and led a discussion about them, demonstrating the desired behaviors through his own leadership of the meeting. The purpose of these rules was to introduce new standards of interpersonal behavior and, in the process, to combat several dysfunctional routines.

One serious test of Levy’s ability to reinforce these norms came a month and a half after he was named CEO. After a staff meeting at which all the department chairs were present, one chief—who had remained silent—sent an e-mail to Levy complaining about a decision made during the meeting. The e-mail copied the other chiefs as well as the chairman of the board. Many CEOs would choose to criticize such behavior privately. But Levy responded in an e-mail to the same audience, publicly denouncing the chief for his tone, his lack of civility, and his failure to speak up earlier in the process, as required by the new meeting rules. It was as close to a public hanging as anyone could get. Several of the chiefs privately expressed their support to Levy; they too had been offended by their peer’s presumptuousness. More broadly, the open criticism served to powerfully reinforce new norms while curbing disruptive behavior.

Even as they must set expectations and reinforce behaviors, effective change leaders also recognize that many employees simply do not know how to make decisions as a group or work cooperatively. By delegating critical decisions and responsibilities, a leader can provide employees with ample opportunities to practice new ways of working; in such cases, employees’ performance should be evaluated as much on their adherence to the new standards and processes as on their substantive choices. In this spirit, Levy chose to think of himself primarily as a kind of appeals court judge. When employees came to him seeking his intervention on an issue or situation, he explained, he would “review the process used by the ‘lower court’ to determine if it followed the rules. If so, the decision stands.” He did not review cases *de novo* and substitute his judgment for that of the individual department or unit. He insisted that employees work through difficult issues themselves, even when they were not so inclined, rather than rely on him to tell them what to do. At other times, he intervened personally and coached employees when they lacked basic skills. When two members of his staff disagreed on a proposed course of action, Levy triggered an open, emotional debate, then worked with the participants and their bosses behind the scenes to resolve the differences. At the next staff meeting, he praised the

participants' willingness to disagree publicly, reemphasizing that vigorous debate was healthy and desirable and that confrontation was not to be avoided. In this way, employees gained experience in working through their problems on their own.

Performance, of course, is the ultimate measure of a successful turnaround. On that score, BIDMC has done exceedingly well since Levy took the helm. The original restructuring plan called for a three-year improvement process, moving from a \$58 million loss in 2001 to breakeven in 2004. At the end of the 2004 fiscal year, performance was far ahead of plan, with the hospital reporting a \$37.4 million net gain from operations. Revenues were up, while costs were sharply reduced. Decision making was now crisper and more responsive, even though there was little change in the hospital's senior staff or medical leadership. Morale, not surprisingly, was up as well. To take just one indicator, annual nursing turnover, which was 15% to 16% when Levy became CEO, had dropped to 3% by mid-2004. Pleased with the hospital's performance, the board signed Levy to a new three-year contract.

Heads, Hearts, and Hands

It's clear that the key to Paul Levy's success at Beth Israel Deaconess Medical Center is that he understood the importance of making sure the cultural soil had been made ready before planting the seeds of change. In a receptive environment, employees not only understand why change is necessary; they're also emotionally committed to making it happen, and they faithfully execute the required steps.

On a cognitive level, employees in receptive environments are better able to let go of competing, unsubstantiated views of the nature and extent of the problems facing their organizations. They hold the same, objective views of the causes of poor performance. They acknowledge the seriousness of current financial, operational, and marketplace difficulties. And they take responsibility for their own contributions to those problems. Such a shared, fact-based diagnosis is crucial for moving forward.

On an emotional level, employees in receptive environments identify with the organization and its values and are committed to its continued existence. They believe that the organization stands for something more than profitability, market share, or stock performance and is therefore worth saving. Equally important, they trust the leader, believing that he or she shares their values and will fight to preserve them. Leaders earn considerable latitude from employees—and their proposals usually get the benefit of the doubt—when their hearts are thought to be in the right place.

Workers in such environments also have physical, hands-on experience with the new behaviors expected of them. They have seen the coming changes up close and understand what they are getting into. In such an atmosphere where it's acceptable for employees to wrestle with decisions on their own and practice unfamiliar ways of working, a leader can successfully allay irrational fears and undercut the myths that so often accompany major change efforts.

There is a powerful lesson in all this for leaders. To create a receptive environment, persuasion is the ultimate tool. Persuasion promotes

understanding; understanding breeds acceptance; acceptance leads to action.
Without persuasion, even the best of turnaround plans will fail to take root.

Originally published in February 2005. Reprint R0502F

Leading Change When Business Is Good

An Interview with Samuel J. Palmisano. by Paul Hemp and Thomas A. Stewart

IN JULY 2003, International Business Machines Corporation conducted a 72-hour experiment whose outcome was as uncertain as anything going on in its research labs. Six months into a top-to-bottom review of its management organization, IBM held a three-day discussion via the corporate intranet about the company's values. The forum, dubbed ValuesJam, joined thousands of employees in a debate about the very nature of the computer giant and what it stood for.

Over the three days, an estimated 50,000 of IBM's employees—including CEO Sam Palmisano—checked out the discussion, posting nearly 10,000 comments about the proposed values. The jam had clearly struck a chord.

But it was a disturbingly dissonant one. Some comments were merely cynical. One had the subject line: "The only value in IBM today is the stock price." Another read, "Company values (ya right)." Others, though, addressed fundamental management issues. "I feel we talk a lot about trust and taking risks. But at the same time, we have endless audits, mistakes are punished and not seen as a welcome part of learning, and managers (and others) are consistently checked," wrote one employee. "There appears to be a great reluctance among our junior executive community to challenge the views of our senior execs," said another. "Many times I have heard expressions like, 'Would you tell Sam that his strategy is wrong!!?'" Twenty-four hours into the exercise, at least one senior executive wanted to pull the plug.

But Palmisano wouldn't hear of it. And then the mood began to shift. After a day marked by critics letting off steam, the countercritics began to weigh

in. While acknowledging the company's shortcomings, they argued that much of IBM's culture and values was worth preserving. "Shortly after joining IBM 18 years ago," wrote one, "I was asked to serve on a jury. When I approached the bench and answered [the lawyers'] questions, I was surprised when the judge said, 'You guys can pick whoever else you want, but I want this IBMer on that jury.' I have never felt so much pride. His statement said it all: integrity, excellence, and quality." Comments like these became more frequent, criticism became more constructive, and the ValuesJam conversation stabilized.

The question of what was worth preserving and what needed to be changed was at the heart of ValuesJam. In 1914—when the company was making tabulating machines, scales for weighing meat, and cheese slicers—president Thomas Watson, Sr., decreed three corporate principles, called the Basic Beliefs: "respect for the individual," "the best customer service," and "the pursuit of excellence." They would inform IBM's culture, and help drive its success, for more than half a century.

By 2002, when Palmisano took over as CEO, much had happened to Big Blue. In the early 1990s, the company had suffered the worst reversal in its history and then, under Lou Gerstner, had fought its way back, transformed from a mainframe maker into a robust provider of integrated hardware, networking, and software solutions. Palmisano felt that the Basic Beliefs could still serve the company—but now as the foundation for a new set of corporate values that could energize employees even more than its near-death experience had. Looking for a modern-day equivalent, Palmisano first queried 300 of his senior executives, then quickly opened up the discussion, through a survey of over a thousand employees, to get a sense of how people at all levels, functions, and locations would articulate IBM's values and their aspirations for the company. Out of this research grew the propositions that were debated in ValuesJam.

Idea in Brief

It's easy to fire up employees' passion for change when your business is about to go up in flames. Lou Gerstner knew this when he seized IBM's helm in 1993 and saved the faltering giant by transforming it from a

mainframe maker into a provider of integrated solutions.

But how do you maintain people's commitment to change when business is *good*? You know your company must constantly adapt if it wants to maintain its competitive edge. Yet without an obvious threat on the horizon, your *employees* may grow complacent.

How to build a workforce of relentless change agents? Replace command-and-control with **values-based management**: Instead of galvanizing people through fear of failure, energize them through hope and aspiration. Inspire them to pursue a common purpose based on values *they* help to define. Ask them what's blocking them from living those values—and launch change initiatives to remove obstacles.

As enduring companies like IBM have discovered, values-based management enables your people to respond quickly, flexibly, and creatively to a never-ending stream of strategic challenges.

After—and even during—the jam, company analysts pored over the postings, mining the million-word text for key themes. Finally, a small team that included Palmisano came up with a revised set of corporate values. The CEO announced the new values to employees in an intranet broadcast in November 2003: “dedication to every client’s success,” “innovation that matters—for our company and for the world,” “trust and personal responsibility in all relationships.” Earthshaking? No, but imbued with legitimacy and packed with meaning and implications for IBM.

To prove that the new values were more than window dressing, Palmisano immediately made some changes. He called on the director of a major business unit—e-business hosting services for the U.S. industrial sector—and charged her with identifying gaps between the values and company practices. He bluntly told his 15 direct reports that they had better follow suit. Another online jam was held in October 2004 (this one informally dubbed a “logjam”) in which employees were asked to identify organizational barriers to innovation and revenue growth.

Idea in Practice

To create your values-based management system:

Gather Employees' Input on Values

Assess the strategic challenges facing your company. Propose values you believe will help your firm meet those challenges. Collect employees' feedback on your ideas.

Example: IBM CEO Sam Palmisano knew that the IT industry was reintegrating: Customers wanted packages of computer products and services from single firms. Despite its far-flung, diverse 320,000-strong workforce, the company had to offer customized solutions at a single price. To achieve the required cooperation, IBM needed a shared set of values to guide people's decision making.

Using feedback from top managers and employees, Palmisano's team developed three working value statements—"Commitment to the customer," "Excellence through innovation," and "Integrity that earns trust." IBM posted these on its intranet and invited employees to debate them. Over three days, 50,000 debated the merits of the value statements.

Analyze Employees' Input

Examine employees' input for themes.

Example: Many IBMers criticized the "integrity that earns trust" statement as vague, outdated, and inwardly focused. They wanted more specific guidance on how to behave with each other and with external stakeholders.

Revise Your Values

Based on the themes in employees' input, create a revised set of values. Gather employees' input again.

Example: Palmisano's team revised the earlier value statements to read: "Dedication to every client's success," "Innovation that matters—for our company and for the world," and "Trust and personal responsibility in all relationships." The team published the revised statements on the intranet and once more invited feedback.

Identify Obstacles to Living the Values

Examine employees' responses to identify what's preventing your company from living its agreed-upon values.

Example: IBMers praised the revised value statements—often in highly emotional language—but wondered whether IBM was willing and able to live those values. They understood the need to reintegrate the company but lamented obstacles—such as frustrating financial controls—that prevented them from serving customers quickly.

Launch Change Initiatives to Remove Obstacles

Initiate change programs that enable people to live the values.

Example: IBM allocated \$5,000 a year to individual managers to use, no questions asked, in order to generate business, develop client relationships, or respond to fellow IBMers' emergency needs. A pilot program run with 700 client-facing teams showed that they spent the money intelligently. The program was expanded to all 22,000 IBM first-line managers. The initiative demonstrated to employees that IBM lives by its values.

Although Palmisano, by his own account, is building on a strategy laid down by Gerstner, the leadership styles of the two men are very different. Under Gerstner, there was little expansive talk about IBM's heritage. He was an outsider, a former CEO of RJR Nabisco and an ex-McKinsey consultant, who was faced with the daunting task of righting a sinking ship. In fact, he famously observed, shortly after taking over, that "the last thing IBM needs right now is a vision." Palmisano, by contrast, is a true-blue IBMer, who started at the company in 1973 as a salesman in Baltimore. Like many of his generation who felt such acute shame when IBM was brought to its knees in the early 1990s, he clearly has a visceral attachment to the firm—and to the hope that it may someday regain its former greatness. At the same time, the erstwhile salesman is, in the words of a colleague, "a results-driven, make-it-rain, close-the-deal sort of guy": not the first person you'd expect to hold forth on a subjective topic like "trust."

In this edited conversation with HBR senior editor Paul Hemp and HBR's editor, Thomas A. Stewart, Palmisano talks about the strategic importance of values to IBM. He begins by explaining why—and how—hard financial metrics and soft corporate values can coexist.

Corporate values generally are feel-good statements that have almost no effect on a company's operations. What made—what makes—you think they can be more than this?

Look at the portrait of Tom Watson, Sr., in our lobby. You've never seen such a stern man. The eyes in the painting stare right through you. This was *not* a soft individual. He was a capitalist. He wanted IBM to make money, lots of it. But he was perceptive enough to build the company in a way that would ensure its prosperity long after he left the scene. His three Basic Beliefs successfully steered this company through persistent change and repeated reinvention for more than 50 years.

An organic system, which is what a company is, needs to adapt. And we think values—that's what we call them today at IBM, but you can call them "beliefs" or "principles" or "precepts" or even "DNA"—are what enable you to do that. They let you change everything, from your products to your strategies to your business model, but remain true to your essence, your basic

mission and identity.

Unfortunately, over the decades, Watson's Basic Beliefs became distorted and took on a life of their own. "Respect for the individual" became entitlement: not fair work for all, not a chance to speak out, but a guaranteed job and culture-dictated promotions. "The pursuit of excellence" became arrogance: We stopped listening to our markets, to our customers, to each other. We were so successful for so long that we could never see another point of view. And when the market shifted, we almost went out of business. We had to cut a workforce of more than 400,000 people in half. Over the course of several years, we wiped out the equivalent of a medium-sized northeastern city—say, Providence, Rhode Island.

If you lived through this, as I did, it was easy to see how the company's values had become part of the problem. But I believe values can once again help guide us through major change and meet some of the formidable challenges we face.

For instance, I feel that a strong value system is crucial to bringing together and motivating a workforce as large and diverse as ours has become. We have nearly one-third of a million employees serving clients in 170 countries. Forty percent of those people don't report daily to an IBM site; they work on the client's premises, from home, or they're mobile. And, perhaps most significant, given IBM's tradition of hiring and training young people for a lifetime of work, half of today's employees have been with the company for fewer than five years because of recent acquisitions and our relatively new practice of hiring seasoned professionals. In a modest hiring year, we now add 20,000 to 25,000 people.

In effect, gradually repopulating Providence, Rhode Island!

Exactly. So how do you channel this diverse and constantly changing array of talent and experience into a common purpose? How do you get people to *passionately* pursue that purpose?

You could employ all kinds of traditional, top-down management processes. But they wouldn't work at IBM—or, I would argue, at an increasing number of twenty-first-century companies. You just can't impose command-and-control mechanisms on a large, highly professional workforce.

I'm not only talking about our scientists, engineers, and consultants. More than 200,000 of our employees have college degrees. The CEO can't say to them, "Get in line and follow me." Or "I've decided what *your* values are." They're too smart for that. And as you know, smarter people tend to be, well, a little more challenging; you might even say cynical.

But even if our people did accept this kind of traditional, hierarchical management system, our clients wouldn't. As we learned at IBM over the years, a top-down system can create a smothering bureaucracy that doesn't allow for the speed, the flexibility, the innovation that clients expect today.

So you're saying that values are about how employees behave when management isn't there, which it can't be—which it shouldn't be—given IBM's size and the need for people to make decisions quickly. You're basically talking about using values to manage.

Yes. A values-based management system. Let me cast the issue in a slightly different light. When you think about it, there's no optimal way to organize IBM. We traditionally were viewed as a large, successful, "well-managed" company. That was a compliment. But in today's fast-changing environment, it's a problem. You can easily end up with a bureaucracy of people overanalyzing problems and slowing down the decision-making process.

Think of our organizational matrix. Remember, we operate in 170 countries. To keep it simple, let's say we have 60 or 70 major product lines. We have more than a dozen customer segments. Well, if you mapped out the entire 3-D matrix, you'd get more than 100,000 cells—cells in which you have to close out P&Ls every day, make decisions, allocate resources, make trade-offs. You'll drive people crazy trying to centrally manage every one of those intersections.

So if there's no way to optimize IBM through organizational structure or by management dictate, you have to empower people while ensuring that they're making the right calls the right way. And by "right," I'm not talking about ethics and legal compliance alone; those are table stakes. I'm talking about decisions that support and give life to IBM's strategy and brand, decisions that shape a culture. That's why values, for us, aren't soft. They're the basis of what we do, our mission as a company. They're a touchstone for

decentralized decision making. It used to be a rule of thumb that “people don’t do what you expect; they do what you inspect.” My point is that it’s just not possible to inspect everyone anymore. But you also can’t just let go of the reins and let people do what they want without guidance or context. You’ve got to create a management system that empowers people and provides a basis for decision making that is consistent with who we are at IBM.

How do the new values help further IBM’s strategy?

In two main ways. Back some 12 years ago, three-fifths of our business was in computer hardware and roughly two-fifths was in software and services. Today, those numbers are more than reversed. Well, if three-fifths of your business is manufacturing, management is basically supervisory: “You do this. You do that.” But that no longer works when your business is primarily based on knowledge. And your business model also changes dramatically.

For one thing, people—rather than products—become your brand. Just as our products have had to be consistent with the IBM brand promise, now more than ever, so do our people. One way to ensure that is to inform their behavior with a globally consistent set of values.

Second, the IT industry has continued to shift toward reintegration. We all know the story of how the industry fragmented in the 1980s and 1990s, with separate companies selling the processors, the storage devices, and the software that make up a computer system—almost killing IBM, the original vertically integrated computer company. Now customers are demanding a package of computer products and services from a single company, a company that can offer them an integrated solution to their business problems. This is a big opportunity for IBM. We probably have a wider array of computer products and services and know-how than anyone. But it’s also a challenge. How can we get our people in far-flung business units with different financial targets and incentives working together in teams that can offer at a single price a comprehensive and customized solution—one that doesn’t show the organizational seams?

Companies usually face the issue of workforce integration after a huge merger. We needed to integrate our existing workforce as a strategic response

to the reintegration of the industry. It won't surprise you that I didn't think the answer lay in a new organizational structure or in more management oversight. What you need to foster this sort of cooperation is a common set of guidelines about how we make decisions, day in and day out. In other words, values.

And what happens when the strategy changes?

Ah, that's why the right set of values is so important. There's always going to be another strategy on the horizon as the market changes, as technologies come and go. So we wanted values that would foster an organization able to quickly execute a new strategy. At the same time, we wanted values that, like Watson's Basic Beliefs, would be enduring, that would guide the company through economic cycles and geopolitical shifts, that would transcend changes in products, technologies, employees, and leaders.

How did IBM distill new values from its past traditions and current employee feedback?

The last time IBM examined its values was nearly a century ago. Watson was an entrepreneur, leading what was, in today's lingo, a start-up. So in 1914, he simply said, "Here are our beliefs. Learn them. Live them." That was appropriate for his day, and there's no question it worked. But 90 years later, we couldn't have someone in headquarters sitting up in bed in the middle of the night and saying, "Here are our new values!" We couldn't be casual about tinkering with the DNA of a company like IBM. We had to come up with a way to get the employees to create the value system, to determine the company's principles. Watson's Basic Beliefs, however distorted they might have become over the years, had to be the starting point.

After getting input from IBM's top 300 executives and conducting focus groups with more than a thousand employees—a statistically representative cross-section—we came up with three perfectly sound values. [For a detailed

description of how IBM got from the Basic Beliefs to its new set of values, see the sidebar “Continuity and Change.”] But I knew we’d eventually throw out the statements to everyone in the company to debate. That’s where ValuesJam came in—this live, companywide conversation on our intranet.

What was your own experience during the jam? Did you have the feeling you’d opened Pandora’s box?

I logged in from China. I was pretty jet-lagged and couldn’t sleep, so I jumped in with postings on a lot of stuff, particularly around client issues. [For a selection of Palmisano’s postings during the ValuesJam, see the sidebar “Sam Joins the Fray.”] And yes, the electronic argument was hot and contentious and messy. But you had to get comfortable with that. Understand, we had done three or four big online jams before this, so we had some idea of how lively they can be. Even so, none of those could have prepared us for the emotions unleashed by this topic.

You had to put your ego aside—not easy for a CEO to do—and realize that this was the best thing that could have happened. You could say, “Oh my God, I’ve unleashed this incredible negative energy.” Or you could say, “Oh my God, I now have this incredible mandate to drive even more change in the company.”

When Lou Gerstner came here in 1993, there was clearly a burning platform. In fact, the whole place was in flames. There was even talk of breaking up the company. And he responded brilliantly. Here’s this outsider who managed to marshal the collective urgency of tens of thousands of people like me to save this company and turn it around: without a doubt one of the greatest saves in business history. But the trick then wasn’t creating a sense of urgency—we had that. Maybe you needed to shake people out of being shell-shocked. But most IBMers were willing to do whatever it took to save the company, not to mention their own jobs. And there was a lot of pride at stake. Lou’s task was mostly to convince people that he was making the right changes.

Once things got better, though, there was another kind of danger: that we would slip back into complacency. As our financial results improved dramatically and we began outperforming our competitors, people—already

weary from nearly a decade of change—would say, “Well, why do I have to do things differently now? The leadership may be different, but the strategy is fundamentally sound. Why do I have to change?” This is, by the way, a problem that everyone running a successful company wrestles with.

So the challenge shifted. Instead of galvanizing people through fear of failure, you have to galvanize them through hope and aspiration. You lay out the opportunity to become a great company again—the greatest in the world, which is what IBM used to be. And you hope people feel the same need, the urgency you do, to get there. Well, I think IBMers today do feel that urgency. Maybe the jam’s greatest contribution was to make that fact unambiguously clear to all of us, very visibly, in public.

Continuity and Change

IBM’S NEW VALUES GREW OUT OF A LONG TRADITION. In 1914, Thomas Watson, Sr., the founder of the modern International Business Machines Corporation, laid out three principles known as the *Basic Beliefs*:

- Respect for the individual
- The best customer service
- The pursuit of excellence

Although these beliefs played a significant role in driving IBM’s success over most of the twentieth century, they eventually were subsumed—and, in effect, redefined—by a sense of entitlement and arrogance within the organization. That, according to CEO Sam Palmisano, contributed to the company’s failure to respond to market changes in the early 1990s and to its near demise.

In February 2003, just under a year after taking over as CEO, at a meeting of IBM’s top 300 managers, Palmisano raised the idea of reinventing the company’s values as a way to manage and reintegrate the sprawling and

diverse enterprise. He put forth *four concepts*, three of them drawn from Watson's Basic Beliefs, as possible bases for the new values:

- Respect
- Customer
- Excellence
- Innovation

These were “test marketed” through surveys and focus groups with more than 1,000 IBM employees. The notion of “respect” was thrown out because of its connotations of the past. It was also decided that statements rather than just words would be more compelling.

Out of this process grew the three *proposed values* discussed during the July 2003 online forum, ValuesJam:

- Commitment to the customer
- Excellence through innovation
- Integrity that earns trust

Using a specially tailored “jamalyzer” tool—based on IBM's e-classifier software, but turbocharged with additional capabilities designed to process constantly changing content—IBM analysts crunched the million-plus words posted during the ValuesJam. Some themes emerged. For example, many people said that a silo mentality pitted the business units against one another, to the detriment of IBM as a whole. Several people characterized this as a trust issue. But the proposed value “integrity that earns trust” was criticized as being too vague. Some thought it was just another way of saying “respect for the individual,” one of the original Basic Beliefs that many now viewed as outdated. And the notion of trust was seen as being too inwardly focused

—management trusting its employees—and not prescriptive enough in terms of how employees should behave with each other or with parties outside the company.

Drawing on this analysis, the results of pre- and post-jam surveys, and a full reading of the raw transcripts, a small team, with input from Palmisano, arrived at a revised set of *new corporate values*:

- **Dedication to every client's success**
- **Innovation that matters—for our company and for the world**
- **Trust and personal responsibility in all relationships**

These were published on the company intranet in November 2003.

What were the chief points of debate—or contention?

There was actually remarkable agreement on *what* we all value. The debate, as it turned out, wasn't over the values themselves so much. The debate was about whether IBM today is willing and able to live them.

For instance, people seemed to understand the need to reintegrate the company, but there were complaints—legitimate complaints—about things that are getting in the way. People would describe extremely frustrating situations. They'd say something like: "I'm in Tokyo, prototyping software for a client, and I need a software engineer based in Austin *right now* to help in a blade server configuration. But I can't just say, 'Please come to Tokyo and help.' I need to get a charge code first so I can pay his department for his time!"

There's a collective impatience that we've been tapping into to drive the change needed to make IBM everything that all of us aspire for it to be. I'm convinced that we wouldn't have gotten to this point if we hadn't found a

way to engage the entire IBM population in a genuine, candid conversation.

Sam Joins the Fray

IBM CEO SAM PALMISANO was in China on business during ValuesJam, and he logged on from there. Following are some of his comments (typos included) on a number of topics raised by employees during the online forum:

YES, values matter!!!! (6 reply)

Samuel J. Palmisano 29 Jul 2003 20:00 GMT

Good discussion about the need for values/principles/beliefs, etc. people can be very cynical and sarcastic about this kind of topic, but I appreciate the thoughtful constructive comments I'm seeing. Personally, I believe "values" should embrace a company's broader role in the world —with customers, society, culture, etc. - as well as how its people work together.. I hope this Jam elevates IBM's ambitions about its mission in the 21st century.. WE have a unique opportunity for IBM to set the pace for ALL companies, not just the techs.

doing the right thing for customers... (21 reply)

Samuel J. Palmisano 29 Jul 2003 20:07 GMT

Early in my career when I was in the field in Baltimore, one of our systems failed for a healthcare customer. The customer went to manual processes, but said they would start losing patients within hours if the system couldn't be fixed. The branch mgr called one of our competitors and ordered another system. so two teams of IBMERS worked side by side.. one to fix the system, the others to bring up the new one. the mgr never asked Hq what to do.. it was a great lesson in how far this company will go to help a customer in time of need. btw, we fixed the system in time.

integrity/trust in ALL our relationships matter!!!! (44 reply)

Samuel J. Palmisano 29 Jul 2003 20:12 GMT

very interesting discussion... one thing I'm noticing, and it was in the broadcast feedback too: not too many of you are talking about integrity and trust when it comes to our OTHER relationships that are key to IBMs success—customers, communities where we live, owners of the company etc. any thoughts on why thats so? maybe we're too inwardly focused?

a world without IBM???? (35 reply)

Samuel J. Palmisano 29 Jul 2003 20:20 GMT

No IBM? the industry would stop growing because no one would invent anything that ran for more than THREE MINUTES.. no IBM means no grownups ... no IBM means no truly global company that brings economic growth, respect progress to societies everywhere... no iBM means no place to work for hundreds of thousands of people who want more than a job, they want to ,MAKE A DIFFERENCE in the world.

suggestion for Sam (9 reply)

Samuel J. Palmisano 29 Jul 2003 20:25 GMT

steve, you make good points about how/when we win... we can blow up more burecracy if we all behave like mature adutls and take into account ALL OF THE INTERESTS of IBm FIRST.. customers, employees, shareholders, doing whats right for the LONG TERM intersts of the company. mgrs have an important role to play in encouraing this kind of behavior... you have my support.

By the way, having a global, universally accessible intranet like ours certainly helps, but the technology isn't the point. I think we would've found

a way to have this companywide dialogue if the Web didn't exist. [For an explanation of how the jam worked, see the sidebar "Managing ValuesJam."]

What happened after the jam?

Well, we got a mountain of employee comments. The team analyzed all of it, and it was clear that the proposed value statements needed to change to reflect some of the nuances and emotion people expressed. So, drawing on this analysis, along with other employee feedback, a small team settled on IBM's new corporate values.

The first value is "dedication to every client's success." At one level, that's pretty straightforward: Bring together all of IBM's capability—in the laboratory, in the field, in the back office, wherever—to help solve difficult problems clients can't solve themselves. But this is also a lot more than the familiar claim of unstinting customer service. "Client success" isn't just "the customer is always right." It means maintaining a long-term relationship where what happens after the deal is more important than what happens before it's signed. It means a persistent focus on outcomes. It means having skin in the game of your client's success, up to and including how your contracts are structured and what triggers your getting paid.

The second is "innovation that matters—for our company and for the world." When employees talked about IBM making a difference in the world, they included more than our work of inventing and building great products. They talked about how their work touches people and society, how we can help save lives—say, through our cutting-edge work with the Mayo Clinic or by helping governments fight terrorism with our data technology. This kind of innovation is a major reason we are able to attract great scientists. They can do cool stuff and maybe make more money in Silicon Valley—for a while, anyway—but they can do work that actually changes business and society at IBM. And it's also about what I mentioned before: a continually experimental attitude toward IBM itself. Over most of our 90 years, with the exception of that one period when we became arrogant and complacent, this company never stopped questioning assumptions, trying out different models, testing the limits—whether in technology or business or in progressive workforce policies. Employees reminded us that those things are innovations

that matter at least as much as new products.

The third value is “trust and personal responsibility in all relationships.” There’s a lot in that statement, too. Interestingly, the feedback from employees on this value has focused on relationships among people at IBM. But we’re also talking about the company’s relationships with suppliers, with investors, with governments, with communities.

We published the values in their final form—along with some elaboration on them and some direct employee postings from the jam—in November 2003. Over the next ten days, more than 200,000 people downloaded the online document. The responses just flooded in, both in the form of postings on the intranet and in more than a thousand e-mails sent directly to me, telling us in often sharp language just where IBM’s operations fell short of, or clashed with, these ideals. Some of the comments were painful to read. But, again, they exhibited something every leader should welcome: People here aren’t complacent about the company’s future. And the comments were, by and large, extremely thoughtful.

Managing ValuesJam

IBM HAD EXPERIMENTED before with jam sessions—relatively unstructured employee discussions around broad topics—both on the corporate intranet and in face-to-face off-site brainstorming sessions. But the 72-hour ValuesJam, held in July 2003, was the most ambitious, focusing as it did on the very nature and future of IBM.

One thing was clear: You wouldn’t be able to orchestrate a forum like this, the verbal equivalent of an improvisational jam session among jazz musicians. In the words of CEO Sam Palmisano, “It just took off.” But, much like a musical jam, the dialogue was informed by a number of themes:

Forum 1. Company Values

Do company values exist? If so, what is involved in establishing them? Most companies today have values statements. But what would a company look and act like that truly lived its beliefs? Is it important for IBM to agree on a

set of lasting values that drive everything it does?

Forum 2. A First Draft

What values are essential to what IBM needs to become? Consider this list: 1. Commitment to the customer. 2. Excellence through innovation. 3. Integrity that earns trust. How might these values change the way we act or the decisions we make? Is there some important aspect or nuance that is missing?

Forum 3. A Company's Impact

If our company disappeared tonight, how different would the world be tomorrow? Is there something about our company that makes a unique contribution to the world?

Forum 4. The Gold Standard

When is IBM at its best? When have you been proudest to be an IBMer? What happened, and what was uniquely meaningful about it? And what do we need to do—or change—to be the gold standard going forward?

What did you do with this feedback?

We collected and collated it. Then I printed all of it out—the stack of paper was about three feet high—and took it home to read over one weekend. On Monday morning, I walked into our executive committee meeting and threw it on the table. I said, “You guys ought to read every one of these comments, because if you think we’ve got this place plumbed correctly, think again.”

Don’t get me wrong. The passion in these e-mails was positive as well as negative. People would say, literally, “I’m weeping. These values describe

the company I joined, the company I believe in. We can truly make this place great again. But we've got all these things in our way... ." The raw emotion of some of the e-mails was really something.

Now, if you've unleashed all this frustration and energy, if you've invited people to feel hope about something they really care about, you'd better be prepared to do something in response. So, in the months since we finalized the values, we've announced some initiatives that begin to close the gaps.

One I have dubbed our "\$100 million bet on trust." We kept hearing about situations like our colleague in Tokyo who needed help from the engineer in Austin, cases in which employees were unable to respond quickly to client needs because of financial control processes that required several levels of management approval. The money would usually be approved, but too late. So we allocated managers up to \$5,000 annually they could spend, no questions asked, to respond to extraordinary situations that would help generate business or develop client relationships or to respond to an IBMer's emergency need. We ran a pilot for a few months with our 700 client-facing teams, and they spent the money intelligently. There were lots of examples of teams winning deals and delighting clients with a small amount of "walk around money" to spend at their discretion. So, based on the success of that pilot, we expanded the program to all 22,000 IBM first-line managers.

You can do the math: \$5,000 times 22,000 managers is a big number. I'm sure there were people in the company who said, "We need to get this under control." But they're not the CEO. Yes, you need financial controls. Yes, not every dollar spent from this Managers' Value Fund will yield some tangible return. But I'm confident that allowing line managers to take some reasonable risks, and trusting them with those decisions, will pay off over time. The program also makes a point: that we live by our values.

The value of "trust and personal responsibility in all relationships"—including those with IBM's shareholders—led to another initiative: a change in the way we grant top executive stock options. After getting a lot of outside experts to study this (and concluding that the complicated algorithms they recommended were wonderful, if you wanted to hire the outsiders as permanent consultants, but terrible if you wanted a simple formula that aligned executive behavior with shareholder interests), we settled on a straightforward idea. Senior executives will benefit from their options only after shareholders have realized at least 10% growth in their investments—that is, the strike price is 10% higher than the market price on the day the

options are issued. Look at it this way: IBM's market value would have to increase by \$17 billion from that date before any of the execs realize a penny of benefit. We think we are the first large company to take such a radical step—and it grew out of our values.

Let me give you one more example. It may not sound like a big deal, but for us, it was radical. We overhauled the way we set prices. We heard time and again from employees about how difficult it was to put together a client-friendly, cross-IBM solution, one involving a variety of products and services at a single, all-inclusive price. We couldn't do it. Every brand unit had its own P&L, and all the people who determine prices had been organized by brand. Remember those 100,000 cells in our 3-D matrix? Our people were pulling their cross-IBM bids apart, running them through our financial-accounting system as separate bids for individual products and services. This was nuts, because it's our ability to offer everything—hardware, software, services, and financing—that gives us a real advantage. When we bid on each of the parts separately, we go head-to-head against rivals by product: EMC in storage, say, or Accenture in services. This was tearing out the very heart of our strategy of integration, not to mention our unique kind of business-plus-technology innovation.

Let me give you a humorous (if somewhat discouraging) illustration. Every senior executive has responsibility for at least one major client—we call them “partnership accounts.” Our former CFO John Joyce, who now heads IBM's services business, put together a deal for his account that involved some hardware, some software, and some services. He was told he couldn't price it as an integrated solution. And he's the CFO! So we figured out a way to set a single price for each integrated offering.

This sounds like a great business move. But what does it have to do with values? Wouldn't you ultimately have decided you had to do that in any case?

To be honest, we'd been debating the pricing issue at the executive level for a long time. But we hadn't done anything about it. The values initiative forced us to confront the issue, and it gave us the impetus to make the change. You know, there are always ingrained operations and habits of mind

in any organization—I don't care whether it's a business or a university or a government. Well, the values and the jam were great inertia-busting vehicles. A small business in this place is \$15 billion, and a big one is \$40 billion. So you have senior vice presidents running *Fortune* 500-sized companies who aren't necessarily looking for bright ideas from the CEO or some task force every day. But when you hear from so many of our people on the front lines, you can't just ignore it. They're crying out: "We say we value 'client success,' and we want to grow our business. This one thing is getting in the way of both!" You've got to pay attention—if not to me, then to them.

So we took the pricers—the people who set the prices for client bids—and we said to them, "You work for IBM. When there's a cross-IBM bid with multiple products, you price it on the IBM income statement, not on the income statements of each product." Needless to say, this involved a series of very difficult meetings with senior executives. There was a huge debate among the finance people about all the reasons why we couldn't do it: "It will be too much work to reallocate all the costs and revenue of a project back to individual profit centers." And they're right: It isn't easy, especially when we now have to certify everything. But the CFO was with me on this: After all, he'd seen the problem firsthand! And we made the change, so that now when we make a truly cross-IBM bid, we can optimize it for the client and for us.

This brings us back to the tension between soft values and hard financial metrics. In the long run, they shouldn't conflict. But along the way, they're going to be jabbing at each other. After all, people still have to make their numbers.

Certainly, there's no getting around that in a commercial enterprise. But I think values inject balance in the company's culture and management system: balance between the short-term transaction and the long-term relationship, balance between the interests of shareholders, employees, and clients. In every case, you have to make a call. Values help you make those decisions, not on an ad hoc basis, but in a way that is consistent with your culture and brand, with who you are as a company.

Look at how we compensate our managing directors, who are responsible for our largest client relationships. We decided to take half their comp and

calculate it not on an annual basis but on a rolling three-year basis. We ask clients to score the managing director's performance at the end of a project or engagement, which might last longer than a single year, and that plays a big part in his bonus. So a big piece of his compensation is based on a combination of the project's profitability—whether the manager made his annual numbers—and on the client's satisfaction over a longer-term horizon. The managing director can't trade off one for the other.

So we've tried to keep balance in the system, to make sure that things aren't completely oriented toward short-term financials. But you're absolutely right: There are times when people will argue, "Well, jeez, you guys are pushing us in both directions." It's a valid debate. I think, though, that the best place to have that debate is at the lowest level of your organization, because that's where these decisions are being made and having an impact. Thousands of these interactions go on every day that none of us at the top will ever, or should ever, know about. But you hope that the values are providing a counterweight to the drive for short-term profitability in all those interactions. In the long term, I think, whether or not you have a values-driven culture is what makes you a winner or a loser.

You've had the new values in place for just about a year now. They've already created strong emotions and high expectations. What's the prognosis?

We're just starting down the road on what is probably a ten- to 15-year process. I was back in Asia not long ago, and I did one of these town hall-style meetings with IBM employees and talked about the values. Probably two-thirds of the people clearly knew about them, had read about them. But a third of the people—you could look at their faces and see it—hadn't even heard of the values. Or at least the values hadn't resonated with them yet. So we have work to do. Not just in getting everyone to memorize three pithy statements. We need to do a heck of a lot to close the gaps between our stated values and the reality of IBM today. That's the point of it all.

I know that not everyone on my executive team is as enthusiastic about the values initiative as I am—though they'd never admit it! But people on the senior team who lived through IBM's near-death experience will do anything

not to go back to that. The blow to everyone's pride when IBM became the laughingstock of the business world was almost too much to bear. I have zero resistance from the senior team to initiatives that can save us from a return to that. And our values work is one of the most important of those initiatives.

Then look at the employee response to ValuesJam. There is an unmistakable yearning for this to be a great company. I mean, why have people joined IBM over the years? There are a lot of places to make money, if that's what drives you. Why come here?

I believe it's because they want to be part of a progressive company that makes a difference in the world. They want to be in the kind of company that supports research that wins Nobel Prizes, that changes the way people think about business itself, that is willing to take firm positions on unpopular issues based on principle.

You know, back in the 1950s, Watson, Jr., wrote the governors of southern states that IBM would not adhere to separate-but-equal laws, and then the company codified an equal-opportunity policy years before it was mandated by law. I've got to believe that a company that conceives of itself that way, and that seriously manages itself accordingly, has strong appeal to a lot of people. We can't offer them the promise of instant wealth, which they may get at a start-up, or a job for life, as in the old days. But we can offer them something worth believing in and working toward.

If we get most people in this company excited about that, they're going to pull the rest of the company with them. If they become dedicated to these values and what we're trying to accomplish, I can go to sleep at night confident of our future.

Originally published in December 2004. Reprint R0412C

Radical Change, the Quiet Way

by Debra E. Meyerson

AT ONE POINT OR ANOTHER, many managers experience a spang of conscience—a yearning to confront the basic or hidden assumptions, interests, practices, or values within an organization that they feel are stodgy, unfair, even downright wrong. A vice president wishes that more people of color would be promoted. A partner at a consulting firm thinks new MBAs are being so overworked that their families are hurting. A senior manager suspects his company, with some extra cost, could be kinder to the environment. Yet many people who want to drive changes like these face an uncomfortable dilemma. If they speak out too loudly, resentment builds toward them; if they play by the rules and remain silent, resentment builds inside them. Is there any way, then, to rock the boat without falling out of it?

Over the past 15 years, I have studied hundreds of professionals who spend the better part of their work lives trying to answer this question. Each one of the people I've studied differs from the organizational status quo in some way—in values, race, gender, or sexual preference, perhaps (see the sidebar “How the Research Was Done”). They all see things a bit differently from the “norm.” But despite feeling at odds with aspects of the prevailing culture, they genuinely like their jobs and want to continue to succeed in them, to effectively use their differences as the impetus for constructive change. They believe that direct, angry confrontation will get them nowhere, but they don't sit by and allow frustration to fester. Rather, they work quietly to challenge prevailing wisdom and gently provoke their organizational cultures to adapt. I call such change agents *tempered radicals* because they work to effect significant changes in moderate ways.

How the Research Was Done

THIS ARTICLE IS BASED ON a multipart research effort that I began in 1986 with Maureen Scully, a professor of management at the Center for Gender in Organizations at Simmons Graduate School of Management in Boston. We had observed a number of people in our own occupation—academia—who, for various reasons, felt at odds with the prevailing culture of their institutions. Initially, we set out to understand how these individuals sustained their sense of self amid pressure to conform and how they managed to uphold their values without jeopardizing their careers. Eventually, this research broadened to include interviews with individuals in a variety of organizations and occupations: business people, doctors, nurses, lawyers, architects, administrators, and engineers at various levels of seniority in their organizations.

Since 1986, I have observed and interviewed dozens of tempered radicals in many occupations and conducted focused research with 236 men and women, ranging from mid-level professionals to CEOs. The sample was diverse, including people of different races, nationalities, ages, religions, and sexual orientations, and people who hold a wide range of values and change agendas. Most of these people worked in one of three publicly traded corporations—a financial services organization, a high-growth computer components corporation, and a company that makes and sells consumer products. In this portion of the research, I set out to learn more about the challenges tempered radicals face and discover their strategies for surviving, thriving, and fomenting change. The sum of this research resulted in the spectrum of strategies described in this article.

In so doing, they exercise a form of leadership within organizations that is more localized, more diffuse, more modest, and less visible than traditional forms—yet no less significant. In fact, top executives seeking to institute cultural or organizational change—who are, perhaps, moving tradition-bound organizations down new roads or who are concerned about reaping the full potential of marginalized employees—might do well to seek out these

tempered radicals, who may be hidden deep within their own organizations. Because such individuals are both dedicated to their companies and masters at changing organizations at the grassroots level, they can prove extremely valuable in helping top managers to identify fundamental causes of discord, recognize alternative perspectives, and adapt to changing needs and circumstances. In addition, tempered radicals, given support from above and a modicum of room to experiment, can prove to be excellent leaders. (For more on management's role in fostering tempered radicals, see the sidebar "Tempered Radicals as Everyday Leaders.")

Idea in Brief

How do you rock your corporate boat—without falling out? You know your firm needs constructive change, but here's your dilemma: If you push your agenda too hard, resentment builds against you. If you remain silent, resentment builds inside you.

What's a manager to do? Become a **tempered radical**—an informal leader who quietly challenges prevailing wisdom and provokes cultural transformation. These radicals bear no banners and sound no trumpets. Their seemingly innocuous changes barely inspire notice. But like steady drops of water, they gradually erode granite.

Tempered radicals embody contrasts. Their commitments are firm, but their means flexible. They yearn for rapid change, but trust in patience. They often work alone, yet unite others. Rather than pressing their agendas, they start conversations. And instead of battling powerful foes, they seek powerful friends. The overall effect? Evolutionary—but relentless—change.

Since the actions of tempered radicals are not, by design, dramatic, their leadership may be difficult to recognize. How, then, do people who run organizations, who want to nurture this diffuse source of cultural adaptation,

find and develop these latent leaders? One way is to appreciate the variety of modes in which tempered radicals operate, learn from them, and support their efforts.

To navigate between their personal beliefs and the surrounding cultures, tempered radicals draw principally on a spectrum of incremental approaches, including four I describe here. I call these *disruptive self-expression*, *verbal jujitsu*, *variable-term opportunism*, and *strategic alliance building*. Disruptive self-expression, in which an individual simply acts in a way that feels personally right but that others notice, is the most inconspicuous way to initiate change. Verbal jujitsu turns an insensitive statement, action, or behavior back on itself. Variable-term opportunists spot, create, and capitalize on short- and long-term opportunities for change. And with the help of strategic alliances, an individual can push through change with more force.

Idea in Practice

Tempered radicals use these tactics:

Disruptive Self-Expression

Demonstrate your values through your language, dress, office décor, or behavior. People notice and talk— often becoming brave enough to try the change themselves. The more people talk, the greater the impact.

Example: Stressed-out manager John Ziwak began arriving at work earlier so he could leave by 6:00 p.m. to be with family. He also refused evening business calls. As his stress eased, his performance improved. Initially skeptical, colleagues soon accommodated, finding more efficient ways of working and achieving balance in their own lives.

Verbal Jujitsu

Redirect negative statements or actions into positive change.

Example: Sales manager Brad Williams noticed that the new marketing director's peers ignored her during meetings. When one of them co-opted a thought she had already expressed, Williams said: "I'm glad George picked up on Sue's concerns. Sue, did George correctly capture what you were thinking?" No one ignored Sue again.

Variable-Term Opportunism

Be ready to capitalize on unexpected opportunities for short-term change, as well as orchestrate deliberate, longer term change.

Example: Senior executive Jane Adams joined a company with a dog-eat-dog culture. To insinuate her collaborative style, she shared power with direct reports, encouraged them to also delegate, praised them publicly, and invited them to give high-visibility presentations. Her division gained reputé as an exceptional training ground for building experience, responsibility, and confidence.

Strategic Alliance Building

Gain clout by working with allies. Enhance your legitimacy and implement change more quickly and directly than you could alone. Don't make "opponents" enemies—they're often your best source of support and resources.

Example: Paul Wielgus started a revolution in his bureaucratic global spirits company—by persuading the opposition to join him. Others derided the training department Wielgus formed to boost employee creativity, and an auditor scrutinized the department for unnecessary expense. Rather than getting defensive, Paul treated the auditor as an equal and sold him on the program's value. The training spread, inspiring employees and enhancing productivity throughout the company.

Each of these approaches can be used in many ways, with plenty of room for creativity and wit. Self-expression can be done with a whisper; an employee who seeks more racial diversity in the ranks might wear her dashiki to company parties. Or it can be done with a roar; that same employee might wear her dashiki to the office every day. Similarly, a person seeking stricter environmental policies might build an alliance by enlisting the help of one person, the more powerful the better. Or he might post his stance on the company intranet and actively seek a host of supporters. Taken together, the approaches form a continuum of choices from which tempered radicals draw at different times and in various circumstances.

But before looking at the approaches in detail, it's worth reconsidering, for a moment, the ways in which cultural change happens in the workplace.

How Organizations Change

Research has shown that organizations change primarily in two ways: through drastic action and through evolutionary adaptation. In the former case, change is discontinuous and often forced on the organization or mandated by top management in the wake of major technological innovations, by a scarcity or abundance of critical resources, or by sudden changes in the regulatory, legal, competitive, or political landscape. Under such circumstances, change may happen quickly and often involves significant pain. Evolutionary change, by contrast, is gentle, incremental, decentralized, and over time produces a broad and lasting shift with less upheaval.

Tempered Radicals as Everyday Leaders

IN THE COURSE OF THEIR DAILY actions and interactions, tempered radicals teach important lessons and inspire change. In so doing, they exercise a form of leadership within organizations that is less visible than traditional forms—but just as important.

The trick for organizations is to locate and nurture this subtle form of leadership. Consider how Barry Coswell, a conservative, yet open-minded lawyer who headed up the securities division of a large, distinguished financial services firm, identified, protected, and promoted a tempered radical within his organization. Dana, a left-of-center, first-year attorney, came to his office on her first day of work after having been fingerprinted—a standard practice in the securities industry. The procedure had made Dana nervous: What would happen when her new employer discovered that she had done jail time for participating in a 1960s-era civil rights protest? Dana quickly understood that her only hope of survival was to be honest about her

background and principles. Despite the difference in their political proclivities, she decided to give Barry the benefit of the doubt. She marched into his office and confessed to having gone to jail for sitting in front of a bus.

“I appreciate your honesty,” Barry laughed, “but unless you’ve broken a securities law, you’re probably okay.” In return for her small confidence, Barry shared stories of his own about growing up in a poor county and about his life in the military. The story swapping allowed them to put aside ideological disagreements and to develop a deep respect for each other. Barry sensed a budding leader in Dana. Here was a woman who operated on the strength of her convictions and was honest about it but was capable of discussing her beliefs without self-righteousness. She didn’t pound tables. She was a good conversationalist. She listened attentively. And she was able to elicit surprising confessions from him.

Barry began to accord Dana a level of protection, and he encouraged her to speak her mind, take risks, and most important, challenge his assumptions. In one instance, Dana spoke up to defend a female junior lawyer who was being evaluated harshly and, Dana believed, inequitably. Dana observed that different standards were being applied to male and female lawyers, but her colleagues dismissed her “liberal” concerns. Barry cast a glance at Dana, then said to the staff, “Let’s look at this and see if we are being too quick to judge.” After the meeting, Barry and Dana held a conversation about double standards and the pervasiveness of bias. In time, Barry initiated a policy to seek out minority legal counsel, both in-house and at outside legal firms. And Dana became a senior vice president.

In Barry’s ability to recognize, mentor, and promote Dana there is a key lesson for executives who are anxious to foster leadership in their organizations. It suggests that leadership development may not rest with expensive external programs or even with the best intentions of the human resources department. Rather it may rest with the open-minded recognition that those who appear to rock the boat may turn out to be the most effective of captains.

The power of evolutionary approaches to promote cultural change is the subject of frequent discussion. For instance, in “We Don’t Need Another Hero” (HBR, September 2001), Joseph L. Badaracco, Jr., asserts that the most effective moral leaders often operate beneath the radar, achieving their reforms without widespread notice. Likewise, tempered radicals gently and continually push against prevailing norms, making a difference in small but steady ways and setting examples from which others can learn. The changes they inspire are so incremental that they barely merit notice—which is exactly why they work so well. Like drops of water, these approaches are innocuous enough in themselves. But over time and in accumulation, they can erode granite.

Consider, for example, how a single individual slowly—but radically—altered the face of his organization. Peter Grant¹ was a black senior executive who held some 18 positions as he moved up the ladder at a large West Coast bank. When he first joined the company as a manager, he was one of only a handful of people of color on the professional staff. Peter had a private, long-term goal: to bring more women and racial minorities into the fold and help them succeed. Throughout his 30-year career running the company’s local banks, regional offices, and corporate operations, one of his chief responsibilities was to hire new talent. Each time he had the opportunity, Peter attempted to hire a highly qualified member of a minority. But he did more than that—every time he hired someone, he asked that person to do the same. He explained to the new recruits the importance of hiring women and people of color and why it was their obligation to do likewise.

Whenever minority employees felt frustrated by bias, Peter would act as a supportive mentor. If they threatened to quit, he would talk them out of it. “I know how you feel, but think about the bigger picture here,” he’d say. “If you leave, nothing here will change.” His example inspired viral behavior in others. Many stayed and hired other minorities; those who didn’t carried a commitment to hire minorities into their new companies. By the time Peter retired, more than 3,500 talented minority and female employees had joined the bank.

Peter was the most tempered, yet the most effective, of radicals. For many years, he endured racial slurs and demeaning remarks from colleagues. He waited longer than his peers for promotions; each time he did move up he was told the job was too big for him and he was lucky to have gotten it. “I worked my rear end off to make them comfortable with me,” he said, late in

his career. “It wasn’t *luck*.” He was often angry, but lashing out would have been the path of least emotional resistance. So without attacking the system, advancing a bold vision, or wielding great power, Peter chipped away at the organization’s demographic base using the full menu of change strategies described below.

Disruptive Self-Expression

At the most tempered end of the change continuum is the kind of self-expression that quietly disrupts others' expectations. Whether waged as a deliberate act of protest or merely as a personal demonstration of one's values, disruptive self-expression in language, dress, office decor, or behavior can slowly change the atmosphere at work. Once people take notice of the expression, they begin to talk about it. Eventually, they may feel brave enough to try the same thing themselves. The more people who talk about the transgressive act or repeat it, the greater the cultural impact.

Consider the case of John Ziwak, a manager in the business development group of a high-growth computer components company. As a hardworking business school graduate who'd landed a plum job, John had every intention of working 80-hour weeks on the fast track to the top. Within a few years, he married a woman who also held a demanding job; soon, he became the father of two. John found his life torn between the competing responsibilities of home and work. To balance the two, John shifted his work hours—coming into the office earlier in the morning so that he could leave by 6 pm. He rarely scheduled late-afternoon meetings and generally refused to take calls at home in the evening between 6:30 and 9. As a result, his family life improved, and he felt much less stress, which in turn improved his performance at work.

At first, John's schedule raised eyebrows; availability was, after all, an unspoken key indicator of commitment to the company. "If John is unwilling to stay past 6," his boss wondered, "is he really committed to his job? Why should I promote him when others are willing and able to work all the time?" But John always met his performance expectations, and his boss didn't want to lose him. Over time, John's colleagues adjusted to his schedule. No one set up conference calls or meetings involving him after 5. One by one, other employees began adopting John's "6 o' clock rule"; calls at home, particularly during dinner hour, took place only when absolutely necessary. Although the 6 o' clock rule was never formalized, it nonetheless became par

for the course in John's department. Some of John's colleagues continued to work late, but they all appreciated these changes in work practice and easily accommodated them. Most people in the department felt more, not less, productive during the day as they adapted their work habits to get things done more efficiently—for example, running meetings on schedule and monitoring interruptions in their day. According to John's boss, the employees appreciated the newfound balance in their lives, and productivity in the department did not suffer in the least.

Tempered radicals know that even the smallest forms of disruptive self-expression can be exquisitely powerful. The story of Dr. Frances Conley offers a case in point. By 1987, Dr. Conley had already established herself as a leading researcher and neurosurgeon at Stanford Medical School and the Palo Alto Veteran's Administration hospital. But as one of very few women in the profession, she struggled daily to maintain her feminine identity in a macho profession and her integrity amid gender discrimination. She had to keep her cool when, for example, in the middle of directing a team of residents through complicated brain surgery, a male colleague would stride into the operating room to say, "Move over, honey." "Not only did that undermine my authority and expertise with the team," Dr. Conley recalled later, "but it was unwarranted—and even dangerous. That kind of thing would happen all the time."

Despite the frustration and anger she felt, Dr. Conley at that time had no intention of making a huge issue of her gender. She didn't want the fact that she was a woman to compromise her position, or vice versa. So she expressed herself in all sorts of subtle ways, including in what she wore. Along with her green surgical scrubs, she donned white lace ankle socks—an unequivocal expression of her femininity. In itself, wearing lace ankle socks could hardly be considered a Gandhian act of civil disobedience. The socks merely said, "I can be a neurosurgeon and be feminine." But they spoke loudly enough in the stolid masculinity of the surgical environment, and, along with other small actions on her part, they sparked conversation in the hospital. Nurses and female residents frequently commented on Dr. Conley's style. "She is as demanding as any man and is not afraid to take them on," they would say, in admiration. "But she is also a woman and not ashamed of it."

Ellen Thomas made a comparable statement with her hair. As a young African-American consultant in a technical services business, she navigated constantly between organizational pressures to fit in and her personal desire

to challenge norms that made it difficult for her to be herself. So from the beginning of her employment, Ellen expressed herself by wearing her hair in neat cornrow braids. For Ellen, the way she wore her hair was not just about style; it was a symbol of her racial identity.

Once, before making an important client presentation, a senior colleague advised Ellen to unbraid her hair “to appear more professional.” Ellen was miffed, but she didn’t respond. Instead, she simply did not comply. Once the presentation was over and the client had been signed, she pulled her colleague aside. “I want you to know why I wear my hair this way,” she said calmly. “I’m a black woman, and I happen to like the style. And as you just saw,” she smiled, “my hairstyle has nothing to do with my ability to do my job.”

Does leaving work at 6 PM or wearing lacy socks or cornrows force immediate change in the culture? Of course not; such acts are too modest. But disruptive self-expression does do two important things. First, it reinforces the tempered radical’s sense of the importance of his or her convictions. These acts are self-affirming. Second, it pushes the status quo door slightly ajar by introducing an alternative *modus operandi*. Whether they are subtle, unspoken, and recognizable by only a few or vocal, visible, and noteworthy to many, such acts, in aggregation, can provoke real reform.

Verbal Jujitsu

Like most martial arts, jujitsu involves taking a force coming at you and redirecting it to change the situation. Employees who practice verbal jujitsu react to undesirable, demeaning statements or actions by turning them into opportunities for change that others will notice.

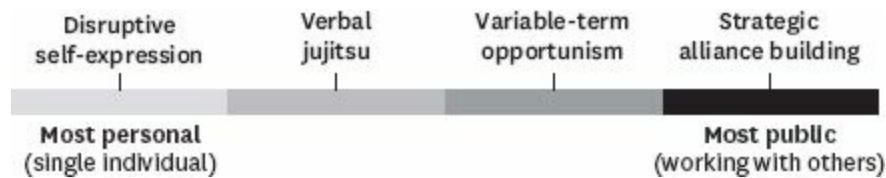
One form of verbal jujitsu involves calling attention to the opposition's own rhetoric. I recall a story told by a man named Tom Novak, an openly gay executive who worked in the San Francisco offices of a large financial services institution. As Tom and his colleagues began seating themselves around a table for a meeting in a senior executive's large office, the conversation briefly turned to the topic of the upcoming Gay Freedom Day parade and to so-called gay lifestyles in general. Joe, a colleague, said loudly, "I can appreciate that some people choose a gay lifestyle. I just don't understand why they have to flaunt it in people's faces."

A Spectrum of Tempered Change Strategies

THE TEMPERED RADICAL'S SPECTRUM of strategies is anchored on the left by *disruptive self-expression*: subtle acts of private, individual style. A slightly more public form of expression, *verbal jujitsu*, turns the opposition's negative expression or behavior into opportunities for change. Further along the spectrum, the tempered radical uses *variable-term opportunism* to recognize and act on short- and long-term chances to motivate others. And through *strategic alliance building*, the individual works directly with others to bring about more extensive change. The more conversations an individual's action inspires and the more people it engages, the stronger the impetus toward change becomes.

In reality, people don't apply the strategies in the spectrum sequentially or

even necessarily separately. Rather, these tools blur and overlap. Tempered radicals remain flexible in their approach, “heating up” or “cooling off” each as conditions warrant.



Stung, Tom was tempted to keep his mouth shut and absorb the injury, but that would have left him resentful and angry. He could have openly condemned Joe’s bias, but that would have made him look defensive and self-righteous. Instead, he countered Joe with an altered version of Joe’s own argument, saying calmly, “I know what you mean, Joe. I’m just wondering about that big picture of your wife on your desk. There’s nothing wrong with being straight, but it seems that you are the one announcing your sexuality.” Suddenly embarrassed, Joe responded with a simple, “Touché.”

Managers can use verbal jujitsu to prevent talented employees, and their valuable contributions, from becoming inadvertently marginalized. That’s what happened in the following story. Brad Williams was a sales manager at a high-technology company. During a meeting one day, Brad noticed that Sue, the new marketing director, had tried to interject a few comments, but everything she said was routinely ignored. Brad waited for the right moment to correct the situation. Later on in the meeting, Sue’s colleague George raised similar concerns about distributing the new business’s products outside the country. The intelligent remark stopped all conversation. During the pause, Brad jumped in: “That’s an important idea,” he said. “I’m glad George picked up on Sue’s concerns. Sue, did George correctly capture what you were thinking?”

With this simple move, Brad accomplished a number of things. First, by indirectly showing how Sue had been silenced and her idea co-opted, he voiced an unspoken fact. Second, by raising Sue’s visibility, he changed the power dynamic in the room. Third, his action taught his colleagues a lesson

about the way they listened—and didn't. Sue said that after that incident she was no longer passed over in staff meetings.

In practicing verbal jujitsu, both Tom and Brad displayed considerable self-control and emotional intelligence. They listened to and studied the situation at hand, carefully calibrating their responses to disarm without harming. In addition, they identified the underlying issues (sexual bias, the silencing of newcomers) without sounding accusatory and relieved unconscious tensions by voicing them. In so doing, they initiated small but meaningful changes in their colleagues' assumptions and behavior.

Variable-Term Opportunism

Like jazz musicians, who build completely new musical experiences from old standards as they go along, tempered radicals must be creatively open to opportunity. In the short-term, that means being prepared to capitalize on serendipitous circumstances; in the long-term, it often means something more proactive. The first story that follows illustrates the former case; the second is an example of the latter.

Tempered radicals like Chris Morgan know that rich opportunities for reform can often appear suddenly, like a \$20 bill found on a sidewalk. An investment manager in the audit department of a New York conglomerate, Chris made a habit of doing whatever he could to reduce waste. To save paper, for example, he would single-space his documents and put them in a smaller font before pressing the “Print” button, and he would use both sides of the paper. One day, Chris noticed that the company cafeteria packaged its sandwiches in Styrofoam boxes that people opened and immediately tossed. He pulled the cafeteria manager aside. “Mary,” he said with a big smile, “those turkey-on-focaccia sandwiches look delicious today! I was wondering, though...would it be possible to wrap sandwiches only when people asked you to?” By making this very small change, Chris pointed out, the cafeteria would save substantially on packaging costs.

Chris gently rocked the boat by taking the following steps. First, he picked low-hanging fruit, focusing on something that could be done easily and without causing a lot of stir. Next, he attacked the problem not by criticizing Mary’s judgment but by enrolling her in his agenda (praising her tempting sandwiches, then making a gentle suggestion). Third, he illuminated the advantages of the proposed change by pointing out the benefits to the cafeteria. And he started a conversation that, through Mary, spread to the rest of the cafeteria staff. Finally, he inspired others to action: Eventually, the cafeteria staff identified and eliminated 12 other wasteful practices.

Add up enough conversations and inspire enough people and, sooner or later, you get real change. A senior executive named Jane Adams offers a

case in point. Jane was hired in 1995 to run a 100-person, mostly male software-development division in an extremely fast-growing, pre-IPO technology company. The CEO of the company was an autocrat who expected his employees to emulate his dog-eat-dog management style. Although Jane was new to the job and wanted very much to fit in and succeed, turf wars and command-and-control tactics were anathema to her. Her style was more collaborative; she believed in sharing power. Jane knew that she could not attack the company's culture by arguing with the CEO; rather, she took charge of her own division and ran it her own way. To that end, she took every opportunity to share power with subordinates. She instructed each of her direct reports to delegate responsibility as much as possible. Each time she heard about someone taking initiative in making a decision, she would praise that person openly before his or her manager. She encouraged people to take calculated risks and to challenge her.

When asked to give high-visibility presentations to the company's executive staff, she passed the opportunities to those who had worked directly on the project. At first, senior executives raised their eyebrows, but Jane assured them that the presenter would deliver. Thus, her subordinates gained experience and won credit that, had they worked for someone else, they would likely never have received.

Occasionally, people would tell Jane that they noticed a refreshing contrast between her approach and the company's prevailing one. "Thanks, I'm glad you noticed," she would say with a quiet smile. Within a year, she saw that several of her own direct reports began themselves to lead in a more collaborative manner. Soon, employees from other divisions, hearing that Jane's was one of the best to work for, began requesting transfers. More important, Jane's group became known as one of the best training grounds and Jane as one of the best teachers and mentors of new talent. Nowhere else did people get the experience, responsibility, and confidence that she cultivated in her employees.

For Chris Morgan, opportunity was short-term and serendipitous. For Jane Adams, opportunity was more long-term, something to be mined methodically. In both cases, though, remaining alert to such variable-term opportunities and being ready to capitalize on them were essential.

Strategic Alliance Building

So far, we have seen how tempered radicals, more or less working alone, can effect change. What happens when these individuals work with allies? Clearly, they gain a sense of legitimacy, access to resources and contacts, technical and task assistance, emotional support, and advice. But they gain much more—the power to move issues to the forefront more quickly and directly than they might by working alone.

When one enlists the help of like-minded, similarly tempered coworkers, the strategic alliance gains clout. That's what happened when a group of senior women at a large professional services firm worked with a group of men sympathetic to their cause. The firm's executive management asked the four-woman group to find out why it was so hard for the company to keep female consultants on staff. In the course of their investigation, the women discussed the demanding culture of the firm: a 70-hour work week was the norm, and most consultants spent most of their time on the road, visiting clients. The only people who escaped this demanding schedule were part-time consultants, nearly all of whom happened to be women with families. These part-timers were evaluated according to the same performance criteria—including the expectation of long hours—as full-time workers. Though many of the part-timers were talented contributors, they consistently failed to meet the time criterion and so left the company. To correct the problem, the senior women first gained the ear of several executive men who, they knew, regretted missing time with their own families. The men agreed that this was a problem and that the company could not continue to bleed valuable talent. They signed on to help address the issue and, in a matter of months, the evaluation system was adjusted to make success possible for all workers, regardless of their hours.

Tempered radicals don't allow preconceived notions about "the opposition" to get in their way. Indeed, they understand that those who represent the majority perspective are vitally important to gaining support for their cause. Paul Wielgus quietly started a revolution at his company by

effectively persuading the opposition to join him. In 1991, Allied Domecq, the global spirits company whose brands include Courvoisier and Beefeater, hired Paul as a marketing director in its brewing and wholesaling division. Originally founded in 1961 as the result of a merger of three British brewing and pub-owning companies, the company had inherited a bureaucratic culture. Tony Hales, the CEO, recognized the need for dramatic change inside the organization and appreciated Paul's talent and fresh perspective. He therefore allowed Paul to quit his marketing job, report directly to the CEO, and found a nine-person learning and training department that ran programs to help participants shake off stodgy thinking and boost their creativity. Yet despite the department's blessing from on high and a two-year record of success, some managers thought of it as fluff. In fact, when David, a senior executive from the internal audit department, was asked to review cases of unnecessary expense, he called Paul on the carpet.

Paul's strategy was to treat David not as a threat but as an equal, even a friend. Instead of being defensive during the meeting, Paul used the opportunity to sell his program. He explained that the trainers worked first with individuals to help unearth their personal values, then worked with them in teams to develop new sets of group values that they all believed in. Next, the trainers aligned these personal and departmental values with those of the company as a whole. "You wouldn't believe the changes, David," he said, enthusiastically. "People come out of these workshops feeling so much more excited about their work. They find more meaning and purpose in it, and as a consequence are happier and much more productive. They call in sick less often, they come to work earlier in the morning, and the ideas they produce are much stronger." Once David understood the value of Paul's program, the two began to talk about holding the training program in the internal audit department itself.

Paul's refusal to be frightened by the system, his belief in the importance of his work, his search for creative and collaborative solutions, his lack of defensiveness with an adversary, and his ability to connect with the auditor paved the way for further change at Allied Domecq. Eventually, the working relationship the two men had formed allowed the internal audit department to transform its image as a policing unit into something more positive. The new Audit Services department came to be known as a partner, rather than an enforcer, in the organization as a whole. And as head of the newly renamed department, David became a strong supporter of Paul's work.

Tempered radicals understand that people who represent the majority perspective can be important allies in more subtle ways as well. In navigating the course between their desire to undo the status quo and the organizational requirements to uphold it, tempered radicals benefit from the advice of insiders who know just how hard to push. When a feminist who wants to change the way her company treats women befriends a conservative Republican man, she knows he can warn her of political minefields. When a Latino manager wants his company to put a Spanish-language version of a manual up on the company's intranet, he knows that the white, monolingual executive who runs operations may turn out to be an excellent advocate.

Of course, tempered radicals know that not everyone is an ally, but they also know it's pointless to see those who represent the status quo as enemies. The senior women found fault with an inequitable evaluation system, not with their male colleagues. Paul won David's help by giving him the benefit of the doubt from the very beginning of their relationship. Indeed, tempered radicals constantly consider all possible courses of action: "Under what conditions, for what issues, and in what circumstances does it make sense to join forces with others?"; "How can I best use this alliance to support my efforts?"

Clearly, there is no one right way to effect change. What works for one individual under one set of circumstances may not work for others under different conditions. The examples above illustrate how tempered radicals use a spectrum of quiet approaches to change their organizations. Some actions are small, private, and muted; some are larger and more public. Their influence spreads as they recruit others and spawn conversations. Top managers can learn a lot from these people about the mechanics of evolutionary change.

Tempered radicals bear no banners; they sound no trumpets. Their ends are sweeping, but their means are mundane. They are firm in their commitments, yet flexible in the ways they fulfill them. Their actions may be small but can spread like a virus. They yearn for rapid change but trust in patience. They often work individually yet pull people together. Instead of

stridently pressing their agendas, they start conversations. Rather than battling powerful foes, they seek powerful friends. And in the face of setbacks, they keep going. To do all this, tempered radicals understand revolutionary change for what it is—a phenomenon that can occur suddenly but more often than not requires time, commitment, and the patience to endure.

Originally published in October 2001. Reprint 7923

Notes

[1.](#) With the exception of those in the VA hospital and Allied Domecq cases, all the names used through this article are fictitious.

Tippling Point Leadership

by W. Chan Kim and Renée Mauborgne

IN FEBRUARY 1994, William Bratton was appointed police commissioner of New York City. The odds were against him. The New York Police Department, with a \$2 billion budget and a workforce of 35,000 police officers, was notoriously difficult to manage. Turf wars over jurisdiction and funding were rife. Officers were underpaid relative to their counterparts in neighboring communities, and promotion seemed to bear little relationship to performance. Crime had gotten so far out of control that the press referred to the Big Apple as the Rotten Apple. Indeed, many social scientists had concluded, after three decades of increases, that New York City crime was impervious to police intervention. The best the police could do was react to crimes once they were committed.

Yet in less than two years, and without an increase in his budget, Bill Bratton turned New York into the safest large city in the nation. Between 1994 and 1996, felony crime fell 39%; murders, 50%; and theft, 35%. Gallup polls reported that public confidence in the NYPD jumped from 37% to 73%, even as internal surveys showed job satisfaction in the police department reaching an all-time high. Not surprisingly, Bratton's popularity soared, and in 1996, he was featured on the cover of *Time*. Perhaps most impressive, the changes have outlasted their instigator, implying a fundamental shift in the department's organizational culture and strategy. Crime rates have continued to fall: Statistics released in December 2002 revealed that New York's overall crime rate is the lowest among the 25 largest cities in the United States.

The NYPD turnaround would be impressive enough for any police chief. For Bratton, though, it is only the latest of no fewer than five successful

turnarounds in a 20-year career in policing. In the hope that Bratton can repeat his New York and Boston successes, Los Angeles has recruited him to take on the challenge of turning around the LAPD. (For a summary of his achievements, see the table “Bratton in action.”)

So what makes Bill Bratton tick? As management researchers, we have long been fascinated by what triggers high performance or suddenly brings an ailing organization back to life. In an effort to find the common elements underlying such leaps in performance, we have built a database of more than 125 business and nonbusiness organizations. Bratton first caught our attention in the early 1990s, when we heard about his turnaround of the New York Transit Police. Bratton was special for us because in all of his turnarounds, he succeeded in record time despite facing all four of the hurdles that managers consistently claim block high performance: an organization wedded to the status quo, limited resources, a demotivated staff, and opposition from powerful vested interests. If Bratton could succeed against these odds, other leaders, we reasoned, could learn a lot from him.

Over the years, through our professional and personal networks and the rich public information available on the police sector, we have systematically compared the strategic, managerial, and performance records of Bratton’s turnarounds. We have followed up by interviewing the key players, including Bratton himself, as well as many other people who for professional—or sometimes personal—reasons tracked the events.

Our research led us to conclude that all of Bratton’s turnarounds are textbook examples of what we call tipping point leadership. The theory of tipping points, which has its roots in epidemiology, is well known; it hinges on the insight that in any organization, once the beliefs and energies of a critical mass of people are engaged, conversion to a new idea will spread like an epidemic, bringing about fundamental change very quickly. The theory suggests that such a movement can be unleashed only by agents who make unforgettable and unarguable calls for change, who concentrate their resources on what really matters, who mobilize the commitment of the organization’s key players, and who succeed in silencing the most vocal naysayers. Bratton did all of these things in all of his turnarounds.

How can you overcome the hurdles facing any organization struggling to change: addiction to the status quo, limited resources, demotivated employees, and opposition from powerful vested interests?

Take lessons from police chief Bill Bratton, who's pulled the trick off five times. Most dramatically, he transformed the U.S.'s most dangerous city—New York—into its safest. Bratton used **tipping point leadership** to make unarguable calls for change, concentrate resources on what really mattered, mobilize key players' commitment, and silence naysayers.

Not every executive has Bratton's personality, but most have his potential—if they follow his success formula.

Most managers only dream of pulling off the kind of performance leaps Bratton delivered. Even Jack Welch needed some ten years and tens of millions of dollars of restructuring and training to turn GE into the powerhouse it is today. Few CEOs have the time and money that Welch had, and most—even those attempting relatively mild change—are soon daunted by the scale of the hurdles they face. Yet we have found that the dream can indeed become a reality. For what makes Bratton's turnarounds especially exciting to us is that his approach to overcoming the hurdles standing in the way of high performance has been remarkably consistent. His successes, therefore, are not just a matter of personality but also of method, which suggests that they can be replicated. Tipping point leadership is learnable.

In the following pages, we'll lay out the approach that has enabled Bratton to overcome the forces of inertia and reach the tipping point. We'll show first how Bratton overcame the cognitive hurdles that block companies from recognizing the need for radical change. Then we'll describe how he successfully managed around the public sector's endemic constraints on resources, which he even turned to his advantage. In the third section, we'll explain how Bratton overcame the motivational hurdles that had discouraged and demoralized even the most eager police officers. Finally, we'll describe how Bratton neatly closed off potentially fatal resistance from vocal and

powerful opponents. (For a graphic summary of the ideas expressed in this article, see the figure “Tipping point leadership at a glance.”)

Idea in Practice

Four Steps to the Tipping Point

1. Break through the cognitive hurdle.

To make a compelling case for change, don’t just point at the numbers and demand better ones. Your abstract message won’t stick. Instead, make key managers *experience* your organization’s problems.

Example: New Yorkers once viewed subways as the most dangerous places in their city. But the New York Transit Police’s senior staff pooh-poohed public fears—because none had ever ridden subways. To shatter their complacency, Bratton required all NYTP officers— himself included—to commute by subway. Seeing the jammed turnstiles, youth gangs, and derelicts, they grasped the need for change—and embraced responsibility for it.

2. Sidestep the resource hurdle.

Rather than trimming your ambitions (dooming your company to mediocrity) or fighting for more resources (draining attention from the underlying problems), concentrate *current* resources on areas *most* needing change.

Example: Since the majority of subway crimes occurred at only a few stations, Bratton focused manpower there—instead of putting a cop on every subway line, entrance, and exit.

3. Jump the motivational hurdle.

To turn a mere strategy into a movement, people must recognize what needs to be done and yearn to do it themselves. But don't try reforming your whole organization; that's cumbersome and expensive. Instead, motivate *key influencers*—persuasive people with multiple connections. Like bowling kingpins hit straight on, they topple all the other pins. Most organizations have several key influencers who share common problems and concerns—making it easy to identify and motivate them.

Example: Bratton put the NYPD's key influencers—precinct commanders—under a spotlight during semiweekly crime strategy review meetings, where peers and superiors grilled commanders about precinct performance. Results? A culture of performance, accountability, and learning that commanders replicated down the ranks.

Also make challenges attainable. Bratton exhorted staff to make NYC's streets safe “block by block, precinct by precinct, and borough by borough.”

4. Knock over the political hurdle.

Even when organizations reach their tipping points, powerful vested interests resist change. Identify and silence key naysayers early by putting a respected senior insider on your top team.

Example: At the NYPD, Bratton appointed 20-year veteran cop John Timoney as his number two. Timoney knew the key players and how they played the political game. Early on, he identified likely saboteurs and resisters among top staff—prompting a changing of the guard.

Also, silence opposition with indisputable facts. When Bratton proved his proposed crime-reporting system required less than 18 minutes a day, time-crunched precinct commanders adopted it.

Break Through the Cognitive Hurdle

In many turnarounds, the hardest battle is simply getting people to agree on the causes of current problems and the need for change. Most CEOs try to make the case for change simply by pointing to the numbers and insisting that the company achieve better ones. But messages communicated through numbers seldom stick. To the line managers—the very people the CEO needs to win over—the case for change seems abstract and remote. Those whose units are doing well feel that the criticism is not directed at them, that the problem is top management's. Managers of poorly performing units feel that they have been put on notice—and people worried about job security are more likely to be scanning the job market than trying to solve the company's problems.

For all these reasons, tipping point leaders like Bratton do not rely on numbers to break through the organization's cognitive hurdles. Instead, they put their key managers face-to-face with the operational problems so that the managers cannot evade reality. Poor performance becomes something they witness rather than hear about. Communicating in this way means that the message—performance is poor and needs to be fixed—sticks with people, which is essential if they are to be convinced not only that a turnaround is necessary but that it is something they can achieve.

Bratton in action

The New York Police Department was not Bill Bratton's first turnaround. The table describes his biggest challenges and achievements during his 20 years as a policy reformer.

Domain	Boston Police District 4	Massachusetts Bay Transit Authority (MBTA)	Boston Metropolitan Police ("The Mets")	New York Transit Police (NYTP)	New York Police Department (NYPD)
Years	1977-1982	1983-1986	1986-1990	1990-1992	1994-1996
Position	Sergeant, lieutenant	Superintendent	Superintendent	Chief of police	Commissioner
Setting	Assaults, drug dealing, prostitution, public drinking, and graffiti were endemic to the area. The Boston public shied away from attending baseball games and other events and from shopping in the Fenway neighborhood for fear of being robbed or attacked or having their cars stolen.	Subway crime had been on the rise for the past five years. The media dubbed the Boston subway the Terror Train. The <i>Boston Globe</i> published a series on police incompetence in the MBTA.	The Mets lacked modern equipment, procedures, and discipline. Physical facilities were crumbling. Accountability, discipline, and morale were low in the 600-person Mets workforce.	Crime had risen 25% per year in the past three years—twice the overall rate for the city. Subway use by the public had declined sharply; polls indicated that New Yorkers considered the subway the most dangerous place in the city. There were 170,000 fare evaders per day, costing the city \$80 million annually. Aggressive panhandling and vandalism were endemic. More than 5,000 people were living in the subway system.	The middle class was fleeing to the suburbs in search of a better quality of life. There was public despair in the face of the high crime rate. Crime was seen as part of a breakdown of social norms. The budget for policing was shrinking. The NYPD budget (aside from personnel) was being cut by 35%. The staff was demoralized and relatively underpaid.

Results	Crime throughout the Fenway area was dramatically reduced. Tourists, residents, and investment returned as an entire area of the city rebounded.	Crime on the MBTA decreased by 27%; arrests rose to 1,600 per year from 600. The MBTA police met more than 800 standards of excellence to be accredited by the National Commission on Accreditation for Police Agencies. It was only the 13th police department in the country to meet this standard. Equipment acquired during his tenure: 55 new mid-size cars, new uniforms, and new logos. Ridership began to grow.	Employee morale rose as Bratton instilled accountability, protocol, and pride. In three years, the Metropolitan Police changed from a dispirited, doing nothing, reactive organization with a poor self-image and an even worse public image to a very proud, proactive department. Equipment acquired during his tenure: 100 new vehicles, a helicopter, and a state-of-the-art radio system.	In two years, Bratton reduced felony crime by 22%, with robberies down by 40%. Increased confidence in the subway led to increased ridership. Fare evasion was cut in half. Equipment acquired during his tenure: a state-of-the-art communication system, advanced handguns for officers, and new patrol cars (the number of cars doubled).	Overall crime fell by 17%. Felony crime fell by 39%. Murders fell by 50%. Theft fell by 35% (robberies were down by one-third, burglaries by one-quarter). There were 200,000 fewer victims a year than in 1990. By the end of Bratton's tenure, the NYPD had a 73% positive rating, up from 37% four years earlier.

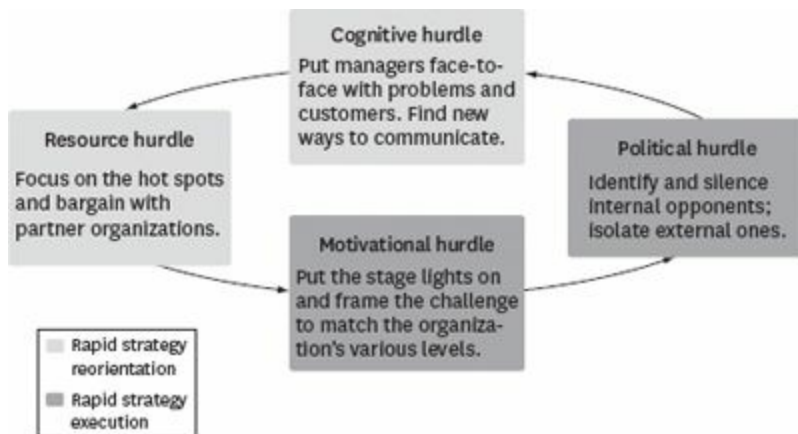
When Bratton first went to New York to head the transit police in April 1990, he discovered that none of the senior staff officers rode the subway. They commuted to work and traveled around in cars provided by the city. Comfortably removed from the facts of underground life—and reassured by statistics showing that only 3% of the city's major crimes were committed in the subway—the senior managers had little sensitivity to riders' widespread concern about safety. In order to shatter the staff's complacency, Bratton began requiring that all transit police officials—beginning with himself—ride the subway to work, to meetings, and at night. It was many staff officers' first occasion in years to share the ordinary citizen's subway experience and see the situation their subordinates were up against: jammed turnstiles, aggressive beggars, gangs of youths jumping turnstiles and jostling people on the platforms, winos and homeless people sprawled on benches. It was clear that even if few major crimes took place in the subway, the whole place

reeked of fear and disorder. With that ugly reality staring them in the face, the transit force's senior managers could no longer deny the need for a change in their policing methods.

Bratton uses a similar approach to help sensitize his superiors to his problems. For instance, when he was running the police division of the Massachusetts Bay Transit Authority (MBTA), which runs the Boston-area subway and buses, the transit authority's board decided to purchase small squad cars that would be cheaper to buy and run. Instead of fighting the decision, Bratton invited the MBTA's general manager for a tour of the district. He picked him up in a small car just like the ones that were to be ordered. He jammed the seats forward to let the general manager feel how little legroom a six-foot cop would have, then drove him over every pothole he could find. Bratton also put on his belt, cuffs, and gun for the trip so the general manager could see how little space there was for the tools of the officer's trade. After just two hours, the general manager wanted out. He said he didn't know how Bratton could stand being in such a cramped car for so long on his own—let alone if there were a criminal in the backseat. Bratton got the larger cars he wanted.

Tipping point leadership at a glance

Leaders like Bill Bratton use a four-step process to bring about rapid, dramatic, and lasting change with limited resources. The cognitive and resource hurdles shown here represent the obstacles that organizations face in reorienting and formulating strategy. The motivational and political hurdles prevent a strategy's rapid execution. Tipping all four hurdles leads to rapid strategy reorientation and execution. Overcoming these hurdles is, of course, a continuous process because the innovation of today soon becomes the conventional norm of tomorrow.



Bratton reinforces direct experiences by insisting that his officers meet the communities they are protecting. The feedback is often revealing. In the late 1970s, Boston's Police District 4, which included Symphony Hall, the Christian Science Mother Church, and other cultural institutions, was experiencing a surge in crime. The public was increasingly intimidated; residents were selling and leaving, pushing the community into a downward spiral. The Boston police performance statistics, however, did not reflect this reality. District 4 police, it seemed, were doing a splendid job of rapidly clearing 911 calls and tracking down perpetrators of serious crimes. To solve this paradox, Bratton had the unit organize community meetings in schoolrooms and civic centers so that citizens could voice their concerns to district sergeants and detectives. Obvious as the logic of this practice sounds, it was the first time in Boston's police history that anyone had attempted such an initiative—mainly because the practice up to that time had argued for detachment between police and the community in order to decrease the chances of police corruption.

The limitations of that practice quickly emerged. The meetings began with a show-and-tell by the officers: This is what we are working on and why. But afterward, when citizens were invited to discuss the issues that concerned them, a huge perception gap came to light. While the police officers took pride in solving serious offenses like grand larceny and murder, few citizens felt in any danger from these crimes. They were more troubled by constant minor irritants: prostitutes, panhandlers, broken-down cars left on the streets,

drunks in the gutters, filth on the sidewalks. The town meetings quickly led to a complete overhaul of the police priorities for District 4. Bratton has used community meetings like this in every turnaround since.

Bratton's internal communications strategy also plays an important role in breaking through the cognitive hurdles. Traditionally, internal police communication is largely based on memos, staff bulletins, and other documents. Bratton knows that few police officers have the time or inclination to do more than throw these documents into the wastebasket. Officers rely instead on rumor and media stories for insights into what headquarters is up to. So Bratton typically calls on the help of expert communication outsiders. In New York, for instance, he recruited John Miller, an investigative television reporter known for his gutsy and innovative style, as his communication czar. Miller arranged for Bratton to communicate through video messages that were played at roll calls, which had the effect of bringing Bratton—and his opinions—closer to the people he had to win over. At the same time, Miller's journalistic savvy made it easier for the NYPD to ensure that press interviews and stories echoed the strong internal messages Bratton was sending.

Sidestep the Resource Hurdle

Once people in an organization accept the need for change and more or less agree on what needs to be done, leaders are often faced with the stark reality of limited resources. Do they have the money for the necessary changes? Most reformist CEOs do one of two things at this point. They trim their ambitions, dooming the company to mediocrity at best and demoralizing the workforce all over again, or they fight for more resources from their bankers and shareholders, a process that can take time and divert attention from the underlying problems.

That trap is completely avoidable. Leaders like Bratton know how to reach the organization's tipping point without extra resources. They can achieve a great deal with the resources they have. What they do is concentrate their resources on the places that are most in need of change and that have the biggest possible payoffs. This idea, in fact, is at the heart of Bratton's famous (and once hotly debated) philosophy of zero-tolerance policing.

Having won people over to the idea of change, Bratton must persuade them to take a cold look at what precisely is wrong with their operating practices. It is at this point that he turns to the numbers, which he is adept at using to force through major changes. Take the case of the New York narcotics unit. Bratton's predecessors had treated it as secondary in importance, partly because they assumed that responding to 911 calls was the top priority. As a result, less than 5% of the NYPD's manpower was dedicated to fighting narcotics crimes.

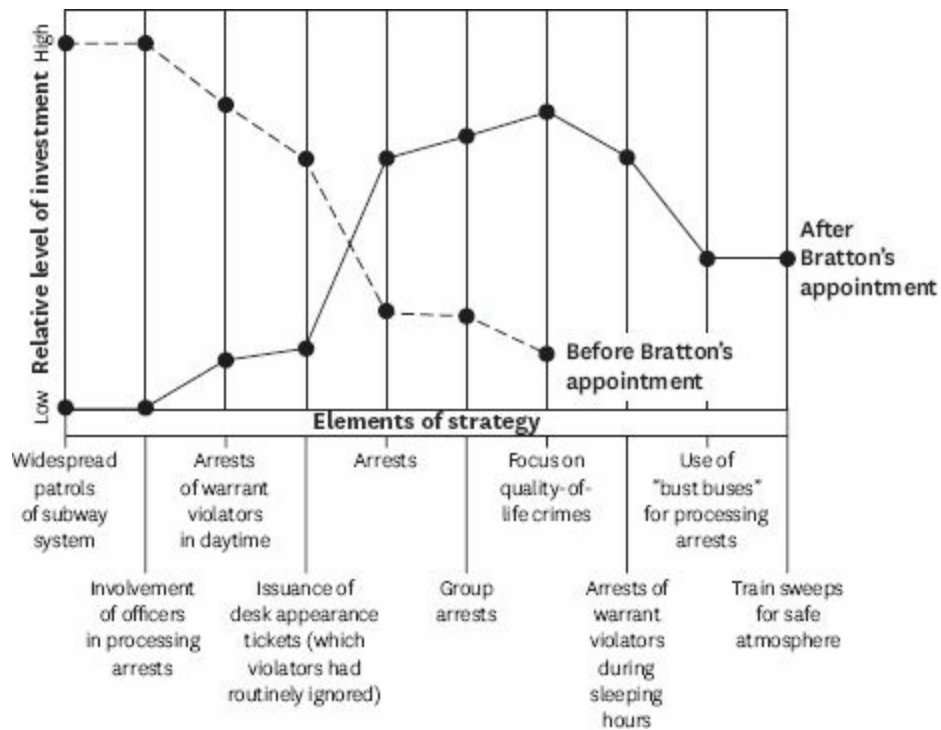
At an initial meeting with the NYPD's chiefs, Bratton's deputy commissioner of crime strategy, Jack Maple, asked people around the table for their estimates of the percentage of crimes attributable to narcotics use. Most said 50%; others, 70%; the lowest estimate was 30%. On that basis, a narcotics unit consisting of less than 5% of the police force was grossly understaffed, Maple pointed out. What's more, it turned out that the narcotics squad largely worked Monday through Friday, even though drugs were sold in large quantities—and drug-related crimes persistently occurred—on the

weekends. Why the weekday schedule? Because it had always been done that way; it was an unquestioned modus operandi. Once these facts were presented, Bratton's call for a major reallocation of staff and resources within the NYPD was quickly accepted.

The strategy canvas of transit:

How Bratton refocused resources

In comparing strategies across companies, we like to use a tool we call the strategy canvas, which highlights differences in strategies and resource allocation. The strategy canvas shown here compares the strategy and allocation of resources of the New York Transit Police before and after Bill Bratton's appointment as chief. The vertical axis shows the relative level of resource allocation. The horizontal axis shows the various elements of strategy in which the investments were made. Although a dramatic shift in resource allocation occurred and performance rose dramatically, overall investment of resources remained more or less constant. Bratton did this by de-emphasizing or virtually eliminating some traditional features of transit police work while increasing emphasis on others or creating new ones. For example, he was able to reduce the time police officers spent processing suspects by introducing mobile processing centers known as "bust buses."



A careful examination of the facts can also reveal where changes in key policies can reduce the need for resources, as Bratton demonstrated during his tenure as chief of New York's transit police. His predecessors had lobbied hard for the money to increase the number of subway cops, arguing that the only way to stop muggers was to have officers ride every subway line and patrol each of the system's 700 exits and entrances. Bratton, by contrast, believed that subway crime could be resolved not by throwing more resources at the problem but by better targeting those resources. To prove the point, he had members of his staff analyze where subway crimes were being committed. They found that the vast majority occurred at only a few stations and on a couple of lines, which suggested that a targeted strategy would work well. At the same time, he shifted more of the force out of uniform and into plain clothes at the hot spots. Criminals soon realized that an absence of uniforms did not necessarily mean an absence of cops.

Distribution of officers was not the only problem. Bratton's analysis revealed that an inordinate amount of police time was wasted in processing arrests. It took an officer up to 16 hours per arrest to book the suspect and file

papers on the incident. What's more, the officers so hated the bureaucratic process that they avoided making arrests in minor cases. Bratton realized that he could dramatically increase his available policing resources—not to mention the officers' motivation—if he could somehow improvise around this problem. His solution was to park “bust buses”—old buses converted into arrest-processing centers—around the corner from targeted subway stations. Processing time was cut from 16 hours to just one. Innovations like that enabled Bratton to dramatically reduce subway crime—even without an increase in the number of officers on duty at any given time. (The figure “The strategy canvas of transit: How Bratton refocused resources” illustrates how radically Bratton refocused the transit police's resources.)

Bratton's drive for data-driven policing solutions led to the creation of the famous Compstat crime database. The database, used to identify hot spots for intense police intervention, captures weekly crime and arrest activity—including times, locations, and associated enforcement activities—at the precinct, borough, and city levels. The Compstat reports allowed Bratton and the entire police department to easily discern established and emerging hot spots for efficient resource targeting and retargeting.

In addition to refocusing the resources he already controls, Bratton has proved adept at trading resources he doesn't need for those he does. The chiefs of public-sector organizations are reluctant to advertise excess resources, let alone lend them to other agencies, because acknowledged excess resources tend to get reallocated. So over time, some organizations end up well endowed with resources they don't need—even if they are short of others. When Bratton took over as chief of the transit police, for example, his general counsel and policy adviser, Dean Esserman, now police chief of Providence, Rhode Island, discovered that the transit unit had more unmarked cars than it needed but was starved of office space. The New York Division of Parole, on the other hand, was short of cars but had excess office space. Esserman and Bratton offered the obvious trade. It was gratefully accepted by the parole division, and transit officials were delighted to get the first floor of a prime downtown building. The deal stoked Bratton's credibility within the organization, which would make it easier for him to introduce more fundamental changes later, and it marked him, to his political bosses, as a man who could solve problems.

Jump the Motivational Hurdle

Alerting employees to the need for change and identifying how it can be achieved with limited resources are necessary for reaching an organization's tipping point. But if a new strategy is to become a movement, employees must not only recognize what needs to be done, they must also want to do it. Many CEOs recognize the importance of getting people motivated to make changes, but they make the mistake of trying to reform incentives throughout the whole organization. That process takes a long time to implement and can prove very expensive, given the wide variety of motivational needs in any large company.

One way Bratton solves the motivation problem is by singling out the key influencers—people inside or outside the organization with disproportionate power due to their connections with the organization, their ability to persuade, or their ability to block access to resources. Bratton recognizes that these influencers act like kingpins in bowling: When you hit them just right, all the pins topple over. Getting the key influencers motivated frees an organization from having to motivate everyone, yet everyone in the end is touched and changed. And because most organizations have relatively small numbers of key influencers, and those people tend to share common problems and concerns, it is relatively easy for CEOs to identify and motivate them.

Bratton's approach to motivating his key influencers is to put them under a spotlight. Perhaps his most significant reform of the NYPD's operating practices was instituting a semiweekly strategy review meeting that brought the top brass together with the city's 76 precinct commanders. Bratton had identified the commanders as key influential people in the NYPD, because each one directly managed 200 to 400 officers. Attendance was mandatory for all senior staff, including three-star chiefs, deputy commissioners, and borough chiefs. Bratton was there as often as possible.

At the meetings, which took place in an auditorium at the police command center, a selected precinct commander was called before a panel of the senior

staff (the selected officer was given only two days' notice, in order to keep all the commanders on their toes). The commander in the spotlight was questioned by both the panel and other commanders about the precinct's performance. He or she was responsible for explaining projected maps and charts that showed, based on the Compstat data, the precinct's patterns of crimes and when and where the police responded. The commander would be required to provide a detailed explanation if police activity did not mirror crime spikes and would also be asked how officers were addressing the precinct's issues and why performance was improving or deteriorating. The meetings allowed Bratton and his senior staff to carefully monitor and assess how well commanders were motivating and managing their people and how well they were focusing on strategic hot spots.

The meetings changed the NYPD's culture in several ways. By making results and responsibilities clear to everyone, the meetings helped to introduce a culture of performance. Indeed, a photo of the commander who was about to be grilled appeared on the front page of the handout that each meeting participant received, emphasizing that the commander was accountable for the precinct's results. An incompetent commander could no longer cover up his failings by blaming his precinct's results on the shortcomings of neighboring precincts, because his neighbors were in the room and could respond. By the same token, the meetings gave high achievers a chance to be recognized both for making improvements in their own precincts and for helping other commanders. The meetings also allowed police leaders to compare notes on their experiences; before Bratton's arrival, precinct commanders hardly ever got together as a group. Over time, this management style filtered down through the ranks, as the precinct commanders tried out their own versions of Bratton's meetings. With the spotlight shining brightly on their performance, the commanders were highly motivated to get all the officers under their control marching to the new strategy.

The great challenges in applying this kind of motivational device, of course, are ensuring that people feel it is based on fair processes and seeing to it that they can draw lessons from both good and bad results. Doing so increases the organization's collective strength and everyone's chance of winning. Bratton addresses the issue of fair process by engaging all key influencers in the procedures, setting clear performance expectations, and explaining why these strategy meetings, for example, are essential for fast

execution of policy. He addresses the issue of learning by insisting that the team of top brass play an active role in meetings and by being an active moderator himself. Precinct commanders can talk about their achievements or failures without feeling that they are showing off or being shown up. Successful commanders aren't seen as bragging, because it's clear to everyone that they were asked by Bratton's top team to show, in detail, how they achieved their successes. And for commanders on the receiving end, the sting of having to be taught a lesson by a colleague is mitigated, at least, by their not having to suffer the indignity of asking for it. Bratton's popularity soared when he created a humorous video satirizing the grilling that precinct commanders were given; it showed the cops that he understood just how much he was asking of them.

Bratton also uses another motivational lever: framing the reform challenge itself. Framing the challenge is one of the most subtle and sensitive tasks of the tipping point leader; unless people believe that results are attainable, a turnaround is unlikely to succeed. On the face of it, Bratton's goal in New York was so ambitious as to be scarcely believable. Who would believe that the city could be made one of the safest in the country? And who would want to invest time and energy in chasing such an impossible dream?

To make the challenge seem manageable, Bratton framed it as a series of specific goals that officers at different levels could relate to. As he put it, the challenge the NYPD faced was to make the streets of New York safe "block by block, precinct by precinct, and borough by borough." Thus framed, the task was both all encompassing and doable. For the cops on the street, the challenge was making their beats or blocks safe—no more. For the commanders, the challenge was making their precincts safe—no more. Borough heads also had a concrete goal within their capabilities: making their boroughs safe—no more. No matter what their positions, officers couldn't say that what was being asked of them was too tough. Nor could they claim that achieving it was out of their hands. In this way, responsibility for the turnaround shifted from Bratton to each of the thousands of police officers on the force.

Knock Over the Political Hurdle

Organizational politics is an inescapable reality in public and corporate life, a lesson Bratton learned the hard way. In 1980, at age 34 one of the youngest lieutenants in Boston's police department, he had proudly put up a plaque in his office that said: "Youth and skill will win out every time over age and treachery." Within just a few months, having been shunted into a dead-end position due to a mixture of office politics and his own brashness, Bratton took the sign down. He never again forgot the importance of understanding the plotting, intrigue, and politics involved in pushing through change. Even if an organization has reached the tipping point, powerful vested interests will resist the impending reforms. The more likely change becomes, the more fiercely and vocally these negative influencers—both internal and external—will fight to protect their positions, and their resistance can seriously damage, even derail, the reform process.

Bratton anticipates these dangers by identifying and silencing powerful naysayers early on. To that end, he always ensures that he has a respected senior insider on the top team. At the NYPD, for instance, Bratton appointed John Timoney, now Miami's police commissioner, as his number two. Timoney was a cop's cop, respected and feared for his dedication to the NYPD and for the more than 60 decorations he had received. Twenty years in the ranks had taught him who all the key players were and how they played the political game. One of the first tasks Timoney carried out was to report to Bratton on the likely attitudes of the top staff toward Bratton's concept of zero-tolerance policing, identifying those who would fight or silently sabotage the new initiatives. This led to a dramatic changing of the guard.

Of course, not all naysayers should face the ultimate sanction—there might not be enough people left to man the barricades. In many cases, therefore, Bratton silences opposition by example and indisputable fact. For instance, when first asked to compile detailed crime maps and information packages for the strategy review meetings, most precinct commanders complained that the task would take too long and waste valuable police time

that could be better spent fighting crime. Anticipating this argument, deputy commissioner Jack Maple set up a reporting system that covered the city's most crime-ridden areas. Operating the system required no more than 18 minutes a day, which worked out, as he told the precinct commanders, to less than 1% of the average precinct's workload. Try to argue with that.

Often the most serious opposition to reform comes from outside. In the public sector, as in business, an organization's change of strategy has an impact on other organizations—partners and competitors alike. The change is likely to be resisted by those players if they are happy with the status quo and powerful enough to protest the changes. Bratton's strategy for dealing with such opponents is to isolate them by building a broad coalition with the other independent powers in his realm. In New York, for example, one of the most serious threats to his reforms came from the city's courts, which were concerned that zero-tolerance policing would result in an enormous number of small-crimes cases clogging the court schedule.

To get past the opposition of the courts, Bratton solicited the support of no less a personage than the mayor, Rudolph Giuliani, who had considerable influence over the district attorneys, the courts, and the city jail on Rikers Island. Bratton's team demonstrated to the mayor that the court system had the capacity to handle minor "quality of life" crimes, even though doing so would presumably not be palatable for them.

The mayor decided to intervene. While conceding to the courts that a crackdown campaign would cause a short-term spike in court work, he also made clear that he and the NYPD believed it would eventually lead to a workload reduction for the courts. Working together in this way, Bratton and the mayor were able to maneuver the courts into processing quality-of-life crimes. Seeing that the mayor was aligned with Bratton, the courts appealed to the city's legislators, advocating legislation to exempt them from handling minor-crime cases on the grounds that such cases would clog the system and entail significant costs to the city. Bratton and the mayor, who were holding weekly strategy meetings, added another ally to their coalition by placing their case before the press, in particular the *New York Times*. Through a series of press conferences and articles and at every interview opportunity, the issue of zero tolerance was put at the front and center of public debate with a clear, simple message: If the courts did not help crack down on quality-of-life crimes, the city's crime rates would not improve. It was a matter not of saving dollars but of saving the city.

Bratton's alliance with the mayor's office and the city's leading media institution successfully isolated the courts. The courts could hardly be seen as publicly opposing an initiative that would not only make New York a more attractive place to live but would ultimately reduce the number of cases brought before them. With the mayor speaking aggressively in the press about the need to pursue quality-of-life crimes and the city's most respected—and liberal—newspaper giving credence to the policy, the costs of fighting Bratton's strategy were daunting. Thanks to this savvy politicking, one of Bratton's biggest battles was won, and the legislation was not enacted. The courts would handle quality-of-life crimes. In due course, the crime rates did indeed come tumbling down.

Of course, Bill Bratton, like any leader, must share the credit for his successes. Turning around an organization as large and as wedded to the status quo as the NYPD requires a collective effort. But the tipping point would not have been reached without him—or another leader like him. And while we recognize that not every executive has the personality to be a Bill Bratton, there are many who have that potential once they know the formula for success. It is that formula that we have tried to present, and we urge managers who wish to turn their companies around, but have limited time and resources, to take note. By addressing the hurdles to tipping point change described in these pages, they will stand a chance of achieving the same kind of results for their shareholders as Bratton has delivered to the citizens of New York.

Originally published in April 2003. Reprint R0304D

A Survival Guide for Leaders

by Ronald A. Heifetz and Marty Linsky

THINK OF THE MANY top executives in recent years who, sometimes after long periods of considerable success, have crashed and burned. Or think of individuals you have known in less prominent positions, perhaps people spearheading significant change initiatives in their organizations, who have suddenly found themselves out of a job. Think about yourself: In exercising leadership, have *you* ever been removed or pushed aside?

Let's face it, to lead is to live dangerously. While leadership is often depicted as an exciting and glamorous endeavor, one in which you inspire others to follow you through good times and bad, such a portrayal ignores leadership's dark side: the inevitable attempts to take you out of the game.

Those attempts are sometimes justified. People in top positions must often pay the price for a flawed strategy or a series of bad decisions. But frequently, something more is at work. We're not talking here about conventional office politics; we're talking about the high-stake risks you face whenever you try to lead an organization through difficult but necessary change. The risks during such times are especially high because change that truly transforms an organization, be it a multibillion-dollar company or a ten-person sales team, demands that people give up things they hold dear: daily habits, loyalties, ways of thinking. In return for these sacrifices, they may be offered nothing more than the possibility of a better future.

We refer to this kind of wrenching organizational transformation as "adaptive change," something very different from the "technical change" that occupies people in positions of authority on a regular basis. Technical problems, while often challenging, can be solved applying existing know-how and the organization's current problem-solving processes. Adaptive

problems resist these kinds of solutions because they require individuals throughout the organization to alter their ways; as the people themselves are the problem, the solution lies with them. (See the sidebar “Adaptive Versus Technical Change: Whose Problem Is It?”) Responding to an adaptive challenge with a technical fix may have some short-term appeal. But to make real progress, sooner or later those who lead must ask themselves and the people in the organization to face a set of deeper issues—and to accept a solution that may require turning part or all of the organization upside down.

It is at this point that danger lurks. And most people who lead in such a situation—swept up in the action, championing a cause they believe in—are caught unawares. Over and over again, we have seen courageous souls blissfully ignorant of an approaching threat until it was too late to respond.

The hazard can take numerous forms. You may be attacked directly in an attempt to shift the debate to your character and style and avoid discussion of your initiative. You may be marginalized, forced into the position of becoming so identified with one issue that your broad authority is undermined. You may be seduced by your supporters and, fearful of losing their approval and affection, fail to demand they make the sacrifices needed for the initiative to succeed. You may be diverted from your goal by people overwhelming you with the day-to-day details of carrying it out, keeping you busy and preoccupied.

Each one of these thwarting tactics—whether done consciously or not—grows out of people’s aversion to the organizational disequilibrium created by your initiative. By attempting to undercut you, people strive to restore order, maintain what is familiar to them, and protect themselves from the pains of adaptive change. They want to be comfortable again, and you’re in the way.

Idea in Brief

It’s exciting—even glamorous—to lead others through good times and bad. But leadership also has its dark side: the inevitable attempts to take you out of the game when you’re steering your organization through difficult change.

Leading change requires asking people to confront painful issues and give up habits and beliefs they hold dear. Result? Some people try to eliminate change's visible agent—you. Whether they attack you personally, undermine your authority, or seduce you into seeing things their way, their goal is the same: to derail you, easing *their* pain and restoring familiar order.

How to resist attempts to remove you—and continue to propel change forward? Manage your hostile *environment*—your organization and its people—and your own *vulnerabilities*.

So how do you protect yourself? Over a combined 50 years of teaching and consulting, we have asked ourselves that question time and again—usually while watching top-notch and well-intentioned folks get taken out of the game. On occasion, the question has become painfully personal; we as individuals have been knocked off course or out of the action more than once in our own leadership efforts. So we are offering what we hope are some pragmatic answers that grow out of these observations and experiences. We should note that while our advice clearly applies to senior executives, it also applies to people trying to lead change initiatives from positions of little or no formal organizational authority.

This “survival guide” has two main parts. The first looks outward, offering tactical advice about relating to your organization and the people in it. It is designed to protect you from those trying to push you aside before you complete your initiative. The second looks inward, focusing on your own human needs and vulnerabilities. It is designed to keep you from bringing yourself down.

A Hostile Environment

Leading major organizational change often involves radically reconfiguring a complex network of people, tasks, and institutions that have achieved a kind of *modus vivendi*, no matter how dysfunctional it appears to you. When the status quo is upset, people feel a sense of profound loss and dashed expectations. They may go through a period of feeling incompetent or disloyal. It's no wonder they resist the change or try to eliminate its visible agent. We offer here a number of techniques—relatively straightforward in concept but difficult to execute—for minimizing these external threats.

Idea in Practice

Managing Your Environment

To minimize threats to eliminate you:

Operate in and above the fray.

Observe what's happening to your initiative, *as* it's happening. Frequently move back and forth from the dance floor to the balcony, asking, "What's really going on here?" "Who's defending old habits?"

Court the uncommitted.

The uncommitted but wary are crucial to your success. Show your intentions are serious, for example, by dismissing individuals who can't make required changes. And practice what you preach.

Example: The editor of the *St. Petersburg Times* wanted to create a harder-hitting newspaper. He knew that reporters—no longer sparing interviewees from warranted criticism—faced intense public pressure. He subjected *himself* to the same by insisting a story about his drunk-driving arrest appear on the paper's front page.

Cook the conflict.

Keep the heat high enough to motivate, but low enough to prevent explosions. *Raise the temperature* to make people confront hidden conflicts and other tough issues. Then *lower the heat* to reduce destructive turmoil. Slow the pace of change. Deliver humor, breaks, and images of a brighter future.

Place the work where it belongs.

Resist resolving conflicts yourself—people will blame *you* for whatever turmoil results. Mobilize *others* to solve problems.

Example: When a star Chicago Bulls basketball player sat out a play, miffed because he wasn't tapped to take the game's final shot, the coach let the *team* handle the insubordination. An emotional conversation led by a team veteran reunited the players, who took the NBA series to a seventh game.

Managing Yourself

To avoid self-destructing during difficult change:

Restrain your desire for control and need for importance

Order for its own sake prevents organizations from handling contentious issues. And an inflated self-image fosters unhealthy dependence on you.

Example: Ken Olson, head of once-mighty Digital Equipment Corporation, encouraged such dependence that colleagues rarely challenged him. When he shunned the PC market (believing few people wanted PCs), top managers went along—initiating DEC’s downfall.

Anchor yourself.

- Use a safe place (e.g., a friend’s kitchen table) or routine (a daily walk) to repair psychological damage and recalibrate your moral compass.
- Acquire a confidant (*not* an ally from your organization) who supports you—not necessarily your initiative.
- Read attacks as reactions to your professional role, not to you personally. You’ll remain calmer and keep people engaged.



Operate in and above the fray

The ability to maintain perspective in the midst of action is critical to lowering resistance. Any military officer knows the importance of maintaining the capacity for reflection, especially in the “fog of war.” Great athletes must simultaneously play the game and observe it as a whole. We call this skill “getting off the dance floor and going to the balcony,” an image that captures the mental activity of stepping back from the action and asking, “What’s really going on here?”

Leadership is an improvisational art. You may be guided by an overarching vision, clear values, and a strategic plan, but what you actually do from moment to moment cannot be scripted. You must respond as events unfold. To use our metaphor, you have to move back and forth from the balcony to the dance floor, over and over again throughout the days, weeks, months, and years. While today’s plan may make sense now, tomorrow you’ll discover the unanticipated effects of today’s actions and have to adjust accordingly. Sustaining good leadership, then, requires first and foremost the capacity to see what is happening to you and your initiative as it is happening and to understand how today’s turns in the road will affect tomorrow’s plans.

But taking a balcony perspective is extremely tough to do when you’re fiercely engaged down below, being pushed and pulled by the events and people around you—and doing some pushing and pulling of your own. Even if you are able to break away, the practice of stepping back and seeing the big picture is complicated by several factors. For example, when you get some distance, you still must accurately interpret what you see and hear. This is easier said than done. In an attempt to avoid difficult change, people will naturally, even unconsciously, defend their habits and ways of thinking. As you seek input from a broad range of people, you’ll constantly need to be aware of these hidden agendas. You’ll also need to observe your own actions; seeing yourself objectively as you look down from the balcony is perhaps the hardest task of all.

Fortunately, you can learn to be both an observer and a participant at the same time. When you are sitting in a meeting, practice by watching what is

happening while it is happening—even as you are part of what is happening. Observe the relationships and see how people's attention to one another can vary: supporting, thwarting, or listening. Watch people's body language. When you make a point, resist the instinct to stay perched on the edge of your seat, ready to defend what you said. A technique as simple as pushing your chair a few inches away from the table after you speak may provide the literal as well as metaphorical distance you need to become an observer.

Court the uncommitted

It's tempting to go it alone when leading a change initiative. There's no one to dilute your ideas or share the glory, and it's often just plain exciting. It's also foolish. You need to recruit partners, people who can help protect you from attacks and who can point out potentially fatal flaws in your strategy or initiative. Moreover, you are far less vulnerable when you are out on the point with a bunch of folks rather than alone. You also need to keep the opposition close. Knowing what your opponents are thinking can help you challenge them more effectively and thwart their attempts to upset your agenda—or allow you to borrow ideas that will improve your initiative. Have coffee once a week with the person most dedicated to seeing you fail.

Adaptive Versus Technical Change: Whose Problem Is It?

THE IMPORTANCE—AND DIFFICULTY—of distinguishing between adaptive and technical change can be illustrated with an analogy. When your car has problems, you go to a mechanic. Most of the time, the mechanic can fix the car. But if your car troubles stem from the way a family member drives, the problems are likely to recur. Treating the problems as purely technical ones—taking the car to the mechanic time and again to get it back on the road—masks the real issues. Maybe you need to get your mother to stop drinking and driving, get your grandfather to give up his driver's license, or get your teenager to be more cautious. Whatever the underlying problems, the mechanic can't solve them. Instead, changes in the family need to occur, and that won't be easy. People will resist the moves, even denying that such problems exist. That's because even those not directly affected by an adaptive change typically experience discomfort when someone upsets a group's or an organization's equilibrium.

Such resistance to adaptive change certainly happens in business. Indeed, it's the classic error: Companies treat adaptive challenges as if they were technical problems. For example, executives attempt to improve the bottom line by cutting costs across the board. Not only does this avoid the need to make tough choices about which areas should be trimmed, it also masks the fact that the company's real challenge lies in redesigning its strategy.

Treating adaptive challenges as technical ones permits executives to do what they have excelled at throughout their careers: solve other people's problems. And it allows others in the organization to enjoy the primordial peace of mind that comes from knowing that their commanding officer has a plan to maintain order and stability. After all, the executive doesn't have to instigate—and the people don't have to undergo—uncomfortable change. Most people would agree that, despite the selective pain of a cost-cutting exercise, it is less traumatic than reinventing a company.

But while relationships with allies and opponents are essential, the people who will determine your success are often those in the middle, the uncommitted who nonetheless are wary of your plans. They have no substantive stake in your initiative, but they do have a stake in the comfort, stability, and security of the status quo. They've seen change agents come and go, and they know that your initiative will disrupt their lives and make their futures uncertain. You want to be sure that this general uneasiness doesn't evolve into a move to push you aside.

These people will need to see that your intentions are serious—for example, that you are willing to let go of those who can't make the changes your initiative requires. But people must also see that you understand the loss you are asking them to accept. You need to name the loss, be it a change in time-honored work routines or an overhaul of the company's core values, and explicitly acknowledge the resulting pain. You might do this through a series of simple statements, but it often requires something more tangible and public—recall Franklin Roosevelt's radio “fireside chats” during the Great Depression—to convince people that you truly understand.

Beyond a willingness to accept casualties and acknowledge people's losses, two very personal types of action can defuse potential resistance to

you and your initiatives. The first is practicing what you preach. In 1972, Gene Patterson took over as editor of the *St. Petersburg Times*. His mandate was to take the respected regional newspaper to a higher level, enhancing its reputation for fine writing while becoming a fearless and hard-hitting news source. This would require major changes not only in the way the community viewed the newspaper but also in the way *Times* reporters thought about themselves and their roles. Because prominent organizations and individuals would no longer be spared warranted criticism, reporters would sometimes be angrily rebuked by the subjects of articles.

Several years after Patterson arrived, he attended a party at the home of the paper's foreign editor. Driving home, he pulled up to a red light and scraped the car next to him. The police officer called to the scene charged Patterson with driving under the influence. Patterson phoned Bob Haiman, a veteran *Times* newsman who had just been appointed executive editor, and insisted that a story on his arrest be run. As Haiman recalls, he tried to talk Patterson out of it, arguing that DUI arrests that didn't involve injuries were rarely reported, even when prominent figures were involved. Patterson was adamant, however, and insisted that the story appear on page one.

Patterson, still viewed as somewhat of an outsider at the paper, knew that if he wanted his employees to follow the highest journalistic standards, he would have to display those standards, even when it hurt. Few leaders are called upon to disgrace themselves on the front page of a newspaper. But adopting the behavior you expect from others—whether it be taking a pay cut in tough times or spending a day working next to employees on a reconfigured production line—can be crucial in getting buy-in from people who might try to undermine your initiative.

The second thing you can do to neutralize potential opposition is to acknowledge your own responsibility for whatever problems the organization currently faces. If you have been with the company for some time, whether in a position of senior authority or not, you've likely contributed in some way to the current mess. Even if you are new, you need to identify areas of your own behavior that could stifle the change you hope to make.

In our teaching, training, and consulting, we often ask people to write or talk about a leadership challenge they currently face. Over the years, we have read and heard literally thousands of such challenges. Typically, in the first version of the story, the author is nowhere to be found. The underlying message: "If only other people would shape up, I could make progress here."

But by too readily pointing your finger at others, you risk making yourself a target. Remember, you are asking people to move to a place where they are frightened to go. If at the same time you're blaming them for having to go there, they will undoubtedly turn against you.

In the early 1990s, Leslie Wexner, founder and CEO of the Limited, realized the need for major changes at the company, including a significant reduction in the workforce. But his consultant told him that something else had to change: long-standing habits that were at the heart of his self-image. In particular, he had to stop treating the company as if it were his family. The indulgent father had to become the chief personnel officer, putting the right people in the right jobs and holding them accountable for their work. "I was an athlete trained to be a baseball player," Wexner recalled during a recent speech at Harvard's Kennedy School. "And one day, someone tapped me on the shoulder and said, 'Football.' And I said, 'No, I'm a baseball player. 'And he said, 'Football.' And I said, 'I don't know how to play football. I'm not 6'4", and I don't weigh 300 pounds.' But if no one values baseball anymore, the baseball player will be out of business. So I looked into the mirror and said, 'Schlemiel, nobody wants to watch baseball. Make the transformation to football.'" His personal makeover—shedding the role of forgiving father to those widely viewed as not holding their own—helped sway other employees to back a corporate makeover. And his willingness to change helped protect him from attack during the company's long—and generally successful—turnaround period.

Cook the conflict

Managing conflict is one of the greatest challenges a leader of organizational change faces. The conflict may involve resistance to change, or it may involve clashing viewpoints about how the change should be carried out. Often, it will be latent rather than palpable. That's because most organizations are allergic to conflict, seeing it primarily as a source of danger, which it certainly can be. But conflict is a necessary part of the change process and, if handled properly, can serve as the engine of progress.

Thus, a key imperative for a leader trying to achieve significant change is to manage people's passionate differences in a way that diminishes their destructive potential and constructively harnesses their energy. Two techniques can help you achieve this. First, create a secure place where the conflicts can freely bubble up. Second, control the temperature to ensure that the conflict doesn't boil over—and burn you in the process.

The vessel in which a conflict is simmered—in which clashing points of view mix, lose some of their sharpness, and ideally blend into consensus—will look and feel quite different in different contexts. It may be a protected physical space, perhaps an off-site location where an outside facilitator helps a group work through its differences. It may be a clear set of rules and processes that give minority voices confidence that they will be heard without having to disrupt the proceedings to gain attention. It may be the shared language and history of an organization that binds people together through trying times. Whatever its form, it is a place or a means to contain the roiling forces unleashed by the threat of major change.

But a vessel can withstand only so much strain before it blows. A huge challenge you face as a leader is keeping your employees' stress at a productive level. The success of the change effort—as well as your own authority and even survival—requires you to monitor your organization's tolerance for heat and then regulate the temperature accordingly.

You first need to raise the heat enough that people sit up, pay attention, and deal with the real threats and challenges facing them. After all, without some distress, there's no incentive to change. You can constructively raise

the temperature by focusing people's attention on the hard issues, by forcing them to take responsibility for tackling and solving those issues, and by bringing conflicts occurring behind closed doors out into the open.

But you have to lower the temperature when necessary to reduce what can be counterproductive turmoil. You can turn down the heat by slowing the pace of change or by tackling some relatively straightforward technical aspect of the problem, thereby reducing people's anxiety levels and allowing them to get warmed up for bigger challenges. You can provide structure to the problem-solving process, creating work groups with specific assignments, setting time parameters, establishing rules for decision making, and outlining reporting relationships. You can use humor or find an excuse for a break or a party to temporarily ease tensions. You can speak to people's fears and, more critically, to their hopes for a more promising future. By showing people how the future might look, you come to embody hope rather than fear, and you reduce the likelihood of becoming a lightning rod for the conflict.

The aim of both these tactics is to keep the heat high enough to motivate people but low enough to prevent a disastrous explosion—what we call a “productive range of distress.” Remember, though, that most employees will reflexively want you to turn down the heat; their complaints may in fact indicate that the environment is just right for hard work to get done.

We've already mentioned a classic example of managing the distress of fundamental change: Franklin Roosevelt during the first few years of his presidency. When he took office in 1933, the chaos, tension, and anxiety brought on by the Depression ran extremely high. Demagogues stoked class, ethnic, and racial conflict that threatened to tear the nation apart. Individuals feared an uncertain future. So Roosevelt first did what he could to reduce the sense of disorder to a tolerable level. He took decisive and authoritative action—he pushed an extraordinary number of bills through Congress during his fabled first 100 days—and thereby gave Americans a sense of direction and safety, reassuring them that they were in capable hands. In his fireside chats, he spoke to people's anxiety and anger and laid out a positive vision for the future that made the stress of the current crisis bearable and seem a worthwhile price to pay for progress.

But he knew the problems facing the nation couldn't be solved from the White House. He needed to mobilize citizens and get them to dream up, try out, fight over, and ultimately own the sometimes painful solutions that would transform the country and move it forward. To do that, he needed to

maintain a certain level of fermentation and distress. So, for example, he orchestrated conflicts over public priorities and programs among the large cast of creative people he brought into the government. By giving the same assignment to two different administrators and refusing to clearly define their roles, he got them to generate new and competing ideas. Roosevelt displayed both the acuity to recognize when the tension in the nation had risen too high and the emotional strength to take the heat and permit considerable anxiety to persist.

Place the work where it belongs

Because major change requires people across an entire organization to adapt, you as a leader need to resist the reflex reaction of providing people with the answers. Instead, force yourself to transfer, as Roosevelt did, much of the work and problem solving to others. If you don't, real and sustainable change won't occur. In addition, it's risky on a personal level to continue to hold on to the work that should be done by others.

As a successful executive, you have gained credibility and authority by demonstrating your capacity to solve other people's problems. This ability can be a virtue, until you find yourself faced with a situation in which you cannot deliver solutions. When this happens, all of your habits, pride, and sense of competence get thrown out of kilter because you must mobilize the work of others rather than find the way yourself. By trying to solve an adaptive challenge for people, at best you will reconfigure it as a technical problem and create some short-term relief. But the issue will not have gone away.

In the 1994 National Basketball Association Eastern Conference semifinals, the Chicago Bulls lost to the New York Knicks in the first two games of the best-of-seven series. Chicago was out to prove that it was more than just a one-man team, that it could win without Michael Jordan, who had retired at the end of the previous season.

In the third game, the score was tied at 102 with less than two seconds left. Chicago had the ball and a time-out to plan a final shot. Coach Phil Jackson called for Scottie Pippen, the Bulls' star since Jordan had retired, to make the inbound pass to Toni Kukoc for the final shot. As play was about to resume, Jackson noticed Pippen sitting at the far end of the bench. Jackson asked him whether he was in or out. "I'm out," said Pippen, miffed that he was not tapped to take the final shot. With only four players on the floor, Jackson quickly called another time-out and substituted an excellent passer, the reserve Pete Myers, for Pippen. Myers tossed a perfect pass to Kukoc, who spun around and sank a miraculous shot to win the game.

The Bulls made their way back to the locker room, their euphoria deflated

by Pippen's extraordinary act of insubordination. Jackson recalls that as he entered a silent room, he was uncertain about what to do. Should he punish Pippen? Make him apologize? Pretend the whole thing never happened? All eyes were on him. The coach looked around, meeting the gaze of each player, and said, "What happened has hurt us. Now you have to work this out."

Jackson knew that if he took action to resolve the immediate crisis, he would have made Pippen's behavior a matter between coach and player. But he understood that a deeper issue was at the heart of the incident: Who were the Chicago Bulls without Michael Jordan? It wasn't about who was going to succeed Jordan, because no one was; it was about whether the players could jell as a team where no one person dominated and every player was willing to do whatever it took to help. The issue rested with the players, not him, and only they could resolve it. It did not matter what they decided at that moment; what mattered was that they, not Jackson, did the deciding. What followed was a discussion led by an emotional Bill Cartwright, a team veteran. According to Jackson, the conversation brought the team closer together. The Bulls took the series to a seventh game before succumbing to the Knicks.

Jackson gave the work of addressing both the Pippen and the Jordan issues back to the team for another reason: If he had taken ownership of the problem, he would have become the issue, at least for the moment. In his case, his position as coach probably wouldn't have been threatened. But in other situations, taking responsibility for resolving a conflict within the organization poses risks. You are likely to find yourself resented by the faction that you decide against and held responsible by nearly everyone for the turmoil your decision generates. In the eyes of many, the only way to neutralize the threat is to get rid of you.

Despite that risk, most executives can't resist the temptation to solve fundamental organizational problems by themselves. People expect you to get right in there and fix things, to take a stand and resolve the problem. After all, that is what top managers are paid to do. When you fulfill those expectations, people will call you admirable and courageous—even a "leader"—and that is flattering. But challenging your employees' expectations requires greater courage and leadership.

The Dangers Within

We have described a handful of leadership tactics you can use to interact with the people around you, particularly those who might undermine your initiatives. Those tactics can help advance your initiatives and, just as important, ensure that you remain in a position where you can bring them to fruition. But from our own observations and painful personal experiences, we know that one of the surest ways for an organization to bring you down is simply to let you precipitate your own demise.

In the heat of leadership, with the adrenaline pumping, it is easy to convince yourself that you are not subject to the normal human frailties that can defeat ordinary mortals. You begin to act as if you are indestructible. But the intellectual, physical, and emotional challenges of leadership are fierce. So, in addition to getting on the balcony, you need to regularly step into the inner chamber of your being and assess the tolls those challenges are taking. If you don't, your seemingly indestructible self can self-destruct. This, by the way, is an ideal outcome for your foes—and even friends who oppose your initiative—because no one has to feel responsible for your downfall.

Manage your hungers

We all have hungers, expressions of our normal human needs. But sometimes those hungers disrupt our capacity to act wisely or purposefully. Whether inherited or products of our upbringing, some of these hungers may be so strong that they render us constantly vulnerable. More typically, a stressful situation or setting can exaggerate a normal level of need, amplifying our desires and overwhelming our usual self-discipline. Two of the most common and dangerous hungers are the desire for control and the desire for importance.

Everyone wants to have some measure of control over his or her life. Yet some people's need for control is disproportionately high. They might have grown up in a household that was either tightly structured or unusually chaotic; in either case, the situation drove them to become masters at taming chaos not only in their own lives but also in their organizations.

That need for control can be a source of vulnerability. Initially, of course, the ability to turn disorder into order may be seen as an attribute. In an organization facing turmoil, you may seem like a godsend if you are able (and desperately want) to step in and take charge. By lowering the distress to a tolerable level, you keep the kettle from boiling over.

But in your desire for order, you can mistake the means for the end. Rather than ensuring that the distress level in an organization remains high enough to mobilize progress on the issues, you focus on maintaining order as an end in itself. Forcing people to make the difficult trade-offs required by fundamental change threatens a return to the disorder you loathe. Your ability to bring the situation under control also suits the people in the organization, who naturally prefer calm to chaos. Unfortunately, this desire for control makes you vulnerable to, and an agent of, the organization's wish to avoid working through contentious issues. While this may ensure your survival in the short term, ultimately you may find yourself accused, justifiably, of failing to deal with the tough challenges when there was still time to do so.

Most people also have some need to feel important and affirmed by others. The danger here is that you will let this affirmation give you an

inflated view of yourself and your cause. A grandiose sense of self-importance often leads to self-deception. In particular, you tend to forget the creative role that doubt—which reveals parts of reality that you wouldn't otherwise see—plays in getting your organization to improve. The absence of doubt leads you to see only that which confirms your own competence, which will virtually guarantee disastrous missteps.

Another harmful side effect of an inflated sense of self-importance is that you will encourage people in the organization to become dependent on you. The higher the level of distress, the greater their hopes and expectations that you will provide deliverance. This relieves them of any responsibility for moving the organization forward. But their dependence can be detrimental not only to the group but to you personally. Dependence can quickly turn to contempt as your constituents discover your human shortcomings.

Two well-known stories from the computer industry illustrate the perils of dependency—and how to avoid them. Ken Olsen, the founder of Digital Equipment Corporation, built the company into a 120,000-person operation that, at its peak, was the chief rival of IBM. A generous man, he treated his employees extraordinarily well and experimented with personnel policies designed to increase the creativity, teamwork, and satisfaction of his workforce. This, in tandem with the company's success over the years, led the company's top management to turn to him as the sole decision maker on all key issues. His decision to shun the personal computer market because of his belief that few people would ever want to own a PC, which seemed reasonable at the time, is generally viewed as the beginning of the end for the company. But that isn't the point; everyone in business makes bad decisions. The point is, Olsen had fostered such an atmosphere of dependence that his decisions were rarely challenged by colleagues—at least not until it was too late.

Contrast that decision with Bill Gates's decision some years later to keep Microsoft out of the Internet business. It didn't take long for him to reverse his stand and launch a corporate overhaul that had Microsoft's delivery of Internet services as its centerpiece. After watching the rapidly changing computer industry and listening carefully to colleagues, Gates changed his mind with no permanent damage to his sense of pride and an enhanced reputation due to his nimble change of course.

Anchor yourself

To survive the turbulent seas of a change initiative, you need to find ways to steady and stabilize yourself. First, you must establish a safe harbor where each day you can reflect on the previous day's journey, repair the psychological damage you have incurred, renew your stores of emotional resources, and recalibrate your moral compass. Your haven might be a physical place, such as the kitchen table of a friend's house, or a regular routine, such as a daily walk through the neighborhood. Whatever the sanctuary, you need to use and protect it. Unfortunately, seeking such respite is often seen as a luxury, making it one of the first things to go when life gets stressful and you become pressed for time.

Second, you need a confidant, someone you can talk to about what's in your heart and on your mind without fear of being judged or betrayed. Once the undigested mess is on the table, you can begin to separate, with your confidant's honest input, what is worthwhile from what is simply venting. The confidant, typically not a coworker, can also pump you up when you're down and pull you back to earth when you start taking praise too seriously. But don't confuse confidants with allies: Instead of supporting your current initiative, a confidant simply supports you. A common mistake is to seek a confidant among trusted allies, whose personal loyalty may evaporate when a new issue more important to them than you begins to emerge and take center stage.

Perhaps most important, you need to distinguish between your personal self, which can serve as an anchor in stormy weather, and your professional role, which never will. It is easy to mix up the two. And other people only increase the confusion: Colleagues, subordinates, and even bosses often act as if the role you play is the real you. But that is not the case, no matter how much of yourself—your passions, your values, your talents—you genuinely and laudably pour into your professional role. Ask anyone who has experienced the rude awakening that comes when they leave a position of authority and suddenly find that their phone calls aren't returned as quickly as they used to be.

That harsh lesson holds another important truth that is easily forgotten: When people attack someone in a position of authority, more often than not they are attacking the role, not the person. Even when attacks on you are highly personal, you need to read them primarily as reactions to how you, in your role, are affecting people's lives. Understanding the criticism for what it is prevents it from undermining your stability and sense of self-worth. And that's important because when you feel the sting of an attack, you are likely to become defensive and lash out at your critics, which can precipitate your downfall.

We hasten to add that criticism may contain legitimate points about how you are performing your role. For example, you may have been tactless in raising an issue with your organization, or you may have turned the heat up too quickly on a change initiative. But, at its heart, the criticism is usually about the issue, not you. Through the guise of attacking you personally, people often are simply trying to neutralize the threat they perceive in your point of view. Does anyone ever attack you when you hand out big checks or deliver good news? People attack your personality, style, or judgment when they don't like the message.

When you take "personal" attacks personally, you unwittingly conspire in one of the common ways you can be taken out of action—you make yourself the issue. Contrast the manner in which presidential candidates Gary Hart and Bill Clinton handled charges of philandering. Hart angrily counterattacked, criticizing the scruples of the reporters who had shadowed him. This defensive personal response kept the focus on his behavior. Clinton, on national television, essentially admitted he had strayed, acknowledging his piece of the mess. His strategic handling of the situation allowed him to return the campaign's focus to policy issues. Though both attacks were extremely personal, only Clinton understood that they were basically attacks on positions he represented and the role he was seeking to play.

Do not underestimate the difficulty of distinguishing self from role and responding coolly to what feels like a personal attack—particularly when the criticism comes, as it will, from people you care about. But disciplining yourself to do so can provide you with an anchor that will keep you from running aground and give you the stability to remain calm, focused, and persistent in engaging people with the tough issues.

Why Lead?

We will have failed if this “survival manual” for avoiding the perils of leadership causes you to become cynical or callous in your leadership effort or to shun the challenges of leadership altogether. We haven’t touched on the thrill of inspiring people to come up with creative solutions that can transform an organization for the better. We hope we have shown that the essence of leadership lies in the capacity to deliver disturbing news and raise difficult questions in a way that moves people to take up the message rather than kill the messenger. But we haven’t talked about the reasons that someone might want to take these risks.

Of course, many people who strive for high-authority positions are attracted to power. But in the end, that isn’t enough to make the high stakes of the game worthwhile. We would argue that, when they look deep within themselves, people grapple with the challenges of leadership in order to make a positive difference in the lives of others.

When corporate presidents and vice presidents reach their late fifties, they often look back on careers devoted to winning in the marketplace. They may have succeeded remarkably, yet some people have difficulty making sense of their lives in light of what they have given up. For too many, their accomplishments seem empty. They question whether they should have been more aggressive in questioning corporate purposes or creating more ambitious visions for their companies.

Our underlying assumption in this article is that you can lead *and* stay alive—not just register a pulse, but really be alive. But the classic protective devices of a person in authority tend to insulate them from those qualities that foster an acute experience of living. Cynicism, often dressed up as realism, undermines creativity and daring. Arrogance, often posing as authoritative knowledge, snuffs out curiosity and the eagerness to question. Callousness, sometimes portrayed as the thick skin of experience, shuts out compassion for others.

The hard truth is that it is not possible to know the rewards and joys of

leadership without experiencing the pain as well. But staying in the game and bearing that pain is worth it, not only for the positive changes you can make in the lives of others but also for the meaning it gives your own.

Originally published in June 2002. Reprint R0206C

The Real Reason People Won't Change

by Robert Kegan and Lisa Laskow Lahey

EVERY MANAGER IS FAMILIAR with the employee who just won't change. Sometimes it's easy to see why—the employee fears a shift in power, the need to learn new skills, the stress of having to join a new team. In other cases, such resistance is far more puzzling. An employee has the skills and smarts to make a change with ease, has shown a deep commitment to the company, genuinely supports the change—and yet, inexplicably, does nothing.

What's going on? As organizational psychologists, we have seen this dynamic literally hundreds of times, and our research and analysis have recently led us to a surprising yet deceptively simple conclusion. Resistance to change does not reflect opposition, nor is it merely a result of inertia. Instead, even as they hold a sincere commitment to change, many people are unwittingly applying productive energy toward a hidden *competing commitment*. The resulting dynamic equilibrium stalls the effort in what looks like resistance but is in fact a kind of personal immunity to change.

When you, as a manager, uncover an employee's competing commitment, behavior that has seemed irrational and ineffective suddenly becomes stunningly sensible and masterful—but unfortunately, on behalf of a goal that conflicts with what you and even the employee are trying to achieve. You find out that the project leader who's dragging his feet has an unrecognized competing commitment to avoid the even tougher assignment—one he fears he can't handle—that might come his way next if he delivers too successfully on the task at hand. Or you find that the person who won't collaborate despite a passionate and sincere commitment to teamwork is equally dedicated to avoiding the conflict that naturally attends any ambitious team activity.

In these pages, we'll look at competing commitments in detail and take you through a process to help your employees overcome their immunity to change. The process may sound straightforward, but it is by no means quick or easy. On the contrary, it challenges the very psychological foundations upon which people function. It asks people to call into question beliefs they've long held close, perhaps since childhood. And it requires people to admit to painful, even embarrassing, feelings that they would not ordinarily disclose to others or even to themselves. Indeed, some people will opt not to disrupt their immunity to change, choosing instead to continue their fruitless struggle against their competing commitments.

As a manager, you must guide people through this exercise with understanding and sensitivity. If your employees are to engage in honest introspection and candid disclosure, they must understand that their revelations won't be used against them. The goal of this exploration is solely to help them become more effective, not to find flaws in their work or character. As you support your employees in unearthing and challenging their innermost assumptions, you may at times feel you're playing the role of a psychologist. But in a sense, managers *are* psychologists. After all, helping people overcome their limitations to become more successful at work is at the very heart of effective management.

We'll describe this delicate process in detail, but first let's look at some examples of competing commitments in action.

Shoveling Sand Against the Tide

Competing commitments cause valued employees to behave in ways that seem inexplicable and irremediable, and this is enormously frustrating to managers. Take the case of John, a talented manager at a software company. (Like all examples in this article, John's experiences are real, although we have altered identifying features. In some cases, we've constructed composite examples.) John was a big believer in open communication and valued close working relationships, yet his caustic sense of humor consistently kept colleagues at a distance. And though he wanted to move up in the organization, his personal style was holding him back. Repeatedly, John was counseled on his behavior, and he readily agreed that he needed to change the way he interacted with others in the organization. But time after time, he reverted to his old patterns. Why, his boss wondered, did John continue to undermine his own advancement?

Idea in Brief

Tearing out your managerial hair over employees who just won't change—especially the ones who are clearly smart, skilled, and deeply committed to your company and your plans for improvement?

Before you throw up your hands in frustration, listen to recent psychological research: These otherwise valued employees aren't *purposefully* subversive or resistant. Instead, they may be unwittingly caught in a **competing commitment**—a subconscious, hidden goal that conflicts with their *stated* commitments. For example: A project leader dragging his feet has an unrecognized competing commitment to avoid tougher assignments that may come his way if he delivers too successfully on the current project.

Competing commitments make people personally immune to change. Worse, they can undermine your best employees'—and your company's—success.

If the thought of tackling these hidden commitments strikes you as a psychological quagmire, you're not alone. However, you can help employees uncover and move beyond their competing commitments—*without* having to “put them on the couch.” But take care: You'll be challenging employees' deepest psychological foundations and questioning their longest-held beliefs.

Why bother, you ask? Consider the rewards: You help talented employees become much more effective and make far more significant contributions to your company. And, you discover what's *really* going on when people who seem genuinely committed to change dig in their heels.

Idea in Practice

Use these steps to break through an employee's immunity to change:

Diagnose the Competing Commitment

Take two to three hours to explore these questions with the employee:

“What would you like to see changed at work, so you could be more effective, or so work would be more satisfying?” Responses are usually complaints—e.g., Tom, a manager, grumbled, “My subordinates keep me out of the loop.”

“What commitment does your complaint imply?” Complaints indicate what people care about most—e.g., Tom revealed, “I believe in

open, candid communication.”

“What are you doing, or not doing, to keep your commitment from being more fully realized?” Tom admitted, “When people bring bad news, I tend to shoot the messenger.”

“Imagine doing the *opposite* of the undermining behavior. Do you feel any discomfort, worry, or vague fear?” Tom imagined listening calmly and openly to bad news and concluded, “I’m afraid I’ll hear about a problem I can’t fix.”

“By engaging in this undermining behavior, what worrisome outcome are you committed to preventing?” The answer is the competing commitment—what causes them to dig in their heels against change. Tom conceded, *“I’m committed to not learning about problems I can’t fix.”*

Identify the Big Assumption

This is the worldview that colors everything we see and that generates our competing commitment.

People often form big assumptions early in life and then seldom, if ever, examine them. They’re woven into the very fabric of our lives. But only by bringing them into the light can people finally challenge their deepest beliefs and recognize why they’re engaging in seemingly contradictory behavior.

To identify the big assumption, guide an employee through this exercise:

Create a sentence stem that inverts the competing commitment, then “fill in the blank.” Tom turned his competing commitment to not hearing about problems he couldn’t fix into this big assumption: “I assume that if I *did* hear about problems I can’t fix, *people would discover I’m not qualified to do the job.*”

Test—and Consider Replacing—the Big Assumption

By analyzing the circumstances leading up to and reinforcing their big assumptions, employees empower themselves to test those assumptions. They can now carefully and safely experiment with behaving differently than they usually do.

After running several such tests, employees may feel ready to reevaluate the big assumption itself—and possibly even replace it with a new worldview that more accurately reflects their abilities.

At the very least, they'll eventually find more effective ways to support their competing commitment *without* sabotaging other commitments. *They* achieve ever-greater accomplishments—and your *organization* benefits by finally gaining greater access to their talents.

As it happened, John was a person of color working as part of an otherwise all-white executive team. When he went through an exercise designed to help him unearth his competing commitments, he made a surprising discovery about himself. Underneath it all, John believed that if he became too well integrated with the team, it would threaten his sense of loyalty to his own racial group. Moving too close to the mainstream made him feel very uncomfortable, as if he were becoming “one of them” and betraying his family and friends. So when people gathered around his ideas and suggestions, he'd tear down their support with sarcasm, inevitably (and effectively) returning himself to the margins, where he was more at ease. In short, while John was genuinely committed to working well with his colleagues, he had an equally powerful competing commitment to keeping his distance.

Consider, too, a manager we'll call Helen, a rising star at a large manufacturing company. Helen had been assigned responsibility for speeding up production of the company's most popular product, yet she was spinning her wheels. When her boss, Andrew, realized that an important deadline was only two months away and she hadn't filed a single progress report, he called her into a meeting to discuss the project. Helen agreed that she was far behind schedule, acknowledging that she had been stalling in pulling together the

team. But at the same time she showed a genuine commitment to making the project a success. The two developed a detailed plan for changing direction, and Andrew assumed the problem was resolved. But three weeks after the meeting, Helen still hadn't launched the team.

Getting Groups to Change

ALTHOUGH COMPETING COMMITMENTS and big assumptions tend to be deeply personal, groups are just as susceptible as individuals to the dynamics of immunity to change. Face-to-face teams, departments, and even companies as a whole can fall prey to inner contradictions that “protect” them from significant changes they may genuinely strive for. The leadership team of a video production company, for instance, enjoyed a highly collaborative, largely flat organizational structure. A year before we met the group, team members had undertaken a planning process that led them to a commitment of which they were unanimously in favor: In order to ensure that the company would grow in the way the team wished, each of the principals would take responsibility for aggressively overseeing a distinct market segment.

The members of the leadership team told us they came out of this process with a great deal of momentum. They knew which markets to target, they had formed some concrete plans for moving forward, and they had clearly assigned accountability for each market. Yet a year later, the group had to admit it had accomplished very little, despite the enthusiasm. There were lots of rational explanations: “We were unrealistic; we thought we could do new things and still have time to keep meeting our present obligations.” “We didn’t pursue new clients aggressively enough.” “We tried new things but gave up too quickly if they didn’t immediately pay off.”

Efforts to overcome these barriers—to pursue clients more aggressively, for instance—didn’t work because they didn’t get to the cause of the unproductive behavior. But by seeing the team’s explanations as a potential window into the bigger competing commitment, we were able to help the group better understand its predicament. We asked, “Can you identify even

the vaguest fear or worry about what might happen if you *did* more aggressively pursue the new markets? Or if you reduced some of your present activity on behalf of building the new business?” Before long, a different discourse began to emerge, and the other half of a striking groupwide contradiction came into view: The principals were worried that pursuing the plan would drive them apart functionally and emotionally.

“We now realize we are also committed to preserving the noncompetitive, intellectually rewarding, and cocreative spirit of our corporate enterprise,” they concluded. On behalf of this commitment, the team members had to commend themselves on how “noncompetitively” and “cocreatively” they were finding ways to undermine the strategic plans they still believed were the best route to the company’s future success. The team’s big assumptions? “We assumed that pursuing the target-market strategy, with each of us taking aggressive responsibility for a given segment, would create the ‘silos’ we have long happily avoided and would leave us more isolated from one another. We also assumed the strategy would make us more competitively disposed toward one another.” Whether or not the assumptions were true, they would have continued to block the group’s efforts until they were brought to light. In fact, as the group came to discover, there were a variety of moves that would allow the leadership team to preserve a genuinely collaborative collegiality while pursuing the new corporate strategy.

Why was Helen unable to change her behavior? After intense self-examination in a workshop with several of her colleagues, she came to an unexpected conclusion: Although she truly wanted the project to succeed, she had an accompanying, unacknowledged commitment to maintaining a subordinate position in relation to Andrew. At a deep level, Helen was concerned that if she succeeded in her new role—one she was excited about and eager to undertake—she would become more a peer than a subordinate. She was uncertain whether Andrew was prepared for the turn their relationship would take. Worse, a promotion would mean that she, not Andrew, would be ultimately accountable for the results of her work—and Helen feared she wouldn’t be up to the task.

These stories shed some light on the nature of immunity to change. The

inconsistencies between John's and Helen's stated goals and their actions reflect neither hypocrisy nor unspoken reluctance to change but the paralyzing effect of competing commitments. Any manager who seeks to help John communicate more effectively or Helen move her project forward, without understanding that each is also struggling unconsciously toward an opposing agenda, is shoveling sand against the tide.

Diagnosing Immunity to Change

Competing commitments aren't distressing only to the boss; they're frustrating to employees as well. People with the most sincere intentions often unwittingly create for themselves Sisyphean tasks. And they are almost always tremendously relieved when they discover just why they feel as if they are rolling a boulder up a hill only to have it roll back down again. Even though uncovering a competing commitment can open up a host of new concerns, the discovery offers hope for finally accomplishing the primary, stated commitment.

Based on the past 15 years of working with hundreds of managers in a variety of companies, we've developed a three-stage process to help organizations figure out what's getting in the way of change. First, managers guide employees through a set of questions designed to uncover competing commitments. Next, employees examine these commitments to determine the underlying assumptions at their core. And finally, employees start the process of changing their behavior.

We'll walk through the process fairly quickly below, but it's important to note that each step will take time. Just uncovering the competing commitment will require at least two or three hours, because people need to reflect on each question and the implications of their answers. The process of challenging competing commitments and making real progress toward overcoming immunity to change unfolds over a longer period—weeks or even months. But just getting the commitments on the table can have a noticeable effect on the decisions people make and the actions they take.

A diagnostic test for immunity to change

The most important steps in diagnosing immunity to change are uncovering employees' competing commitments and unearthing their big assumptions.

To do so, we ask a series of questions and record key responses in a simple grid. Below we've listed the responses for six people who went through this exercise, including the examples described in the text. The grid paints a picture of the change-immunity system, making sense of a previously puzzling dynamic.

	Stated commitment I am committed to . . .	What am I doing, or not doing, that is keeping my stated commitment from being fully realized?	Competing commitments	Big assumptions
John	. . .high quality communication with my colleagues.	Sometimes I use sarcastic humor to get my point across.	I am committed to maintaining a distance from my white colleagues.	I assume I will lose my authentic connection to my racial group if I get too integrated into the mainstream.
Helen	. . .the new initiative.	I don't push for top performance from my team members or myself; I accept mediocre products and thinking too often; I don't prioritize.	I am committed to not upsetting my relationship with my boss by leaving the mentee role.	I assume my boss will stop supporting me if I move toward becoming his peer; I assume that I don't have what it takes to successfully carry out a cutting-edge project.

Tom	...hearing from my subordinates and maximizing the flow of information into my office.	I don't ask questions or ask to be kept in the loop on sensitive or delicate matters; I shoot the messenger when I hear bad news.	I am committed to not learning about things I can't do anything about.	I assume as a leader I should be able to address all problems; I assume I will be seen as incompetent if I can't solve all problems that come up.
Mary	...distributed leadership by enabling people to make decisions.	I don't delegate enough; I don't pass on the necessary information to the people I distribute leadership to.	I am committed to having things go my way, to being in control, and to ensuring that the work is done to my high standards.	I assume that other people will waste my time and theirs if I don't step in; I assume others aren't as smart as I am.
Bill	...being a team player.	I don't collaborate enough; I make unilateral decisions too often; I don't really take people's input into account.	I am committed to being the one who gets the credit and to avoiding the frustration or conflict that comes with collaboration.	I assume that no one will appreciate me if I am not seen as the source of success; I assume nothing good will come of my being frustrated or in conflict.
Jane	...turning around my department.	Too often I let things slide; I'm not proactive enough in getting people to follow through with their tasks.	I am committed to not setting full sail until I have a clear map of how we get our department from here to there.	I assume that if I take my group out into deep waters and discover I am unable to get us to the other side, I will be seen as an incompetent leader who is undeserving of trust or responsibility.

Uncovering Competing Commitments

Overcoming immunity to change starts with uncovering competing commitments. In our work, we've found that even though people keep their competing commitments well hidden, you can draw them out by asking a series of questions—as long as the employees believe that personal and potentially embarrassing disclosures won't be used inappropriately. It can be very powerful to guide people through this diagnostic exercise in a group—typically with several volunteers making their own discoveries public—so people can see that others, even the company's star performers, have competing commitments and inner contradictions of their own.

The first question we ask is, *What would you like to see changed at work, so that you could be more effective or so that work would be more satisfying?* Responses to this question are nearly always couched in a complaint—a form of communication that most managers bemoan because of its negative, unproductive tone. But complaints can be immensely useful. People complain only about the things they care about, and they complain the loudest about the things they care about most. With little effort, people can turn their familiar, uninspiring gripes into something that's more likely to energize and motivate them—a commitment, genuinely their own.

To get there, you need to ask a second question: *What commitments does your complaint imply?* A project leader we worked with, we'll call him Tom, had grumbled, "My subordinates keep me out of the loop on important developments in my project." This complaint yielded the statement, "I believe in open and candid communication." A line manager we'll call Mary lamented people's unwillingness to speak up at meetings; her complaint implied a commitment to shared decision making.

While undoubtedly sincere in voicing such commitments, people can nearly always identify some way in which they are in part responsible for preventing them from being fulfilled. Thus, the third question is: *What are you doing, or not doing, that is keeping your commitment from being more fully realized?* Invariably, in our experience, people can identify these

undermining behaviors in just a couple of seconds. For example, Tom admitted: “When people bring me bad news, I tend to shoot the messenger.” And Mary acknowledged that she didn’t delegate much and that she sometimes didn’t release all the information people needed in order to make good decisions.

In both cases, there may well have been other circumstances contributing to the shortfalls, but clearly both Tom and Mary were engaging in behavior that was affecting the people around them. Most people recognize this about themselves right away and are quick to say, “I need to stop doing that.” Indeed, Tom had repeatedly vowed to listen more openly to potential problems that would slow his projects. However, the purpose of this exercise is not to make these behaviors disappear—at least not now. The purpose is to understand why people behave in ways that undermine their own success.

The next step, then, is to invite people to consider the consequences of forgoing the behavior. We do this by asking a fourth question: *If you imagine doing the opposite of the undermining behavior, do you detect in yourself any discomfort, worry, or vague fear?* Tom imagined himself listening calmly and openly to some bad news about a project and concluded, “I’m afraid I’ll hear about a problem that I can’t fix, something that I can’t do anything about.” And Mary? She considered allowing people more latitude and realized that, quite frankly, she feared people wouldn’t make good decisions and she would be forced to carry out a strategy she thought would lead to an inferior result.

The final step is to transform that passive fear into a statement that reflects an active commitment to preventing certain outcomes. We ask, *By engaging in this undermining behavior, what worrisome outcome are you committed to preventing?* The resulting answer is the competing commitment, which lies at the very heart of a person’s immunity to change. Tom admitted, “I am committed to not learning about problems I can’t fix.” By intimidating his staff, he prevented them from delivering bad news, protecting himself from the fear that he was not in control of the project. Mary, too, was protecting herself—in her case, against the consequences of bad decisions. “I am committed to making sure my group does not make decisions that I don’t like.”

Such revelations can feel embarrassing. While primary commitments nearly always reflect noble goals that people would be happy to shout from the rooftops, competing commitments are very personal, reflecting

vulnerabilities that people fear will undermine how they are regarded both by others and themselves. Little wonder people keep them hidden and hasten to cover them up again once they're on the table.

But competing commitments should not be seen as weaknesses. They represent some version of self-protection, a perfectly natural and reasonable human impulse. The question is, if competing commitments are a form of self-protection, what are people protecting themselves from? The answers usually lie in what we call their *big assumptions*—deeply rooted beliefs about themselves and the world around them. These assumptions put an order to the world and at the same time suggest ways in which the world can go out of order. Competing commitments arise from these assumptions, driving behaviors unwittingly designed to keep the picture intact.

Examining the Big Assumption

People rarely realize they hold big assumptions because, quite simply, they accept them as reality. Often formed long ago and seldom, if ever, critically examined, big assumptions are woven into the very fabric of people's existence. (For more on the grip that big assumptions hold on people, see the sidebar "Big Assumptions: How Our Perceptions Shape Our Reality.") But with a little help, most people can call them up fairly easily, especially once they've identified their competing commitments. To do this, we first ask people to create the beginning of a sentence by inverting the competing commitment, and then we ask them to fill in the blank. For Tom ("I am committed to not hearing about problems I can't fix"), the big assumption turned out to be, "I assume that if I *did* hear about problems I can't fix, people would discover I'm not qualified to do my job." Mary's big assumption was that her teammates weren't as smart or experienced as she and that she'd be wasting her time and others' if she didn't maintain control. Returning to our earlier story, John's big assumption might be, "I assume that if I develop unambivalent relationships with my white coworkers, I will sacrifice my racial identity and alienate my own community."

This is a difficult process, and it doesn't happen all at once, because admitting to big assumptions makes people uncomfortable. The process can put names to very personal feelings people are reluctant to disclose, such as deep-seated fears or insecurities, highly discouraging or simplistic views of human nature, or perceptions of their own superior abilities or intellect. Unquestioning acceptance of a big assumption anchors and sustains an immune system: A competing commitment makes all the sense in the world, and the person continues to engage in behaviors that support it, albeit unconsciously, to the detriment of his or her "official," stated commitment. Only by bringing big assumptions to light can people finally challenge their assumptions and recognize why they are engaging in seemingly contradictory behavior.

Big Assumptions: How Our Perceptions Shape Our Reality

BIG ASSUMPTIONS REFLECT the very human manner in which we invent or shape a picture of the world and then take our inventions for reality. This is easiest to see in children. The delight we take in their charming distortions is a kind of celebration that they are actively making sense of the world, even if a bit eccentrically. As one story goes, two youngsters had been learning about Hindu culture and were taken with a representation of the universe in which the world sits atop a giant elephant, and the elephant sits atop an even more giant turtle. “I wonder what the turtle sits on,” says one of the children. “I think from then on,” says the other, “it’s turtles all the way down.”

But deep within our amusement may lurk a note of condescension, an implication that this is what distinguishes children from grown-ups. Their meaning-making is subject to youthful distortions, we assume. Ours represents an accurate map of reality.

But does it? Are we really finished discovering, once we have reached adulthood, that our maps don’t match the territory? The answer is clearly no. In our 20 years of longitudinal and cross-sectional research, we’ve discovered that adults must grow into and out of several qualitatively different views of the world if they are to master the challenges of their life experiences (see Robert Kegan, *In Over Our Heads*, Harvard University Press, 1994).

A woman we met from Australia told us about her experience living in the United States for a year. “Not only do you drive on the wrong side of the street over here,” she said, “your steering wheels are on the wrong side, too. I would routinely pile into the right side of the car to drive off, only to discover I needed to get out and walk over to the other side.

“One day,” she continued, “I was thinking about six different things, and I got into the right side of the car, took out my keys, and was prepared to drive off. I looked up and thought to myself, ‘My God, here in the violent and lawless United States, they are even stealing *steering wheels!*’”

Of course, the countervailing evidence was just an arm’s length to her left,

but—and this is the main point—*why should she look?* Our big assumptions create a disarming and deluding sense of certainty. If we know where a steering wheel belongs, we are unlikely to look for it some place else. If we know what our company, department, boss, or subordinate can and can't do, why should we look for countervailing data—even if it is just an arm's length away?

Questioning the Big Assumption

Once people have identified their competing commitments and the big assumptions that sustain them, most are prepared to take some immediate action to overcome their immunity. But the first part of the process involves observation, not action, which can be frustrating for high achievers accustomed to leaping into motion to solve problems. Let's take a look at the steps in more detail.

Step 1: Notice and record current behavior

Employees must first take notice of what does and doesn't happen as a consequence of holding big assumptions to be true. We specifically ask people *not* to try to make any changes in their thinking or behavior at this time but just to become more aware of their actions in relation to their big assumptions. This gives people the opportunity to develop a better appreciation for how and in what contexts big assumptions influence their lives. John, for example, who had assumed that working well with his white colleagues would estrange him from his ethnic group, saw that he had missed an opportunity to get involved in an exciting, high-profile initiative because he had mocked the idea when it first came up in a meeting.

Step 2: Look for contrary evidence

Next, employees must look actively for experiences that might cast doubt on the validity of their big assumptions. Because big assumptions are held as fact, they actually inform what people see, leading them to systematically (but unconsciously) attend to certain data and avoid or ignore other data. By asking people to search specifically for experiences that would cause them to question their assumptions, we help them see that they have filtering out certain types of information—information that could weaken the grip of the big assumptions.

When John looked around him, he considered for the first time that an African-American manager in another department had strong working relationships with her mostly white colleagues, yet seemed not to have compromised her personal identity. He also had to admit that when he had been thrown onto an urgent task force the year before, he had worked many hours alongside his white colleagues and found the experience satisfying; he had felt of his usual ambivalence.

Step 3: Explore the history

In this step, we people to become the “biographers” of their assumptions: How and when did the assumptions first take hold? How long have they been around? What have been some of their critical turning points?

Typically, this step leads people to earlier life experiences, almost always to times before their current jobs and relationships with current coworkers. This reflection usually makes people dissatisfied with the foundations of their big assumptions, especially when they see that these have accompanied them to their current positions and have been coloring their experiences for many years. Recently, a CEO expressed astonishment as she realized she’d been applying the same self-protective stance in her work that she’d developed during a difficult divorce years before. Just as commonly, as was the case for John, people trace their big assumptions to early experiences with parents, siblings, or friends. Understanding the circumstances that influenced the formation of the assumptions can free people to consider whether these beliefs apply to their present selves.

Step 4: Test the assumption

This step entails creating and running a modest test of the big assumption. This is the first time we ask people to consider making changes in their behavior. Each employee should come up with a scenario and run it by a partner who serves as a sounding board. (Left to their own devices, people tend to create tests that are either too risky or so tentative that they don't actually challenge the assumption and in fact reaf-firm its validity.) After conferring with a partner, John, for instance, volunteered to join a short-term committee looking at his department's process for evaluating new product ideas. Because the team would dissolve after a month, he would be able to extricate himself fairly quickly if he grew too uncomfortable with the relationships. But the experience would force him to spend a significant amount of time with several of his white colleagues during that month and would provide him an opportunity to test his sense of the real costs of being a full team member.

Step 5: Evaluate the results

In the last step, employees evaluate the test results, evaluate the test itself, design and run new tests, and eventually question the big assumptions. For John, this meant signing up for other initiatives and making initial social overtures to white coworkers. At the same time, by engaging in volunteer efforts within his community outside of work, he made sure that his ties to his racial group were not compromised.

It is worth noting that revealing a big assumption doesn't necessarily mean it will be exposed as false. But even if a big assumption does contain an element of truth, an individual can often find more effective ways to operate once he or she has had a chance to challenge the assumption and its hold on his or her behavior. Indeed, John found a way to support the essence of his competing commitment—to maintain his bond with his racial group—while minimizing behavior that sabotaged his other stated commitments.

Uncovering Your Own Immunity

As you go through this process with your employees, remember that managers are every bit as susceptible to change immunity as employees are, and your competing commitments and big assumptions can have a significant impact on the people around you. Returning once more to Helen's story: When we went through this exercise with her boss, Andrew, it turned out that he was harboring some contradictions of his own. While he was committed to the success of his subordinates, Andrew at some level assumed that he alone could meet his high standards, and as a result he was laboring under a competing commitment to maintain absolute control over his projects. He was unintentionally communicating this lack of confidence to his subordinates—including Helen—in subtle ways. In the end, Andrew's and Helen's competing commitments were, without their knowledge, mutually reinforcing, keeping Helen dependent on Andrew and allowing Andrew to control her projects.

Helen and Andrew are still working through this process, but they've already gained invaluable insight into their behavior and the ways they are impeding their own progress. This may seem like a small step, but bringing these issues to the surface and confronting them head-on is challenging and painful—yet tremendously effective. It allows managers to see, at last, what's really going on when people who are genuinely committed to change nonetheless dig in their heels. It's not about identifying unproductive behavior and systematically making plans to correct it, as if treating symptoms would cure a disease. It's not about coaxing or cajoling or even giving poor performance reviews. It's about understanding the complexities of people's behavior, guiding them through a productive process to bring their competing commitments to the surface, and helping them cope with the inner conflict that is preventing them from achieving their goals.

Cracking the Code of Change

by Michael Beer and Nitin Nohria

THE NEW ECONOMY HAS ushered in great business opportunities—and great turmoil. Not since the Industrial Revolution have the stakes of dealing with change been so high. Most traditional organizations have accepted, in theory at least, that they must either change or die. And even Internet companies such as eBay, Amazon.com, and America Online recognize that they need to manage the changes associated with rapid entrepreneurial growth. Despite some individual successes, however, change remains difficult to pull off, and few companies manage the process as well as they would like. Most of their initiatives—installing new technology, downsizing, restructuring, or trying to change corporate culture—have had low success rates. The brutal fact is that about 70% of all change initiatives fail.

In our experience, the reason for most of those failures is that in their rush to change their organizations, managers end up immersing themselves in an alphabet soup of initiatives. They lose focus and become mesmerized by all the advice available in print and on-line about why companies should change, what they should try to accomplish, and how they should do it. This proliferation of recommendations often leads to muddle when change is attempted. The result is that most change efforts exert a heavy toll, both human and economic. To improve the odds of success, and to reduce the human carnage, it is imperative that executives understand the nature and process of corporate change much better. But even that is not enough. Leaders need to crack the code of change.

For more than 40 years now, we've been studying the nature of corporate change. And although every business's change initiative is unique, our research suggests there are two archetypes, or theories, of change. These

archetypes are based on very different and often unconscious assumptions by senior executives—and the consultants and academics who advise them—about why and how changes should be made. Theory E is change based on economic value. Theory O is change based on organizational capability. Both are valid models; each theory of change achieves some of management's goals, either explicitly or implicitly. But each theory also has its costs—often unexpected ones.

Theory E change strategies are the ones that make all the headlines. In this “hard” approach to change, shareholder value is the only legitimate measure of corporate success. Change usually involves heavy use of economic incentives, drastic layoffs, downsizing, and restructuring. E change strategies are more common than O change strategies among companies in the United States, where financial markets push corporate boards for rapid turnarounds. For instance, when William A. Anders was brought in as CEO of General Dynamics in 1991, his goal was to maximize economic value—however painful the remedies might be. Over the next three years, Anders reduced the workforce by 71,000 people—44,000 through the divestiture of seven businesses and 27,000 through layoffs and attrition. Anders employed common E strategies.

Managers who subscribe to Theory O believe that if they were to focus exclusively on the price of their stock, they might harm their organizations. In this “soft” approach to change, the goal is to develop corporate culture and human capability through individual and organizational learning—the process of changing, obtaining feedback, reflecting, and making further changes. U.S. companies that adopt O strategies, as Hewlett-Packard did when its performance flagged in the 1980s, typically have strong, long-held, commitment-based psychological contracts with their employees.

Idea in Brief

Here's the brutal fact: 70% of all change initiatives fail. Why? Managers flounder in an alphabet soup of change methods, drowning in conflicting advice. Change efforts exact a heavy toll—human *and* economic—as companies flail from one change method to another.

To effect successful change, first **grasp the two basic theories of change**:

1. **Theory E** change emphasizes economic value—as measured *only* by shareholder returns. This “hard” approach boosts returns through economic incentives, drastic layoffs, and restructuring. “Chainsaw Al” Dunlop’s firing 11,000 Scott Paper employees and selling several businesses—tripling shareholder value to \$9 billion—is a stunning example.
2. **Theory O** change—a “softer” approach—focuses on developing corporate culture and human capability, patiently building trust and emotional commitment to the company through teamwork and communication.

Then, carefully and simultaneously **balance these very different approaches**. It’s not easy. Employees distrust leaders who alternate between nurturing and cutthroat behavior. But, done well, you’ll boost profits and productivity, and achieve sustainable competitive advantage.

Managers at these companies are likely to see the risks in breaking those contracts. Because they place a high value on employee commitment, Asian and European businesses are also more likely to adopt an O strategy to change.

Few companies subscribe to just one theory. Most companies we have studied have used a mix of both. But all too often, managers try to apply theories E and O in tandem without resolving the inherent tensions between them. This impulse to combine the strategies is directionally correct, but theories E and O are so different that it’s hard to manage them simultaneously—employees distrust leaders who alternate between nurturing and cutthroat corporate behavior. Our research suggests, however, that there is a way to resolve the tension so that businesses can satisfy their shareholders while building viable institutions. Companies that effectively combine hard and soft approaches to change can reap big payoffs in

profitability and productivity. Those companies are more likely to achieve a sustainable competitive advantage. They can also reduce the anxiety that grips whole societies in the face of corporate restructuring.

Idea in Practice

The UK grocery chain, ASDA, teetered on bankruptcy in 1991. Here's how CEO Archie Norman combined change Theories E and O with spectacular results: a culture of trust and openness—and an eightfold increase in shareholder value.

Change dimension	How to combine theories E and O	Examples from ASDA
Goals	Embrace the paradox between economic value and organizational capability	Norman started his tenure by stating, "Our number one objective is to secure value for our shareholders" and "We need a culture built around common ideas . . . and listening, learning, and speed of response, from the stores upwards."
Leadership	Set direction from the top and engage people from below	Norman unilaterally set a new pricing strategy and shifted power from headquarters to stores. His forthright "Tell Archie" program encouraged dialogue with all employees. He hired warm, accessible Allan Leighton to complement his own Theory O leadership style and strengthened emotional commitment to the new ASDA.
Focus	Focus on both hard and soft sides of the organization	Norman set out to win both hearts and minds. He boosted economic value through hard, structural changes, e.g., removing top layers of hierarchy and freezing all wages. He paid equal attention to the soft side by spending 75% of his early months as HR director creating a more egalitarian and transparent organization—"a great place for everyone to work."

Process	Plan for spontaneity	Norman encouraged experimentation, setting up three “risk-free” stores where employees could fail without penalty. Managers experimented with store layout, product range, employee roles. A cross-functional team redesigned ASDA’s entire retail organization—and produced significant innovations.
Reward system	Use Incentives to reinforce rather than drive change	ASDA applied Theory E incentives in an O-like way. It encouraged all employees to participate actively in changing ASDA. And it rewarded their commitment with stock ownership and variable pay based on corporate and store performance.

In this article, we will explore how one company successfully resolved the tensions between E and O strategies. But before we do that, we need to look at just how different the two theories are.

A Tale of Two Theories

To understand how sharply theories E and O differ, we can compare them along several key dimensions of corporate change: goals, leadership, focus, process, reward system, and use of consultants. (For a side-by-side comparison, see the table “Comparing theories of change.”) We’ll look at two companies in similar businesses that adopted almost pure forms of each archetype. Scott Paper successfully used Theory E to enhance shareholder value, while Champion International used Theory O to achieve a complete cultural transformation that increased its productivity and employee commitment. But as we will soon observe, both paper producers also discovered the limitations of sticking with only one theory of change. Let’s compare the two companies’ initiatives.

Goals

When Al Dunlap assumed leadership of Scott Paper in May 1994, he immediately fired 11,000 employees and sold off several businesses. His determination to restructure the beleaguered company was almost monomaniacal. As he said in one of his speeches: “Shareholders are the number one constituency. Show me an annual report that lists six or seven constituencies, and I’ll show you a mismanaged company.” From a shareholder’s perspective, the results of Dunlap’s actions were stunning. In just 20 months, he managed to triple shareholder returns as Scott Paper’s market value rose from about \$3 billion in 1994 to about \$9 billion by the end of 1995. The financial community applauded his efforts and hailed Scott Paper’s approach to change as a model for improving shareholder returns.

Champion’s reform effort couldn’t have been more different. CEO Andrew Sigler acknowledged that enhanced economic value was an appropriate target for management, but he believed that goal would be best achieved by transforming the behaviors of management, unions, and workers alike. In 1981, Sigler and other managers launched a long-term effort to restructure corporate culture around a new vision called the Champion Way, a set of values and principles designed to build up the competencies of the workforce. By improving the organization’s capabilities in areas such as teamwork and communication, Sigler believed he could best increase employee productivity and thereby improve the bottom line.

Leadership

Leaders who subscribe to Theory E manage change the old-fashioned way: from the top down. They set goals with little involvement from their management teams and certainly without input from lower levels or unions. Dunlap was clearly the commander in chief at Scott Paper. The executives who survived his purges, for example, had to agree with his philosophy that shareholder value was now the company's primary objective. Nothing made clear Dunlap's leadership style better than the nickname he gloried in: "Chainsaw Al."

By contrast, participation (a Theory O trait) was the hallmark of change at Champion. Every effort was made to get all its employees emotionally committed to improving the company's performance. Teams drafted value statements, and even the industry's unions were brought into the dialogue. Employees were encouraged to identify and solve problems themselves. Change at Champion sprouted from the bottom up.

Focus

In E-type change, leaders typically focus immediately on streamlining the “hardware” of the organization—the structures and systems. These are the elements that can most easily be changed from the top down, yielding swift financial results. For instance, Dunlap quickly decided to outsource many of Scott Paper’s corporate functions—benefits and payroll administration, almost all of its management information systems, some of its technology research, medical services, telemarketing, and security functions. An executive manager of a global merger explained the E rationale: “I have a [profit] goal of \$176 million this year, and there’s no time to involve others or develop organizational capability.”

By contrast, Theory O’s initial focus is on building up the “software” of an organization—the culture, behavior, and attitudes of employees. Throughout a decade of reforms, no employees were laid off at Champion. Rather, managers and employees were encouraged to collectively reexamine their work practices and behaviors with a goal of increasing productivity and quality. Managers were replaced if they did not conform to the new philosophy, but the overall firing freeze helped to create a culture of trust and commitment. Structural change followed once the culture changed. Indeed, by the mid-1990s, Champion had completely reorganized all its corporate functions. Once a hierarchical, functionally organized company, Champion adopted a matrix structure that empowered employee teams to focus more on customers.

Comparing theories of change

Our research has shown that all corporate transformations can be compared along the six dimensions shown here. The table outlines the differences between the E and O archetypes and illustrates what an integrated approach

might look like.

Dimensions of change	Theory E	Theory O	Theories E and O combined
Goals	Maximize shareholder value	Develop organizational capabilities	Explicitly embrace the paradox between economic value and organizational capability
Leadership	Manage change from the top down	Encourage participation from the bottom up	Set direction from the top and engage the people below
Focus	Emphasize structure and systems	Build up corporate culture: employees' behavior and attitudes	Focus simultaneously on the hard (structures and systems) and the soft (corporate culture)
Process	Plan and establish programs	Experiment and evolve	Plan for spontaneity
Reward system	Motivate through financial incentives	Motivate through commitment—use pay as fair exchange	Use incentives to reinforce change but not to drive it
Use of consultants	Consultants analyze problems and shape solutions	Consultants support management in shaping their own solutions	Consultants are expert resources who empower employees

Process

Theory E is predicated on the view that no battle can be won without a clear, comprehensive, common plan of action that encourages internal coordination and inspires confidence among customers, suppliers, and investors. The plan lets leaders quickly motivate and mobilize their businesses; it compels them to take tough, decisive actions they presumably haven't taken in the past. The changes at Scott Paper unfolded like a military battle plan. Managers were instructed to achieve specific targets by specific dates. If they didn't adhere to Dunlap's tightly choreographed marching orders, they risked being fired.

Meanwhile, the changes at Champion were more evolutionary and emergent than planned and programmatic. When the company's decade-long reform began in 1981, there was no master blueprint. The idea was that innovative work processes, values, and culture changes in one plant would be adapted and used by other plants on their way through the corporate system. No single person, not even Sigler, was seen as the driver of change. Instead, local leaders took responsibility. Top management simply encouraged experimentation from the ground up, spread new ideas to other workers, and transferred managers of innovative units to lagging ones.

Reward System

The rewards for managers in E-type change programs are primarily financial. Employee compensation, for example, is linked with financial incentives, mainly stock options. Dunlap's own compensation package—which ultimately netted him more than \$100 million—was tightly linked to shareholders' interests. Proponents of this system argue that financial incentives guarantee that employees' interests match stockholders' interests. Financial rewards also help top executives feel compensated for a difficult job—one in which they are often reviled by their onetime colleagues and the larger community.

The O-style compensation systems at Champion reinforced the goals of culture change, but they didn't drive those goals. A skills-based pay system and a corporatewide gains-sharing plan were installed to draw union workers and management into a community of purpose. Financial incentives were used only as a supplement to those systems and not to push particular reforms. While Champion did offer a companywide bonus to achieve business goals in two separate years, this came late in the change process and played a minor role in actually fulfilling those goals.

Use of Consultants

Theory E change strategies often rely heavily on external consultants. A SWAT team of Ivy League-educated MBAs, armed with an arsenal of state-of-the-art ideas, is brought in to find new ways to look at the business and manage it. The consultants can help CEOs get a fix on urgent issues and priorities. They also offer much-needed political and psychological support for CEOs who are under fire from financial markets. At Scott Paper, Dunlap engaged consultants to identify many of the painful cost-savings initiatives that he subsequently implemented.

Theory O change programs rely far less on consultants. The handful of consultants who were introduced at Champion helped managers and workers make their own business analyses and craft their own solutions. And while the consultants had their own ideas, they did not recommend any corporate program, dictate any solutions, or whip anyone into line. They simply led a process of discovery and learning that was intended to change the corporate culture in a way that could not be foreseen at the outset.

In their purest forms, both change theories clearly have their limitations. CEOs who must make difficult E-style choices understandably distance themselves from their employees to ease their own pain and guilt. Once removed from their people, these CEOs begin to see their employees as part of the problem. As time goes on, these leaders become less and less inclined to adopt O-style change strategies. They fail to invest in building the company's human resources, which inevitably hollows out the company and saps its capacity for sustained performance. At Scott Paper, for example, Dunlap trebled shareholder returns but failed to build the capabilities needed for sustained competitive advantage—commitment, coordination, communication, and creativity. In 1995, Dunlap sold Scott Paper to its longtime competitor Kimberly-Clark.

CEOs who embrace Theory O find that their loyalty and commitment to their employees can prevent them from making tough decisions. The temptation is to postpone the bitter medicine in the hopes that rising productivity will improve the business situation. But productivity gains aren't

enough when fundamental structural change is required. That reality is underscored by today's global financial system, which makes corporate performance instantly transparent to large institutional shareholders whose fund managers are under enormous pressure to show good results. Consider Champion. By 1997, it had become one of the leaders in its industry based on most performance measures. Still, newly instated CEO Richard Olsen was forced to admit a tough reality: Champion shareholders had not seen a significant increase in the economic value of the company in more than a decade. Indeed, when Champion was sold recently to Finland-based UPM-Kymmene, it was acquired for a mere 1.5 times its original share value.

Managing the Contradictions

Clearly, if the objective is to build a company that can adapt, survive, and prosper over the years, Theory E strategies must somehow be combined with Theory O strategies. But unless they're carefully handled, melding E and O is likely to bring the worst of both theories and the benefits of neither. Indeed, the corporate changes we've studied that arbitrarily and haphazardly mixed E and O techniques proved destabilizing to the organizations in which they were imposed. Managers in those companies would certainly have been better off to pick either pure E or pure O strategies—with all their costs. At least one set of stakeholders would have benefited.

The obvious way to combine E and O is to sequence them. Some companies, notably General Electric, have done this quite successfully. At GE, CEO Jack Welch began his sequenced change by imposing an E-type restructuring. He demanded that all GE businesses be first or second in their industries. Any unit that failed that test would be fixed, sold off, or closed. Welch followed that up with a massive downsizing of the GE bureaucracy. Between 1981 and 1985, total employment at the corporation dropped from 412,000 to 299,000. Sixty percent of the corporate staff, mostly in planning and finance, was laid off. In this phase, GE people began to call Welch “Neutron Jack,” after the fabled bomb that was designed to destroy people but leave buildings intact. Once he had wrung out the redundancies, however, Welch adopted an O strategy. In 1985, he started a series of organizational initiatives to change GE culture. He declared that the company had to become “boundaryless,” and unit leaders across the corporation had to submit to being challenged by their subordinates in open forum. Feedback and open communication eventually eroded the hierarchy. Soon Welch applied the new order to GE's global businesses.

Unfortunately for companies like Champion, sequenced change is far easier if you begin, as Welch did, with Theory E. Indeed, it is highly unlikely that E would successfully follow O because of the sense of betrayal that would involve. It is hard to imagine how a draconian program of layoffs and

downsizing can leave intact the psychological contract and culture a company has so patiently built up over the years. But whatever the order, one sure problem with sequencing is that it can take a very long time; at GE it has taken almost two decades. A sequenced change may also require two CEOs, carefully chosen for their contrasting styles and philosophies, which may create its own set of problems. Most turnaround managers don't survive restructuring—partly because of their own inflexibility and partly because they can't live down the distrust that their ruthlessness has earned them. In most cases, even the best-intentioned effort to rebuild trust and commitment rarely overcomes a bloody past. Welch is the exception that proves the rule.

So what should you do? How can you achieve rapid improvements in economic value while simultaneously developing an open, trusting corporate culture? Paradoxical as those goals may appear, our research shows that it is possible to apply theories E and O together. It requires great will, skill—and wisdom. But precisely because it is more difficult than mere sequencing, the simultaneous use of O and E strategies is more likely to be a source of sustainable competitive advantage.

One company that exemplifies the reconciliation of the hard and soft approaches is ASDA, the UK grocery chain that CEO Archie Norman took over in December 1991, when the retailer was nearly bankrupt. Norman laid off employees, flattened the organization, and sold off losing businesses—acts that usually spawn distrust among employees and distance executives from their people. Yet during Norman's eight-year tenure as CEO, ASDA also became famous for its atmosphere of trust and openness. It has been described by executives at Wal-Mart—itsself famous for its corporate culture—as being “more like Wal-Mart than we are.” Let's look at how ASDA resolved the conflicts of E and O along the six main dimensions of change.

Explicitly confront the tension between E and O goals

With his opening speech to ASDA's executive team—none of whom he had met—Norman indicated clearly that he intended to apply both E and O strategies in his change effort. It is doubtful that any of his listeners fully understood him at the time, but it was important that he had no conflicts about recognizing the paradox between the two strategies for change. He said as much in his maiden speech: “Our number one objective is to secure value for our shareholders and secure the trading future of the business. I am not coming in with any magical solutions. I intend to spend the next few weeks listening and forming ideas for our precise direction....We need a culture built around common ideas and goals that include listening, learning, and speed of response, from the stores upwards. [But] there will be management reorganization. My objective is to establish a clear focus on the stores, shorten lines of communication, and build one team.” If there is a contradiction between building a high-involvement organization and restructuring to enhance shareholder value, Norman embraced it.

Set direction from the top and engage people below

From day one, Norman set strategy without expecting any participation from below. He said ASDA would adopt an everyday-low-pricing strategy, and Norman unilaterally determined that change would begin by having two experimental store formats up and running within six months. He decided to shift power from the headquarters to the stores, declaring: “I want everyone to be close to the stores. We must love the stores to death; that is our business.” But even from the start, there was an O quality to Norman’s leadership style. As he put it in his first speech: “First, I am forthright, and I like to argue. Second, I want to discuss issues as colleagues. I am looking for your advice and your disagreement.” Norman encouraged dialogue with employees and customers through colleague and customer circles. He set up a “Tell Archie” program so that people could voice their concerns and ideas.

Making way for opposite leadership styles was also an essential ingredient to Norman’s—and ASDA’s—success. This was most clear in Norman’s willingness to hire Allan Leighton shortly after he took over. Leighton eventually became deputy chief executive. Norman and Leighton shared the same E and O values, but they had completely different personalities and styles. Norman, cool and reserved, impressed people with the power of his mind—his intelligence and business acumen. Leighton, who is warmer and more people oriented, worked on employees’ emotions with the power of his personality. As one employee told us, “People respect Archie, but they love Allan.” Norman was the first to credit Leighton with having helped to create emotional commitment to the new ASDA. While it might be possible for a single individual to embrace opposite leadership styles, accepting an equal partner with a very different personality makes it easier to capitalize on those styles. Leighton certainly helped Norman reach out to the organization. Together they held quarterly meetings with store managers to hear their ideas, and they supplemented those meetings with impromptu talks.

Focus simultaneously on the hard and soft sides of the organization

Norman's immediate actions followed both the E goal of increasing economic value and the O goal of transforming culture. On the E side, Norman focused on structure. He removed layers of hierarchy at the top of the organization, fired the financial officer who had been part of ASDA's disastrous policies, and decreed a wage freeze for everyone—management and workers alike. But from the start, the O strategy was an equal part of Norman's plan. He bought time for all this change by warning the markets that financial recovery would take three years. Norman later said that he spent 75% of his early months at ASDA as the company's human resource director, making the organization less hierarchical, more egalitarian, and more transparent. Both Norman and Leighton were keenly aware that they had to win hearts and minds. As Norman put it to workers: "We need to make ASDA a great place for everyone to work."

Plan for spontaneity

Training programs, total-quality programs, and top-driven culture change programs played little part in ASDA's transformation. From the start, the ASDA change effort was set up to encourage experimentation and evolution. To promote learning, for example, ASDA set up an experimental store that was later expanded to three stores. It was declared a risk-free zone, meaning there would be no penalties for failure. A cross-functional task force "renewed," or redesigned, ASDA's entire retail proposition, its organization, and its managerial structure. Store managers were encouraged to experiment with store layout, employee roles, ranges of products offered, and so on. The experiments produced significant innovations in all aspects of store operations. ASDA's managers learned, for example, that they couldn't renew a store unless that store's management team was ready for new ideas. This led to an innovation called the Driving Test, which assessed whether store managers' skills in leading the change process were aligned with the intended changes. The test perfectly illustrates how E and O can come together: it bubbled up O-style from the bottom of the company, yet it bound managers in an E-type contract. Managers who failed the test were replaced.

Let incentives reinforce change, not drive it

Any synthesis of E and O must recognize that compensation is a double-edged sword. Money can focus and motivate managers, but it can also hamper teamwork, commitment, and learning. The way to resolve this dilemma is to apply Theory E incentives in an O way. Employees' high involvement is encouraged to develop their commitment to change, and variable pay is used to reward that commitment. ASDA's senior executives were compensated with stock options that were tied to the company's value. These helped attract key executives to ASDA. Unlike most E-strategy companies, however, ASDA had a stock-ownership plan for all employees. In addition, store-level employees got variable pay based on both corporate performance and their stores' records. In the end, compensation represented a fair exchange of value between the company and its individual employees. But Norman believed that compensation had not played a major role in motivating change at the company.

Use consultants as expert resources who empower employees

Consultants can provide specialized knowledge and technical skills that the company doesn't have, particularly in the early stages of organizational change. Management's task is figuring out how to use those resources without abdicating leadership of the change effort. ASDA followed the middle ground between Theory E and Theory O. It made limited use of four consulting firms in the early stages of its transformation. The consulting firms always worked alongside management and supported its leadership of change. However, their engagement was intentionally cut short by Norman to prevent ASDA and its managers from becoming dependent on the consultants. For example, an expert in store organization was hired to support the task force assigned to renew ASDA's first few experimental stores, but later stores were renewed without his involvement.

By embracing the paradox inherent in simultaneously employing E and O change theories, Norman and Leighton transformed ASDA to the advantage of its shareholders and employees. The organization went through personnel changes, unit sell-offs, and hierarchical upheaval. Yet these potentially destructive actions did not prevent ASDA's employees from committing to change and the new corporate culture because Norman and Leighton had won employees' trust by constantly listening, debating, and being willing to learn. Candid about their intentions from the outset, they balanced the tension between the two change theories.

Change Theories in the New Economy

Historically, the study of change has been restricted to mature, large companies that needed to reverse their competitive declines. But the arguments we have advanced in this article also apply to entrepreneurial

companies that need to manage rapid growth. Here, too, we believe that the most successful strategy for change will be one that combines theories E and O.

Just as there are two ways of changing, so there are two kinds of entrepreneurs. One group subscribes to an ideology akin to Theory E. Their primary goal is to prepare for a cash-out, such as an IPO or an acquisition by an established player. Maximizing market value before the cash-out is their sole and abiding purpose. These entrepreneurs emphasize shaping the firm's strategy, structure, and systems to build a quick, strong market presence. Mercurial leaders who drive the company using a strong top-down style are typically at the helm of such companies. They lure others to join them using high-powered incentives such as stock options. The goal is to get rich quick.

Other entrepreneurs, however, are driven by an ideology more akin to Theory O—the building of an institution. Accumulating wealth is important, but it is secondary to creating a company that is based on a deeply held set of values and that has a strong culture. These entrepreneurs are likely to subscribe to an egalitarian style that invites everyone's participation. They look to attract others who share their passion about the cause—though they certainly provide generous stock options as well. The goal in this case is to make a difference, not just to make money.

Many people fault entrepreneurs who are driven by a Theory E view of the world. But we can think of other entrepreneurs who have destroyed businesses because they were overly wrapped up in the Theory O pursuit of a higher ideal and didn't pay attention to the pragmatics of the market. Steve Jobs's venture, Next, comes to mind. Both types of entrepreneurs have to find some way of tapping the qualities of theories E and O, just as large companies do.

By 1999, the company had multiplied shareholder value eightfold. The organizational capabilities built by Norman and Leighton also gave ASDA the sustainable competitive advantage that Dunlap had been unable to build at Scott Paper and that Sigler had been unable to build at Champion. While Dunlap was forced to sell a demoralized and ineffective organization to

Kimberly-Clark, and while a languishing Champion was sold to UPM-Kymmene, Norman and Leighton in June 1999 found a friendly and culturally compatible suitor in Wal-Mart, which was willing to pay a substantial premium for the organizational capabilities that ASDA had so painstakingly developed.

In the end, the integration of theories E and O created major change—and major payoffs—for ASDA. Such payoffs are possible for other organizations that want to develop a sustained advantage in today's economy. But that advantage can come only from a constant willingness and ability to develop organizations for the long term combined with a constant monitoring of shareholder value—E dancing with O, in an unending minuet.

Originally published in May 2000. Reprint R00301

The Hard Side of Change Management

by Harold L. Sirkin, Perry Keenan, and Alan Jackson

WHEN FRENCH NOVELIST JEAN-BAPTISTE Alphonse Karr wrote “*Plus ça change, plus c’est la même chose*,” he could have been penning an epigram about change management. For over three decades, academics, managers, and consultants, realizing that transforming organizations is difficult, have dissected the subject. They’ve sung the praises of leaders who communicate vision and walk the talk in order to make change efforts succeed. They’ve sanctified the importance of changing organizational culture and employees’ attitudes. They’ve teased out the tensions between top-down transformation efforts and participatory approaches to change. And they’ve exhorted companies to launch campaigns that appeal to people’s hearts and minds. Still, studies show that in most organizations, two out of three transformation initiatives fail. The more things change, the more they stay the same.

Managing change is tough, but part of the problem is that there is little agreement on what factors most influence transformation initiatives. Ask five executives to name the one factor critical for the success of these programs, and you’ll probably get five different answers. That’s because each manager looks at an initiative from his or her viewpoint and, based on personal experience, focuses on different success factors. The experts, too, offer different perspectives. A recent search on Amazon.com for books on “change and management” turned up 6,153 titles, each with a distinct take on the topic. Those ideas have a lot to offer, but taken together, they force companies to tackle many priorities simultaneously, which spreads resources and skills thin. Moreover, executives use different approaches in different parts of the organization, which compounds the turmoil that usually accompanies change.

In recent years, many change management gurus have focused on soft issues, such as culture, leadership, and motivation. Such elements are important for success, but managing these aspects alone isn't sufficient to implement transformation projects. Soft factors don't directly influence the outcomes of many change programs. For instance, visionary leadership is often vital for transformation projects, but not always. The same can be said about communication with employees. Moreover, it isn't easy to change attitudes or relationships; they're deeply ingrained in organizations and people. And although changes in, say, culture or motivation levels can be indirectly gauged through surveys and interviews, it's tough to get reliable data on soft factors.

What's missing, we believe, is a focus on the not-so-fashionable aspects of change management: the hard factors. These factors bear three distinct characteristics. First, companies are able to measure them in direct or indirect ways. Second, companies can easily communicate their importance, both within and outside organizations. Third, and perhaps most important, businesses are capable of influencing those elements quickly. Some of the hard factors that affect a transformation initiative are the time necessary to complete it, the number of people required to execute it, and the financial results that intended actions are expected to achieve. Our research shows that change projects fail to get off the ground when companies neglect the hard factors. That doesn't mean that executives can ignore the soft elements; that would be a grave mistake. However, if companies don't pay attention to the hard issues first, transformation programs will break down before the soft elements come into play.

Idea in Brief

Two out of every three transformation programs fail. Why? Companies overemphasize the soft side of change: leadership style, corporate culture, employee motivation. Though these elements are critical for success, change projects can't get off the ground unless companies address harder elements first.

The essential hard elements? Think of them as DICE:

- **Duration:** time between milestone reviews—the shorter, the better
- **Integrity:** project teams' skill
- **Commitment:** senior executives' and line managers' dedication to the program
- **Effort:** the extra work employees must do to adopt new processes—the less, the better

By assessing each DICE element *before* you launch a major change initiative, you can identify potential problem areas and make the necessary adjustments (such as reconfiguring a project team's composition or reallocating resources) to ensure the program's success. You can also use DICE *after* launching a project—to make midcourse corrections if the initiative veers off track.

DICE helps companies lay the foundation for successful change. Using the DICE assessment technique, one global beverage company executed a multiproject organization-wide change program that generated hundreds of millions of dollars, breathed new life into its once-stagnant brands, and cracked open new markets.

That's a lesson we learned when we identified the common denominators of change. In 1992, we started with the contrarian hypothesis that organizations handle transformations in remarkably similar ways. We researched projects in a number of industries and countries to identify those common elements. Our initial 225-company study revealed a consistent correlation between the outcomes (success or failure) of change programs and four hard factors: project *duration*, particularly the time between project reviews; performance *integrity*, or the capabilities of project teams; the

commitment of both senior executives and the staff whom the change will affect the most; and the additional *effort* that employees must make to cope with the change. We called these variables the DICE factors because we could load them in favor of projects' success.

Idea in Practice

Conducting a DICE Assessment

Your project has the greatest chance of success if the following hard elements are in place:

Duration

A long project reviewed frequently stands a far better chance of succeeding than a short project reviewed infrequently. Problems can be identified at the first sign of trouble, allowing for prompt corrective actions. Review complex projects every two weeks; more straightforward initiatives, every six to eight weeks.

Integrity

A change program's success hinges on a high-integrity, high-quality project team. To identify team candidates with the right portfolio of skills, solicit names from key colleagues, including top performers in functions other than your own. Recruit people who have problem-solving skills, are results oriented, and are methodical but tolerate ambiguity. Look also for organizational savvy, willingness to accept responsibility for decisions, and a disdain for the limelight.

Commitment

If employees don't see company leaders supporting a change initiative, they won't change. Visibly endorse the initiative—no amount of public support is too much. When you feel you're "talking up" a change effort at least three times more than you need to, you've hit it right.

Also continually communicate why the change is needed and what it means for employees. Ensure that all messages about the change are consistent and clear. Reach out to managers and employees through one-on-one conversations to win them over.

Effort

If adopting a change burdens employees with too much additional effort, they'll resist. Calculate how much work employees will have to do beyond their existing responsibilities to implement the change. Ensure that no one's workload increases more than 10%. If necessary, remove nonessential regular work from employees with key roles in the transformation project. Use temporary workers or outsource some processes to accommodate additional workload.

Using the DICE Framework

Conducting a DICE assessment fosters successful change by sparking valuable senior leadership debate about project strategy. It also improves change effectiveness by enabling companies to manage large portfolios of projects.

Example: A manufacturing company planned 40 projects as part of a profitability-improvement program. After conducting a DICE assessment for each project, leaders and project owners identified the five most important projects and asked, "How can we ensure these projects' success?" They moved people around on teams, reconfigured some projects, and identified initiatives senior managers should pay more attention to—setting up their most crucial projects for resounding success.

We completed our study in 1994, and in the 11 years since then, the Boston Consulting Group has used those four factors to predict the outcomes, and guide the execution, of more than 1,000 change management initiatives worldwide. Not only has the correlation held, but no other factors (or combination of factors) have predicted outcomes as well.

The Four Key Factors

If you think about it, the different ways in which organizations combine the four factors create a continuum—from projects that are set up to succeed to those that are set up to fail. At one extreme, a short project led by a skilled, motivated, and cohesive team, championed by top management and implemented in a department that is receptive to the change and has to put in very little additional effort, is bound to succeed. At the other extreme, a long, drawn-out project executed by an inexperienced, unenthusiastic, and disjointed team, without any top-level sponsors and targeted at a function that dislikes the change and has to do a lot of extra work, will fail. Businesses can easily identify change programs at either end of the spectrum, but most initiatives occupy the middle ground where the likelihood of success or failure is difficult to assess. Executives must study the four DICE factors carefully to figure out if their change programs will fly—or die.

The Four Factors

These factors determine the outcome of any transformation initiative.

- D.** The **duration** of time until the change program is completed if it has a short life span; if not short, the amount of time between reviews of milestones.
- I.** The project team's performance **integrity**; that is, its ability to complete the initiative on time. That depends on members' skills and traits relative to the project's requirements.

C. The **commitment** to change that top management (C1) and employees affected by the change (C2) display.

E. The **effort** over and above the usual work that the change initiative demands of employees.

Duration

Companies make the mistake of worrying mostly about the time it will take to implement change programs. They assume that the longer an initiative carries on, the more likely it is to fail—the early impetus will peter out, windows of opportunity will close, objectives will be forgotten, key supporters will leave or lose their enthusiasm, and problems will accumulate. However, contrary to popular perception, our studies show that a long project that is reviewed frequently is more likely to succeed than a short project that isn't reviewed frequently. Thus, the time between reviews is more critical for success than a project's life span.

Companies should formally review transformation projects at least bimonthly since, in our experience, the probability that change initiatives will run into trouble rises exponentially when the time between reviews exceeds eight weeks. Whether reviews should be scheduled even more frequently depends on how long executives feel the project can carry on without going off track. Complex projects should be reviewed fortnightly; more familiar or straightforward initiatives can be assessed every six to eight weeks.

Scheduling milestones and assessing their impact are the best way by which executives can review the execution of projects, identify gaps, and spot new risks. The most effective milestones are those that describe major actions or achievements rather than day-to-day activities. They must enable senior executives and project sponsors to confirm that the project has made progress since the last review took place. Good milestones encompass a number of tasks that teams must complete. For example, describing a particular milestone as "Consultations with Stakeholders Completed" is more effective than "Consult Stakeholders" because it represents an achievement and shows that the project has made headway. Moreover, it suggests that several activities were completed—identifying stakeholders, assessing their needs, and talking to them about the project. When a milestone looks as though it won't be reached on time, the project team must try to understand why, take corrective actions, and learn from the experience to prevent problems from recurring.

Review of such a milestone—what we refer to as a “learning milestone”—isn’t an impromptu assessment of the Monday-morning kind. It should be a formal occasion during which senior-management sponsors and the project team evaluate the latter’s performance on all the dimensions that have a bearing on success and failure. The team must provide a concise report of its progress, and members and sponsors must check if the team is on track to complete, or has finished all the tasks to deliver, the milestone. They should also determine whether achieving the milestone has had the desired effect on the company; discuss the problems the team faced in reaching the milestone; and determine how that accomplishment will affect the next phase of the project. Sponsors and team members must have the power to address weaknesses. When necessary, they should alter processes, agree to push for more or different resources, or suggest a new direction. At these meetings, senior executives must pay special attention to the dynamics within teams, changes in the organization’s perceptions about the initiative, and communications from the top.

Integrity

By performance integrity, we mean the extent to which companies can rely on teams of managers, supervisors, and staff to execute change projects successfully. In a perfect world, every team would be flawless, but no business has enough great people to ensure that. Besides, senior executives are often reluctant to allow star performers to join change efforts because regular work can suffer. But since the success of change programs depends on the quality of teams, companies must free up the best staff while making sure that day-to-day operations don't falter. In companies that have succeeded in implementing change programs, we find that employees go the extra mile to ensure their day-to-day work gets done.

Since project teams handle a wide range of activities, resources, pressures, external stimuli, and unforeseen obstacles, they must be cohesive and well led. It's not enough for senior executives to ask people at the watercooler if a project team is doing well; they must clarify members' roles, commitments, and accountability. They must choose the team leader and, most important, work out the team's composition.

Smart executive sponsors, we find, are very inclusive when picking teams. They identify talent by soliciting names from key colleagues, including human resource managers; by circulating criteria they have drawn up; and by looking for top performers in all functions. While they accept volunteers, they take care not to choose only supporters of the change initiative. Senior executives personally interview people so that they can construct the right portfolio of skills, knowledge, and social networks. They also decide if potential team members should commit all their time to the project; if not, they must ask them to allocate specific days or times of the day to the initiative. Top management makes public the parameters on which it will judge the team's performance and how that evaluation fits into the company's regular appraisal process. Once the project gets under way, sponsors must measure the cohesion of teams by administering confidential surveys to solicit members' opinions.

Executives often make the mistake of assuming that because someone is a

good, well-liked manager, he or she will also make a decent team leader. That sounds reasonable, but effective managers of the status quo aren't necessarily good at changing organizations. Usually, good team leaders have problem-solving skills, are results oriented, are methodical in their approach but tolerate ambiguity, are organizationally savvy, are willing to accept responsibility for decisions, and while being highly motivated, don't crave the limelight. A CEO who successfully led two major transformation projects in the past ten years used these six criteria to quiz senior executives about the caliber of nominees for project teams. The top management team rejected one in three candidates, on average, before finalizing the teams.

Commitment

Companies must boost the commitment of two different groups of people if they want change projects to take root: They must get visible backing from the most influential executives (what we call C1), who are not necessarily those with the top titles. And they must take into account the enthusiasm—or often, lack thereof—of the people who must deal with the new systems, processes, or ways of working (C2).

Top-level commitment is vital to engendering commitment from those at the coal face. If employees don't see that the company's leadership is backing a project, they're unlikely to change. No amount of top-level support is too much. In 1999, when we were working with the CEO of a consumer products company, he told us that he was doing much more than necessary to display his support for a nettlesome project. When we talked to line managers, they said that the CEO had extended very little backing for the project. They felt that if he wanted the project to succeed, he would have to support it more visibly! A rule of thumb: When you feel that you are talking up a change initiative at least three times more than you need to, your managers will feel that you are backing the transformation.

Sometimes, senior executives are reluctant to back initiatives. That's understandable; they're often bringing about changes that may negatively affect employees' jobs and lives. However, if senior executives do not communicate the need for change, and what it means for employees, they endanger their projects' success. In one financial services firm, top management's commitment to a program that would improve cycle times, reduce errors, and slash costs was low because it entailed layoffs. Senior executives found it gut-wrenching to talk about layoffs in an organization that had prided itself on being a place where good people could find lifetime employment. However, the CEO realized that he needed to tackle the thorny issues around the layoffs to get the project implemented on schedule. He tapped a senior company veteran to organize a series of speeches and meetings in order to provide consistent explanations for the layoffs, the timing, the consequences for job security, and so on. He also appointed a

well-respected general manager to lead the change program. Those actions reassured employees that the organization would tackle the layoffs in a professional and humane fashion.

Companies often underestimate the role that managers and staff play in transformation efforts. By communicating with them too late or inconsistently, senior executives end up alienating the people who are most affected by the changes. It's surprising how often something senior executives believe is a good thing is seen by staff as a bad thing, or a message that senior executives think is perfectly clear is misunderstood. That usually happens when senior executives articulate subtly different versions of critical messages. For instance, in one company that applied the DICE framework, scores for a project showed a low degree of staff commitment. It turned out that these employees had become confused, even distrustful, because one senior manager had said, "Layoffs will not occur," while another had said, "They are not expected to occur."

Organizations also underestimate their ability to build staff support. A simple effort to reach out to employees can turn them into champions of new ideas. For example, in the 1990s, a major American energy producer was unable to get the support of mid-level managers, supervisors, and workers for a productivity improvement program. After trying several times, the company's senior executives decided to hold a series of one-on-one conversations with mid-level managers in a last-ditch effort to win them over. The conversations focused on the program's objectives, its impact on employees, and why the organization might not be able to survive without the changes. Partly because of the straight talk, the initiative gained some momentum. This allowed a project team to demonstrate a series of quick wins, which gave the initiative a new lease on life.

Effort

When companies launch transformation efforts, they frequently don't realize, or know how to deal with the fact, that employees are already busy with their day-to-day responsibilities. According to staffing tables, people in many businesses work 80-plus-hour weeks. If, on top of existing responsibilities, line managers and staff have to deal with changes to their work or to the systems they use, they will resist.

Project teams must calculate how much work employees will have to do beyond their existing responsibilities to change over to new processes. Ideally, no one's workload should increase more than 10%. Go beyond that, and the initiative will probably run into trouble. Resources will become overstretched and compromise either the change program or normal operations. Employee morale will fall, and conflict may arise between teams and line staff. To minimize the dangers, project managers should use a simple metric like the percentage increase in effort the employees who must cope with the new ways feel they must contribute. They should also check if the additional effort they have demanded comes on top of heavy workloads and if employees are likely to resist the project because it will demand more of their scarce time.

Companies must decide whether to take away some of the regular work of employees who will play key roles in the transformation project. Companies can start by ridding these employees of discretionary or nonessential responsibilities. In addition, firms should review all the other projects in the operating plan and assess which ones are critical for the change effort. At one company, the project steering committee delayed or restructured 120 out of 250 subprojects so that some line managers could focus on top-priority projects. Another way to relieve pressure is for the company to bring in temporary workers, like retired managers, to carry out routine activities or to outsource current processes until the changeover is complete. Handing off routine work or delaying projects is costly and time-consuming, so companies need to think through such issues before kicking off transformation efforts.

Calculating DICE Scores

COMPANIES CAN DETERMINE if their change programs will succeed by asking executives to calculate scores for each of the four factors of the DICE framework—duration, integrity, commitment, and effort. They must grade each factor on a scale from 1 to 4 (using fractions, if necessary); the lower the score, the better. Thus, a score of 1 suggests that the factor is highly likely to contribute to the program's success, and a score of 4 means that it is highly unlikely to contribute to success. We find that the following questions and scoring guidelines allow executives to rate transformation initiatives effectively:

Duration [D]

Ask: Do formal project reviews occur regularly? If the project will take more than two months to complete, what is the average time between reviews?

Score: If the time between project reviews is less than two months, you should give the project 1 point. If the time is between two and four months, you should award the project 2 points; between four and eight months, 3 points; and if reviews are more than eight months apart, give the project 4 points.

Integrity of Performance [I]

Ask: Is the team leader capable? How strong are team members' skills and motivations? Do they have sufficient time to spend on the change initiative?

Score: If the project team is led by a highly capable leader who is respected by peers, if the members have the skills and motivation to complete the project in the stipulated time frame, and if the company has assigned at least 50% of the team members' time to the project, you can give the project 1 point. If the team is lacking on all those dimensions, you should award the project 4 points. If the team's capabilities are somewhere in between, assign

the project 2 or 3 points.

Senior Management Commitment [C₁]

Ask: Do senior executives regularly communicate the reason for the change and the importance of its success? Is the message convincing? Is the message consistent, both across the top management team and over time? Has top management devoted enough resources to the change program?

Score: If senior management has, through actions and words, clearly communicated the need for change, you must give the project 1 point. If senior executives appear to be neutral, it gets 2 or 3 points. If managers perceive senior executives to be reluctant to support the change, award the project 4 points.

Local-Level Commitment [C₂]

Ask: Do the employees most affected by the change understand the reason for it and believe it's worthwhile? Are they enthusiastic and supportive or worried and obstructive?

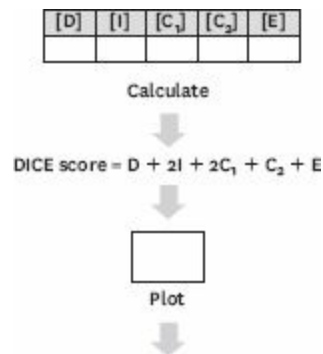
Score: If employees are eager to take on the change initiative, you can give the project 1 point, and if they are just willing, 2 points. If they're reluctant or strongly reluctant, you should award the project 3 or 4 points.

Effort [E]

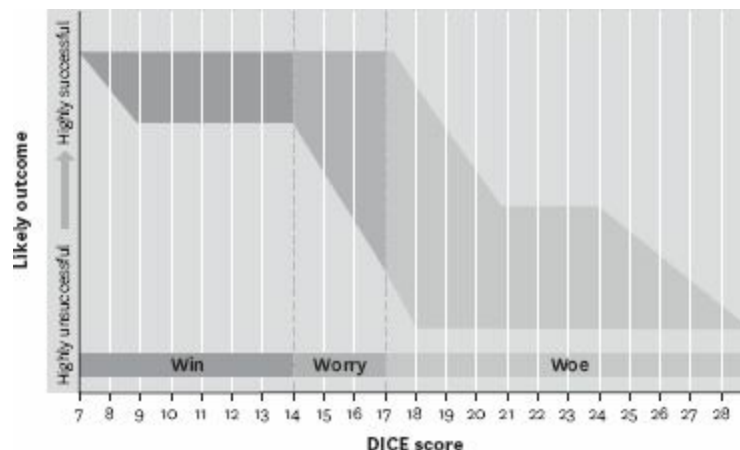
Ask: What is the percentage of increased effort that employees must make to implement the change effort? Does the incremental effort come on top of a heavy workload? Have people strongly resisted the increased demands on them?

Score: If the project requires less than 10% extra work by employees, you can give it 1 point. If it's 10% to 20% extra, it should get 2 points. If it's 20% to 40%, it must be 3 points. And if it's more than 40% additional work, you

should give the project 4 points.



Executives can combine the four elements into a project score. When we conducted a regression analysis of our database of change efforts, we found that the combination that correlates most closely with actual outcomes doubles the weight given to team performance (I) and senior management commitment (C1). That translates into the following formula:



$$\text{DICE Score} = D + (2 \times I) + (2 \times C_1) + C_2 + E$$

In the 1-to-4 scoring system, the formula generates overall scores that range from 7 to 28. Companies can compare a project's score with those of past

projects and their outcomes to assess if the project is slated for success or failure. Our data show a clear distribution of scores:

Scores between 7 and 14: The project is very likely to succeed. We call this the Win Zone.

Scores higher than 14 but lower than 17: Risks to the project's success are rising, particularly as the score approaches 17. This is the Worry Zone.

Scores over 17: The project is extremely risky. If a project scores over 17 and under 19 points, the risks to success are very high. Beyond 19, the project is unlikely to succeed. That's why we call this the Woe Zone.

We have changed the boundaries of the zones over time. For instance, the Worry Zone was between 14 and 21 points at first, and the Woe Zone from 21 to 28 points. But we found that companies prefer to be alerted to trouble as soon as outcomes become unpredictable (17 to 20 points). We therefore compressed the Worry Zone and expanded the Woe Zone.

Creating the Framework

As we came to understand the four factors better, we created a framework that would help executives evaluate their transformation initiatives and shine a spotlight on interventions that would improve their chances of success. We developed a scoring system based on the variables that affect each factor. Executives can assign scores to the DICE factors and combine them to arrive at a project score. (See the sidebar “Calculating DICE Scores.”)

Although the assessments are subjective, the system gives companies an objective framework for making those decisions. Moreover, the scoring mechanism ensures that executives are evaluating projects and making trade-offs more consistently across projects.

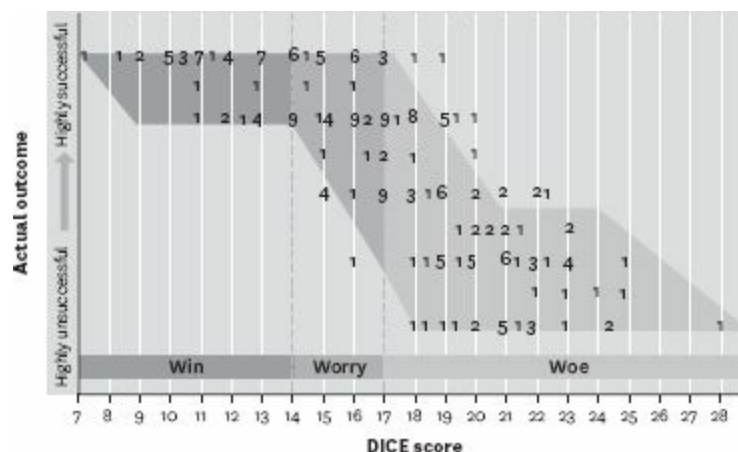
A company can compare its DICE score on the day it kicks off a project with the scores of previous projects, as well as their outcomes, to check if the initiative has been set up for success. When we calculated the scores of the 225 change projects in our database and compared them with the outcomes, the analysis was compelling. Projects clearly fell into three categories, or zones: *Win*, which means that any project with a score in that range is statistically likely to succeed; *worry*, which suggests that the project’s outcome is hard to predict; and *woe*, which implies that the project is totally unpredictable or fated for mediocrity or failure. (See the figure “DICE scores predict project outcomes.”)

Companies can track how change projects are faring by calculating scores over time or before and after they have made changes to a project’s structure. The four factors offer a litmus test that executives can use to assess the probability of success for a given project or set of projects. Consider the case of a large Australian bank that in 1994 wanted to restructure its back-office operations. Senior executives agreed on the rationale for the change but differed on whether the bank could achieve its objectives, since the transformation required major changes in processes and organizational structures. Bringing the team and the senior executives together long enough to sort out their differences proved impossible; people were just too busy.

That's when the project team decided to analyze the initiative using the DICE framework.

DICE scores predict project outcomes

When we plotted the DICE scores of 225 change management initiatives on the horizontal axis, and the outcomes of those projects on the vertical axis, we found three sets of correlations. Projects with DICE scores between 7 and 14 were usually successful; those with scores over 14 and under 17 were unpredictable; and projects with scores over 17 were usually unsuccessful. We named the three zones Win, Worry, and Woe, respectively. (Each number plotted on the graph represents the number of projects, out of the 225 projects, having a particular DICE score.)



Doing so condensed what could have been a free-flowing two-day debate into a sharp two-hour discussion. The focus on just four elements generated a clear picture of the project's strengths and weaknesses. For instance, managers learned that the restructuring would take eight months to implement but that it had poorly defined milestones and reviews. Although the project team was capable and senior management showed reasonable commitment to the effort, there was room for improvement in both areas. The

back-office workforce was hostile to the proposed changes since more than 20% of these people would lose their jobs. Managers and employees agreed that the back-office staff would need to muster 10% to 20% more effort on top of its existing commitments during the implementation. On the DICE scale, the project was deep in the Woe Zone.

However, the assessment also led managers to take steps to increase the possibility of success before they started the project. The bank decided to split the project time line into two—one short-term and one long-term. Doing so allowed the bank to schedule review points more frequently and to maximize team members' ability to learn from experience before the transformation grew in complexity. To improve staff commitment, the bank decided to devote more time to explaining why the change was necessary and how the institution would support the staff during the implementation. The bank also took a closer look at the people who would be involved in the project and changed some of the team leaders when it realized that they lacked the necessary skills. Finally, senior managers made a concerted effort to show their backing for the initiative by holding a traveling road show to explain the project to people at all levels of the organization. Taken together, the bank's actions and plans shifted the project into the Win Zone. Fourteen months later, the bank completed the project—on time and below budget.

Applying the DICE Framework

The simplicity of the DICE framework often proves to be its biggest problem; executives seem to desire more complex answers. By overlooking the obvious, however, they often end up making compromises that don't work. Smart companies try to ensure that they don't fall into that trap by using the DICE framework in one of three ways.

Track Projects

Some companies train managers in how to use the DICE framework before they start transformation programs. Executives use spreadsheet-based versions of the tool to calculate the DICE scores of the various components of the program and to compare them with past scores. Over time, every score must be balanced against the trajectory of scores and, as we shall see next, the portfolio of scores.

Senior executives often use DICE assessments as early warning indicators that transformation initiatives are in trouble. That's how Amgen, the \$10.6 billion biotechnology company, used the DICE framework. In 2001, the company realigned its operations around some key processes, broadened its offerings, relaunched some mature products, allied with some firms and acquired others, and launched several innovations. To avoid implementation problems, Amgen's top management team used the DICE framework to gauge how effectively it had allocated people, senior management time, and other resources. As soon as projects reported troubling scores, designated executives paid attention to them. They reviewed the projects more often, reconfigured the teams, and allocated more resources to them. In one area of the change project, Amgen used DICE to track 300 initiatives and reconfigured 200 of them.

Both big and small organizations can put the tool to good use. Take the case of a hospital that kicked off six change projects in the late 1990s. Each initiative involved a lot of investment, had significant clinical implications, or both. The hospital's general manager felt that some projects were going well but was concerned about others. He wasn't able to attribute his concerns to anything other than a bad feeling. However, when the general manager used the DICE framework, he was able to confirm his suspicions. After a 45-minute discussion with project managers and other key people, he established that three projects were in the Win Zone but two were in the Woe Zone and one was in the Worry Zone.

The strongest projects, the general manager found, consumed more than their fair share of resources. Senior hospital staff sensed that those projects

would succeed and spent more time promoting them, attending meetings about them, and making sure they had sufficient resources. By contrast, no one enjoyed attending meetings on projects that were performing poorly. So the general manager stopped attending meetings for the projects that were on track; he attended only sessions that related to the three underperforming ones. He pulled some managers from the projects that were progressing smoothly and moved them to the riskier efforts. He added more milestones to the struggling enterprises, delayed their completion, and pushed hard for improvement. Those steps helped ensure that all six projects met their objectives.

Manage portfolios of projects

When companies launch large transformation programs, they kick off many projects to attain their objectives. But if executives don't manage the portfolio properly, those tasks end up competing for attention and resources. For instance, senior executives may choose the best employees for projects they have sponsored or lavish attention on pet projects rather than on those that need attention. By deploying our framework before they start transformation initiatives, companies can identify problem projects in portfolios, focus execution expertise and senior management attention where it is most needed, and defuse political issues.

Take, for example, the case of an Australasian manufacturing company that had planned a set of 40 projects as part of a program to improve profitability. Since some had greater financial implications than others, the company's general manager called for a meeting with all the project owners and senior managers. The group went through each project, debating its DICE score and identifying the problem areas. After listing all the scores and issues, the general manager walked to a whiteboard and circled the five most important projects. "I'm prepared to accept that some projects will start off in the Worry Zone, though I won't accept anything outside the middle of this zone for more than a few weeks. For the top five, we're not going to start until these are well within the Win Zone. What do we have to do to achieve that?" he asked.

The group began thinking and acting right away. It moved people around on teams, reconfigured some projects, and identified those that senior managers should pay more attention to—all of which helped raise DICE scores before implementation began. The most important projects were set up for resounding success while most of the remaining ones managed to get into the Win Zone. The group left some projects in the Worry Zone, but it agreed to track them closely to ensure that their scores improved. In our experience, that's the right thing to do. When companies are trying to overhaul themselves, they shouldn't have all their projects in the Win Zone; if they do, they are not ambitious enough. Transformations should entail fundamental

changes that stretch an organization.

Force conversation

When different executives calculate DICE scores for the same project, the results can vary widely. The difference in scores is particularly important in terms of the dialogue it triggers. It provokes participants and engages them in debate over questions like “Why do we see the project in these different ways?” and “What can we agree to do to ensure that the project will succeed?” That’s critical, because even people within the same organization lack a common framework for discussing problems with change initiatives. Prejudices, differences in perspectives, and a reluctance or inability to speak up can block effective debates. By using the DICE framework, companies can create a common language and force the right discussions.

Sometimes, companies hold workshops to review floundering projects. At those two- to four-hour sessions, groups of eight to 15 senior and middle managers, along with the project team and the project sponsors, hold a candid dialogue. The debate usually moves beyond the project’s scores to the underlying causes of problems and possible remedies. The workshops bring diverse opinions to light, which often can be combined into innovative solutions. Consider, for example, the manner in which DICE workshops helped a telecommunications service provider that had planned a major transformation effort. Consisting of five strategic initiatives and 50 subprojects that needed to be up and running quickly, the program confronted some serious obstacles. The projects’ goals, time lines, and revenue objectives were unclear. There were delays in approving business cases, a dearth of rigor and focus in planning and identifying milestones, and a shortage of resources. There were leadership issues, too. For example, executive-level shortcomings had resulted in poor coordination of projects and a misjudgment of risks.

To put the transformation program on track, the telecom company incorporated DICE into project managers’ tool kits. The Project Management Office arranged a series of workshops to analyze issues and decide future steps. One workshop, for example, was devoted to three new product development projects, two of which had landed in the Woe Zone and one in

the Worry Zone. Participants traced the problems to tension between managers and technology experts, underfunding, lack of manpower, and poor definition of the projects' scopes. They eventually agreed on three remedial actions: holding a conflict-resolution meeting between the directors in charge of technology and those responsible for the core business; making sure senior leadership paid immediate attention to the resource issues; and bringing together the project team and the line-of-business head to formalize project objectives. With the project sponsor committed to those actions, the three projects had improved their DICE scores and thus their chances of success at the time this article went to press.

Conversations about DICE scores are particularly useful for large-scale transformations that cut across business units, functions, and locations. In such change efforts, it is critical to find the right balance between centralized oversight, which ensures that everyone in the organization takes the effort seriously and understands the goals, and the autonomy that various initiatives need. Teams must have the flexibility and incentive to produce customized solutions for their markets, functions, and competitive environments. The balance is difficult to achieve without an explicit consideration of the DICE variables.

Take the case of a leading global beverage company that needed to increase operational efficiency and focus on the most promising brands and markets. The company also sought to make key processes such as consumer demand development and customer fulfillment more innovative. The CEO's goals were ambitious and required investing significant resources across the company. Top management faced enormous challenges in structuring the effort and in spawning projects that focused on the right issues. Executives knew that this was a multiyear effort, yet without tight schedules and oversight of individual projects, there was a risk that projects would take far too long to be completed and the results would taper off.

To mitigate the risks, senior managers decided to analyze each project at several levels of the organization. Using the DICE framework, they reviewed each effort every month until they felt confident that it was on track. After that, reviews occurred when projects met major milestones. No more than two months elapsed between reviews, even in the later stages of the program. The time between reviews at the project-team level was even shorter: Team leaders reviewed progress biweekly throughout the transformation. Some of the best people joined the effort full time. The human resources department

took an active role in recruiting team members, thereby creating a virtuous cycle in which the best people began to seek involvement in various initiatives. During the course of the transformation, the company promoted several team members to line- and functional leadership positions because of their performance.

The company's change program resulted in hundreds of millions of dollars of value creation. Its once-stagnant brands began to grow, it cracked open new markets such as China, and sales and promotion activities were aligned with the fastest-growing channels. There were many moments during the process when inertia in the organization threatened to derail the change efforts. However, senior management's belief in focusing on the four key variables helped move the company to a higher trajectory of performance.

By providing a common language for change, the DICE framework allows companies to tap into the insight and experience of their employees. A great deal has been said about middle managers who want to block change. We find that most middle managers are prepared to support change efforts even if doing so involves additional work and uncertainty and puts their jobs at risk. However, they resist change because they don't have sufficient input in shaping those initiatives. Too often, they lack the tools, the language, and the forums in which to express legitimate concerns about the design and implementation of change projects. That's where a standard, quantitative, and simple framework comes in. By enabling frank conversations at all levels within organizations, the DICE framework helps people do the right thing by change.

Originally published in October 2005. Reprint R0510G

Why Change Programs Don't Produce Change

by Michael Beer, Russell A. Eisenstat, and Bert Spector

IN THE MID-1980S, THE NEW CEO of a major international bank—call it U.S. Financial—announced a companywide change effort. Deregulation was posing serious competitive challenges—challenges to which the bank's traditional hierarchical organization was ill-suited to respond. The only solution was to change fundamentally how the company operated. And the place to begin was at the top.

The CEO held a retreat with his top 15 executives where they painstakingly reviewed the bank's purpose and culture. He published a mission statement and hired a new vice president for human resources from a company well-known for its excellence in managing people. And in a quick succession of moves, he established companywide programs to push change down through the organization: a new organizational structure, a performance appraisal system, a pay-for-performance compensation plan, training programs to turn managers into “change agents,” and quarterly attitude surveys to chart the progress of the change effort.

As much as these steps sound like a textbook case in organizational transformation, there was one big problem: two years after the CEO launched the change program, virtually nothing in the way of actual changes in organizational behavior had occurred. What had gone wrong?

The answer is “everything.” Every one of the assumptions the CEO made—about who should lead the change effort, what needed changing, and how to go about doing it—was wrong.

U.S. Financial's story reflects a common problem. Faced with changing markets and increased competition, more and more companies are struggling to reestablish their dominance, regain market share, and in some cases,

ensure their survival. Many have come to understand that the key to competitive success is to transform the way they function. They are reducing reliance on managerial authority, formal rules and procedures, and narrow divisions of work. And they are creating teams, sharing information, and delegating responsibility and accountability far down the hierarchy. In effect, companies are moving from the hierarchical and bureaucratic model of organization that has characterized corporations since World War II to what we call the task-driven organization where what has to be done governs who works with whom and who leads.

But while senior managers understand the necessity of change to cope with new competitive realities, they often misunderstand what it takes to bring it about. They tend to share two assumptions with the CEO of U.S. Financial: that promulgating companywide programs—mission statements, “corporate culture” programs, training courses, quality circles, and new pay-for-performance systems—will transform organizations, and that employee behavior is changed by altering a company’s formal structure and systems.

In a four-year study of organizational change at six large corporations (see the sidebar, “Tracking Corporate Change”; the names are fictitious), we found that exactly the opposite is true: the greatest obstacle to revitalization is the idea that it comes about through companywide change programs, particularly when a corporate staff group such as human resources sponsors them. We call this “the fallacy of programmatic change.” Just as important, formal organization structure and systems cannot lead a corporate renewal process.

While in some companies, wave after wave of programs rolled across the landscape with little positive impact, in others, more successful transformations did take place. They usually started at the periphery of the corporation in a few plants and divisions far from corporate headquarters. And they were led by the general managers of those units, not by the CEO or corporate staff people.

Idea in Brief

Two years after launching a change program to counter competitive threats, a bank CEO realized his effort had produced...no change.

Surprising, since he and his top executives had reviewed the company's purpose and culture, published a mission statement, and launched programs (e.g., pay for-performance compensation) designed to push change throughout the organization.

But revitalization doesn't come from the top. It starts at an organization's periphery, led by unit managers creating ad hoc arrangements to solve concrete problems. Through **task alignment**—directing employees' responsibilities and relationships toward the company's central competitive task—these managers focus energy on *work*, not abstractions like “empowerment” or “culture.”

Senior managers' role in this process? Specify the company's desired *general* direction, without dictating solutions. Then spread the lessons of revitalized units throughout the company.

The general managers did not focus on formal structures and systems; they created ad hoc organizational arrangements to solve concrete business problems. By aligning employee roles, responsibilities, and relationships to address the organization's most important competitive task—a process we call “task alignment”—they focused energy for change on the work itself, not on abstractions such as “participation” or “culture.” Unlike the CEO at U.S. Financial, they didn't employ massive training programs or rely on speeches and mission statements. Instead, we saw that general managers carefully developed the change process through a sequence of six basic managerial interventions.

Once general managers understand the logic of this sequence, they don't have to wait for senior management to start a process of organizational revitalization. There is a lot they can do even without support from the top. Of course, having a CEO or other senior managers who are committed to change does make a difference—and when it comes to changing an entire organization, such support is essential. But top management's role in the change process is very different from that which the CEO played at U.S. Financial.

Idea in Practice

Successful change requires commitment, coordination, and competency.

1. Mobilize commitment to change through joint diagnosis of problems

Example: Navigation Devices had never made a profit or high-quality, cost-competitive product—because top-down decisions ignored cross-functional coordination. To change this, a new general manager had his *entire* team broadly assess the business. Then, his task force of engineers, production workers, managers, and union officials visited successful manufacturing organizations to identify improvement ideas. One plant's *team* approach impressed them, illuminated their own problem, and suggested a solution. Commitment to change intensified.

2. Develop a shared vision of how to organize for competitiveness

Remove functional and hierarchical barriers to information sharing and problem solving—by changing roles and responsibilities, not titles or compensation.

Example: Navigation's task force proposed developing products through cross-functional teams. A larger team refined this model and presented it to all employees—who supported it because it stemmed from their own analysis of their business problems.

3. Foster consensus for the new vision, competence to enact it, and cohesion to advance it

This requires the general manager's strong leadership.

Example: Navigation's general manager fostered *consensus* by supporting those who were committed to change and offering

outplacement and counseling to those who weren't; *competence* by providing requested training; and *cohesion* by redeploying managers who couldn't function in the new organization. Change accelerated.

4. Spread revitalization to all departments—without pushing from the top

Example: Navigation's new team structure required engineers to collaborate with production workers. Encouraged to develop their own approach to teamwork and coordination, the engineers selected matrix management. People willingly learned needed skills and attitudes, because the new structure was *their* choice.

5. Institutionalize revitalization through formal policies, systems, and structures . . . only *after* your new approach is up and running.

Example: Navigation boosted its profits—without changing reporting relationships, evaluation procedures, or compensation. Only then did the general manager alter formal structures; e.g., eliminating a VP so that engineering and manufacturing reported directly to him.

6. Monitor the revitalization process, adjusting in response to problems

Example: At Navigation, an oversight team of managers, a union leader, an engineer, and a financial analyst kept watch over the change process—continually learning, adapting, and strengthening the commitment to change.

Grass-roots change presents senior managers with a paradox: directing a “nondirective” change process. The most effective senior managers in our study recognized their limited power to mandate corporate renewal from the top. Instead, they defined their roles as creating a climate for change, then

spreading the lessons of both successes and failures. Put another way, they specified the general direction in which the company should move without insisting on specific solutions.

In the early phases of a companywide change process, any senior manager can play this role. Once grass-roots change reaches a critical mass, however, the CEO has to be ready to transform his or her own work unit as well—the top team composed of key business heads and corporate staff heads. At this point, the company's structure and systems must be put into alignment with the new management practices that have developed at the periphery. Otherwise, the tension between dynamic units and static top management will cause the change process to break down.

We believe that an approach to change based on task alignment, starting at the periphery and moving steadily toward the corporate core, is the most effective way to achieve enduring organizational change. This is not to say that change can never start at the top, but it is uncommon and too risky as a deliberate strategy. Change is about learning. It is a rare CEO who knows in advance the fine-grained details of organizational change that the many diverse units of a large corporation demand. Moreover, most of today's senior executives developed in an era in which top-down hierarchy was the primary means for organizing and managing. They must learn from innovative approaches coming from younger unit managers closer to the action.

The Fallacy of Programmatic Change

Most change programs don't work because they are guided by a theory of change that is fundamentally flawed. The common belief is that the place to begin is with the knowledge and attitudes of individuals. Changes in attitudes, the theory goes, lead to changes in individual behavior. And changes in individual behavior, repeated by many people, will result in organizational change. According to this model, change is like a conversion experience. Once people "get religion," changes in their behavior will surely follow.

This theory gets the change process exactly backward. In fact, individual behavior is powerfully shaped by the organizational roles that people play. The most effective way to change behavior, therefore, is to put people into a new organizational context, which imposes new roles, responsibilities, and relationships on them. This creates a situation that, in a sense, "forces" new attitudes and behaviors on people. (See the table, "Contrasting assumptions about change.")

One way to think about this challenge is in terms of three interrelated factors required for corporate revitalization. *Coordination* or teamwork is especially important if an organization is to discover and act on cost, quality, and product development opportunities. The production and sale of innovative, high-quality, low-cost products (or services) depend on close coordination among marketing, product design, and manufacturing departments, as well as between labor and management. High levels of *commitment* are essential for the effort, initiative, and cooperation that coordinated action demands. New *competencies* such as knowledge of the business as a whole, analytical skills, and interpersonal skills are necessary if people are to identify and solve problems as a team. If any of these elements are missing, the change process will break down.

WHICH STRATEGIES FOR CORPORATE change work, and which do not? We sought the answers in a comprehensive study of 12 large companies where top management was attempting to revitalize the corporation. Based on preliminary research, we identified 6 for in-depth analysis: 5 manufacturing companies and 1 large international bank. All had revenues between \$4 billion and \$10 billion. We studied 26 plants and divisions in these 6 companies and conducted hundreds of interviews with human resource managers; line managers engaged in change efforts at plants, branches, or business units; workers and union leaders; and, finally, top management.

Based on this material, we ranked the 6 companies according to the success with which they had managed the revitalization effort. Were there significant improvements in interfunctional coordination, decision making, work organizations, and concern for people? Research has shown that in the long term, the quality of these 4 factors will influence performance. We did not define success in terms of improved financial performance because, in the short run, corporate financial performance is influenced by many situational factors unrelated to the change process.

To corroborate our rankings of the companies, we also administered a standardized questionnaire in each company to understand how employers viewed the unfolding change process. Respondents rated their companies on a scale of 1 to 5. A score of 3 meant that no change had taken place; a score below 3 meant that, in the employee's judgment, the organization had actually gotten worse. As the table suggests, with one exception—the company we call Livingston Electronics—employees' perceptions of how much their companies had changed were identical to ours. And Livingston's relatively high standard of deviation (which measures the degree of consensus among employees about the outcome of the change effort) indicates that within the company there was considerable disagreement as to just how successful revitalization had been.

Researchers and employees—similar conclusions

Extent of revitalization

Company	Ranked by researchers	Rated by employees	
		Average	Standard deviation
General Products	1	4.04	.35
Fairweather	2	3.58	.45
Livingston Electronics	3	3.61	.76
Scranton Steel	4	3.30	.65
Continental Glass	5	2.96	.83
U.S. Financial	6	2.78	1.07

The problem with most companywide change programs is that they address only one or, at best, two of these factors. Just because a company issues a philosophy statement about teamwork doesn't mean its employees necessarily know what teams to form or how to function within them to improve coordination. A corporate reorganization may change the boxes on a formal organization chart but not provide the necessary attitudes and skills to make the new structure work. A pay-for-performance system may force managers to differentiate better performers from poorer ones, but it doesn't help them internalize new standards by which to judge subordinates' performances. Nor does it teach them how to deal effectively with performance problems. Such programs cannot provide the cultural context (role models from whom to learn) that people need to develop new competencies, so ultimately they fail to create organizational change.

Similarly, training programs may target competence, but rarely do they change a company's patterns of coordination. Indeed, the excitement engendered in a good corporate training program frequently leads to increased frustration when employees get back on the job only to see their new skills go unused in an organization in which nothing else has changed. People end up seeing training as a waste of time, which undermines whatever commitment to change a program may have roused in the first place.

Contrasting assumptions about change

Programmatic change	Task alignment
Problems in behavior are a function of individual knowledge, attitudes, and beliefs.	Individual knowledge, attitudes and beliefs are shaped by recurring patterns of behavioral interactions.
The primary target of renewal should be the content of attitudes and ideas; actual behavior should be secondary.	The primary target of renewal should be behavior; attitudes and ideas should be secondary.
Behavior can be isolated and changed individually.	Problems in behavior come from a circular pattern, but the effects of the organizational system on the individual are greater than those of the individual on the system.
The target for renewal should be at the individual level.	The target for renewal should be at the level of roles, responsibilities, and relationships.

When one program doesn't work, senior managers, like the CEO at U.S. Financial, often try another, instituting a rapid progression of programs. But this only exacerbates the problem. Because they are designed to cover everyone and everything, programs end up covering nobody and nothing particularly well. They are so general and standardized that they don't speak to the day-to-day realities of particular units. Buzzwords like "quality," "participation," "excellence," "empowerment," and "leadership" become a substitute for a detailed understanding of the business.

And all these change programs also undermine the credibility of the change effort. Even when managers accept the potential value of a particular program for others—quality circles, for example, to solve a manufacturing problem—they may be confronted with another, more pressing business problem such as new product development. One-size-fits-all change programs take energy away from efforts to solve key business problems—which explains why so many general managers don't support programs, even when they acknowledge that their underlying principles may be useful.

This is not to state that training, changes in pay systems or organizational structure, or a new corporate philosophy are always inappropriate. All can play valuable roles in supporting an integrated change effort. The problems

come when such programs are used in isolation as a kind of “magic bullet” to spread organizational change rapidly through the entire corporation. At their best, change programs of this sort are irrelevant. At their worst, they actually inhibit change. By promoting skepticism and cynicism, programmatic change can inoculate companies against the real thing.

Six Steps to Effective Change

Companies avoid the shortcomings of programmatic change by concentrating on “task alignment”—reorganizing employee roles, responsibilities, and relationships to solve specific business problems. Task alignment is easiest in small units—a plant, department, or business unit—where goals and tasks are clearly defined. Thus the chief problem for corporate change is how to promote task-aligned change across many diverse units.

We saw that general managers at the business unit or plant level can achieve task alignment through a sequence of six overlapping but distinctive steps, which we call the *critical path*. This path develops a self-reinforcing cycle of commitment, coordination, and competence. The sequence of steps is important because activities appropriate at one time are often counterproductive if started too early. Timing is everything in the management of change.

1. Mobilize commitment to change through joint diagnosis of business problems. As the term task alignment suggests, the starting point of any effective change effort is a clearly defined business problem. By helping people develop a shared diagnosis of what is wrong in an organization and what can and must be improved, a general manager mobilizes the initial commitment that is necessary to begin the change process.

Consider the case of a division we call Navigation Devices, a business unit of about 600 people set up by a large corporation to commercialize a product originally designed for the military market. When the new general manager took over, the division had been in operation for several years without ever making a profit. It had never been able to design and produce a high-quality, cost-competitive product. This was due largely to an organization in which decisions were made at the top, without proper involvement of or coordination with other functions.

The first step the new general manager took was to initiate a broad review

of the business. Where the previous general manager had set strategy with the unit's marketing director alone, the new general manager included his entire management team. He also brought in outside consultants to help him and his managers function more effectively as a group.

Next, he formed a 20-person task force representing all the stakeholders in the organization—managers, engineers, production workers, and union officials. The group visited a number of successful manufacturing organizations in an attempt to identify what Navigation Devices might do to organize more effectively. One high-performance manufacturing plant in the task force's own company made a particularly strong impression. Not only did it highlight the problems at Navigation Devices but it also offered an alternative organizational model, based on teams, that captured the group's imagination. Seeing a different way of working helped strengthen the group's commitment to change.

The Navigation Devices task force didn't learn new facts from this process of joint diagnosis; everyone already knew the unit was losing money. But the group came to see clearly the organizational roots of the unit's inability to compete and, even more important, came to share a common understanding of the problem. The group also identified a potential organizational solution: to redesign the way it worked, using ad hoc teams to integrate the organization around the competitive task.

2. Develop a shared vision of how to organize and manage for competitiveness. Once a core group of people is committed to a particular analysis of the problem, the general manager can lead employees toward a task-aligned vision of the organization that defines new roles and responsibilities. These new arrangements will coordinate the flow of information and work across interdependent functions at all levels of the organization. But since they do not change formal structures and systems like titles or compensation, they encounter less resistance.

At Navigation Devices, the 20-person task force became the vehicle for this second stage. The group came up with a model of the organization in which cross-functional teams would accomplish all work, particularly new product development. A business-management team composed of the general manager and his staff would set the unit's strategic direction and review the work of lower level teams. Business-area teams would develop plans for

specific markets. Product-development teams would manage new products from initial design to production. Production-process teams composed of engineers and production workers would identify and solve quality and cost problems in the plant. Finally, engineering-process teams would examine engineering methods and equipment. The teams got to the root of the unit's problems—functional and hierarchical barriers to sharing information and solving problems.

To create a consensus around the new vision, the general manager commissioned a still larger task force of about 90 employees from different levels and functions, including union and management, to refine the vision and obtain everyone's commitment to it. On a retreat away from the workplace, the group further refined the new organizational model and drafted a values statement, which it presented later to the entire Navigation Devices work force. The vision and the values statement made sense to Navigation Devices employees in a way many corporate mission statements never do—because it grew out of the organization's own analysis of real business problems. And it was built on a model for solving those problems that key stakeholders believed would work.

3. Foster consensus for the new vision, competence to enact it, and cohesion to move it along. Simply letting employees help develop a new vision is not enough to overcome resistance to change—or to foster the skills needed to make the new organization work. Not everyone can help in the design, and even those who do participate often do not fully appreciate what renewal will require until the new organization is actually in place. This is when strong leadership from the general manager is crucial. Commitment to change is always uneven. Some managers are enthusiastic; others are neutral or even antagonistic. At Navigation Devices, the general manager used what his subordinates termed the “velvet glove.” He made it clear that the division was going to encourage employee involvement and the team approach. To managers who wanted to help him, he offered support. To those who did not, he offered outplacement and counseling.

Once an organization has defined new roles and responsibilities, people need to develop the competencies to make the new setup work. Actually, the very existence of the teams with their new goals and accountabilities will force learning. The changes in roles, responsibilities, and relationships foster

new skills and attitudes. Changed patterns of coordination will also increase employee participation, collaboration, and information sharing.

But management also has to provide the right supports. At Navigation Devices, six resource people—three from the unit's human resource department and three from corporate headquarters—worked on the change project. Each team was assigned one internal consultant, who attended every meeting, to help people be effective team members. Once employees could see exactly what kinds of new skills they needed, they asked for formal training programs to develop those skills further. Since these courses grew directly out of the employees' own experiences, they were far more focused and useful than traditional training programs.

Some people, of course, just cannot or will not change, despite all the direction and support in the world. Step three is the appropriate time to replace those managers who cannot function in the new organization—after they have had a chance to prove themselves. Such decisions are rarely easy, and sometimes those people who have difficulty working in a participatory organization have extremely valuable specialized skills. Replacing them early in the change process, before they have worked in the new organization, is not only unfair to individuals; it can be demoralizing to the entire organization and can disrupt the change process. People's understanding of what kind of manager and worker the new organization demands grows slowly and only from the experience of seeing some individuals succeed and others fail.

Once employees have bought into a vision of what's necessary and have some understanding of what the new organization requires, they can accept the necessity of replacing or moving people who don't make the transition to the new way of working. Sometimes people are transferred to other parts of the company where technical expertise rather than the new competencies is the main requirement. When no alternatives exist, sometimes they leave the company through early retirement programs, for example. The act of replacing people can actually reinforce the organization's commitment to change by visibly demonstrating the general manager's commitment to the new way.

Some of the managers replaced at Navigation Devices were high up in the organization—for example, the vice president of operations, who oversaw the engineering and manufacturing departments. The new head of manufacturing was far more committed to change and skilled in leading a critical path

change process. The result was speedier change throughout the manufacturing function.

4. Spread revitalization to all departments without pushing it from the top. With the new ad hoc organization for the unit in place, it is time to turn to the functional and staff departments that must interact with it. Members of teams cannot be effective unless the department from which they come is organized and managed in a way that supports their roles as full-fledged participants in team decisions. What this often means is that these departments will have to rethink their roles and authority in the organization.

At Navigation Devices, this process was seen most clearly in the engineering department. Production department managers were the most enthusiastic about the change effort; engineering managers were more hesitant. Engineering had always been king at Navigation Devices; engineers designed products to the military's specifications without much concern about whether manufacturing could easily build them or not. Once the new team structure was in place, however, engineers had to participate on product-development teams with production workers. This required them to re-examine their roles and rethink their approaches to organizing and managing their own department.

The impulse of many general managers faced with such a situation would be to force the issue—to announce, for example, that now all parts of the organization must manage by teams. The temptation to force newfound insights on the rest of the organization can be great, particularly when rapid change is needed, but it would be the same mistake that senior managers make when they try to push programmatic change throughout a company. It short-circuits the change process.

It's better to let each department "reinvent the wheel"—that is, to find its own way to the new organization. At Navigation Devices, each department was allowed to take the general concepts of coordination and teamwork and apply them to its particular situation. Engineering spent nearly a year agonizing over how to implement the team concept. The department conducted two surveys, held off-site meetings, and proposed, rejected, then accepted a matrix management structure before it finally got on board. Engineering's decision to move to matrix management was not surprising, but because it was its own choice, people committed themselves to learning

the necessary new skills and attitudes.

5. Institutionalize revitalization through formal policies, systems, and structures. There comes a point where general managers have to consider how to institutionalize change so that the process continues even after they've moved on to other responsibilities. Step five is the time: the new approach has become entrenched, the right people are in place, and the team organization is up and running. Enacting changes in structures and systems any earlier tends to backfire. Take information systems. Creating a team structure means new information requirements. Why not have the MIS department create new systems that cut across traditional functional and departmental lines early in the change process? The problem is that without a well-developed understanding of information requirements, which can best be obtained by placing people on task-aligned teams, managers are likely to resist new systems as an imposition by the MIS department. Newly formed teams can often pull together enough information to get their work done without fancy new systems. It's better to hold off until everyone understands what the team's information needs are.

What's true for information systems is even more true for other formal structures and systems. Any formal system is going to have some disadvantages; none is perfect. These imperfections can be minimized, however, once people have worked in an ad hoc team structure and learned what interdependencies are necessary. Then employees will commit to them too.

Again, Navigation Devices is a good example. The revitalization of the unit was highly successful. Employees changed how they saw their roles and responsibilities and became convinced that change could actually make a difference. As a result, there were dramatic improvements in value added per employee, scrap reduction, quality, customer service, gross inventory per employee, and profits. And all this happened with almost no formal changes in reporting relationships, information systems, evaluation procedures, compensation, or control systems.

When the opportunity arose, the general manager eventually did make some changes in the formal organization. For example, when he moved the vice president of operations out of the organization, he eliminated the position altogether. Engineering and manufacturing reported directly to him

from that point on. For the most part, however, the changes in performance at Navigation Devices were sustained by the general manager's expectations and the new norms for behavior.

6. Monitor and adjust strategies in response to problems in the revitalization process. The purpose of change is to create an asset that did not exist before—a learning organization capable of adapting to a changing competitive environment. The organization has to know how to continually monitor its behavior—in effect, to learn how to learn.

Some might say that this is the general manager's responsibility. But monitoring the change process needs to be shared, just as analyzing the organization's key business problem does.

At Navigation Devices, the general manager introduced several mechanisms to allow key constituents to help monitor the revitalization. An oversight team—composed of some crucial managers, a union leader, a secretary, an engineer, and an analyst from finance—kept continual watch over the process. Regular employee attitude surveys monitored behavior patterns. Planning teams were formed and reformed in response to new challenges. All these mechanisms created a long-term capacity for continual adaptation and learning.

The six-step process provides a way to elicit renewal without imposing it. When stakeholders become committed to a vision, they are willing to accept a new pattern of management—here the ad hoc team structure—that demands changes in their behavior. And as the employees discover that the new approach is more effective (which will happen only if the vision aligns with the core task), they have to grapple with personal and organizational changes they might otherwise resist. Finally, as improved coordination helps solve relevant problems, it will reinforce team behavior and produce a desire to learn new skills. This learning enhances effectiveness even further and results in an even stronger commitment to change. This mutually reinforcing cycle of improvements in commitment, coordination, and competence creates a growing sense of efficacy. It can continue as long as the ad hoc team structure is allowed to expand its role in running the business.

The Role of Top Management

To change an entire corporation, the change process we have described must be applied over and over again in many plants, branches, departments, and divisions. Orchestrating this companywide change process is the first responsibility of senior management. Doing so successfully requires a delicate balance. Without explicit efforts by top management to promote conditions for change in individual units, only a few plants or divisions will attempt change, and those that do will remain isolated. The best senior manager leaders we studied held their subordinates responsible for starting a change process without specifying a particular approach.

Create a market for change. The most effective approach is to set demanding standards for all operations and then hold managers accountable to them. At our best-practice company, which we call General Products, senior managers developed ambitious product and operating standards. General managers unable to meet these product standards by a certain date had to scrap their products and take a sharp hit to their bottom lines. As long as managers understand that high standards are not arbitrary but are dictated by competitive forces, standards can generate enormous pressure for better performance, a key ingredient in mobilizing energy for change.

But merely increasing demands is not enough. Under pressure, most managers will seek to improve business performance by doing more of what they have always done—overmanage—rather than alter the fundamental way they organize. So, while senior managers increase demands, they should also hold managers accountable for fundamental changes in the way they use human resources.

For example, when plant managers at General Products complained about the impossibility of meeting new business standards, senior managers pointed them to the corporate organization-development department within human resources and emphasized that the plant managers would be held accountable

for moving revitalization along. Thus top management had created a demand system for help with the new way of managing, and the human resource staff could support change without appearing to push a program.

Use successfully revitalized units as organizational models for the entire company. Another important strategy is to focus the company's attention on plants and divisions that have already begun experimenting with management innovations. These units become developmental laboratories for further innovation.

There are two ground rules for identifying such models. First, innovative units need support. They need the best managers to lead them, and they need adequate resources—for instance, skilled human resource people and external consultants. In the most successful companies that we studied, senior managers saw it as their responsibility to make resources available to leading-edge units. They did not leave it to the human resource function.

Second, because resources are always limited and the costs of failure high, it is crucial to identify those units with the likeliest chance of success. Successful management innovations can appear to be failures when the bottom line is devastated by environmental factors beyond the unit's control. The best models are in healthy markets.

Obviously, organizational models can serve as catalysts for change only if others are aware of their existence and are encouraged to learn from them. Many of our worst-practice companies had plants and divisions that were making substantial changes. The problem was, nobody knew about them. Corporate management had never bothered to highlight them as examples to follow. In the leading companies, visits, conferences, and educational programs facilitated learning from model units.

Develop career paths that encourage leadership development. Without strong leaders, units cannot make the necessary organizational changes, yet the scarcest resource available for revitalizing corporations is leadership. Corporate renewal depends as much on developing effective change leaders as it does on developing effective organizations. The personal learning associated with leadership development—or the realization by higher management that a manager does not have this capacity—cannot occur in the classroom. It only happens in an organization where the teamwork, high

commitment, and new competencies we have discussed are already the norm.

The only way to develop the kind of leaders a changing organization needs is to make leadership an important criterion for promotion, and then manage people's careers to develop it. At our best-practice companies, managers were moved from job to job and from organization to organization based on their learning needs, not on their position in the hierarchy. Successful leaders were assigned to units that had been targeted for change. People who needed to sharpen their leadership skills were moved into the company's model units where those skills would be demanded and therefore learned. In effect, top management used leading-edge units as hothouses to develop revitalization leaders.

But what about the top management team itself? How important is it for the CEO and his or her direct reports to practice what they preach? It is not surprising—indeed, it's predictable—that in the early years of a corporate change effort, top managers' actions are often not consistent with their words. Such inconsistencies don't pose a major barrier to corporate change in the beginning, though consistency is obviously desirable. Senior managers can create a climate for grass-roots change without paying much attention to how they themselves operate and manage. And unit managers will tolerate this inconsistency so long as they can freely make changes in their own units in order to compete more effectively.

There comes a point, however, when addressing the inconsistencies becomes crucial. As the change process spreads, general managers in the ever-growing circle of revitalized units eventually demand changes from corporate staff groups and top management. As they discover how to manage differently in their own units, they bump up against constraints of policies and practices that corporate staff and top management have created. They also begin to see opportunities for better coordination between themselves and other parts of the company over which they have little control. At this point, corporate organization must be aligned with corporate strategy, and coordination between related but hitherto independent businesses improved for the benefit of the whole corporation.

None of the companies we studied had reached this "moment of truth." Even when corporate leaders intellectually understood the direction of change, they were just beginning to struggle with how they would change themselves and the company as a whole for a total corporate revitalization.

This last step in the process of corporate renewal is probably the most

important. If the CEO and his or her management team do not ultimately apply to themselves what they have been encouraging their general managers to do, then the whole process can break down. The time to tackle the tough challenge of transforming companywide systems and structures comes finally at the end of the corporate change process.

At this point, senior managers must make an effort to adopt the team behavior, attitudes, and skills that they have demanded of others in earlier phases of change. Their struggle with behavior change will help sustain corporate renewal in three ways. It will promote the attitudes and behavior needed to coordinate diverse activities in the company; it will lend credibility to top management's continued espousal of change; and it will help the CEO identify and develop a successor who is capable of learning the new behaviors. Only such a manager can lead a corporation that can renew itself continually as competitive forces change.

Companies need a particular mind-set for managing change: one that emphasizes process over specific content, recognizes organization change as a unit-by-unit learning process rather than a series of programs, and acknowledges the payoffs that result from persistence over a long period of time as opposed to quick fixes. This mind-set is difficult to maintain in an environment that presses for quarterly earnings, but we believe it is the only approach that will bring about successful renewal.

Originally published in November 1990. Reprint 90601

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